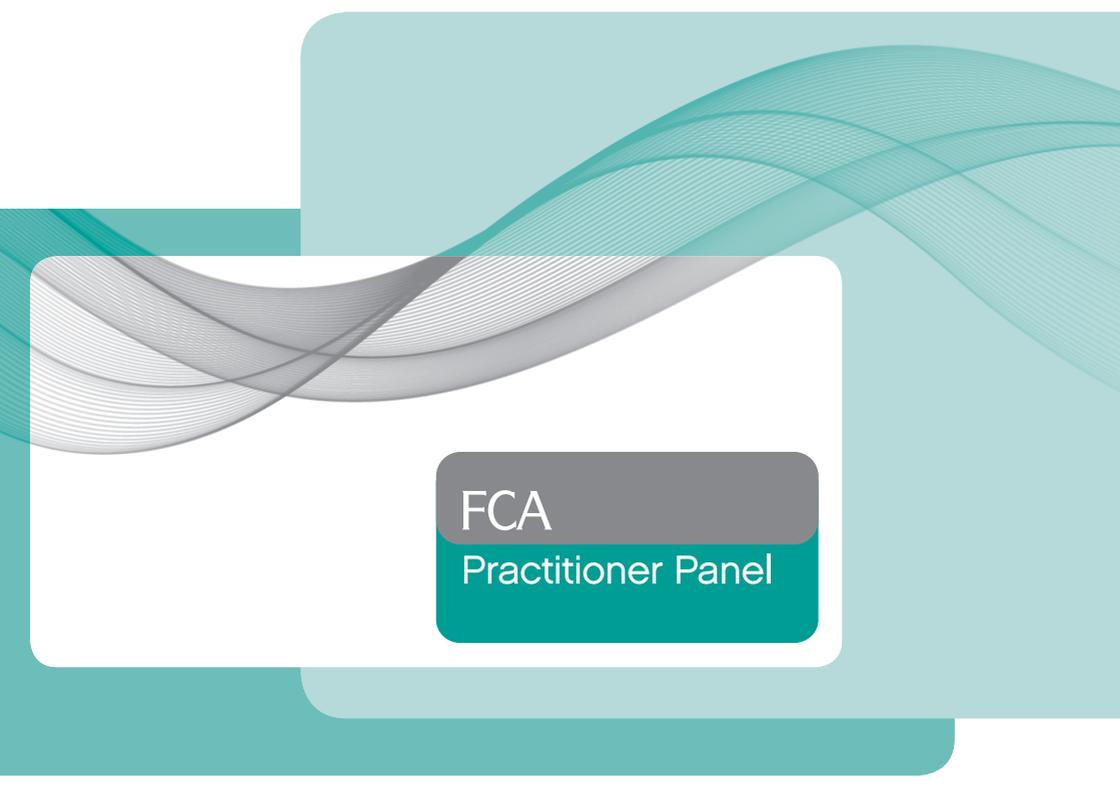


Annual Report

2014/15



FCA

Practitioner Panel



Chair's foreword

This year, we have been working within an environment of both planned and unanticipated challenges to the regulatory landscape. The work which had been planned included projects such as the implementation of the Financial Services (Banking Reform) Act, the regulation of consumer credit and the implementation of the Mortgage Market Review. In addition to this, there were further calls on the regulator's resources as a result of the Government's pensions initiatives and the significant challenges to the operation of the FCA following the events surrounding the 2014/15 Business Plan.

The FCA has made good progress against the delivery of its statutory objectives. The latest annual survey of industry views and perceptions shows a year on year improvement across most metrics and an increased confidence that the FCA can fulfil its objectives. The detailed findings of the survey will be available in a separate report on the Panel's website.

A significant area where the FCA has been challenged this year is in its communications strategy, specifically by the Davis Review and the Treasury Committee's review of the launch of the Business Plan. The Panel's main message to the regulator has been that communication should be fact and evidence based, and that there should be balance in its communications to rebuild confidence in the marketplace. We have encouraged the use of good practice examples to generate desired behaviours as well as publicising where firms have fallen short of the standards required.

We provided evidence to the Davis Review and the Treasury Committee and both have commented on the role of the statutory Panels, the expertise they provide, and their relationship with the FCA. We believe that the work of the Practitioner Panel is at its most effective when it has early access to policymaking, and when it has the opportunity to advise, to warn, and to provide practical information at a strategic level. Ensuring a good working relationship is one of our key priorities for next year.

