

**The Financial Services
Practitioner Panel
Annual Report
2008/09**



www.fs-pp.org.uk

Chairman's Foreword

I am delighted to present the Annual Report of the Practitioner Panel for 2008/09. This has again been a busy year for the Panel with a significant number of fundamental issues being discussed and plenty of vigorous debate with FSA senior management.



The Panel's Fifth Survey of the FSA's regulatory performance, published last December, indicated that larger firms held broadly positive views about the FSA. The Panel believes that some good progress has been made in a number of areas but continues to express its concerns across a range of important issues.

The current economic conditions make an improvement in the quality of supervision an even more vital priority than previously. The Panel will accordingly continue to monitor keenly the progress of the FSA's Supervisory Enhancement Programme. We consider that strong risk and outcome based regulation is the right and proper course to take. In implementing this approach it will be important to recognise sectoral differences: we will be particularly vigilant in pointing out where an inappropriate 'one size fits all' approach is being taken by the FSA.

My two year tenure as Chairman of the Practitioner Panel comes to an end in November and I will be replaced as Chairman by Iain Cornish. Iain has been an enthusiastic member of the Panel since March 2007 and I am certain that, under his leadership, the Panel will continue to add value to the regulatory process through frank and timely interaction with the FSA's senior management. I have greatly enjoyed my time both as a member and as Chairman of the Practitioner Panel and would like to thank all my fellow members, both past and present, for their support. I wish the Panel well for the future.

A handwritten signature in dark ink, appearing to read 'Nick Prettejohn', written in a cursive style.

Nick Prettejohn
Panel Chairman
July 2009



Introduction and Background

The Financial Services and Markets Act 2000 granted the Financial Services Authority (FSA) its powers and, as part of its accountability framework, the FSA was required to set up and maintain two statutory bodies – the Practitioner Panel (the Panel) and the Consumer Panel. These two bodies monitor the regulator’s activities, ensuring that both buyers and sellers of financial products have a voice in the regulatory process. In 1999 the FSA also set up the Smaller Businesses Practitioner Panel to represent the views and interests of smaller regulated firms; its Chairman is an ex officio member of the Panel.

Membership of the Panel comprises senior practitioners drawn from firms operating across the main sectors of the financial services industry. These include retail and investment banks, building societies, insurance companies, investment managers and financial services markets, custodians and administrators. The Panel Chairman is Nick Prettejohn who took office in December 2007.

This Report looks at the Panel’s objectives and then considers specific actions that have been taken in fulfilment of those objectives. The main issues considered by the Panel during the year are reviewed and consideration is then given to how the Panel can develop its effectiveness further in the future.

Panel Effectiveness

- The Panel has broadly aligned its agendas with those of the FSA Board, Executive Policy Committee, Smaller Businesses Practitioner Panel and the Consumer Panel so that similar issues can be identified and discussed at the same stage.
- Notwithstanding the desire to be covering broadly the same ground as the FSA and other panels the Panel has tried to maintain an active agenda of its own; this has been more difficult given the pressing priorities of recent months, but we have identified a number of recurring themes – for instance cost benefit analysis, the need for an overhaul of the Financial Services Compensation Scheme (FSCS), and the urgent need to show demonstrable improvements in supervisory quality – which have permeated our specific deliberations.
- The Panel Chairman submits monthly reports to the FSA Board. The Panel values this mechanism as an effective and appropriate form of regular communication.
- The Panel does not reply to Consultation Papers unless the subject matter contains significant issues which have not been taken forward by the relevant trade bodies, or where market controversy persists. Instead, the Panel seeks to be engaged with any relevant regulatory proposal from the point of its conception to the point before which the final proposal is presented to the FSA’s Board.



- The Panel has welcomed the opportunity it has had for engagement with non-FSA officials which has provided added benefit to the Panel's overall effectiveness, for example; Commissioner McCreevy (European Commissioner, Internal Markets and Services), Lord Hunt of Wirral and Lord Lipsey.



The Panel aims to add effective value to the regulatory process through positive and constructive engagement within the regulatory process. As the Panel's role is advisory, it recognises that its views will not always accord with those of the FSA, and will not always be accepted. The Panel tries to be a 'constructive critic'. As a result we are not afraid to voice strong views on the FSA's policy and supervisory initiatives, and this has made for some vigorous debates. By and large early flagging of issues to the Panel by the FSA has made the debates more relevant and constructive.

Treasury Select Committee

The Panel Chairman, together with the Chairman of the Smaller Businesses Practitioner Panel and the then Acting Chairman of the Consumer Panel appeared before the Treasury Select Committee on 15 December 2008 as part of its investigation into the "Work of the Financial Services Authority 2007/08".

