

HM Treasury – A new approach to financial regulation

The following extract is taken from the Treasury consultation document 'A new approach to financial regulation: judgement, focus and stability' (HMT, July 2010). The original text was read by Simon Morris, Partner at CMS Cameron McKenna, who highlights important details from the paper below.

1. Introduction

The financial crisis and the failure of the UK regulatory framework

The UK banking system is **emerging from the most serious financial crisis** in over a hundred years. In order to avert a total banking collapse, the last Government had to part-nationalise two of the largest banks in the world, and introduce financial sector interventions costing hundreds of billions of pounds.

There is now an **emerging consensus on the fundamental causes** of the crisis, citing factors such as:

- global economic imbalances;
- mispriced and misunderstood risk;
- unsustainable funding and business models for banks;
- excessive build up of debt across the financial system; and
- the growth of an unregulated 'shadow banking' system.

The UK financial system, which is one of the most open, globalised and successful in the world, was impacted by these factors as much as, if not more than, any other. Attempting to explain the crisis purely in terms of global trends, however, is to **ignore a fundamentally important point; there were real and significant failings in the UK regulatory framework**. This meant that regulators failed in recognising and responding to the problems that were emerging in the financial system.

The UK's '**tripartite**' regulatory system made three authorities – the Bank of England (the Bank), the Financial Services Authority (FSA) and the Treasury – collectively responsible for financial stability, and, as a result, this system **failed in a number of important ways**. For example, it failed:

- to identify the problems that were building up in the financial system;
- to take steps to mitigate them before they led to significant instability in financial markets; and
- to deal adequately with the crisis when it did break, especially during the first part of the crisis in the summer of 2007.

These failures arose because **the tripartite model contains a number of inherent weaknesses and contradictions**. For example:

- it places responsibility for all financial regulation in the hands of a single, monolithic financial regulator, the Financial Services Authority (FSA), which is expected to deal with issues ranging from the safety and soundness of the largest global investment banks to the customer practices of the smallest high-street financial adviser;
- it gives the Bank nominal responsibility – and, since the Banking Act 2009, statutory obligations – for financial stability, but does not provide it with the tools or levers to carry out this role effectively; and
- it gives the Treasury responsibility for maintaining the overall legal and institutional framework, but no clear responsibility for dealing with a crisis which put tens of billions of pounds worth of public funds at risk.

Perhaps the most obvious failing of the UK system, however, is the fact that **no single institution has the responsibility, authority or powers** to monitor the system as a whole, identify potentially destabilising trends, and respond to them with concerted action ... a phenomenon whereby macro-prudential risk analysis and mitigation fell between the gaps in the UK regulatory system.

... In the run up to the financial crisis, **financial supervision relied too much on 'tick-box' compliance with rules and directives at the expense of proper in-depth and strategic risk analysis**. Effective prudential regulation of firms requires an approach based on understanding of their business models, and the ability to make judgements about the risks that firms' activities pose to themselves and to the wider financial system as a whole. (1.1 – 1.9)

Reforming the tripartite model

In addition to dealing with the operational failings of the system introduced between 1997 and 2000, the Government believes that reform to the regulatory framework must address a number of fundamental issues.

Financial Policy Committee

Macro-prudential policy has two main objectives:

- improving the **overall resilience** of the financial system by addressing aggregate risks and vulnerabilities across the system that have the potential to threaten stability; and
- enhancing **macroeconomic stability** by addressing cyclical imbalances through the financial system, e.g. by damping the credit cycle. (Box 2A)

There must be a **dedicated focus on macro-prudential analysis and action**, to ensure that risks developing across the financial system as a whole are identified and responded to ... the Government will **create a new Financial Policy Committee (FPC) in the Bank of England**, with primary statutory responsibility for maintaining financial stability ... with control of macro-prudential tools to ensure that systemic risks to financial stability are dealt with. The FPC will work internationally with similar systemically-focused authorities, such as the G20 Financial Stability Board, and the European Systemic Risk Board, as well as national regulators where appropriate, to coordinate macro-prudential policy. (1.10 – 1.12)

Prudential Regulation Authority

Prudential regulation ... macro-prudential regulation of the financial system [must be] coordinated effectively with the prudential regulation of individual firms, **and a new, more judgement-focused approach to regulation of firms is adopted** so that business models can be challenged, risks identified and action taken to preserve stability.

