Financial Regulatory Briefing

The monthly digest of official pronouncements

AUGUST 2010

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Accountancy and Actuarial Discipline Board

AADB Launches Consultation On Guidance For Prosecution Decisions Under Its Accountancy Scheme

The Accountancy and Actuarial Discipline Board, an operating body of the Financial Reporting Council (FRC), has published a consultation document on guidance it proposes to issue in respect of decisions to file disciplinary complaints under its Accountancy Scheme.

The Guidance has been developed following changes that were made to the Accountancy Scheme earlier in the year.

It is intended that the Guidance should provide further transparency in the AADB's processes and promote consistency in the decision-making process.

The Guidance has been developed taking particular account of the absence of any alternative to a disciplinary hearing for dealing with any misconduct identified and is designed to ensure that a viable case should normally go forward to a disciplinary hearing unless it is clearly not in the public interest for it to do so.

Responses to the consultation are requested by 22 October 2010.

The consultation document, "The Referral of Formal Complaints to Disciplinary Tribunals", is available on the AADB website (at: http://www.frc.org.uk/aadb/publications/).

The Actuarial Profession

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The Launch Of The Institute And Faculty Of Actuaries

The Institute and Faculty of Actuaries, launched on 1 August 2010, will be led by Ronnie Bowie, former president of the Faculty of Actuaries.

Ronnie outlined his three ambitions for the year: "I want the newly formed Institute and Faculty of Actuaries to engage, deliver and inspire. We will engage by making the body relevant to the work of our members. We will deliver effective and efficient services to our members, including a revitalised research programme and further expansion into the field of risk management. And we will inspire by helping our members feel proud of their profession, proud of their work and proud of how actuaries can make a positive difference to the financial world."

Caroline Instance, chief executive of the Profession, added: "We will continue to operate publically as the Actuarial Profession so, in many respects, it will be business as usual as we continue with our key objective of supporting members achieve their career goals."

The launch of the Institute and Faculty of Actuaries follows the vote of 25 May 2010 when voting members of the Faculty of Actuaries and Institute of Actuaries agreed to merge both organisations. The final approval came in June when the Privy Council gave its approval.

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Association of British Insurers

Kerrie Kelly Steps Down As ABI Director General

The Association of British Insurers has confirmed that Kerrie Kelly is stepping down from her role as Director General to return to Australia for personal reasons.

Maggie Craig, Director of Life and Savings at the ABI, will serve as acting-Director General while a permanent replacement for Ms Kelly is found.

ABI Calls For No More Delays To Pension Reform

The ABI is calling for more action to get people saving at its Savings and Protection Conference. Over 40% of people are not taking basic steps to save sufficiently for their retirement. This means a vast number of Britons will not have enough money to live comfortably in retirement unless we tackle the problem of under saving urgently.

To get people saving now, we need:

* No significant delays to the introduction of auto-enrolment in 2012;
* employers to be engaged with pensions and make it as straightforward as possible to enrol employees into existing pension schemes;
* honest communication, to tackle the lack of consumer understanding of pension saving;
* simplified consumer advice about pension saving.

Faster Transfers For Pension Customers As Options Progress Continues

Pension and annuity providers using Origo's Options transfer initiative have reported continued progress in Q1 2010, according to figures released by the ABI. The news means more customers are experiencing faster transfers than ever before when moving to a new pension or annuity provider. Average transfer times remained steady for the third successive quarter, at 11 calendar days for OMO transfers, despite the addition of several new providers and a major increase in the numbers of transfers completed via the service. Twenty providers are now using Options for OMO and Immediate Vesting Personal Pension (IVPP) transfers, with 13 providers live for pension transfers.

The improvements achieved to date by Options have also been extended to customers with occupational defined contribution pension schemes, following the extension of the service to cover these types of transfers in June. Further new joiners are also expected in the coming months.

Open Market Option (OMO)
Over 14,000 OMO and IVPP transfers were completed on Options in Q1 2010, up 53% since Q1 2009. The average Q1 transfer time was 11 calendar days – down from a pre-Options industry average of 31 days. 36% of transfers were completed in less than seven days, and a further 47% in less than 14. Abbey Life and Windsor Life joined this part of the service in April, as did Scottish Life in July.

Pension Transfers
Average pension transfer times have fallen from a pre-Options industry average of 36 days to just 10 calendar days in Q1 2010. Over 9,000 pension transfers were completed in Q1, with 44% of these completed in less than seven days and a further 44% in less than 14 days. Abbey Life, Friends Provident, AXA and Nucleus are the latest providers to go live for pension transfers, bringing the total to 13. Nucleus is the first wrap provider to join Options, with others expected to follow shortly.

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Association for Financial Markets in Europe

AFME Comment On European Bank Stress Tests

Commenting on the announcement of the results of the Committee of European Banking Supervisors' stress tests on European Banks, Mark Austen, acting CEO of AFME said: "This information goes some way to helping investors understand the underlying strength of individual banks and make their decisions accordingly. But direct comparisons between banks that have been assessed using differing criteria should be made with caution. These results do not, and should not, create a 'league table' of European banks."

European Commission Short Selling Proposals - Right Intentions, Wrong Solutions

Short selling is no riskier than any other buying and selling of securities and does not warrant specific rules, says the Association for Financial Markets in Europe (AFME) in its response to a European Commission consultation on short selling.

Short selling, including uncovered short selling, is a well-established, legitimate trading activity, essential for market making and widely accepted by investors and regulators as helping to enhance price discovery, counteract supply/demand imbalances and provide liquidity to the market.

Whilst AFME supports the Commission's objectives of harmonising rules across Europe, reducing systemic risk and deterring abusive short selling, it believes that the Commission has identified risks from short selling that do not exist.

AFME agrees with the proposal to prevent short selling where the seller has little or no intention of covering the sale. However, the Commission's proposed ban on 'uncovered' short selling will not succeed in its aim of reducing volatility and could have the opposite effect. Studies show that banning short selling can actually lead to wider bid-ask spreads and steeper price falls.

On short selling disclosure
AFME generally supports moves to greater transparency but agrees with the Committee of European Securities Regulators (CESR) view that firms which engage in market making should be exempt from disclosure requirements on uncovered short selling. AFME believes, however, that CESR's proposal – that equity investors should publicly disclose their short positions to the market at very low thresholds (just 0.5% of issued share capital) may expose them to unfair risks. Despite this, it is recognized that regulators need information to supervise market activity and therefore AFME does support the principle of private disclosure of short positions to regulators.

To enhance marketwide transparency for equities on a basis that is fair to all investors, the regulator could then publish the aggregated reported short position of the market. This would provide more value to investors than a list of individual disclosures.For fixed income, AFME strongly advises against similar aggregated disclosure measures, since the potential adverse effects of such transparency on government bonds are not yet well understood.

Mark Austen, acting CEO of AFME, said: "We agree with many of the European Commission's objectives and believe that disclosure should be made in a way that provides regulators with the information necessary for them to mitigate systemic risk. However, market participants strongly believe that the Commission's recent regulatory

proposals are disproportionate to the potential risks being addressed.

