

The Association of Corporate Treasurers

Comments in response to
***A new approach to financial regulation:
judgement, focus and stability***
HM Treasury
July 2010

18th October 2010

The Association of Corporate Treasurers (ACT)

The ACT is a professional body for those working in corporate treasury, risk and corporate finance. Further information is provided at the back of these comments and on our website www.treasurers.org.

Contact details are also at the back of these comments.

We canvas the opinion of our members through seminars and conferences, our monthly e-newsletter to members and others, *The Treasurer magazine*, topic-specific working groups and our Policy and Technical Committee.

General

The ACT welcomes the opportunity to comment on this matter.

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Response

We welcome the fact that you are addressing the structure of financial regulation in the UK. The recent financial crisis highlighted significant failings within the existing tripartite regulatory framework, notably the failure to monitor and analyse overall financial market exposures at a macro level. This lack of attention to aggregate and systemic risk has had a knock on impact to the management of financial risks within corporates. Since the crisis Corporate Treasurers have faced a number of challenges including but not limited to: lack of available funding, increased volatility in the markets and a changed attitude to risk – arguably an overreaction.

The ACT has responded to your consultation as our members, working in non-financial companies, are active users and in many ways dependent on the finance sector and financial markets.

Overall, we regret the proposed further fragmentation of UK financial regulation into three bodies, FPC, PRA and CPMA. We believe fragmentation can lead to problems similar to those the US faced during the financial crisis with its multiplicity of regulators. The relationship between the players and the role of HM Treasury above the regulators will be very important for smooth working of the UK regulatory system and its interrelation with the European level system.

The Bank of England and Financial Policy Committee (FPC) consultation questions:

Q1. Should the FPC have a single, clear, unconstrained objective relating to financial stability and its macro-prudential role, or should its objective be supplemented with secondary factors?

Refer general comment below Q3.

Q2. If you support the idea of secondary factors, what types of factors should be applied to the FPC?

Refer general comment below Q3.

Q3. How should these factors be formulated in legislation – for example, as a list of ‘have regards’ as is currently the case in the Financial Services and Markets Act 2000 (FSMA), or as a set of secondary statutory objectives which the FPC must balance?

We have not responded to all of the above consultation questions but provide the following comments:

- We agree with the sentiment that the FPC’s objectives need to be the objectives of the whole financial regulatory system.
- We believe the primary focus of the FPC should be at the macro level and that the FPC should be responsible for working internationally with national regulators. However our view is that the objectives of the FPC should be clarified and broadened to be not purely focused on financial stability but also promoting and fine tuning the real economy and finance sector. The quiet markets of financial stability must not turn into the silence of the grave.

- For clarity of objectives and to foster cooperation there should be a statutory obligation to take into account the objectives of the other bodies (PRA and CPMA).

Prudential regulation authority (PRA):

Q4. *The Government welcomes respondents' views on:*

- *Whether the PRA should have regard to the primary objectives of the CPMA and FPC;*
- *Whether some or all of the principles for good regulation currently set out in section 2 of FSMA, particularly those relating to good regulatory practice, should be retained for the PRA;*
- *Whether, specifically, the requirement to have regard to potential adverse impacts on innovation or the competitiveness of the UK financial services sector of regulatory action should be retained; and*
- *Whether there are any additional broader public interest considerations to which the PRA should have regard.*

The objectives of the PRA need to be such that at a minimum it will facilitate the work of the other bodies (FPC and CPMA). Directly responsible for supervision at the micro (individual firm) level it needs to do that in a way which enables, or at least does not make more difficult, the work of those responsible for meso (industry) level and macro (whole economy) levels.

We believe it is important that all authorities consider the impact of their actions on the competitiveness of the UK economy as a whole, including the finance sector and financial markets, and not merely "have regard tothe competitiveness of the UK financial services sector".

Q5. *Is the model proposed in paragraph 3.16 – with each authority responsible for all decisions within their remit subject to financial stability considerations – appropriate, or would an integrated model (for example, giving one authority responsibility for authorisation and removal of permissions) be preferable?*

Refer general comment below Q9.

Q6. *Is the approach outlined in paragraphs 3.17 to 3.23 for transfer of regulatory functions and rule making sufficient to enable the PRA to take a more risk-based, judgement-focussed approach to supervision?*

Refer general comment below Q9.