One of the FCA's main tasks this year has been to implement the work of the Parliamentary Commission on Banking Standards. The main

challenge of this work has been to balance the demands of individual responsibility with the concept of collective decision making. Our view is that the regime must be realistic and practical in order to attract and retain talented individuals within the industry.

The industry has now had a chance to adapt to the requirements of the Retail Distribution Review, and although both the FCA and the Panel's own post-implementation research have showed that there have been benefits in the form of increased professionalism and clearer charging structures, there remains work to be done on communicating the status of advisers to customers. This will be part of the FCA's ongoing work on better consumer communications.

The past year has seen the FCA taking on the significant responsibility for the regulation of the consumer credit sector. It has also been given the task of setting and implementing a cap on the cost of high-cost short-term credit, which the Panel supported as a pragmatic approach.

The Panel's objectives last year focused on challenging the effectiveness of the FCA as a regulator; considering the strategic impact of regulation; and evaluating the advice regime. For next year, we will aim to build on the previous work of the Panel, and so will continue with two of our previous priorities: the FCA as an effective regulator; and the strategic impact of regulation. In addition we are keen to build a more effective relationship and two-way dialogue between the Panel and the FCA and so this will become our third priority.

My predecessor Graham Beale, in his foreword to the Panel's Annual Report described 2013/14 as 'a positive year dealing with some complicated issues but not without challenges'. Last year saw no reduction in either the number or the complexity of the challenges. I would like to thank Graham for his contribution as Chair over the past two years and we look forward to driving forward the Panel's objectives, based on the firm foundations he put in place.

Alison Brittain
Chair, FCA Practitioner Panel

1

Introduction

The FCA Practitioner Panel is a statutory Panel for the Financial Conduct Authority (FCA). It is one of a number of Panels which the FCA is required to establish and maintain under the Financial Services and Markets Act. The FCA Practitioner Panel is set up to represent the interests of practitioners to the FCA on the extent to which its general policies and practices are consistent with its general duties.

The Panel meets on a monthly basis to provide senior industry level input into the FCA, with membership selected to reflect the major sectors of the UK financial services industry. We focus predominantly on issues with a strategic cross-sectoral impact, and provide advice and feedback directly to the FCA Board and Executive.

We have contributed our opinions to the FCA on a range of topics, and have added to the debate by commissioning independent research and conducting an annual survey of industry practitioners about their view of the regulator.

For the second year of operation of the FCA, the Panel adopted the following priorities for its work, which provide the structure for this report:

The FCA as an effective regulator;

The strategic impact of regulation;

The advice regime and consumer responsibility.

2

The FCA as an effective regulator

This year the FCA has faced a number of new challenges, including the regulation of Consumer Credit, the implementation of the Financial Services (Banking Reform) Act 2013 and the launch of the Payment Systems Regulator.

There have also been unexpected challenges to the way the FCA operates, as result of the events surrounding the launch of the Business Plan in March/April 2014. These challenges have led to rigorous scrutiny of the way the FCA operates. Following on from that, there has been scrutiny of the role of the statutory Panels and the way they interact with the regulator.

In our Annual Report last year we encouraged the FCA to set out a clear long-term vision for regulation which would foster a well-functioning competitive market place for consumers and a successful, thriving industry for firms.

The Panel continues to be involved in the development of the FCA's plans at an early stage, to inform, advise and challenge. We have been, as would be expected of an independent body, robust but constructive in our input to the FCA's work. We continue to believe that early consultation will lead to more effective outcomes.

The Panel's Annual Survey for 2015 shows a small but significant increase in firms' perceptions of the effectiveness of the regulator.

Industry feedback

The FCA's objectives are to ensure an appropriate degree of protection for consumers, to protect and enhance the integrity of the UK financial system and to promote competition in the interests of consumers in the financial markets.

We commission an annual survey which aims to understand firms' views of the way the FCA is regulating the industry. Fieldwork for the 2014/15 survey took place in early 2015.

It is very positive that for the third year in a row, both the perceived effectiveness of the regulator and firms satisfaction with their relationship with the FCA have improved.

There has been a continued improvement in the confidence of the industry that the FCA will deliver against its statutory objectives, although confidence in the objective of promoting effective competition remains lower than confidence in the consumer protection and integrity objectives.