“Any regulation of short selling must also recognise the role played by banks and other liquidity providers that underwrite or sub-underwrite new share issues.

“In addition, we support the Europe-wide desire for a harmonised approach to regulation as the costs and increased complexity of complying with different regimes would be high and have a negative impact on market efficiency.”

Association of Investment Companies

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Tax Changes Mean Greater Competitiveness And Lower Costs For Investment Trusts

The Association of Investment Companies (AIC) supports Government proposals that will increase the investment flexibility and reduce the compliance costs of investment trusts.

Ian Sayers, Director General of the AIC, said: "This announcement is an important step in modernising the rules for investment trusts which have stayed largely the same since their introduction in 1965. Traditionally the tax rules have meant investment trusts have focused on equity investment. These new rules offer the opportunity to diversify and offer new means of generating shareholder returns.

"Reform should also help reduce ongoing administrative costs. It will move investment trusts to a new system of ongoing self-assessment and away from a requirement for annual approval. This will reduce the bureaucracy involved with maintaining an investment trust's tax status and bring the sector into line with other collective investment products.

"While for the most part the proposals are very positive, care will have to be taken to ensure that the transition to a new regime takes account of the needs of all investment trusts. We look forward to working with officials to fine tune the proposals to secure the best possible result."

Auditing Practices Board

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Draft Revised Guidance For The Audit Of Banks And Building Societies In The United Kingdom

The Auditing Practices Board (APB) of the FRC has issued for comment a consultation draft of a revision of Practice Note 19 *The audit of banks and building societies in the United Kingdom*. The consultation period ends on 29 October 2010.

The consultation draft updates the current guidance to reflect the issuance of the new ISAs (UK and Ireland) which apply to audits of financial statements for periods ending on or after 15 December 2010 and for changes in legislation. In addition the APB has also revised and enhanced the guidance in a number of areas, including in relation to the audit of accounting estimates and impairment provisions and related disclosures. The APB has also added guidance on bilateral and other periodic meetings between auditors and the FSA.

The consultation draft of Practice Note 19 (Revised) may be downloaded, free of charge, from the Publications (Exposure Drafts) section of the FRC website.

Draft Revised Guidance On The Audit Of Occupational Pension Schemes

The APB has published an exposure draft of a revision of Practice Note (PN) 15: 'The Audit of Occupational Pension Schemes in the United Kingdom (Revised)'. The consultation period ends on 29 October 2010.

When finalised, the guidance proposed in the exposure draft will apply to the audits of occupational pension schemes for periods ending on or after 15 Dec. 2010. The exposure draft updates the current guidance, which was issued in March 2007, to reflect:

* the issuance of the new ISAs (UK and Ireland) (which apply to audits of financial statements of occupational pension schemes for periods ending on or after 15 Dec. 2010); and

* changes in the legislative and regulatory framework.

The new ISAs (UK and Ireland) primarily improve the overall readability and understandability of the ISAs (UK and Ireland). The core guidance contained in the exposure draft is largely unchanged from the current guidance. However, new, enhanced or revised guidance has been included with respect to:

* Communicating Deficiencies in Internal Control to Those Charged with Governance and Management.

* Audit Considerations Relating to an Entity Using a Service Organisation.

* Auditing Accounting Estimates, Including Fair Value Accounting Estimates and Related Disclosures.

* Going Concern.

* The illustrative examples of various auditor's reports.

A copy of the exposure draft may be downloaded from the publications section of the APB's web site (at: http://www.frc.org.uk/apb/publications/pub2334.html).

APB Issues A Feedback And Consultation Paper On The Provision Of Non-Audit Services By Auditors And FRC Consults On Related New Guidance On Audit Committees

The APB has published stakeholder feedback following its consultation in October last year on whether there should be a prohibition on auditors providing non-audit services to the entities that they audit. In parallel the FRC is publishing for consultation updated guidance to audit committees on determining whether a company's auditor should be permitted to provide particular non-audit services.

The APB's October consultation followed a report last year by the House of Commons Treasury Committee which proposed a ban on the auditor providing non-audit services. The consultation generated a substantial number of responses from all APB's stakeholder groups, in particular, including the views of a range of investors. The overwhelming view of respondents (irrespective of the constituency involved) is that there should be no outright prohibition on non-audit services.

There is agreement, however, that auditor objectivity and independence is perceived to be adversely affected by the provision of non-audit services and that improved transparency and governance would address these concerns. The APB is therefore proposing changes to the APB Ethical Standards for Auditors and amendments to the FRC's Guidance on Audit Committees, both of which are now being published.

As part of the consultation APB asked commentators whether there were any other views that they would like to be taken into account and has also held discussions with the FRC's Audit Inspection Unit on their findings from audit inspections. As a result, APB is now consulting on three particular issues relating to the provision of non-audit services by auditors (restructuring services, contingent fees and conflicts of interest).

Richard Fleck, Chairman of APB commented: "The consultation process was extremely worthwhile as it increased the general understanding of the reasons why there are concerns about auditors providing non-audit services to the entities they audit and the impact this has on the perception of auditor independence. We welcome the fact that a common view emerged from all constituencies as to how to address these concerns, namely through improved transparency and governance.

"APB remains conscious of the effect that the provision of non-audit services by auditors has on confidence in auditor objectivity and independence and we will monitor the effectiveness of our proposals and continue to respond to other issues that may arise. We are also consulting on whether to prohibit auditors from providing restructuring services to listed companies in distress, to prohibit auditors from providing any non-audit services on a contingent fee basis and to extend the threats and safeguards approach to non-audit services provided to an audited entity's connected parties."

Baroness Hogg, FRC Chairman, said: "There remains concern that substantial provision by audit firms of other services to the companies they audit may pose a threat to their independence. We believe that audit committees can help by having a clear framework for assessing when it would be appropriate for the auditor to provide other services, and are consulting about how to make this more transparent."

A copy of the APB's Feedback and Consultation Paper (incorporating as an Appendix, the FRC's Consultation Paper) may be downloaded free of charge from the publications section of the APB's web site (http://www.frc.org.uk/apb/publications/exposure.cfm).

A copy of the FRC's Consultation Paper may be downloaded free of charge from the FRC web site (http://www.frc.org.uk/publications/pubs.cfm?mode=list&year=2010).

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Bank for International Settlements

‘Long-Term Issues In International Banking’: New Report From The Committee On The Global Financial System

The Committee on the Global Financial System (CGFS) has released ‘Long-term issues in international banking’, a report prepared by a CGFS Study Group chaired by Hans-Helmut Kotz, former Executive Board member of the Deutsche Bundesbank.

The report addresses structural issues in international banking from three angles: a historical perspective, what the drivers have been, and what might happen next:

* *The development of international banking*: the report documents its evolution over the last 30 years in terms of size, form and geographical coverage.