... the Government will **transfer operational responsibility for prudential regulation** from the FSA to a new subsidiary of the Bank of England. This new Prudential Regulation Authority (PRA) will be responsible for prudential regulation of all deposit-taking institutions insurers and investment banks. By placing firm-specific prudential regulation under the auspices of the Bank, the Government **will bring together responsibility for macro- and micro-prudential regulation in a single institution** ... The FPC will be able, within the remit of macro-prudential policy, to require the PRA to take regulatory action with respect to all firms, for example ... an increase in the capital held by firms during an upswing in the credit cycle ... the FPC could have similar macro-prudential controls over the new conduct regulator ... the PRA will also be **operationally responsible for the regulation and supervision of individual firms**. It will provide firm-specific information to the FPC to illustrate the potential impact of emerging system-level risks on specific types of institution. (1.13 – 18)

Consumer Protection & Markets Authority

... including the conduct of firms towards their retail customers, and the conduct of participants in wholesale financial markets – will be carried out by a dedicated, specialist body with focused and clear statutory objectives and regulatory functions ... The Government will create a **dedicated consumer protection and markets authority** (CPMA) with a primary statutory responsibility to promote confidence in financial services and markets ...

... the Government will take the creation of the CPMA as an opportunity to examine how consumer protection is enshrined in FSMA and **what changes may be needed** to update or strengthen the regime. Combined with a **more proactive, interventionist approach** to retail conduct regulation by the new regulator, the Government's new framework will ensure that consumers are able to operate with greater certainty and confidence in financial services. (4.50 – 52)

The impact

Most of the approximately 20,000 firms currently regulated by the FSA will be **regulated solely by the CPMA** after the reforms have been implemented. These firms are unlikely to suffer any significant costs as a result of the reforms.

About 1,500 – 2,000 firms are likely to **prudentially supervised** by the PRA while also subject to **conduct of business** regulation by the CPMA. There are about 100 – 200 groups containing both PRA and CPMA firms. These firms/groups are likely to incur transitional costs ... and may face higher ongoing costs.

The Government will also be considering **whether to extend supervisory powers** to cover currently unregulated holding companies and unregulated entities within the group structure of financial institutions such as banks and insurers. (From the Cost Benefit Analysis)

Interim steps & timetable

The FSA will work to introduce a '**shadow**' internal structure, which will allocate FSA staff and responsibilities in anticipation of the formal creation of the CPMA and the PRA ... in the first quarter of 2011 ... The FSA will continue to engage with external stakeholders as appropriate as its thinking develops, and it and the Bank will continue to work closely with the Government on the development of the new regulatory structure. (7.9)

The content of the **legislation** [in mid-2011] will cover, at a minimum:

- the creation of the FPC, its objectives and governance arrangements;
- any related reforms to the governance of the Bank of England, including the removal from statute of the Bank's Financial Stability Committee (FSC);
- the creation of the PRA and the CPMA (along with their objectives and governance arrangements);
- assigning regulatory functions to the PRA and CPMA; and
- practical and transitional arrangements such as staff and property transfer.

In order to minimise uncertainty for regulated firms the Government will seek to ensure the passage of the necessary primary legislation within two years. (7.12 – 14)

2. The specific proposals

Macro-prudential regulation

There is an established international consensus on two points:

- that a macro-prudential or systemic perspective on regulation must be incorporated into financial regulatory systems around the world.
- that central banks' broad overview of the financial sector and the close link between monetary stability and systemic regulation **make them ideally placed** to lead on macro-prudential regulation.

The **intimate relationship** between macro-prudential regulation, micro-prudential regulation and supervision, and the provision of liquidity insurance to banks means that there are clear advantages and synergies in having these functions being carried out within the same organisation – namely the central bank ... **central banks have a competitive edge** due to their first hand exposure to markets and the depth of their staff's experience in the functioning of financial firms and markets. In addition, the **information and knowledge that the central bank would acquire** as supervisory authority would support it in performing its other functions more effectively, such as fulfilling its role as provider of liquidity insurance, because information would flow more smoothly into its lender of last resort function. (2.7 – 14)

The Financial Policy Committee

... the Government will create a new FPC within the Bank of England, with responsibility for macro-prudential regulation. The committee will **monitor and address systemic or aggregate risks and vulnerabilities** that could threaten the stability of the sector as a whole and endanger the wider economy.