Although the survey indicates steady support for the work of the FCA, it has highlighted a measurable increase in concerns about cost of regulation. Nine out of ten of the largest firms stated that they have had to increase resource as a result of regulation over the past year. More than a third have stated that regulation has increased the cost of a product or caused them to withdraw a product or service. Within smaller firms the impact is not so great but almost

half have increased resources dealing with regulation.

Between 2014 and 2015 there has been an increase in the use of FCA communications as sources of information, with the main channels used being Regulation Roundup and the FCA website. Despite having a lower score than last year, the research shows that the use of external advisors is still the most important source of information for learning about regulation.

FCA Communications Strategy

In its Business Plan the FCA stated: 'We will be clear, consistent and constructive in our communications, engaging directly with consumers, firms and stakeholders as appropriate.'

The FCA's communications strategy has been under particular scrutiny this year following the events of April 2014, which led to the publication of the Davis report in December 2014 (see more in the 'launch of the 2014-2015 Business Plan' section below).

Our view is that broad policy, strategy and direction of regulation can be communicated at a macro level, but that the way in which these messages are conveyed is hugely important. An approach that is based on fact and evidence and that seeks to remove the likelihood of a sensational headline is a better way of communicating than courting such headlines in order to seek coverage. We have consistently encouraged the FCA to take into

account the quality as well as quantity of publicity received as a success measure for its communications strategy. The launch of the 2015-2016 Business Plan was a good example of a more fact-based approach.

We have said the FCA needs to be more balanced in its communications. As a regulator, the FCA should aim to assist in rebuilding confidence within the marketplace. We have encouraged the use of good practice examples which highlight areas where the industry has made improvements. Such recognition of improvements that firms have made, albeit with issues along the way, is a welcome positive tone.

The launch of the 2014-2015 Business Plan

The Panel provided input to the review by Simon Davis into the events surrounding publication of the FCA Business Plan in 2014. The Chairman of the Panel was also invited to provide evidence to the Treasury Committee for its report into the events in January 2015.

The Panel expressed its concerns about the events relating to the release and publicity of the 2014-15 Business Plan. We have noted the references in both the independent report by Simon Davis and the Treasury Committee to the work of the Panels and the extent to which their input had been sought. We welcomed the Treasury Committee's view, expressed in their report in March 2015, that the expertise of both the

Consumer and the Practitioner Panels needs to be used to better effect.

We agreed with the Davis Report's point that consultation about the nature and scope of initiatives such as thematic reviews serves a useful purpose and we look forward to discussions with the FCA about how best to do this.

In evidence to the Treasury Committee as well as input to the FCA, we have encouraged the FCA to look at the industry's risk and governance frameworks and ensure that the FCA's frameworks are at least as good. We have welcomed a further opportunity to engage, as recommended by the Davis Report, in providing input to the FCA's Internal Audit Division's reviews of internal and external communications and have started to provide this. We have suggested that the reviews include a challenge to the overall appropriateness of the FCA's communications framework, which states that communications must be clear, consistent, concise, constructive and compelling. The Panel's 2015 annual survey indicates that there has been a reduction in the use of the media as a source of regulatory information and we encourage the FCA to bear this in mind when considering its media strategy.

Enforcement as a regulatory tool

In its Business Plan for 2014-15 the FCA stated that if it found poor practice, it would use its enforcement powers to ensure that firms and individuals that don't follow its rules do not damage consumer interests or the integrity of and confidence in the markets. This is referred to as the 'credible deterrence' approach.