* *The factors behind the development*: the report provides a critical review of the literature on the various drivers of international banking. A noteworthy conclusion is that the fast growth of internationally active banks, which contributed to the vulnerability of their business model, is difficult to explain on efficiency grounds, at least at an aggregate level. This suggests that institutions’ incentives might have been distorted, which warrants further investigation.

* *Potential future developments*: in addressing this more speculative question, the report pays particular attention to the regulatory reform environment, the pattern of economic growth worldwide and the rapidly evolving interactions between markets and banks.

‘Long-term issues in international banking’ is the last in a series of three CGFS studies analysing current challenges for international banks. Mark Carney, CGFS Chairman and Governor of the Bank of Canada, says the CGFS is confident these reports will make a valuable contribution to the current debate about policy responses to the financial crisis.

Bank of England

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Monetary Policy And Financial Stability - Speech By David Miles

In a speech to the Bristol Business Forum, David Miles – an external member of the Bank of England's Monetary Policy Committee (MPC) – explains his view of the appropriate policy response to the financial crisis

In describing the unprecedented level to which interest rates have fallen, David Miles argues that "...it has been right to loosen aggressively the stance of monetary policy because of the scale of the deflationary and recessionary forces unleashed by ... the crisis in the banking sector". He adds that "...fragilities in the banking system remain and pose risks that the recovery in demand and activity we have seen across Europe – including the UK – falters". The MPC's challenge is to balance "...risks that inflation of 1.0-1.5pp above target lasts long enough to become ingrained in expectations and affect behaviour so that it is hard to bring down, versus risks that the recovery in output becomes weaker and then disappears, leaving inflation pressures lower than is consistent with the target further ahead". David Miles notes: "I look forward to the day when it will be appropriate to tighten monetary policy since a return to more normal levels of interest rates would be a welcome sign that economic conditions were also more normal. But I do not think that is where we are today." David Miles counters those who argue that monetary policy should be set in a different way, so as to reduce the chances of banking crises in future, rather than aimed at ensuring price stability: "capital requirements are a better means to that end". At the heart of the current economic situation, he says, is "...a banking system which proved catastrophically fragile". "On the eve of the crisis", he notes, "...the capital of UK banks, relative to their assets, was around half the level that was typical fifty years earlier". And banks' liquid assets were "...a fraction of what would have been normal twenty years earlier and a tiny fraction of what would have been normal before the 1970's".

The speech goes on to argue that the fragility of the banking system can be reduced without incurring a high cost in terms of lower economic activity. Miles says: "I am rather sceptical about the claims that substantially higher capital requirements must mean significantly higher costs of funds for those who borrow to invest and that total investment and output in the economy will be significantly lower", noting that "...there is little evidence that investment or the average (or potential) growth rate of the UK economy picked up as spreads on bank lending narrowed over the past decade, and the volume of credit expanded sharply". The analysis he presents suggests that, under a plausible range of assumptions, the economic costs of higher bank capital requirements may be small, but the impact on the robustness of the financial system large.

In conclusion, David Miles says that "using the interest rate as a tool to maintain the stability of the banking system strikes me as a strange assignment of policy tools to targets. Changes in interest rates have an uncertain impact on financial stability; often it would be unclear in which direction to move interest rates to help make the banking sector more robust. But in the UK changes in interest rates have a powerful – and relatively predictable – impact on the wider economy. In contrast capital requirements may have a powerful and relatively clear impact on bank robustness and an uncertain – but quite likely relatively small – impact on the wider economy. So it seems to me natural to use interest rates as the active tool to affect the balance between demand and supply in the economy – and so control inflation pressures – and use capital requirements to maintain stability in the banking sector.... If banks do come to hold much more capital this would make the job of setting monetary policy easier."

The Financial Crisis Reform Agenda - Speech By Andrew Bailey

In a speech to the British Bankers Association's Annual Banking Conference, Andrew Bailey, Executive Director of Banking Services (and Head of the Special Resolution Unit), Chief Cashier of the Bank of England and designated Deputy CEO of the new Prudential Regulation Authority (PRA), talked about the recently announced changes in prudential supervision and the resolution of large banks when they get into trouble

Andrew Bailey began by reviewing the Bank's previous role in banking supervision. He explained: "My own view on this record is that the Bank was relatively good at the prudential competencies of capital adequacy and liquidity, but it was relatively weak at identifying and dealing with fraud and abuses of risk controls. The world is now a very different place to the 1990s, and it is very important to be clear that the new organisation of supervision will not be a return to the way it used to be done at the Bank…a slavish return to the past would be a mistake." He went on to explain: "...we are not trying to design a regime in which no bank should ever fail…it would not create the right incentives around risk taking...". Creating the PRA would tackle the issue of overlapping responsibilities between the FSA and the Bank but would not solve the reliance on public money. On how to handle the process of creating the PRA, Andrew Bailey set out three guiding principles:

* That the process must be harmonious and constructive. He says: "Hector and I are fully committed to working together to get the right outcome, which is a robust, fair and transparent system of prudential supervision…the PRA's role will be distinctive. Its approach and culture will be built around judging and dealing with the build-up of unwanted risk in the financial system, and thus the robustness of the business models of individual institutions...";

* The need for various parts of the system to work together on the basis of clear roles; and

* The Bank will change in order to deliver its new responsibility, but in doing so it will remain focused on its two core purposes – monetary and financial stability. It will continue to work closely with the financial sector.

Andrew Bailey then turns to the "unacceptable" use of public money to sort out insolvent banks that are large and important to the financial system and thus the wider economy. He explores potential solutions:

* He repeats the message from the Bank's recent Financial Stability Report: "UK banks have raised their capital and liquidity buffers substantially…but they need to maintain this resilience while refinancing substantial sums of funding in the period ahead and providing sufficient lending to support economic recovery, something that is in their collective interest. Over time they will need to build larger buffers...an extended transition to the new quantums of capital liquidity will enable banks to build resilience through greater retention of earnings, while sustaining lending".

* "...the capital instruments issued by banks must absorb losses in situations either where the bank is preserved as a going concern, or where it is wound down..."

* Andrew Bailey looks at the issues for how banks could be restructured, and suggests that, on its own, creating "narrow banks" is not necessarily the answer because of the remaining "non-narrow" parts of the industry.

* Finally, he explores the approach whereby failing banks would be recapitalised. Drawing on practices in the non-bank world, he concludes that: "We need something to give us a credible chance of covering the losses and most likely recapitalising a big bank. Such an event should avoid the use of public money."

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Basel Committee on Banking Supervision

Broad Agreement On Basel Committee Capital And Liquidity Reform Package

The Group of Governors and Heads of Supervision, the oversight body of the Basel Committee on Banking Supervision, met on 26 July 2010 to review the Basel Committee's capital and liquidity reform package. Governors and Heads of Supervision are deeply committed to increase the quality, quantity, and international consistency of capital, to strengthen liquidity standards, to discourage excessive leverage and risk taking, and reduce procyclicality. Governors and Heads of Supervision reached broad agreement on the overall design of the capital and liquidity reform package. In particular, this includes the definition of capital, the treatment of counterparty credit risk, the leverage ratio, and the global liquidity standard. The Committee will finalise the regulatory buffers before the end of this year. The Governors and Heads of Supervision agreed to finalise the calibration and phase-in arrangements at their meeting in September.