Within the Bank's overall financial stability remit, the **objective of the FPC** will be to protect financial stability by:

- **improving the resilience of the financial system** by identifying and addressing aggregate risks and vulnerabilities across the system; and
- **enhancing macroeconomic stability** by addressing imbalances through the financial system, e.g. by damping the credit cycle.

Decisions taken by the FPC [are] ... likely to affect the levels of lending to businesses and families and the competitiveness and profitability of UK banks in relation to foreign competitors ... (2.22 – 29)

The FPC's main function will be to **undertake macro-prudential regulation** ... [which splits into]

Monitoring functions:

- monitoring the financial stability of the UK's financial system, identifying emerging risks and vulnerabilities, and cyclical imbalances;
- monitoring and assessing the activities of the PRA and the CPMA, in order to identify any financial stability implications that may derive from these authorities' actions;
- monitoring the regulatory perimeter, both to ensure that the split ... between the PRA and the CPMA remains appropriate and to ensure that activities ... on or outside the boundary of prudential regulation with potentially systemic consequences are understood;
- assessing the effectiveness of the FPC's macro-prudential tools and considering any potential additions or adjustments to the toolkit.

Acting in response to risks and vulnerabilities identified:

- deciding whether macro-prudential tools should be used to address specific vulnerabilities and imbalances;
- giving directions to the PRA or the CPMA) on the regulatory tools that should be deployed in pursuit of macro-prudential policy, and how they should be formulated or calculated;
- making recommendations to the PRA and the CPMA where the FPC believes that specific regulatory actions ... are required in order to protect financial stability;
- making recommendations to Court in relation to other areas of the Bank's activities, [for example] to use its liquidity insurance functions to provide additional liquidity;
- making recommendations to the Treasury on changes to the regulatory perimeter and to the FPC's macro-prudential toolkit.

Reporting on action

... the FPC will be externally accountable to the Government, Parliament, and the public ... transparency will be an important aspect of this accountability, ensuring that the FPC fulfils its role effectively. Measures to provide transparency will include:

- publishing regular six-monthly financial stability reports ...
- publishing, after each meeting, a record of the FPC's deliberations, setting out the decisions it has taken and an explanation of the balance of arguments that led to those decisions. (2.30 – 33)

Macro-prudential tools

... the Government intends to provide the FPC with the control of specific macro-prudential tools ... **macro-prudential policy interventions** can (1) attempt to address fundamental vulnerabilities in the system (such as insufficient transparency and structural weaknesses); and (2) **attempt to increase the resilience of the financial system** to cyclical developments (including potentially damping the cycle), for which the following are possible levers:

- **Countercyclical capital requirements:** ... when private sector credit is growing rapidly, banks might be forced to hold additional levels of capital [to] increase the resilience of the banking sector [and also] damp the cycle by reducing lending in the upswing.
- **Variable risk weights:** ... raising capital requirements against specific types of lending if ... financial institutions' exposure to a certain asset class was too great, it could be discouraged
- **Leverage limits:** ... to impose an overall limit on the amount of leverage financial institutions can hold ...
- **Forward-looking loss provisioning:** Banks would be forced to set aside provisions against prospective future losses on their lending ...

- **Collateral requirements:** [to] limit specific types of lending by imposing higher collateral restrictions during times of unsustainable growth in that lending, for example loan-to-value limits on secured lending ...
- **Quantitative credit controls and reserve requirements:** ... by imposing limits on lenders and/or increasing financial institutions' short-term liquidity requirements ...

