Smaller Businesses Practitioner Panel

Financial Services Authority

Annual Report

2011/12

Members of the Smaller Business Practitioner Panel at April 2012

Chairman's foreword

Over the past 12 months, smaller firms in the UK have had to try and survive in an extremely tough economic climate. It has, therefore, been more important than ever for the Smaller Businesses Practitioner Panel (SBPP) to strive to influence the regulators to reduce the burden of unnecessary regulation and costs. This will enable smaller firms to focus on their businesses and customer service and to have a better chance to prosper financially.

Again this year, the SBPP have engaged not only with the FSA, but also with the Government and the Bank of England on plans for creating the new UK regulatory system, which will come into force in 2013. Understandably, much of the focus for the new structure has been on larger firms, but we have highlighted the requirements for approximately 1800 smaller firms who will be dual regulated by the Prudential Regulation Authority as well as the Financial Conduct Authority. We have also pointed out the need for the FCA to take a more cost effective approach to the regulation of smaller firms.

At the same time, the SBPP has continued to be actively involved with the FSA as it continues its regulatory programme. FSA policy initiatives including the Retail Distribution Review and the Mortgage Market Review have continued to be areas of debate, along with the implementation of European policies such as Solvency II for insurance companies.

As well as working closely with the FSA over its financial plans and budget over the past 12 months, we have voiced great concern over the wider costs of the current regulatory system. The costs of the Financial Services Compensation Scheme (FSCS) and the Money Advice Service continue to place a major burden on firms and this looks set to increase. In addition, we have highlighted how the activities of lightly regulated claims management companies in drumming up business, puts huge pressure on firms and the Financial Ombudsman Service, with questionable benefits for consumers.

As we prepare for the new regulatory system in 2012/13, where the SBPP will become a statutory panel for the FCA, there is still much to do on behalf of smaller firms. I am grateful to my colleagues on the Panel for all their time and support. This year we have said goodbye to Paul Etheridge and welcomed James Bawa and Dick Carne to the Panel. I am also grateful to all at the FSA with whom we have had a constructive dialogue over the past year.

Guy Matthews
Panel Chairman

1. Introduction

The Smaller Businesses Practitioner Panel works as an independent Panel to advise the Financial Services Authority (FSA) on its policies and practices from the perspective of smaller regulated firms. The Panel aims to complement the work of the Practitioner Panel, which was set up under the Financial Services and Markets Act 2000 to represent the views of predominantly the larger financial services firms. The Chairman of the SBPP sits on the Practitioner Panel, to ensure the viewpoint of smaller firms is represented in those debates.

Our membership aims to reflect the spread of smaller firms regulated by the FSA, providing a forum for representatives of different sectors to come together to debate how regulatory changes may affect firms, and how to make regulation as effective as possible. In addition, the Panel has regular liaison with trade associations and other industry bodies, to enable there to be joined up thinking across the regulated community.

This year, the Panel has been involved in the key FSA initiatives for 2011/12. We have focused the Panel's active engagement with the FSA on the following core areas from the point of view of small firms:

1. Restructuring of UK regulation
2. Cost and burden of regulation
3. Major UK policy developments
4. EU initiatives
5. Smaller firm supervision

The Annual Report is structured to review the Panel's work in each of these areas for period from 1 April 2011 to 31 March 2012.

2. Restructuring of UK regulation

The Panel has worked with the Practitioner Panel to ensure that the voice of smaller firms is heard in the debate on regulatory reform. It is critical that the Government and regulators understand the balance that needs to be struck between increasing regulation and ensuring the further burdens on smaller regulated firms can be absorbed without undermining their viability.

We have been pleased that the plans to create the FCA have included a proposal to make the Smaller Businesses Practitioner Panel a statutory panel, with the same legislative status as the Financial Services Practitioner Panel. We see this as an appreciation of the need to consider the views and concerns of smaller regulated firms. We have also been encouraged by the fact that proportionality continues to be a key principle in the new regulatory system. However, there are aspects of the new system which concern us from the point of view of smaller firms. We have therefore thought it important to provide specific responses from the smaller firms' perspective, whilst also supporting the Practitioner Panel's work in engaging actively in the process of creating a new regulatory structure in the UK for financial services.