The Panel hopes that it added value to the work of the Treasury Select Committee.

Panel Survey

On 11 December 2008, the Panel published the results of its Fifth Survey of the FSA's regulatory performance. The Panel worked with the FSA to ensure FSA management's confidence in the Survey's transparency, methodology and credibility, and was committed to constructive dialogue around its findings.

The Survey concluded that larger, relationship managed firms had been relatively positive in their views of the FSA, although concern remained about the practical impact of More Principles Based Regulation (MPBR) and Treating Customers Fairly (TCF). Smaller firms, however, were overall more neutral/negative in their feedback on the FSA's performance; with MPBR and TCF as the key drivers of those negative elements. The full Survey Report and an Executive Summary can be found on the Panel's website (www.fs-pp.org.uk/publications/surveys).



Relationship with the FSA

The Panel must remain independent from the FSA, but it recognises the importance for both parties that appropriately close working relationships be developed between the Panel and the FSA's senior management. Relationships and communication with FSA senior management have continued to be very positive over the twelve months.

The Panel was keen to adopt a more risk-based approach to constructing its agendas and determining how best to allocate Panel members' time and resource and to improve the Panel's effectiveness. We have tried to be more active in tracking the FSA's response to Panel representations, and ensure that relevant Panel members are adequately engaged and feed back to the FSA on important issues.

The Panel welcomed and appreciated its recent meeting with the FSA Chairman, Lord Turner, and looks forward to working with him. Hector Sants has been unfailingly generous in spending time at the Panel; in addition the Panel Chairman has bi-monthly bi-laterals with him at which a wide range of mutually relevant issues are discussed in an open, frank and constructive manner. Managing directors and a number of other FSA senior managers have attended Panel meetings throughout the year and presented on a wide range of issues, some of which are considered in more detail below.

The Secretariat has developed a feedback form which is now sent to anyone who makes a presentation or submits a paper to the Panel. This asks, inter alia, whether presenters found the Panel to be informed on the subject matter, whether they found the Panel's comments helpful and whether they intend to make any changes to their proposals in light of the Panel's comments. This type of information is expected to be very useful when measuring the Panel's success. Equally, the Panel feeds back relevant comments on the performance of FSA executives.



Panel Objectives

The Panel has six objectives:

1. **Monitor Overall Effect of FSA Activities on the Industry:** To gauge the cumulative burden of incremental regulatory initiatives and regulation as a whole, including EU and international efforts.
2. **Assess FSA Effectiveness, as seen by Practitioners, against its Objectives:** To evaluate FSA compliance with all objectives and principles of good regulation, including the desirability of facilitating innovation and of maintaining the UK's competitive position.
3. **Actively Communicate Industry Concerns to FSA:** To voice to the FSA issues of general concern to the regulated community over developments that could impact the UK financial services industry.
4. **Actively Promote Broad Industry Views and Interests:** To play an active role in formulating and communicating to the FSA a broad practitioner view on the requirements for fair, efficient, and innovative markets.
5. **Provide Practitioner View to the FSA on Specific Regulation:** To respond when requested to by the FSA with a practitioner view on early drafts of regulatory initiatives and discussion papers.
6. **Promote International Competitiveness of the UK Markets:** To safeguard the competitive standing of the UK financial markets in the context of developments in the European Union and internationally, and to encourage innovation.



Actions taken in fulfilment of the Panel's objectives

The breadth of experience of the Panel's membership means that the Panel can offer wide ranging expertise to the FSA as to the likely impact of any relevant regulatory proposal. The range of this expertise is increased by Panel members' links with the various professional bodies, and through informal and direct links with the Trade Associations. This is further supported by the Panel's ability, and the FSA's willingness, to engage at an early stage on a confidential basis when appropriate.

In late 2008 and early 2009 we suffered an unfortunate hiatus in the Panel Secretariat's regular contact with the Trade Associations as a result of organisational changes. We hope that recent recruitment and resumption of the Trade Association contact programme for 2009/10 will improve things, as such contact is a critical supplement to the direct contact between Panel members and their relevant trade bodies. We will keep this situation under review.

To be effective, the Panel membership must be sufficiently wide to ensure that all major sectors are appropriately represented. Although the current membership is considered to be completely appropriate, succession planning continues to be an important consideration and the membership is continually reviewed. We have welcomed Richard Berliand, Simon Bolam (ex-officio member), Mark Hodges, Xavier Rolet and Malcolm Streatfield, to the Panel over the last year, and are grateful to; Clara Furse, Douglas Gardner, Colin Keogh, Roy Leighton, Mark Rothery (ex-officio member) and Patrick Snowball for their work as they have stepped down. Membership of the Panel continues to represent a substantial commitment of time and effort, which Practitioners freely give, as we have a strong interest in the effectiveness of the FSA.