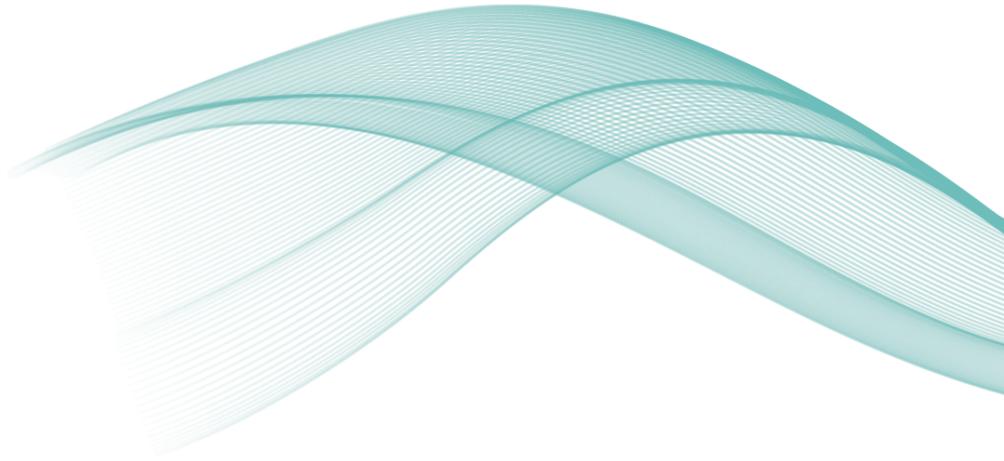
We have been supportive of the FCA's credible deterrence strategy but in responding to HM Treasury's call for evidence on regulatory decision-making in July 2014 we explained that we would welcome a refresh in its application with regard to proportionality, transparency and disclosure. We emphasised that to avoid undermining trust in firms and the industry more generally, the tone and content of communications from the regulators relating to the outcomes of enforcement action need to be balanced and factual, and should demonstrate an appreciation of their audience base.

The Panel's annual survey indicated that the industry overall believes the FCA's approach to enforcement to be a credible deterrent, but we have noted that a small but significant proportion of firms (29%) feel that the publication of fines undermines confidence in the industry.

Value for money of the FCA

This year the FCA worked on implementing the recommendations of the first report from the National Audit Office (NAO) since it took over responsibility for auditing the financial regulators on 1 April 2014.

We registered some concern that the fees required from the industry for the FCA for 2015-16 have increased by 8%. This follows a freeze on existing work, plus a limited increase of 3% to address the FCA's new responsibilities for 2014-15. The planned increase for next year is despite a reduction in expenditure on IT systems development and infrastructure. Following the NAO report we encourage the FCA to seek value for money for all its expenditure, whilst investing adequately in its information systems and technology platform to ensure that they support the key regulatory functions.



3

Strategic Impact of Regulation

Consumer confidence

In July 2014 the FCA's investigations showed that there had been an improvement in firms' handling of PPI complaints, which was welcome recognition of the work being done in this area. Complaints handling is a key element of customer interaction with firms and it is important for all involved that it is done well.

In response to the FCA's complaints-handling consultation in March 2015 we have alerted the FCA to the issue of 'professionalism' of complaints, meaning an increased complaint culture where a trivial issue is being used as a trigger to receive compensation over and above the financial impact caused, and where customers are using the Financial Ombudsman Service (FOS) as a driver.

A key concern is that the more time firms have to spend on spurious or purely opportunistic complaints the less time they are able to dedicate to resolving issues for customers who have a problem or may be in distress. We have suggested that a helpful way forward would be to agree with the FOS a more flexible way to determine if a complaint is vexatious.

Communication of expected conduct outcomes

Attestations are a supervisory tool used to ensure clear accountability and a focus from senior management on putting things right in regulated firms. When the FCA requests an attestation from an individual it does so to gain personal commitment from an approved person at a regulated firm that specific action has been taken or will be taken.

The Panel raised the use of attestations with the FCA. We highlighted that we believed the tool was in danger of skewing prioritisation of risk at firms, and was leading to much more discussion about terms of the attestation (including requiring legal support) than any party felt was helpful. We encouraged more transparency about the criteria for the use of attestations, and monitoring of their use. As a result, in August 2014 the FCA published more information about the circumstances in which attestations are used and the expected outcomes. Internally, revised guidance has been issued to supervisors, and quarterly statistics are now published.

Specific keynote regulation and regulatory change

We have actively engaged with particular FCA regulatory initiatives.

Senior Managers Regime

We engaged in detail with the FCA's work on accountability in banking which followed up on the recommendations from the Parliamentary Commission on Banking Standards. We have pointed out the potential difficulties in attracting and retaining talented individuals to senior positions if they perceive that they will be held responsible for actions which they could not reasonably be expected to influence. This is in addition to the presumption that senior managers are responsible for any contraventions that occur within their area of responsibility.

We have concerns that an increased focus on individual responsibility in governance structures may affect the balance of individual versus collective decision making. We believe that better decisions are made collectively, and that an excessive focus on the behaviour of individuals could have an adverse effect on businesses.