We submitted responses highlighting small firm issues in the legislation to HM Treasury, to the Pre-legislative Scrutiny Committee, and to the FSA and Bank of England on the initial approach documents for the FCA and PRA.

PRA and small firms

We have sought to emphasise in our discussions that the PRA will not only be dealing with the large and high impact firms. The decision to regulate all deposit takers and insurance companies at the PRA means that all credit unions and insurance companies will also be swept up into PRA regulation. Dealing with two regulators rather than one will consequently be a significant additional burden for many smaller firms. We have supported the Practitioner Panel's work to highlight the importance of having practitioner representation at the PRA, and its stance that this would be an important channel of engagement rather than accountability, with no regulatory capture or preferential status implied. Indeed, a formal and transparent mechanism for engagement with firms would act against any capture or preferential status.

Practitioner representation in PRA discussions

We have therefore said that it is important to have some standing representation of practitioners at the PRA. We accordingly highlighted the following benefits:

a. a panel of practitioners representing the wider industry would be able to recognise the *impact of regulation in one sector on another*. The current proposal of specialist ad hoc groups drawn together would not automatically consider the potential knock-on effect of the regulation in other sectors. So, for example a discussion on tightening capital requirements with banks and building societies, would not encompass the wider industry views on the impact of less capital availability in the market.

b. a panel could comment on and therefore contribute to more *effective coordination between different regulatory bodies*. It could monitor how successfully they coordinate and provide feedback on an ongoing basis and whether there is duplication in some workstreams. This would work best with a panel that has some overlapping membership or coordination requirements with the FCA Practitioner Panels.
c. a panel would have a '*corporate memory*' and so recognise links and repetitions over time that may not be obvious to ad hoc working groups.

Dual regulatory burden

We have pressed for greater clarity during the year of how smaller firms will be regulated in a proportionate way by the PRA. We registered our concern that firms would be expected to have wide data sets available at short notice and that the PRA planned to retain the discretion to set higher requirements than those with which firms are obliged to comply under EU regulations.

However, we were pleased that the PRA has plans to review the business as usual data requirements from firms, as the production of data can be a significant commitment from firms. It is also important that the regulator uses the considerable amount of data it receives in an intelligent way. The plans for the PRA to become more judgement led will be reliant on good quality, rather than requiring more, resources. This is just as important for small firms, and we have encouraged the regulators in their challenge to recruit and retain the appropriate experienced and skilled staff going forward.

Another example of the lack of consideration of small firm issues was in the PRA's document on the approach to insurance supervision, published in June 2011. We were disappointed that there was no mention of smaller firms, despite the fact that some 1,290 are expected to be regulated by the PRA. Although there was clear recognition that supervision should be tailored to different firms and sectors, baseline monitoring might presumably be at a comparatively high level.

FCA and small firms

We were pleased that that the FCA plans to build on existing good practices employed by the FSA and will not abandon all current processes. We were also supportive of the FSA's and FCA's plans to supervise firms on a sectoral basis. However, we continue to be concerned about the lack of

any real overview or representation for the issues facing smaller firms. We have said that there must be a voice for the needs of smaller firms clearly identifiable, at director level and/or as a unit within each regulator.

If the FCA uses a judgement-based approach, it will of course be important to ensure that supervisors exercise sound judgement, and consideration needs to be given to whether any changes need to be made to the current staff skill sets to achieve this. Supervisors will need to carefully balance the interests of consumers and financial services firms over both the short term and longer term in order to maintain the long term viability of the industry. The regulator will also need to accept that a policy of making brave decisions will inevitably result in some mistakes being made and that, in those circumstances, a clear policy of redress or arbitration for impacted firms will need to be in place.

The Panel welcomed the opportunity to engage in more detail on the plans for FCA supervision. We encouraged a consideration of an approach which is seen to differentiate between good and bad firms. We have also encouraged both new regulatory bodies to focus their resources on wayward firms rather than on those that are making every effort to be good corporate citizens. One way in which we feel the regulator could provide useful feedback to the regulated community would be to publish details of what an average firm in a sector looks like so that firms can understand their position relative to their peer group. Guidance, information gathering and the intelligence process will be key to the overall effectiveness of the model. Transparency in what the supervisory function is intending to do will also be important.