A full list of current Panel members can be seen at Appendix 1 below.



Matters considered by the Panel during the year

The Panel has continued to meet on a monthly basis throughout the year (except in August) and has considered a wide range of topics as well as participating in a number of “one off” sessions on particular topics.

The matters considered have included:

- Retail Distribution Review
- Banking Reform
- Financial Services Compensation Scheme (FSCS) Funding Tariff Changes
- FSCS Limits – Temporary High Deposit Balances
- Regulatory Transparency
- Treating Customers Fairly
- Supervisory Enhancement Programme
- Retail Strategy Review
- Short Selling
- Funds of Alternative Investment Funds
- Mortgage Intermediary Sector
- MiFID Transaction Reporting
- Individual Liquidity Adequacy Standards (ILAS)
- Regulation
- The Quality of Advice (Outcomes) Project
- Review of Lamfalussy
- More Principles Based Regulation
- Taping / Firm Records and Cost Benefit Analysis
- The FSA’s Internal Review of Northern Rock
- The Hunt Review
- Commercial Insurance Commission Disclosure
- FSA’s Business Plan 2009/10
- FSA’s Financial Capability Programme
- Payment Services Directive
- CP07/23 Organisational Systems and Controls
- CP08/11 With Profits
- Consumer Responsibility
- Financial Risk Outlook 2009
- Regulating Sale and Rent Back
- Global Regulatory Landscape including the Turner Review
- EU Strategy
- FSCS Reform

The Panel has commented on many of these issues in our Board reports over the past year. A number of general themes and issues are considered below.

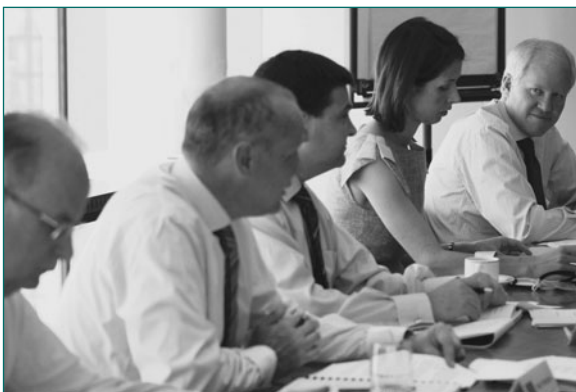


Current Issues

The Panel wholeheartedly supports the work of the FSA in improving the quality of supervision through the Supervisory Enhancement Programme (SEP). Two key preoccupations have emerged from our discussions. First, the need for sufficiently granular metrics to establish whether the actions under the SEP have been taken, and to measure the focus and effectiveness of supervisory activity. In the past, the Panel has been concerned that the emphasis of activity has been wrong – notably, the balance between prudential and conduct of business work. It is vital that FSA management have the management information to judge whether the right issues are

indeed being worked on, and by the right quality of resource.

Second, the Panel (and the Panel's Survey) have identified the need for greater continuity in supervision staff at firm level. This goes to the heart of the FSA's HR model. In financial services, depth of expertise is valued almost above all else. Our feeling is that this has not been the case at the FSA where too often people are switched around



for the breadth of experience equated with career development opportunities. A much better balance must be struck here; greater depth of expertise is essential if higher quality supervision is to be a reality.

The Panel has been encouraged by the commitment of FSA management to SEP, and will continue to keep a close eye on progress.

Equally, the Panel welcomes the intention to look at FSA fees. We have been, albeit reluctantly but with a sense of inevitability, willing to accept a short term increase in the FSA budget. We continue to believe that better, more effective, (and effective as a result of being truly risk based) regulation is the way forward.

In anything other than the very short term, and because of the strains that increased fees will create for the regulated at a time of general strain for the industry, a higher FSA budget will only be supported by firms if there is a demonstrable improvement in the quality of supervision.

Further, firms must be able to see that supervisory costs are allocated fairly in setting fees and therefore be able to assess value for money. The Panel looks forward to working with the FSA as the thinking on fees develops.



The Retail agenda, under new leadership, has seemed to be much more pragmatic in the current market environment. We welcome the shift-away from thematic work, and the concomitant integration of TCF into the ARROW process. We will remain vigilant as the Retail agenda unfolds, to seek a proper balance between conduct of business and prudential activity. The RDR has made progress over the last year; but especially in current conditions, we are concerned about the consequences of the transition towards the changes in 2012 (in particular, the potential for less advice at a time when consumers arguably need more). We are also mindful of the importance of labelling – any signals that one form of advice is less valuable than another need to be approached carefully (e.g. “restricted advice”).