Mr Jean-Claude Trichet, President of the European Central Bank and Chairman of the Group of Governors and Heads of Supervision, said that "the agreements reached today are a landmark achievement to strengthen banking sector resilience in a manner that reflects the key lessons of the crisis." He emphasised that "the Group of Governors and Heads of Supervision have ensured that the reforms are rigorous and promote the long term stability of the banking system. We will put in place transition arrangements that ensure the banking sector is able to support the economic recovery."

Mr Nout Wellink, Chairman of the Basel Committee and President of the Netherlands Bank added that "a strong banking sector is a necessary condition for sustainable economic growth." He added that these announcements should provide additional transparency about the design of the Basel Committee reforms, thus reducing market uncertainty and further supporting the economic recovery. Mr Wellink underscored that "many banks have already made substantial strides in strengthening their capital and liquidity base. The phase-in arrangements will enable the banking sector to meet the new standards through reasonable earnings retention and capital raising."

In reaching their broad agreement, the Governors and Heads of Supervision considered the comments received during the public consultation on the Basel Committee's proposed reforms, which were published in December 2009. They also took account of the results of the Quantitative Impact Study, the assessments of the economic impact over the transition and the long run economic benefits and costs. The Basel Committee will issue publicly its economic impact assessment in August. It will issue the details of the capital and liquidity reforms later this year, together with a summary of the results of the Quantitative Impact Study.

The key broad agreements of the Governors and Heads of Supervision are summarised in an Annex which can be found at: http://www.bis.org/press/p100726.htm.

Progress On Regulatory Reform Package

At its 14-15 July meeting, the Basel Committee on Banking Supervision reviewed the design and overall calibration of the capital and liquidity frameworks, comments on its December 2009 consultation package, the results of its comprehensive quantitative impact study (QIS) and its economic impact assessment analyses.

Based on this review, the Committee has developed concrete recommendations for

completing its package of regulatory reforms. The Basel Committee's oversight body – the Group of Central Bank Governors and Heads of Supervision – reviewed the Committee's progress and recommendations at its meeting in late July. The Committee will present to the Central Bank Governors and Heads of Supervision concrete recommendations for the definition of capital, the treatment of counterparty credit risk, the leverage ratio, the conservation buffer and the liquidity ratios.

The Committee also reviewed proposals for the role of "gone concern" contingent capital in the regulatory capital framework and will issue shortly a proposal for consultation. It continues to assess proposals on contingent capital from a "going concern" perspective.

Mr Nout Wellink, Chairman of the Basel Committee and President of the Netherlands Bank, noted that "the Committee made significant progress at its meeting and remains fully on track to deliver a complete package of capital and liquidity reforms, including design and calibration, in time for the November 2010 G20 Leaders Summit in Seoul."

The Committee has now issued for consultation a fully fleshed out countercyclical capital buffer proposal. The countercyclical buffer would be imposed when, in the view of national authorities, excess aggregate credit growth is judged to be associated with a build-up of system-wide risk. This will help ensure the banking system has an adequate buffer of capital to protect it against future potential losses. The Committee has already consulted on the capital conservation buffer, which was elaborated in the December 2009 reform package.

The Committee also continues to review specific proposals to address the risks of systemic banking institutions. These include a "guided discretion" approach for a systemic capital surcharge in combination with other mitigating regulatory and supervisory measures.

Comments on the countercyclical buffer proposal should be submitted by Friday 10 September 2010 by e-mail to: baselcommittee@bis.org. Alternatively, comments may be sent by post to the Secretariat of the Basel Committee on Banking Supervision, Bank for International Settlements, CH-4002 Basel, Switzerland.

The full publication of the Countercyclical capital buffer proposal can be found at: http://www.bis.org/press/p100716.htm.

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British Bankers Association

BBA Statement Regarding CEBS Bank Stress Testing Announcement

The BBA said: "UK banks have already put in the work to rebuild their businesses and put more money aside against future financial problems. It is no surprise to find they have exceeded the standards set out by CEBS to ensure banks across Europe are well placed to weather any future financial problems.

"Stress testing is a useful tool to manage risk and inform strategy. Banks have undertaken stress and scenario tests for many years on the basis of bilateral discussions between themselves and their regulators. The BBA has always supported stress testing but feels the long-standing bilateral approach is more appropriate as it avoids misinterpretation and adverse effects on institutions."

Banks Committed To Improving Regulation

The BBA said: "The UK's banks are committed to the reform of the regulatory institutions to help ensure the maximum protection for all against future downturns and international crises.

"We welcome the Government's plans for a regulatory structure which combines analysis of global economic factors and the effects of government policies with clarity on how financial firms should carry out their day-to-day business. Consumer confidence in the new structures will be essential, along with clear-sighted analysis of the many factors affecting the economy.

"A smooth transition is vital: there are many international discussions well under way in which the Financial Services Authority currently takes the lead. We will work with the Government to ensure a smooth transition to the new regulatory regime, but a priority for us will be to ensure none of the work already underway is lost in the transition.

"The new regulator needs to be substantial and authoritative: it needs to be able to represent the UK as the world's financial centre to the many new EU and global bodies being created; and it needs to be able to stand above land-grab arguments between regulators which ultimately help no-one.

"In the past two years, the UK has implemented and enacted reforms which in other countries are still only at the discussion stage. In 2009 we were the first country to implement a Banking Act to ensure the orderly winding-down of a failing financial business, and we were also the first to bring the issue of pay and bonuses into statutory regulation. We are already actively involved in the process of change, to provide security and stability for all bank customers."

BBA Response To 'Financing A Private Sector Recovery'

Banks intend to keep playing their full part in financing growth in UK by lending to business.

The major UK banks and the BBA have established a Taskforce to identify, analyse and review ways the banking system can, over the next 3 years, help viable UK businesses of all sizes access appropriate finance and other support. The Taskforce will set in train a number of work streams and aims to report by mid October in time for the Chancellor's autumn statement. UK banks have already agreed with government the following principles for dealing with SMEs.

Banks will:

* Welcome the support of the SME's own professional advisers and are happy to work with them (acknowledging shadow directorship boundaries in the provision of advice);

* set out the factors that determine how much the loan will cost using either in -house guides or industry-standard literature;

* inform customers how long it will take for a lending decision to be taken, starting from the point when a full suite of information is provided to complete an application;

* ensure they have fair and effective processes in place to review decisions to decline a lending request;

* provide proactive and clear feedback wherever possible when a decision has been taken to decline a borrowing request and will suggest possible next steps businesses might take (for example contacting Business Link for further advice and support); and

* promote both these initiatives and the Lending Code itself. with SME representatives and with the Lending Code Standards Board.