The Panel has continued to reiterate its view that, whilst the FCA is set up to be more proactive in identifying and tackling causes of consumer detriment, it must also be balanced in its approach; consumer responsibility is an important concept that must not be forgotten in the new regime.

We have also continued to raise concerns about the appeal mechanisms that will be put in place for the FCA. It remains unclear as to whether the FCA and PRA will have a body similar to the Regulatory Decisions Committee of the FSA or not. We consider it important for there to be a robust, independent challenge process that can be fulfilled by the RDC or a similar body in both of the new organisations.

Cooperation and Memorandum of Understanding for FCA and PRA

From the smaller firms' perspective, and particularly for those that will be dual regulated, the Panel's key concern has been the degree of efficiency at the operational level between the two authorities when the division of responsibilities finally occur. The Panel is of the view that the day to day cooperation between the PRA and the FCA will be important in managing the burden and costs for those smaller firms with dual regulated activity.

We have therefore engaged with the FSA to input to the approach to supervision, and with both the Government and the FSA over the Memorandum of Understanding (MOU) for the PRA and FCA. It will be very important for smaller dual regulated firms that they do not have to double the amount of time and resources dedicated to dealing with regulation in the new system.

FSA transition and Internal Twin Peaks

We have had regular engagement with the people driving the FSA and Bank's transition team, and been impressed with the efficiency of the process. Although we registered concern about the overall cost of the process, we have been pleased that the programme is progressing to time and within budget.

3. Cost and burden of regulation

FSA Business Plan and regulatory costs

The Panel takes an active interest in the development of the FSA's Business Plan, and we were pleased to have a number of opportunities to feed into the process this year. We welcomed the comprehensive presentations provided by the FSA, which were informative and gave more transparency on the detail in the Plan than in previous years. We have been keen to see that, as part of the prioritisation process, consideration is given to the wider cost impact of not undertaking some initiatives, as well as the cost of undertaking them.

We urged the FSA to provide as much clarity as possible in the final publication about the drivers to the Business Plan and the critical elements within it. This included a request for much greater clarity and transparency on the differences between the costs for 'business as usual' and specific transitions costs in the published Business Plan. It is important that there is a fair base for future cost comparisons between the FSA and the new regulators in the future – which should be separate from all transition costs.

Our wider concerns about the ever increasing overall regulatory cost implications for the smaller firms, both direct and indirect, have been highlighted at every opportunity over the year. We believe that these costs are having a significant impact on smaller firms and are presenting a substantial hurdle to new entrants in the sector.

Regulatory Fees and Levies for 2012-13

In 2012, the Practitioner Panels for the first time made a formal response to the Consultation Paper on regulatory fees and levies, as well as being consulted, as usual, prior to publication. We welcomed the retention of the standard minimum fee level at £1,000 and the overall proportionality applied within the fee block allocations. However, both Practitioner Panels wanted to draw attention to the increasing overall cost of regulation. It is the external levies and additional indirect regulatory costs that make it so difficult for smaller firms to continue to withstand such annual increases.

Rules, Principles and Guidance

We had a number of constructive discussions with the FSA this year about the process for issuing guidance to firms. We had registered concern that supervisors would use guidance in the same way as rules – effectively binding firms, without the guidance having been through the more rigorous process required for rule changes. We suggested that cost benefit analysis should be carried out for new guidance in all but exceptional circumstances, and made publicly available. The rationale for not doing any cost benefit should have to be justified. We also suggested that the FSA should consider guidance being issued to be valid for a limited period of, say, twelve months after which time consideration can be given to whether the guidance remains appropriate and, if so, whether a rule should be made or a regulation brought in.

FSA use of s166

We have pressed the FSA over the year about the use of s166 requests, where the regulator directs a firm to undertake a skilled persons report on an aspect of the way their business is being run. Although only a small number of firms were required to undertake s166 processes as a result of the small firms assessment programme, we are concerned that there has been an overall increase in the use of s166 as a tool by the FSA.

Whilst the use of s166 may be cost effective for FSA, this is relatively expensive for smaller firms who are less able to absorb unexpected costs. In addition, although we appreciate that s166 can be a useful tool, we are also concerned that too much use can suggest an undermining of the regulator's responsibilities if not used appropriately.