Q7. *Are safeguard on the PRA's rule-making function required?*

Refer general comment below Q9.

Q8. *If safeguards are required, how should the current FSMA safeguards be streamlined?*

Refer general comment below Q9.

Q9. The Government welcomes views on the measures proposed in paragraphs 3.28 to 3.41, which are designed to ensure that the operation of the PRSA is transparent, operationally independent and accountable.

We have not responded to all of the above consultation questions but provide the following comments:

Multiple front line agencies present a number of practical issues, including sharing of knowledge, duplication of effort etc. You have identified and propose that they “will work together” and have outlined a governance structure, a knowledge gateway and defined roles which should assist with this. However whilst there may be close cooperation there is a risk that a financial services regulator with split roles doesn’t have the same degree of credibility or status that a single integrated financial services regulator would.

You have proposed the following international roles:

- Within the Bank of England, the Financial Policy Committee (FPC) will be responsible for working internationally with national regulators;
- As the prudential regulator, the Prudential Regulatory Authority (PRA) will represent the UK on the new European supervisory authorities for banking and insurance; and
- The markets division of the Consumer Protection & Markets Authority (CPMA) will represent the UK at the new European Securities & Markets Authority (ESMA).

With only the CPMA representing the UK on the ESMA board, there is a real risk that any European market ruling which has a macro-prudential impact will not be authoritatively represented by the UK and will leave us with a weak voice in Europe. This will reduce the strength of the UK as a financial centre which will have a negative impact on the whole financial services industry and its contribution to the UK economy. The timing of this financial regulation restructure is unfortunate. As ESMA comes into being early next year, there is a risk that the UK’s perceived voice in the regulatory field will carry diminished weight when the Authority’s implementing rules and habits are being formed for the first time. We note that a partial solution to this problem has been found by appointing individuals to positions in both the central bank and the market regulator.

Consumer protection and market authority (CPMA):

Q10. The Government welcomes respondents’ views on:

- *Whether the CPMA should have regard to the stability of firms and the financial system as a whole, by reference to the primary objectives of the PRA and FPC;*
- *Whether some or all of the principles for good regulation currently set out in section 2 of FSMA should be retained for the CPMA, and if so, which;*
- *Whether, specifically, the requirement to have regard to potential adverse impacts on innovation or the competitiveness of the UK financial services sector of regulatory action should be retained; and*
- *Whether there are any additional broader public interest considerations to which the CPMA should have regard.*

The consultation document states “the Government considers that the case for regulators being responsible for the innovation and global competitiveness of the industries they regulate may, in particular, need to be reconsidered in the light of lessons learned from the financial crisis.” The argument being that one of the precursors to the crisis was that product innovation and global competitiveness took precedence. There is a risk that the UK financial markets become so heavily regulated and that UK competitiveness is ignored. The longer term detrimental impact could be that London ceases to be the financial capital of Europe.

The CPMA will regulate all conduct, including retail and market conduct. Retail and market regulation are very different and when combined in the one body can cause the following issues:

- We believe that the impact of the mass media and impact on individuals is likely to make the “Consumer Protection” side more politically visible than the Market division and in some ways is seen to be the senior party and prime focus within the CPMA. We therefore would see advantage if at the outset full statutory authority is provided for the Market regulation division to give it sufficient power and robustness so that it is in a position to carry out its role and not become subordinate to the possibly higher profile Consumer Protection division; and
- There is the potential for a conflict of interest between the two divisions and a resolution mechanism to deal with this that recognises the importance of both needs to be in place.

We agree that the CPMA should have regard to broader public interest considerations since too high a level of consumer protection can stifle the economy. There is also the question of defining “what is a consumer?” Small businesses, such as a sole proprietor are more akin to an individual consumer and may require more regulatory protection, whereas a large business, such as a FTSE 100 company, does not and would find it unduly restrictive. Even a small business (or a private investor of substance) may need access to financial services normally deemed unsuitable for retail access. There is a balance which requires defining of where to draw the line.

Q11. Are the accountability mechanisms proposed for the CPMA appropriate and sufficient for its role as an independent conduct regulator?