... these policy tools are likely to prove more effective **if adopted at the international level** and will continue to work with international counterparts to deliver such a system. (2.34 & Box 2C)

FPC Membership

- The FPC will have a total **membership** of 11, comprising six executives of the Bank of England and five members from outside the Bank. In addition, the FPC will include a Treasury representative.
- The FPC will be **chaired** by the Governor and will include the existing Deputy Governors for monetary policy and financial stability and the newly created Deputy Governor for prudential regulation. There will also be two Bank executives (responsible for financial stability and markets) on the FPC.
- The chief executive of the CPMA will sit on the FPC ...
- The FPC will have strong, credible **external representation** ... ensuring the credibility of the system and providing a wider range of experience and knowledge and divergent points of view to the committee's discussions. In particular, it will provide scope for the FPC to challenge the prevailing consensus ... (2.39 – 42)

Interaction with monetary policy

The Government proposes the following mechanisms to manage this interaction:

- Executive **cross-membership** of the FPC and MPC ...
- **Sequencing of meetings.** Meetings of the MPC and the FPC will be carefully sequenced in order to ensure that both committees are able to fully take into account the most recent decisions of the other.

The relationship between monetary policy and macro-prudential regulation

The objectives of **price stability and financial stability** should generally be consistent and complementary. A stable financial system makes the effects of monetary policy more predictable and supports the orderly operation of monetary policy. Price stability should, in turn, generally support financial stability ...

The MPC should be able to calibrate its monetary policy settings appropriately in response to macro-prudential regulation in a similar manner to the interaction between fiscal policy and monetary policy, allowing monetary policy to retain its primacy as the marginal instrument for macroeconomic policy ... (2.46 & Box 2D)

Links with the PRA and CPMA

... there will need to be **close cooperation** between the FPC and the PRA and the CPMA to ensure that the FPC is kept fully informed of any developments ... that may have an impact on financial stability. As the chief executives of the PRA and the CPMA are both FPC members, this interchange will **primarily take place within the FPC meetings themselves** ...

... the PRA and CPMA will also be under a **statutory obligation to consult the FPC** on any rules they intend to make which they feel would have material implications for financial stability.

The PRA (and CPMA where the FPC requires conduct-related information) will also be responsible for **collecting the supervisory information** which the FPC considers necessary for its role in monitoring systemic risk ... (2.48 – 51)

Transparency and accountability

The Government intends to legislate to establish that the FPC will publish a **regular six-monthly Financial Stability Report** (FSR). These reports will include the FPC's assessment of the outlook for the financial sector and a summary and description of the systemic risks and vulnerabilities it has identified, including an assessment of their severity. If the FPC has decided to take specific action in reaction to these threats, it will set out what this action consists of, and its rationale for the decision. (2.53)

Interim FPC

While the legislation to establish this new structure is being drafted and considered by Parliament, an interim FPC will be established by the autumn. Its membership will include, in addition to members of the Bank's executive, the chairman and chief executive of the FSA. The Government expects this body's role to be twofold:

- to carry out preparatory work and analysis in advance of the creation of the permanent FPC.
- to undertake, as far as practical, the permanent body's macro-prudential role. (7.11)

The role and functions of the PRA

The PRA will have a **primary objective to promote the stable and prudent operation of the financial system** through the effective regulation of financial firms, in a way which minimises the disruption caused by any firms which do fail. This objective will support the PRA in taking a **credible and appropriately intrusive approach** to regulation and supervision.

The PRA will also be provided with a **statutory range of factors** to which it must have regard in the carrying out of functions in pursuit of its primary objective ... The Government considers that such factors potentially fall into three categories:

- first, the **objectives of other regulatory authorities**, to which the PRA must have regard in carrying out its own functions in order to support effective coordination;
- second, **principles of good regulation** to which the PRA must have regard to ensure that the regulatory burden placed on firms is appropriate; and
- third, **other considerations** ... which relate to the public interest.

... the PRA will ... be **required to act proportionately and in accordance with regulatory good practice** ... [but] not all of the principles of good regulation which currently apply to the FSA ... should necessarily apply to the PRA ... making global competitiveness and innovation in financial services part of the responsibility of a regulator charged with ensuring the safety and soundness of risk-taking financial firms **needs to be reconsidered** ... one of the reasons for regulatory failure ... was **excessive concern for competitiveness** leading to a generalised acceptance of a **'light-touch' orthodoxy** and that lack of sufficient consideration or understanding of the impact of complex new financial transactions and products was facilitated by the view that financial innovation should be supported at all costs. (3.5 – 3.9)

... the PRA will be responsible for the **authorisation, regulation and day-to-day supervision** of all firms who are subject to significant prudential regulation ...