Money Advice Service (MAS)

Although we have been broadly supportive of the objectives of MAS, we have questioned the external control of the MAS activities and budget. We do not believe that there are clear enough accountability measures on a service whose potential scope is extremely broad. There seems to be little opportunity for external scrutiny of the quality of the advice and service provided by MAS, as well as answerability on the level of expenditure. The service is funded through FSA industry levies – with a budget of £46.3m for 2012-13 – and yet the industry has no say in the operation of MAS. The Chief Executive has presented outline business plans to the Panel, but we have no channel through which to challenge any decisions; the FSA Board approves the MAS budget, but does do not have the power to demand action from MAS.

Our concern has increased since the Government announced in July 2011 that it would transfer the Debt Advice Service to MAS from April 2012 and that funding would come from the regulated community. The FSA's Fees and Levies Consultation (CP12/3) consulted industry on a proposed levy framework for debt advice to fund the 2012/13 MAS debt advice budget of £34.5m. The levy will be funded via deposit takers, home finance providers and administrators. It will take the total industry funding of the Money Advice Service to £80.1m for 2012-13.

We have questioned the FSA on whether or not the potential liabilities arising from the service had been fully determined at the outset. We still maintain that there could be problems going forward with the boundary between regulated advice and the non regulated advice being offered through MAS. We will continue to take an interest in the activities of MAS as they are developed over the coming year.

We have also pointed out potential overlap as the FSA – and FCA going forward – plans to continue a role in consumer engagement and consumer awareness. We have said that it will be vital for there to be clarity as to the remit of the FCA, to ensure it does not replicate some of the responsibilities of the MAS. For instance, we suggested that the FSA's disclosure proposals for deposit takers might be more appropriate within the remit, and budget, of the MAS.

Financial Services Compensation Scheme

Increasing concern about funding of the FSCS has been a constant theme during this year. The size of the FSCS interim levy when the cross subsidy was triggered at the beginning of 2011 was much higher than had been expected. We pointed out that this might result in some small firms being put out of business, or coming near to breaching their capital adequacy requirements. It seems that the size of the levy in 2011 may not be an isolated event: there is still the need to repay or renegotiate payment terms for the £20bn borrowed from the Bank of England during the banking crisis. There are also indications that a good number of smaller firms that sold PPI have already failed and the numbers are continuing, so increasing the overall liability of the FSCS.

We recommended that there should be a greater interaction between the regulator and the FSCS. We believe the FSA or new regulators should take on a role to consider the impact on firms of sudden increases in FSCS levies. The FSCS levy is becoming such a significant and yet unpredictable expenditure for smaller firms, that the regulator must have a responsibility to consider its impact.

We suggested that the Government, FSA and FSCS should consider whether self-insurance of this type is becoming too expensive to be continued. It seems unfair that clients of well-run, successful companies should have to finance compensation payments to clients of firms that have not been so prudent. We also warned that firms might consider migrating outside the UK and passporting back into the UK to avoid incurring an FSCS liability.

We were pleased that the FSA announced in October 2011 that it was re-starting the FSCS funding review process in advance of total clarity in Europe. We appreciate that this is a complex subject where it is difficult to satisfy all parties. Our concern is naturally the impact of the funding model costs for smaller firms. We need a model that will be sustainable for all sectors of the industry and does not inadvertently divert those businesses that can move outside the UK to circumvent the liabilities due from the scheme.

We have highlighted the general lack of understanding that firms have in applying current areas of the scheme such as for example, the calculation of eligible income. We therefore suggested the FSA clarified these points in the consultation as well as setting out all the funding options that could be considered, and why they have been rejected. As the funding model consultation is due to be published during 2012, we will continue to engage actively with the FSA on this issue.

Financial Ombudsman Service

We have met regularly with the Chief Executive of the Financial Ombudsman Service, and she provided an overview of the Ombudsman Service's Business Plans and Budget implications for 2012/13. This sets out an increase in operating costs for the next business year, thus increasing the required funding level.