Bank Lending To Businesses Explained In New Factsheet

The process of how banks calculate interest rates for loans to businesses are set out in detail in a new factsheet from the BBA. *Small Business Lending – How Banks Set The Price For Loans To Small Businesses* sets out the factors which govern the cost of credit, focussing on the three key drivers:

* Cost of funds (the price banks pay to borrow money to lend on to businesses, and the cost of using multiple short-term deposits to fund long-term arrangements with businesses);

* Cost of risk and capital (the calculated likelihood of the borrower's ability to pay back the loan, and the amount the bank is required to set aside as regulatory capital); and

* Administration costs (often proportionately more expensive with small businesses than with larger enterprises).

The factsheet follows the publication of six commitments from banks to their SME customers announced with the Budget last month. Banks will continue to work with SME bodies on improving access to finance further, including tips on how to prepare for the banking relationship.

Support for the factsheet also comes from the Institute of Credit Management and the National Federation of Enterprise Agencies and the Forum of Private Business. The Confederation of British Industry welcomed the publication. Russell Griggs, chair of the CBI's UK SME (small and medium-sized enterprises) national council, said: "This document is yet another good sign that we are moving to a situation where banks and SMEs are engaged in a good and proper dialogue about how they do business together. It shows that we are all committed to making sure that SMEs have the best information they can get to help them make decisions and prepare their cases for the banks, should they need to. It really helps us all move forward into the new economic and credit environment in which we all now live."

BBA Statement Regarding Basel Committee's Capital And Liquidity Reforms

Further steps to bolster banks against future financial problems have been welcomed by the UK industry.

The BBA said the Basel committee's broad agreement on its 'more capital, more liquidity' proposals helped reduce uncertainty about the shape of new regulation. But the BBA warned that the Committee must strike the right balance between greater financial stability and allowing banks to play their full part in economic recovery.

The Committee has taken on board industry's concerns about the capital proposals, for instance by amending the treatment of minority interests and deferred tax assets. But the BBA's Simon Hills said more still needed to be done on the liquidity proposals, particularly the Net Stable Funding Ratio (NSFR), which currently cuts across the banks fundamental role of maturity transformation. He said it was important that any unintended consequences were corrected during the trial run before the NSFR was introduced at the beginning of 2018.

BBA Executive Director, Simon Hills said "We urge the Committee to finalise the arrangements on calibration and phase-in at its September meeting so banks can continue to play a full part in the economic recovery."

BBA Response To Mervyn King's Comments On Banking Relationships

"The UK's banks have three priorities: to support individual customers and businesses through the global downturn; to ensure taxpayer support is repaid in full, and to ensure regulatory change is coordinated and appropriate.

"The relationship manager is not the sole decision maker when it comes to dealing with a business loan. Regional specialists and experts on the business sector may also complement the local manager's decision, and this has always been the case. But in order for the relationship to succeed, the customer needs to be confident that the right decision is being arrived at fairly. The BBA small business panel will look further into this issue.

"We agree with the Governor's view that more competition in the banking sector will mean more choice for customers, and alternative sources of funding for businesses need to be explored. This is the subject of the Government's recently-published green paper on Financing a Private Sector Recovery, and we will be responding to this in due course."

BBA Statement On FSA Review Of Remuneration Code

The BBA said: "UK banks recognise that reform of pay structures plays a significant part in restoring confidence in the industry. Banks link pay and bonuses to the long term success of the business and do not reward staff in ways which encourage undue risk taking. Indeed, for the past year, pay and bonus policies have been regulated by the Financial Services Authority. Banks have also paid additional tax on bonuses, and individual policies at state-supported banks have been closely monitored by the government.

"The UK has moved further and faster on reform of pay and bonuses than any other country. Today's proposals from the FSA represent the UK's contribution to levelling the playing field for all EU financial institutions, as they will implement the EU-wide rule changes which will come into force next January.

"The BBA maintains that reform of the bonus system in financial services must be globally coordinated. A global industry needs to conform to global standards, as any country which takes a lighter approach will prove to be a magnet for business. We now need other countries to coordinate their reforms with the UK and EU rules. We will work with the FSA to ensure rule changes do not damage the banks' ability to recruit and retain staff in the UK."

BBA Publishes Annual Abstract Of Banking Statistics

The 27th Annual Abstract of Banking Statistics from the BBA reveals an industry changed radically by the global economic crisis, but still undertaking enormous volumes of business for its customers. The publication provides a wealth of information on the activities of the UK's banks during the calendar year 2009, including figures on banks' assets, lending volumes, mortgages, current accounts and cards – even the current numbers of ATMs.

June figures For Main High Street Banks

The annual growth in the banks' net mortgage lending is 4.1% compared to 1.1% for the whole mortgage market in May. Gross mortgage lending of £8.6bn in June was slightly below the average of the previous six months. High street banks continued to see strong repayments. Net mortgage lending increased by £2.1bn in June compared with £2.5bn in May and £2.9bn for June 2009.

BBA statistics director, David Dooks said: "The banks' mortgage lending position was little changed in June. The abolition of HIPs and a reported increase in the number of house sellers is expected to encourage activity in the market, though this may be tempered by households' uncertainty over job prospects and the impacts of fiscal tightening. Overall lending to business continued to reflect subdued demand, and contraction in lending to most non-financial sectors slowed."

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Building Societies Association

BSA Responds To FSA's Proposals On Responsible Lending

The FSA has published further proposals on reforming the mortgage market.

Commenting on the FSA's consultation paper on responsible lending, Paul Broadhead, Head of Mortgage Policy at the BSA, said: "Assessing affordability and a customer's ability to meet regular mortgage payments have always been central to building societies' lending decisions.

"There is a risk that the FSA's proposals will prevent some credit-worthy customers getting a mortgage and create mortgage prisoners. To ensure borrowers are not adversely affected, it will be important that when the rules are implemented they provide clarity for lenders and are enforced consistently across the market."

The consultation also sets out the FSA's current thinking on interest only mortgages. Paul Broadhead added: "Interest only mortgages are not inherently bad or high risk. However, it is important that borrowers with interest only mortgages understand the importance of having a plan in place to repay their mortgage at the end of its term. The FSA needs to proceed with caution so as not to restrict the use of interest only as a way of helping borrowers overcome repayment difficulties.

Broadhead also called for the FSA to ensure there is a greater balance between responsible lending and responsible borrowing, saying: "Borrowers must be empowered to take ownership of their choices and decisions. Well informed decisions are more likely to deliver consumer benefit. Placing all the responsibility and burden on lenders only weakens the position of consumers in the long term and should be avoided."

The BSA remains concerned that the FSA is conducting the Mortgage Market Review against a backdrop of significant prudential and supervisory change. Broadhead calls for the FSA to think carefully about how it proceeds, adding: "Decisions and implementation should not be rushed. We have seen several changes at a prudential and supervisory level, and the impact of these should be fully assessed before conduct of business rules are changed. This will enable the FSA to make targeted changes where consumer detriment persists."