The whole strategy for the FSCS must be reviewed. The current situation is unsatisfactory, with both levels of compensation and their funding needing to be examined together. Events in the banking sector have exposed the potential inadequacies of the thinking behind the FSCS and the Panel welcomes any moves to re-open a fundamental examination of it.

The Panel has become increasingly concerned about Cost Benefit Analysis (CBA). We have spent time hearing from the team responsible for the process and, while we acknowledge that CBA is frequently and necessarily highly judgmental, and benefits in particular can be hard to quantify, the Panel feels that where significant judgments are made, these should be more explicitly highlighted. In cases where the CBA case is weak or non-existent for an initiative, the decision should be taken not to proceed or any decision to proceed in the face of the CBA should require more extensive justification.

The Panel remains highly sceptical about the thinking on Regulatory Transparency. We can see scant if any justification for the proposals regarding the publication of complaints data, and plenty of downside for individual firms and the sector as a whole. It is extremely unlikely that the data will be published and commented upon by the media with all of the appropriate context. Therefore the data could mislead consumers, who may be ill equipped to supply that context for themselves. The definition of ‘complaint’ covers many issues over which firms have no or little control; and the focus on the number of complaints will automatically bias exposure towards large firms, who may or may not be the worst offenders versus other more fragmented parts of the market. Most fundamentally, for these larger firms, the ARROW process is a much more appropriate, direct and effective process for dealing with firms who have an unsatisfactory complaints performance than the publication of data. The Panel will examine closely the CBA, especially to establish whether the benefits can be properly justified, by reference for instance to analogous initiatives in other countries or sectors and to the alternative tools available to the FSA to achieve their objectives.



The Panel is broadly supportive of the Regulatory Philosophy that is emerging from the FSA. We welcome the stated preference for outcomes over process and rules based prescription. Particularly important will be the need for a risk based approach. For us to maintain our competitiveness as a financial services centre where it is attractive to do business, strong, risk based regulation is in everybody's best interests: consumers (in the widest sense) and firms. Additional and 'one size fits all' regulation will add cost without necessarily reducing risk. The FSA should tread carefully when seeking to apply the lessons learned from banking to other sectors. There must be recognition that important differences exist between sectors which will need to be reflected in both policy and supervision.

Finally, the Panel is concerned that the FSA's practical assessment of 'burden of proof' seems in danger of shifting. Given the increasingly personalised public atmosphere surrounding banking and financial services, and the increasing focus of the FSA on individuals (Approved Persons, the role of the Non-executives), this is a potentially worrying development.

The Year Ahead

It is tempting to set out a long list of priorities for the Panel for next year. The reality is that much of the focus of the Panel will be to continue to work on the current issues identified above. The Panel will be particularly keen to see real progress in implementing existing initiatives and policies. As such the implementation of the SEP will be core to success. In the current climate, there is an even greater need for effective, risk based regulation, reflecting a deep understanding of the financial services market as a whole and the different characteristics of its individual sectors. Specific topics will obviously be added during the year, but the current agenda represents a fundamental set of issues and as such will be the starting point for next year's agenda.

The Panel is looking forward to a continuing effective and constructive working relationship with the FSA and our thanks go to all the FSA's staff and senior management for their willingness to provide the comprehensive submission papers, attend Panel meetings, and to engage in open dialogue with the Panel.



Appendix 1

List of Panel Members (as at 1 July 2009)

Panel Member	Position
Nick Prettejohn Chairman	Chief Executive, UK & Europe, Prudential plc
Iain Cornish Deputy Chairman	Chief Executive, Yorkshire Building Society
Richard Berliand	Head of Global Cash Equities & Prime Services, JP Morgan Securities Ltd
Simon Bolam	Principal, EH Ranson and Company
Russell Collins	Head of UK Financial Services Practice, Deloitte
Mark Hodges	Chief Executive, Norwich Union Life
Roger Liddell	Chief Executive Officer, LCH Clearnet Group Ltd
Helena Morrissey	Chief Executive Officer, Newton Investment Management
Gordon Pell	Deputy Chief Executive, Royal Bank of Scotland Group
Xavier Rolet	Chief Executive, London Stock Exchange
Andrew Ross	Chief Executive, Cazenove Capital Management
Malcolm Streatfield	Chief Executive, Lighthouse Group
Alan Yarrow	Vice Chairman, Dresdner Kleinwort Wasserstein