However, we were also very interested in the preliminary consultation by the Ombudsman Service on modernising case fee arrangements from 2013. We contributed a joint response, together with the Practitioner Panel, which was supportive overall of the suggested new approach. We agree that, other things being equal, an individual firm's fees should reflect the costs it brings to the FOS, and the new approach seems to go a long way towards achieving this. This would be a significant step in the right direction of ensuring that those who are responsible for the greater part of FOS's costs contribute proportionately. The move to increase the number of free cases for small and medium sized firms was also welcomed, and will provide a great deal of comfort for these firms, for whom complaints may be a significant cost and worry.

The Panel also expressed concern regarding the role of Claims Management Companies in referring cases to the FOS. Whilst remaining strongly supportive of consumers' rights to complain and seek redress, we have noted worrying tendencies for CMC's to encourage individuals to complain in instances where they have no chance of winning, including in cases to banks with whom they have not had an account. Individual firms have to devote more internal resources to dealing with complaints which may be vexacious or frivolous claims, as well as the industry as a whole having to pay for the increased time and resources for the FOS to investigate such claims – costs which may ultimately be passed onto consumers. We have called for stronger regulation in this area.

4. Major UK policy developments

Retail Distribution Review (RDR)

The majority of firms are now putting in place the requirements resulting from the RDR. However, we have continued to raise concerns and questions about its implementation. One of the biggest questions is whether the RDR will align with the European requirements from MiFID, which will need to be implemented in the next few years. We appreciate that the UK is negotiating hard in this space, but we have urged the FSA not to push ahead with requirements on firms until the approach to be taken by the rest of Europe is clear. Currently there are indications of a disparity between MiFID and the RDR about who can receive commissions. If this continues, the UK will either have to gold-plate the directive, if it allows domestic discretion, or change the requirements of the RDR shortly after it has been implemented. Neither of these would be good outcomes for the industry.

We welcomed the FSA's decision to publish a guidance consultation paper on independent and restricted advice in response to industry requests. We highlighted the fact that, as a relatively high hurdle is being set to comply with independence, it may lead to more firms taking alternate business routes, such as the provision of restricted advice or discretionary investment management services, rather than the provision of independent advice.

We were encouraged to hear that the FSA would monitor the impact on the market of the RDR and would adapt it as necessary, but we have asked for an articulation of the trigger points for change. We have questioned whether a significant reduction of "independent" advice is an acceptable outcome. We suggested the FSA should issue some base level statistics on "independent" versus restricted advice provision, so that this could be monitored post implementation of the RDR. We think it is important for the FSA to construct a clear post-implementation plan to review the RDR to see what criteria and metrics are being used to assess the success or otherwise of the RDR. The FSA must consider contingency plans in the event that the RDR has detrimental unintended consequences.

VAT and the Retail Distribution Review

The Panel has expressed concern that changes to the charging of advice following the introduction of the RDR may have implications for firms' VAT liabilities. The lack of clarity around these VAT implications for firms has been a cause of considerable worry for

industry. The Treasury Committee also raised this as an issue as part of its RDR review and asked HMRC for further clarification, with support from the FSA as appropriate.

We have had ongoing engagement with the FSA and HMRC over the year in order to press for greater clarity on this point. We were pleased that HMRC has now issued further guidance on when VAT will be relevant, which will assist small firms. We have encouraged the FSA to promote this advice on its website in relation to the RDR.

Platforms

It was sensible that the FSA decided to take more time to review how to deal with the disclosure of commission payments as a potential solution for payments from platform providers earlier in 2011. This seemed inconsistent and damaging compared to the proposals for advisers, particularly as consumers are even less likely to understand the payment systems set up for platforms than commission payments to an adviser. We were worried that if fund managers and product providers were still allowed to give rebates to platforms, it would undermine the whole justification of the RDR; prevent clarity of relationships and charges; and fail to eliminate product bias.

We were pleased therefore that in August 2011, the FSA announced that they had decided it would be desirable, in principle, to ban both cash rebates from product providers to investors and product provider payments to platforms. However, given the potential impact of these changes on the business models of platform service providers, the FSA concluded that further research would be needed to ensure that the implications for consumers are fully understood before proposing new rules.

Simplified advice

We have continued to press the FSA for greater clarity on simplified advice as we believe there is considerable uncertainty and confusion in the industry on this issue. This is particularly as the RDR is expected to reduce the availability of independent advice, and so some type of simplified advice will be needed to fill the likely gap in financial advice provision for consumers.