- banks and other deposit-takers (including building societies and credit unions);
- broker-dealers (or investment banks); and
- insurers (including friendly societies).

... the PRA[**'s regulated activities**] will include taking deposits, effecting and carrying out contracts of insurance, and dealing in investments as principal.

The PRA and CPMA will each be responsible for **granting or amending permissions** to undertake the regulated activities ... falling within their remit [and] for **approving persons** to undertake significant influence functions in authorised firms ... and for **rule-making, supervision and enforcement**.

The two authorities **will need to work closely** in making their respective decisions [which] will require a **significant degree of cooperation and coordination** by the authorities to ensure that they avoid duplicating efforts, or cutting across each other's work ... through a number of **formal processes** ...

- by putting in statute the requirement that each authority will have regard to the objectives of the other ...
- cross-membership of boards will form the basis of ongoing information exchange between the bodies ...
- statutory Memoranda of Understanding between the PRA and CPMA ... will set out in detail the mechanics of day to day cooperation and working together, as well as coordination on more strategic long-term thinking;
- where necessary [there will be] formal college-style mechanisms to support close joint working on the supervision of firms where both the CPMA and PRA have a supervisory interest ...

- ... information gateways between the PRA and CPMA to allow the flow of supervisory information
- the PRA and CPMA will ... consult each other on rules which they think may be relevant to the activities of the other [and] consult the FPC [where] there is a risk that the rule it proposes could have material adverse financial stability consequences; and
- ... the CPMA will be required to consult the PRA in advance of taking any decision that could cause a firm-specific financial stability risk, and [be guided by] the PRA's advice in such matters. (3.12 – 16; Box 3B)

Powers and functions of the PRA

... the legal framework for the PRA should underpin a **more informed and judgemental approach to regulation** ... The Government will consider whether any modifications or alternatives to FSMA are required to accomplish the objective of judgement-led prudential regulation, bearing in mind the importance of adhering to the two-year legislative timetable to which the Government is committed ...

Assuming that FSMA is to be the model for the PRA's legal framework, the Government will legislate to divide the powers and functions set out in FSMA into separate standalone prudential and conduct regulation frameworks ... The Government will consult on draft legislation ... in early 2011 ...

The **key functions of the PRA**, supported by the necessary legal powers, will include:

- **exercising judgements** about the safety and soundness of financial firms, and taking appropriate action;
- making **prudential rules** for the firms it regulates, covering all issues affecting the safety and soundness of individual firms (including, for example, remuneration).
- **authorisation of firms** by permissions to firms to engage in regulated activities;
- **supervision**, and where necessary, **enforcement** of compliance with rules ... the PRA and CPMA will work together to **coordinate action** where both authorities have a supervisory interest through **supervisory colleges** where appropriate, supported by information gateways;
- the **approval of individuals** to perform certain controlled functions within financial firms; and
- the **raising of levies** to fund the activities of the PRA. (3.17 – 26)

Board and management structures

The Deputy Governor for prudential regulation will be chief executive of the PRA. The Deputy Governor for financial stability and the chief executive of the CPMA will both be ex officio members of the PRA board. To ensure effective working between the PRA and CPMA, the chief executive of the PRA will sit on the CPMA's board, and vice versa ... the supervision of UK financial firms will benefit from the expertise, experience and credibility of the central bank ... (3.33 – 34)

Consumer Protection and Markets Authority

The new consumer protection and markets authority (CPMA) will be a **strong consumer champion** in pursuit of a single objective ... and a dedicated focus on the importance of proper conduct [to] ensure that the **interests of consumers and participants in financial markets** are placed at the heart of the conduct regulatory system and given the appropriate degree of priority.