The Committee of European Banking Supervisors

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Exposure Draft ED/2010/4 Fair Value Option For Financial Liabilities

The CEBS welcomes the opportunity to comment on the IASB's Exposure Draft on the Fair Value Option for Financial Liabilities (ED/2010/4). Banking supervisory authorities and central banks have a strong interest in promoting sound and high quality accounting and disclosure standards for the banking and financial industry, as well as transparent and comparable financial statements that would strengthen market discipline.

CEBS welcomes the efforts of the IASB to improve financial reporting in the area of financial instruments, and in particular the IASB's careful analysis of the phenomenon of 'own credit risk' (OCR).

(For further information go to: http://www.c-ebs.org/News--Communications/Latest-news/CEBS-has-commented-on-the-IASB-s-Exposure-Draf-%283%29.aspx.)

CEBS Has Commented On The IASB's Reporting Entity ED

CEBS has submitted its comments on the IASB's Exposure Draft ED/2010/2 Conceptual Framework for Financial Reporting - The Reporting Entity.

(For further information go to: http://www.c-ebs.org/News--Communications/Latest-news/CEBS-has-commented-on-the-IASB-s-Exposure-Draf-%282%29.aspx.)

CEBS Consultation – Draft Guidelines On Revised Article 3 Of Directive 2006/48/EC

The CEBS has published its consultation paper (CP41) on its draft guidelines on revised Article 3 of the Directive 2006/48/EC (hereafter "Article 3"). The consultation is open to all interested parties, including supervised institutions and other market participants. Currently, Article 3 allows Member States to provide for special prudential regimes for credit institutions which have been permanently affiliated to a central body since 15 December 1977, provided that those regimes were introduced into national law by 15 December 1979. Those time limits prevent Member States, especially those which acceded to the European Union since 1980, from introducing or maintaining such special prudential regimes for similarly affiliated credit institutions which were set up on their territories.

In order to ensure equal conditions for competition between credit institutions in Member States, Article 3 has been revised and the time limits removed. This means that from 31 December 2010 – the application date of the revised article – all Member States could provide for the special prudential regime, set out in Article 3, for all existing or future affiliated credit institutions that meet the conditions defined in that Article. This consultation paper sets out CEBS's draft guidelines on the amended Article 3 as requested in CRD II. The main objective of the draft guidelines is to enhance the convergence of the supervisory practices on the application of Article 3 across Member States. To achieve this objective, the draft guidelines provide clarity on the interpretation and guidance on the application of several aspects of Article 3.

CEBS submits its initial views for a public consultation which runs until 27 August 2010. CEBS welcomes market participants' views on the proposals set out in this paper; in particular, on whether its proposals will be sufficient to ensure the convergence of supervisory practices in this area. Comments received will be published on CEBS's website unless respondents request otherwise. Please send your comments to the following email address: cp41@c-ebs.org.

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The Committee of European Securities Regulators

CESR Announces Next Steps On European Access To Financial Information Disclosed By Listed Companies

CESR has announced a series of proposed measures for developing pan-European access to financial information disclosed by listed entities. The purpose of the various measures is to harmonise and enhance pan-European search facilities for financial information and to investigate the possible introduction of XBRL reporting.

As such, the first measure consists of a consultation paper on the development of pan-European access to financial information published by listed entities (CESR/10-719c). The consultation paper introduces CESR's proposals for improving the search functions and interconnection between national storage facilities for financial information. Two options are presented in the consultation paper. The first consists of organising national information depositories that would be accessible through one European search engine while the second option would centralise all data in a European central database. The responses to the consultation paper will provide CESR with feedback for a report to be submitted to the European Commission in Q4 2010. Links to existing national storage mechanisms (called OAMs) are now available on CESR's website under corporate reporting, either by share (through the MiFID database or via a list of links to OAMs themselves).

The second measure, builds on the call for evidence on *The Use of a Standard Reporting Format for Financial Reporting of Issuers Having Securities Traded on Regulated Markets* published in October 2009 (CESR 09-859). CESR announces its decision to move forward with an investigation of the possible use of eXtensible Business Reporting Language (XBRL) for the financial reporting of listed issuers.

In particular, CESR will conduct a cost-benefit analysis on the use of XBRL. The analysis will consider a scenario under which there is a 5 year transitional period to introduce a mandatory requirement for issuers preparing consolidated financial statements using IFRS to file XBRL, based primary financial statements with the national Officially Appointed Mechanisms for central storage of regulated information (OAMs). The transitional period would also allow for voluntary implementation commencing 2 years prior to the requirement itself.

Whether CESR will ultimately recommend the introduction of XBRL reporting depends, among other things, on a detailed analysis identifying the needs of users of financial information, the impact on reporting entities, the quality of the XBRL Taxonomy as developed by the IFRS Foundation and possible interactions with other regulatory bodies and requirements. CESR anticipates issuing a consultation paper on this issue in 2011.

CESR Proposes Changes To MiFID To Improve Securities Markets' Functioning, Transparency And Investor Protection

CESR has published the first set of technical advice to the European Commission (Commission) in the context of reviewing MiFID, the Markets in Financial Instruments Directive, which entered into force in November 2007. This covers CESR's advice on equity markets (Ref. CESR/10-802), non-equity markets transparency (Ref. CESR/10-799), transaction reporting (Ref. CESR/10-808) and investor protection and intermediaries (Ref. CESR/10-859) as well as part of the responses (Ref. CESR/10-860) to the request for additional information in relation to the review of MiFID that the Commission presented to CESR in March 2010.

The advice that CESR puts forward is both extensive and highly significant, tackling the key issues that CESR and market participants have identified as needing action. They aim at improving pre- and post-trade transparency and the orderly functioning of the markets, strengthening investor protection and ensuring securities regulators are equipped with tools which enable them to effectively monitor trading. CESR's recommendations take into account market developments since MiFID was originally drafted. Importantly, if taken forward by the Commission, they would impact many elements of securities market regulation and constitute a major change in the EU regulatory landscape.The development of the advice has benefited from a number of public consultations, open hearings and other types of exchange of views in a range of meetings and workshops organised with market participants as well as with representatives of retail investors. These contacts have been pivotal in shaping CESR's advice.

Eddy Wymeersch, Chair of CESR and Chair of the Supervisory Board of the Belgian Commission Bancaire, Financière et des Assurances (CBFA), stated: "The MiFID Directive is a cornerstone in the regulation of Europe's financial markets; since its entry into force in November 2007, Europe's single market has developed significantly. This very timely review of MiFID now provides an important opportunity to review the availability of pre- and post trade data in equity markets, which has become more complex with the development of multiple trading venues. It also enables us to expand transparency to non-equity markets, which the financial crisis highlighted as being of critical importance. The introduction of minimum harmonised rules on tape recording and the obligatory collection of client IDs when orders are transmitted will also greatly strengthen the tools supervisors have at their disposal to investigate misselling and market abuse. The creation of a consolidated tape however, remains an area where it will be key to see concrete steps being taken in the very short-term as we remain convinced of its necessity. The opportunity to review the MiFID at this juncture has also provided an important step forward towards convergence amongst supervisory practices and brings a single rulebook a step closer, which will be of benefit both to market participants and retail investors alike, strengthening certainty and greater confidence for all."