The accountability mechanisms proposed for the CPMA are: production of an annual report; annual public meetings; consultative panels (see below for details); maintain a complaints mechanism (with appeals in the Upper Tribunal); and reviews and enquiries. We make no detailed comment other than to point out that the new authorities will be subject to ad hoc scrutiny from the Treasury Select Committee, and that this forms a welcome additional strand to accountability.

Q12. The Government welcomes views on the role and membership of the three proposed statutory panels for the CPMA.

The three proposed statutory panels are the Consumer panel, Practitioner panel and the Small Business Practitioner Panel. We believe that these panels do provide a useful feedback mechanism from the markets and should be retained.

Q13. The Government welcomes views on the proposed funding arrangements, in particular, the proposal that the CPMA will be the fee and levy collecting body for all regulatory authorities and associated bodies.

No comment

Q14. The Government welcomes views on the proposed alternative options for operating models for the FSCS.

No comment

Markets and infrastructure:

Q15. The Government welcomes views on the proposed division of responsibilities for markets and infrastructure regulation.

No comment

Q16. The Government welcomes views on the possible rationalisation of the FSMA regimes for regulating exchanges, trading platforms and clearing houses.

The proposal is to rationalise the regulation of trading platforms and CCPs (regulated under FSMA).

At present the Bank of England oversees the Foreign exchange markets through the FX Joint Steering Committee and the NIPS Code. We are unclear as to where this responsibility would sit in the future. London is the global centre of the FX markets and for our members working in non financial companies the FX markets are used extensively for risk management. Some continuation of the present regime, even if brought under the CPMA needs consideration.

Q17. The Government would welcome views on whether the UKLA should be merged with the FRC, as a first step towards creating a companies regulator under BIS.

We are happy to see that the government has kept an open mind to this matter; however we would be dismayed if the proposal to merge the UK Listing Authority (UKLA) with the Financial Reporting Council (FRC) occurred. Whilst both entities are engaged in governance of corporate reporting, the nature of these disclosures is quite different. The UKLA regulates corporate disclosures that are current and forward looking in nature and part of marketing securities. The FRC is responsible for disclosures that report historical performance on an accountability basis, some information from which will be incorporated in the disclosures falling under the UKLA. The risks associated with each of these activities are quite different, both in their compilation and use by the markets.

Furthermore the UKLA would effectively become the primary markets regulator for securities so it is odd to separate primary markets supervision from secondary markets supervision which would sit within the CPMA. Ongoing market conduct, market abuse, and transparency are applicable to primary and secondary markets, so we would question separating regulation between the FRC and CPMA.

No other European country separates primary regulation from secondary. We presume that this is because there is an integrated securities market and therefore supervision must be closely integrated. A separated structure risks the UK's interface with and its reputation in European regulation.

Q18. The Government would also welcome views on whether there are other aspects of financial market regulation which could be made more effective by being moved into the proposed new companies regulator.

No comment

Crisis management:

Q19. Do you have any overall comments on the arrangements for crisis management?

In managing a crisis we believe the overriding interest should be at the macro level and not about individual banks. We thus support the *primus inter pares* role of the FPC.

Q20. What further powers of heightened supervision should be made available to the PRA and the CPMA, and in particular would there be advantages to mandatory intervention, as described in paragraph 6.17?

No comment

Q21. What are your views about changes that may be required to enhance accountability within the SRR, as described in paragraphs 6.21 to 6.24?

No comment

Impact assessment:

Q22. The Government welcomes comments on the assumptions made about transitional and ongoing costs for all types of firms.

No comment

The Association of Corporate Treasurers

The ACT is the international body for finance professionals working in treasury, risk and corporate finance. Through the ACT we come together as practitioners, technical experts and educators in a range of disciplines that underpin the financial security and prosperity of an organisation.

The ACT defines and promotes best practice in treasury and makes representations to government, regulators and standard setters.

We are also the world's leading examining body for international treasury, providing the widest scope of benchmark qualifications and continuing development through training, conferences and publications, including *The Treasurer* magazine and the annual *Treasurer's Handbook*, and online.

Our 4,000 members work widely in companies of all sizes through industry, commerce professional service firms.

Further information is available on our website (below).

Our policy with regards to policy and technical matters is available at <http://www.treasurers.org/technical/manifesto>

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