The CPMA will therefore be established as the single integrated conduct regulator, **taking a tougher, more proactive and more focused approach** to regulating conduct in financial services and markets. The CPMA will regulate:

- **the conduct of all firms** – including all firms authorised and subject to prudential supervision by the Prudential Regulation Authority (PRA) – **in their dealings with ordinary retail consumers**, taking a proactive approach as a strong consumer champion; and
- **dealings in wholesale financial markets**, including the conduct of all financial services firms in wholesale markets, firms providing market services (such as investment exchanges and providers of multilateral trading facilities) and market conduct more generally (including market abuse). (4.3 – 4.4)

The role and functions of the CPMA

... the CPMA [will have] a **primary objective** of ensuring confidence in financial services and markets, with particular focus on protecting consumers and ensuring market integrity ... (4.6)

Scope

... the CPMA will have responsibility for the **conduct-of-business regulation of all financial institutions**, whether they are prudentially regulated by the PRA or not. The CPMA will **regulate all conduct**, including retail conduct of business, **where firms provide services to consumers**; and it will regulate **market conduct** where firms and others (particularly corporate clients of financial services firms) participate in dealings in wholesale financial markets.

The CPMA will be **solely responsible for the authorisation and supervision** of all financial institutions not regulated prudentially by the PRA, and will also write the prudential regulatory framework for those firms.

The CPMA will **create and enforce** retail conduct of business and market conduct rules, and its operations will therefore be supported by a strong and credible enforcement function. (4.14 – 16)

Powers and functions of the CPMA

The legal framework for the CPMA's powers and functions will be **based on the model set out in FSMA** ... the CPMA [will have] the following powers and functions:

- ... **making the rules** which govern the conduct of financial firms, in both the retail and wholesale spheres – conduct of business rules, and prudential rules for firms not regulated by the PRA. This will include rules around systems and controls where these relate to conduct functions. ... the CPMA will build on the progress recently made by the FSA towards a **more interventionist and pre-emptive approach** to retail conduct regulation ... it will adopt the FSA's new Retail Conduct of Business Strategy, and ... the Retail Distribution Review, Mortgage Market Review, and work on responsible lending [which] recognise and respond to [retail market issues] such as long-term product payoffs, product complexity and asymmetry of information between consumers and producers.
- the **granting of permissions** for all regulated activities classified as 'non-prudential'. It will be responsible for the authorisation of firms not regulated by the PRA and for providing permissions for conduct-based regulated activities undertaken by firms authorised by the PRA.;
- **supervision** of compliance with conduct of business rules, and of the prudential activity that sits within its remit.
- [There will be] a **strong approach to enforcement to ensure credible deterrence**.
- the **approval of individuals** to perform conduct-related controlled functions within financial firms that are also prudentially regulated by the PRA, and approval of all controlled functions where firms are solely regulated by the CPMA; and
- ... potentially the **raising of levies** to fund the activities of the PRA and CPMA and the collection of fees on behalf of the Financial Ombudsman Service (FOS), Financial Services Compensation Scheme (FSCS) and the Consumer Financial Education Body (CFEB).

The establishment of a new, focused body presents a key opportunity for a **frank and open debate** about **achieving the appropriate balance** between the regulation and supervision of firms, consumer responsibilities, consumer financial capability and the role of the state. (4.17 – 25)

Board and management structures

The CPMA will be governed by a board with a **majority of non-executives**, appointed by the Treasury. The chief executive of the PRA will sit ex officio on the board of the CPMA. Non-executive board members will be expected to have the necessary skills and background to bring the viewpoint of all relevant stakeholder groups to the board ... (4.32 – 34)

Funding

The CPMA and PRA will each **set the fees** ... in respect of the activities under their remit (with the CPMA setting fees for PRA-regulated firms only by reference to their conduct of business activity) ... avoiding cross-subsidy. ... the CPMA will make rules in respect of industry funding of the **FOS, FSCS and CFEB** ... A possible model would be to have CPMA **collect all fees** ... on their behalf. (4.40 – 42)

The Financial Ombudsman Service

It will be important for FOS to remain independent of the CPMA ... Its claim to impartiality, and hence its legitimacy in making rulings which are binding on firms, is only credible if it does not favour, or appear to favour, consumers. Therefore **it should not be part of a consumer champion** ... (4.44)

The Financial Services Compensation Scheme

The FSCS's ... core business of compensating consumers for the more frequent failures of small firms such as IFAs fits within the remit of the CPMA. However, its role in the failure of a bank, insurer or investment bank means that there is a clear link with the work of the PRA.