The technical advice that CESR has published is four-fold and includes policy proposals on equity markets (I.), non-equity markets transparency (II.), transaction reporting (III.) and investor protection and intermediaries (IV.). CESR also provides its responses to some of the questions presented by the Commission in its request for additional information (V.). In addition, the next steps in CESR's work in relation to the MiFID review are highlighted in section VI.

I. Technical advice on equity markets

The technical advice on equity markets (Ref. CESR/10-802) follows the consultation paper published in April 2010 (Ref. CESR/10-394), to which 76 responses were received. The advice also takes into account the information received in response to CESR's Call for Evidence on micro-structural issues that was also published in April (Ref. CESR/10-142). The advice includes data on dark trading taking place on regulated markets (RMs), Multilateral Trading Facilities (MTFs) and investment firms' crossing systems for 2008, 2009 and Q1/2010. The main recommendations put forward are:

* Improving the pre-trade transparency regime for RMs/MTFs
* Reviewing the definition of and obligations for systematic internalisers
* Enhancing the quality of post-trade transparency information
* Extending the transparency obligations to equity-like instruments
* Improving the regulatory framework for consolidation and addressing cost of market data

* Establishing a new regulatory regime for broker crossing systems
* Addressing certain options and discretions of MiFID
* Tackling market micro-structural issues

CESR's technical advice to the Commission on equity markets has been prepared by the Secondary Markets Standing Committee chaired by Sally Dewar, Managing Director (Risk Business Unit) of the UK FSA, who stated: "CESR proposes important changes to the European regulatory landscape and future ESMA powers aimed at keeping pace with new technological advances, increasingly fragmented equity markets and shortcomings in the quality and consolidation of post-trade information in the European equity markets. The efficient development of a European consolidated tape for shares on the basis of clear rules and a viable economic model involving the industry is amongst one of a number of key proposals which should deliver major transparency benefits."

II. Technical advice on non-equity markets transparency

The technical advice on non-equity markets transparency (Ref. CESR/10-799) follows the consultation paper published in April 2010 (Ref. CESR/10-510), to which 48 responses were received. In its advice, CESR makes detailed proposals on the calibration of the MiFID post-trade transparency regime for non-equity financial instruments following its earlier report on transparency of corporate bond, structured finance product and credit derivatives markets of July 2009 (Ref. CESR/09-348), in which CESR recommended a mandatory post-trade transparency regime for these financial instruments.

The current advice goes beyond CESR's previous report in several aspects. Firstly, it includes within its scope sovereign Credit Default Swaps (CDSs) and 'public bonds'. Since other derivatives than CDS were not analysed in the past, CESR also explored the possibility of a post-trade transparency regime for the most significant subset of these financial instruments: interest rate derivatives, equity derivatives, foreign exchange (FOREX) derivatives and commodity derivatives. At the request of the Commission, CESR also reconsidered whether there is a need for pre-trade transparency for corporate bonds, Asset Backed Securities (ABS), Collateralised Debt Obligations (CDOs), CDS and the other derivatives mentioned above.

The main recommendations include:

* Re-defining the scope of a post-trade transparency regime for bonds
* Defining a phased approach for the introduction of a post-trade transparency regime for structured finance products
* Extending the scope to clearing eligible sovereign CDS
* Enhancing post-trade transparency of derivatives markets
* Conducting a post-implementation review
* Introducing pre-trade transparency requirements for non-equity financial instruments traded on RMs and MTFs

CESR's technical advice to the Commission on non-equity markets transparency has been prepared by the Secondary Markets Standing Committee chaired by Sally Dewar, Managing Director (Risk Business Unit) of the UK FSA, who stated: "Through the introduction of mandatory pre and post-trade transparency requirements for bond, structured finance product and derivatives markets, CESR proposes a fundamental change in the functioning of these markets, for the benefit of both wholesale and retail investors. At the same time, the regimes have been carefully designed in order to avoid harming the liquidity of these markets, many of which are still recovering from the financial crisis."

III. Technical advice on transaction reporting

The technical advice on transaction reporting (Ref. CESR/10-808) follows the consultation paper published in April 2010 (Ref. CESR/10-292), to which 48 responses were received. The advice is published together with a feedback statement on the responses given (Ref. CESR/10-796).

The key purpose behind the suggested amendments is to improve market supervision and ensure greater market integrity. The main recommendations made in the technical advice are the following:

* Introducing a third trading capacity (client facilitation)
* Requiring the collection of and defining standards for client and counterparty identifiers
* Requiring the collection of client ID when orders are transmitted for execution
* Extending transaction reporting obligations to market members not authorised as investment firms

CESR's technical advice to the Commission on transaction reporting has been prepared by CESR-Pol chaired by Anastassios Gabrielides, Chairman of the Hellenic Capital Market Commission, who stated: "Investment firms have been calling for greater consistency in the interpretation and implementation of MiFID transaction reporting obligations, e.g. in relation to the harmonisation of the standards for the use of client and counterparty identifiers in transaction reporting. In order to respond to these requests and, at the same time, improve the regulators' ability to investigate market abuse, CESR proposes several changes to the transaction reporting requirements, the most significant being the requirement to always report the client ID."

IV. Technical advice on investor protection and intermediaries

The technical advice on investor protection and intermediaries (Ref. CESR/10-859) follows a consultation paper published in April 2010 (Ref. CESR/10-417), to which 80 responses were received. The main recommendations addressed in the technical advice propose the following changes:

* Introducing minimum harmonised mandatory recording requirements for telephone conversations and electronic communications
* Requiring trading venues to produce reports demonstrating execution quality
* Clarifying the distinction between MiFID complex and non-complex financial instruments
* Clarifying the scope of the definition of investment advice
* Harmonising the rules for the supervision of tied agents and related issues
* Addressing certain MiFID options and discretions

In addition to the above specific changes, CESR has identified further options and discretions that fall within the investor protection and intermediaries area and has consulted on amending, eliminating or turning them into rules with a view to having the same level of investor protection throughout all Member States. These include preventing competent authorities from delegating certain tasks related to authorisation and supervision, and requiring all Member States to allow competent authorities to have the power to require certain information from all investment firms with branches in their territories (for statistical and supervisory purposes).

CESR's technical advice to the Commission on investor protection and intermediaries issues has been prepared by the Investor Protection and Intermediaries Standing Committee chaired by Jean-Paul Servais, Chairman of the Belgian CBFA, who stated: "Since the implementation of MiFID, financial markets have undergone a number of changes and currently operate within the challenging environment that the global

financial crisis has created. It is all the more important, therefore, not only to facilitate pan-European competition, but also to harmonise the protection of investors throughout Europe as well as to take into account the lessons learned from the financial crisis. In this regard, the proposal made by CESR regarding a mandatory recording requirement for telephone conversations and electronic communications is an important step forward in terms of certainty, consumer protection, and surveillance of markets. It ensures that there is evidence to resolve disputes between investment firms and their clients, assists with supervisory work in relation to conduct of business rules and facilitates the prevention and detection of market abuse."