We had a number of conversations with the relevant FSA team prior to the publication of guidance on simplified advice in March 2012. We were disappointed that the FSA's approach was not going to allow the industry to move this any further forward and deliver a commercially viable approach to simplified advice. We will continue to watch the developments in this area of the market alongside the work on simple products and the implementation of the RDR.

Mortgage Market Review (MMR)

We welcomed the changes that the FSA made following the significant level of feedback from industry, including not going ahead with the assessment of affordability based on a maximum term of 25 years and not banning interest-only mortgages. We believe that the final proposals were more practical than those first proposed, and we were pleased that the FSA undertook a full cost benefit analysis to assess the impact of the MMR on the wider economy.

Nevertheless, the MMR is set to have a significant impact on the mortgage market in the UK, and the FSA and the FCA must monitor its impact on firms' behaviour and consumer access going forward. The MMR is likely to make firms more cautious in developing new mortgage products, which will restrict consumer choice. Also, we have said it is important that the FSA considers the impact of restricting the sale of non-advised mortgages on smaller mortgage providers and their customers.

Product Intervention

The Panel has been pleased to help the FSA in their development of more proactive product intervention in preparation for the work of the FCA. We have been keen to develop a more interactive relationship with the FSA. We would like to work out better ways to encourage the industry to advise the FSA about toxic products or non-toxic products that are being directed to inappropriate markets or being mis-sold.

Nevertheless, we have also highlighted that the problems are more often with the selling of products to a wider audience than they are appropriate for, rather than the selling of products which are innately toxic.

Payment Protection Insurance

We welcomed the FSA undertaking forward analysis to predict the likely impact of PPI mis-selling claims on the FSCS levy. The Panel has been extremely concerned that a significant proportion of smaller firms will have difficulty meeting this potential liability. We have suggested that it may reach a stage where it is unreasonable to ask the firms who have behaved responsibly to pay significantly higher FSCS levies, especially when they have insufficient time to budget properly for this increased liability.

With Profits – Mutual Firms

We have been urging the FSA to make progress on clarifying issues for with-profits and welcomed the publication of the Policy Statement in March 2012. We look forward to further discussions with the FSA during 2012. Smaller firms in particular may need more clarity and information on this subject and the related work pieces that are still in progress.

5. EU initiatives

EU strategy

We have identified that the Panel needs to take an interest in European developments earlier in the process. This will help us to understand more about what the FSA has been directed to achieve, and consequently help us to advise UK regulators where we feel that proposed European rules impose unnecessary burdens on smaller firms.

We plan to work more closely on these issues, both with the Practitioner Panel and the FSA's international team, to enable us to prioritise issues for Panel involvement at an early stage. As part of this, we have started to receive regular updates from the FSA's international team, which provide an overview of the current EU agenda and the background to key European policy initiatives.

Harmonised European CRD reporting

We supported the FSA's efforts to modify or tailor the EU requirements on mandatory EU-wide regulatory reporting under the Capital Requirements Directive however, this is unlikely to result in any benefit. The diverse nature of small firms in the UK that will be caught by this initiative, make it even more important that the UK seeks allies within the EU whenever possible. We were pleased to note that the FSA's proposals in this area indicated that the regulator understood the issues and concerns of industry representatives and had made those representations in Europe.

Solvency II

The members of the Panel who work in insurance have had regular contact with the FSA policy team working on Solvency II over the year. We have been particularly concerned to emphasise the need for proportionality of implementation for smaller firms. There have also been a number of changes to the timescale as driven by European developments, and we have worked with the FSA team to encourage them to ensure that small firms receive appropriate communication and information about the progress and requirements of Solvency II.

We have taken an interest in the future reporting requirements that will be put in place in the UK to comply with Solvency II. We have raised concerns that the national specific template planned for the UK may require information over and above that mandated at EU level. The Panel has repeatedly expressed its concerns around the cost of Solvency II and its impact on smaller firms. We have stressed that the FSA must seek to minimise the burden of this on smaller firms, and make the requirements as simple as possible, in order to save significant amounts of money being spent on compliance consultants so that smaller firms may feel confident that they will comply with Solvency II.