One [approach] would be for the PRA and the CPMA to make rules relating to compensation and levies for the different classes of firm which they regulate – **separate compensation schemes** ... ending the current cross-subsidy between different classes of levy payers [although] it may nevertheless be appropriate for a **single organisation** (such as FSCS) to continue to administer all compensation schemes.

Alternatively, the FSCS could **remain a single scheme** under the remit of the CPMA, who would make all of their rules ... The FSCS would need to work closely with the PRA and with the other authorities on contingency planning and on resolution in both models ... (4.45 – 47)

Consumer Credit

The creation of the CPMA as a strong consumer voice presents an ideal opportunity to look again at the **manner in which consumer credit is regulated**, and where this should be located, in order to maximise consumer protection and increase certainty and transparency for both consumers and businesses. Bringing together the FSA's and OFT's consumer credit functions within the scope of CPMA regulation and creating a regulatory regime covering both consumer credit and financial services **could simplify the regulatory regime** and lead to better, more integrated protection for consumers alongside simpler compliance for lenders and present an opportunity to remove unnecessary regulatory burdens and duplications. The Government therefore **intends to consult** on the merits of a transfer of responsibility for consumer credit from the OFT to the new CPMA ... The Government ... will only make a change to the status quo if there is a positive outcome of the consultation. (4.53 – 56)

Markets and infrastructure

... the Government will establish, within the consumer protection and markets authority (CPMA), a **strong markets division** to lead on all market conduct regulation, and to be the lead authority representing the UK in ESMA ... the Government will transfer regulation and supervision of **settlement systems and central counterparty clearing houses (CCPs)** to the Bank of England [to] sit alongside its existing responsibilities for payment systems oversight. (5.3 – 4)

Market conduct

The Government proposes to make the CPMA responsible for **regulating the conduct of participants** in:

- organised financial markets whose facilities are provided by **investment exchanges and multilateral trading facilities**;
- **over-the-counter (OTC) financial markets** in which off-exchange dealings take place bilaterally between financial institutions and other large wholesale market participants; and
- in relation (in principle) to **all financial instruments and other derivative contracts** traded on those markets. (5.8)

Regulation of infrastructure provision

The Government proposes to make:

- the markets division of the CPMA responsible for **regulating exchanges and other trading platform providers** – this reflects the importance of the facilities they provide for dealing in securities and derivatives and the significance of the activities of the providers and users for market conduct regulation; and
- the Bank responsible for **overseeing CCPs and settlement systems** alongside its existing responsibilities for payment systems oversight – this reflects the systemic importance of these types of infrastructure, the significant capital requirements and exposures that CCPs have and brings the regulation of all three types of body together for the first time.

- The Government expects that the supervision of market infrastructure will follow the same general principles of **cooperation, coordination and consultation** as for any other type of regulated entity. For example:
- in general, when **regulating market infrastructure**, the Bank will cooperate closely with the CPMA, reflecting the CPMA's responsibilities for: on-exchange and OTC financial markets; representing the UK in ESMA; and any conduct aspects of clearing houses and settlement systems; and
- in relation to **individual firms subject to regulation by both the Bank and the CPMA** (for example, where an investment exchange also operates its own in-house CCP) such a firm will be authorised and supervised by the Bank for clearing and settlement but it will be subject to conduct of business regulation and supervision by the CPMA in respect of non-financial stability matters. (5.12 – 16)

Listing and related activities

The Government believes ... that the functions of the **UKLA could be merged with** other regulatory functions relating to companies and corporate information, notably those of **the Financial Reporting Council (FRC)** ... The Government is therefore considering whether the UKLA should be merged with the FRC under the Department for Business, Innovation and Skills (BIS), or whether it should remain within the CPMA markets division. (5.21)

Economic crime

The Government proposes to consider ... whether to transfer responsibility for prosecuting criminal offences involving insider dealing, other forms of market abuse and other criminal law breaches which the FSA currently prosecutes to a new **Economic Crime Agency** ... (5.26)

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