We have also commented on the remuneration proposals. In an environment where potential recruits can opt to work in different sectors, restrictions on the remuneration of financial services staff may result in potential new recruits being driven away from working in the industry and into other jobs where such remuneration rules do not apply.

Cash savings market study

We were concerned when the FCA announced in 2014 its intention to carry out a study into the cash savings market. In particular, we explained that the structural context is such that the FCA could not have chosen a more complicated time to conduct this study and to draw conclusions. We also made the point that price should not be the only factor in assessing consumer outcomes and the competitiveness of the market. There may be other factors which incentivise the same customers to stay with their existing provider.

Price cap on high-cost short-term credit

We noted the extensive research work behind the FCA's proposals on applying a cap to the cost of high-cost short-term credit, and were generally supportive of its proposals. It may be the case that its survey work may turn out to underestimate the potential increase in illegal lending as a result of the cap. It is therefore important that the FCA continues to work closely with the Illegal Money Lending team to monitor trends in illegal lending before and after the cap comes into effect, and takes targeted action where necessary.

Freedom and Choice in Pensions

We responded jointly with the Smaller Business Practitioner Panel to HM Treasury's consultation on Freedom and Choice in Pensions, following the announcements in the 2014 Budget on changes to the pension regime. We support the FCA in providing, monitoring and enforcing robust standards for the provision of pensions

guidance, and in regulating any developing secondary annuity market. This is an area where the FCA will need to be vigilant and consistent, as providers are understandably nervous about the long term responsibility for enabling customers to take control of their pension pots.

Mortgage Market Review (MMR)

We suggested the FCA should monitor and report on the effects of the MMR on the market from Day One. This will include reviewing areas such as how firms are implementing the new affordability rules and how they give advice to customers. The Panel has encouraged the FCA to take into account the importance of segmentation both at the customer level and the degree of sophistication, as well as the channel (whether direct or intermediated). We believe that the messaging should be constructive and not undermine the new process or feed into over-active media stories, and we would welcome definitions of good practice.

We welcomed the FCA's approach to negotiations on implementing the Mortgage Credit Directive, in parallel with MMR implementation, and the thought that has gone into ensuring that where possible the two initiatives are as closely aligned as possible.

FCA influence in EU policy

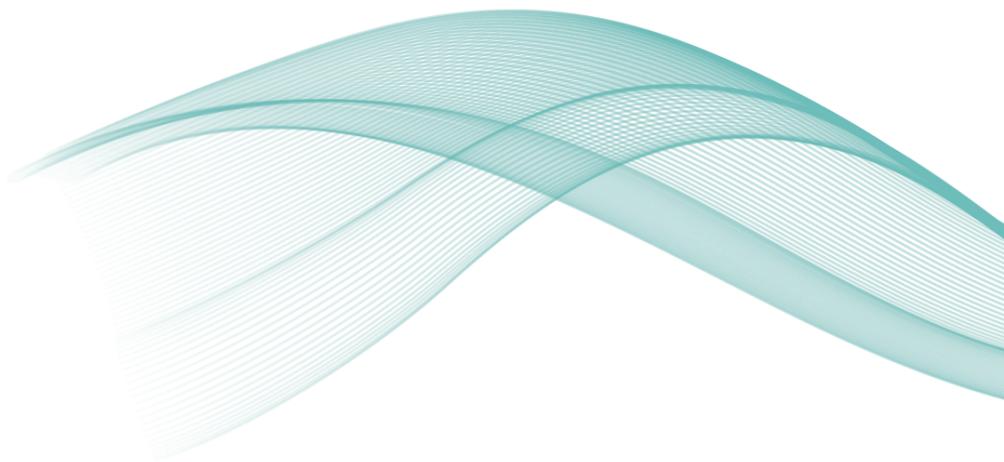
The restructuring of the financial services portfolio following a new European Parliament and Commission in 2014, led to a new post for the Commissioner for Financial Stability, Financial Services and Capital Markets Union being created. The Panel is keen for the FCA to engage effectively on behalf of the industry in the European policy developments which are now driving many aspects of UK regulation.

The Panel has been briefed on the major European initiatives affecting the industry, including MiFID II, the Mortgage Credit Directive and the Packaged Retail Investment and Insurance-based Products initiative. We have been pleased that the FCA has developed communications with the new Commission, and in particular Commissioner Hill. We note that the FCA Business Plan for next year states that active engagement with Europe is essential, and that this is a key part of the new strategic approach. Along with our counterparts in the FCA Markets Practitioner Panel, we have urged the FCA to engage with the development of the Capital Markets Union work, in order to influence at the most crucial stage.