MiFID and IMD2

In the section on the Retail Distribution Review (RDR) in this report (4 – Major UK policy developments) we highlighted our concern about the possible impact of MiFID (markets in Financial Instruments Directive) requirements on financial advice if it necessitates changes to the RDR.

We have also warned that the UK must guard against any subsequent read across from MiFID into the IMD2 (Insurance Mediation Directive) on the definition of "advice" and receipt of commissions. Such a move might lead to a ban on the taking of commissions or require some form of mandatory disclosure. This would have a massive impact on general insurance intermediation within the UK and a dramatic impact on smaller firms in this sector.

6. Smaller firm supervision

Small Firms' Assessment Programme

We were pleased with the generally positive outcomes from the FSA's three year Assessment Programme for small firms and we support the FSA's intention to publish the results. We believe that most firms want to do the right thing: the successful implementation of this programme demonstrates that a supervisory method based on education and good communication can be effective.

There have been occasions when we have registered concern at the perception among some practitioners that there is reluctance among supervisors to work with firms and help them to understand the best way to comply with regulatory requirements. This is particularly the case with smaller firms, and it results in firms being judged against standards that are not always clear. The regulator has responsibilities as well as firms and it does not seem unreasonable to us to expect the FSA to have the necessary expertise to be able to provide greater guidance to firms in these instances.

Communications with firms

As the majority of smaller firms have to rely on generalised communications from the FSA, without an individual supervisor to provide any interpretation, it is all the more important that those generalised communications are correctly targeted and provide clear advice. For instance, we pointed out that the effectiveness of Dear CEO letters is reduced significantly if they are poorly targeted, and that relevant, accurately addressed communications would save considerable time and frustration and would contribute to regulatory effectiveness. We suggested that all communications should clearly state which sector(s) they are relevant to and only be sent to firms in those sectors. They should also be written in language which is meaningful to that target audience.

We were also concerned to hear that the FSA's IT system is not able to support the Communications Division in targeting its information effectively to firms. We have informed the FSA that such facilities are critical to enable the regulator to explain the regulatory requirements to all firms affected by any changes.

We were pleased to provide feedback on the FSA's communication plan for the move towards an internal twin peak operating model. We were very supportive of the positive and proactive approach that was taken.

7. Future plans

In the coming year, we plan to engage actively in the FSA's planning for transfer of regulatory responsibilities to the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA). We will look to help the FCA to have a constructive approach to the needs of small firms, and to communicate effectively with the large constituency of smaller firms that will not have dedicated relationship managers. We will also focus on inputting to the development of the FCA's sector based supervision model so that it recognises the differences between smaller and larger firms. At the same time, as the FCA's operational objective of consumer protection is developed, we will be keen to ensure that the approach is balanced, with active consideration of the FCA's statutory principle of consumer responsibility alongside consumer protection in its policy development.

The cost effectiveness of the regulatory structure will also be a focus for the Panel over the next year. This is not only the balance of cost and benefit in new regulatory policies, but also the wider costs in the funding of the Financial Services Compensation Scheme, Money Advice Service and Financial Ombudsman Service.

Smaller Business Practitioner Panel
April 2011 – March 2012

Panel Member	Position
Guy Matthews *Chairman*	Chief Executive, Sarasin Investment Funds
Clinton Askew	Director, Citywide Financial Partners
James Bawa *(Member from September 2011)*	Chief Executive, Teachers Building Society
Richard Carne *(Member from July 2011)*	Director, Asset Management IFA Ltd
Ian Dickinson	Head of General Insurance Compliance and Training, Brunsdon LLP
Paul Etheridge *(Member to May 2011)*	Chairman, The Prestwood Group of Companies
Peter Evans	Chief Executive, Police Credit Union
Sally Laker	Managing Director, Mortgage Intelligence
Fiona McBain	Chief Executive, Scottish Friendly Assurance
Andy Smith	Governance, Risk and Compliance Director TD Direct Investing
Ian Templeton	Managing Director, UIA (Insurance) Ltd
Andrew Turberville Smith	Chief Operating Officer and Finance Director, Weatherbys Bank Ltd

Smaller Businesses
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