Innovation Hub

In 2014 following a Call for Evidence, the FCA launched its Innovation Hub, a dedicated team to help new and established businesses, both regulated and non-regulated, to overcome regulatory hurdles if they cause unnecessary barriers for the introduction of innovative financial products and services.

The Panel responded to the call for evidence on Project Innovate, highlighting various barriers to innovation faced by firms. These include access to capital, the length of time taken to complete the regulatory process, and the cost and difficulty of accessing adequate compliance resources. We have also raised the issue of the relative positions of existing businesses and new starts, and our concerns that more help may be provided to new entrants than to existing firms. In order to maintain competitiveness it is important that the FCA shares its support equally between new and existing firms.



4

The advice regime and consumer responsibility

Retail distribution review – post implementation

Following the implementation of the Retail Distribution Review in 2013, the FCA has been monitoring the advice sector and the impact of the regulatory change. In July 2014 it published guidance to help clarify the different types of retail investment sales models, the boundaries between them and the associated regulatory requirements, and at the end of the year published the first stage of its post-implementation review (PIR).

We provided feedback to the FCA's post-implementation review of the RDR, both through engagement with the team on their initial findings and through the contribution of Panel-commissioned research conducted by KPMG. We encouraged the FCA team to consider the value for money gained by consumers from advice, rather than simply the level of charges related to the advice and subsequent investment.

The Panel's own research aimed to balance the FCA's findings with views from the industry regarding the impact of the RDR. Whilst our research highlighted the positive outcomes of removing producer bias and increasing the standard of professionalism, it also suggested areas for improvement. In particular, it suggested the need for the clear disclosure not only of costs, but also the level of service being provided and what is expected of consumers themselves. We also believe the terminology of adviser status needs to be clearer and more work should be done on encouraging new entrants into the advice market.

We broadly agreed with many of the intentions outlined in the FCA's work on clarifying the boundaries of advice particularly that there are distribution models which sit between execution-only and full advice. We are aware that there is ongoing work on disclosure to explore how to deliver better, more useful, product information. A joined up approach to these two strands of work, such as the use of behavioural insights to improve both the effectiveness of the information supplied and the way it is used, would help to improve outcomes for both firms and their customers.

Review of the Money Advice Service (MAS)

In May the Government launched an Independent Review of the Money Advice Service which was led by Christine Farnish. The review looked in particular at how MAS discharges its remit and was asked to recommend any changes that would help to improve its effectiveness.

The Panel and its Chairman had a number of meetings to feed in its views to the Review, which were reflected in the final report. These included whether MAS is providing value for money, (particularly its investment in its brand and some of the marketing activity), and the lack of accountability to the industry, which has no input to the budget process although it funds the service. We look forward to seeing the development of the stakeholder group which is being set up as a result of the Review.

Members of FCA Practitioner Panel

1 April 2014 – 31 March 2015

Graham Beale

(Chairman)

Chief Executive

Nationwide Building Society

John Pollock

Deputy Chairman

Chief Executive

Legal & General Assurance Society

David Bellamy

CEO, St. James's Place PLC

Alison Brittain

Group Director of Retail

Lloyds Banking Group

Peter Crook

Chief Executive

Provident Financial plc

Michael Dobson

Chief Executive

Schroders

Paul Geddes

Chief Executive Officer

Direct Line Group

John Hitchins

Global Chief Accountant and Financial Services Partner, PwC

Member until 30.6.14

Jackie Hunt

Chief Executive, Prudential UK,

Europe & Africa

Member from 1.10.14

Stephen Jones

Chief Financial Officer, Executive Director

Santander UK plc

Anne Richards

Chief Investment Officer, Head of EMEA

and Executive Director

Aberdeen Asset Management plc

Antonio Simoes

Chief Executive UK

HSBC Bank plc

Malcolm Streatfield

Chief Executive

Lighthouse Group plc

Member until 31.1.15

Paul Swann

President and Managing Director

ICE Clear Europe

[Markets Panel Chairman]

Member until 31.7.14

Andrew Turberville Smith

Finance Director and Chief Operating Officer, Weatherbys

[Smaller Business Practitioner Panel Chair]

Practitioner Panel

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