V. Commission's request for additional information in relation to the MiFID review

In March 2010, the Commission requested that CESR provide it with some additional information in relation to the MiFID review, in particular asking for information on CESR Members' supervisory experience. It is important to note that the responses published now are almost entirely the result of fact-finding exercises amongst supervisors and generally not part of the broader consultation process, due to the nature of the information requested and the fact that the request for this information was received in March.

The questions presented by the Commission related to secondary markets, transaction and position reporting as well as investor protection and intermediaries issues. As such, CESR is publishing its responses on almost all the questions that relate to the investor protection and intermediaries area of the MiFID review (Ref. CESR/10-860). Responses to the questions on the client categorisation regime (question 19) will be provided at a later stage (see next steps below) on the basis of the ongoing consultation on the topic (see the consultation paper on client categorisation Ref. CESR/10-831 that CESR published on 12 July 2010).

In addition to providing responses to the questions presented by the Commission, CESR makes in the introduction of the document (Ref. CESR/10-860) some additional important recommendations and statements on the basis of its Members' supervisory experience. Important general points developed are, inter alia, the disclosure measures for Over-the-Counter (OTC) derivatives and other complex or tailor-made products and the specific organisational requirements related to the launch of new services or products.

Regarding the answers to the Commission's questions, CESR highlights the following:

UCITS as complex/non-complex financial instruments

CESR believes that there is a case for considering structured UCITS, and UCITS which employ complex portfolio management techniques, to be complex financial instruments for the purposes of the MiFID appropriateness requirements. This is a concept that would need to be elaborated – possibly through ESMA binding technical standards.

Inducements

CESR refers the Commission to the conclusions of its report on good and poor practices concerning inducements (Ref. CESR/09-958) and refers, in particular, to the following supervisory experience: CESR Members wonder whether inducements should not be forbidden when portfolio management services are being provided. Regarding the transparency of inducements, CESR Members think that ex-post disclosure (of the actual amount of the inducement where this cannot be provided prior to the provision of the service) is good practice, as this enhances the quality of the information received by the client and, therefore strengthens investor protection.

Underwriting and 'placing'
Underwriting and 'placing', raise a number of important issues about the application of the framework of EU securities legislation. After the relevant legislation (e.g. Prospectus Directive) was brought in under the Financial Services Action Plan, these issues have not been specifically addressed. Previous CESR guidance on this has not been updated. CESR has noted to the Commission that it will look again at these issues in order to consider providing Level 3 guidance. There might also be a case for including some specific provisions in MiFID on underwriting and 'placing' in the same way that specific conflict of interest provisions are set out for investment research.

Appropriateness/suitability
CESR provides comments on its Members' experiences of the application of the existing rules. CESR Members generally consider that the current requirements are comprehensive, yet sufficiently flexible, to apply to different types of clients, instruments and advised services and therefore do not need modifying. However, CESR Members also suggest clarifying in the MiFID Implementing Directive that advice about hedging of risks is investment advice.

VI. Next steps
The documents published form the most extensive part of CESR's advice to the European Commission in the context of the review of MiFID. However, some work streams still remain to be finalised in the course of the next few months. In the first instance, CESR will publish the feedback statements on the consultations conducted on equity markets, non-equity markets transparency and investor protection and intermediaries. These feedback statements will be published by mid-September. Shortly afterwards, CESR will deliver to the Commission the technical advice to be given on the basis of three ongoing consultations:

* Client categorisation (Ref. CESR/10-831), which is open for consultation until 9 August 2010;
* standardisation and exchange trading of OTC derivatives (Ref. CESR/10-610), which is open for consultation until 16 August 2010; and
* transaction reporting on OTC Derivatives and extension of the scope of transaction reporting obligations (Ref. CESR/10-809), which is open for consultation until 16 August 2010.

The technical advice on binding post-trade transparency standards and obligations which CESR is currently working on with the industry will also be delivered to the Commission in the second set of submissions.

Finally, at the same time as providing the rest of its technical advice, CESR will also respond to questions 1-14 of the Commission request for additional information in relation to the review of MiFID.

For more detailed information view the release dated 2 August 2010 at: http://www.cesr-eu.org/index.php?page=contenu_md&type=press§ion=Press%20Releases

Report On Trends, Risks And Vulnerabilities In Financial Markets

CESR has published for the first time its report on trends risks, and vulnerabilities that are directly relevant to securities markets regulators (Ref. CESR/10-697). Previously, similar reports have been produced for the benefit of the Economic and Financial Committee (EFC) and the Financial Services Committee (FSC).

Over the last decades, financial markets have been transformed by the rapid development of new financial instruments, the rise of new categories of key market participants, and a supportive technological environment. More recently, fundamental areas of the financial sectors in Europe and elsewhere have experienced a severe crisis which is

not yet over. Going forward, CESR would like to contribute more to the understanding of these trends and risks and communicate its insights to the general public through regular reports. These reports will focus mainly on the short and medium term without losing sight, however, of long-term developments. The analysis will naturally focus on the activity in European financial markets, but also take into full account the international dimension of the various markets and instruments analysed.

Carlos Tavares, elected Chair of CESR and Chair of the Portuguese Comissão do Mercado de Valores Mobiliários (CMMV), Chair of the Committee for Economic and Market Analysis that prepared the report, stated: "Today's publication shows CESR's determination to contribute to the promotion of financial stability and the enhancement of consumer protection through regular reporting on trends and risks. CESR's Committee for Economic and Markets Analysis (CEMA) has been put in place to fulfil this task. Its activity covers the pro-active identification, the monitoring, and the assessment from a microprudential perspective of key developments and risks in financial markets. This includes a crossborder and cross-sector dimension, as well as a thorough focus on financial innovations and incentives related to market practices both at the wholesale and retail level. Our first report stresses several trends and risks which should be taken seriously not only by regulators, but also market participants and investors to be better prepared for the future."

At the current juncture, reporting on such risks, trends and vulnerabilities requires reference to the considerable uncertainties that are attached to the general economic and financial environment and their potential impact on markets. Therefore, this report covers developments in European securities markets both by considering broader trends and risks, and by looking into specific areas, such as activities in sovereign and corporate debt markets, securitisation in general, and the fund industry with a particular focus on the hedge fund sector and UCITS. It also considers in its analysis recent developments in mergers and acquisitions (M&A), and initial public offerings (IPOs).

Trends, risk and vulnerabilities identified

In its report, CESR has identified a range of key trends, risk and vulnerabilities. There are non-negligible risks of a new deterioration in securities markets ahead: in particular uncertainties about the worldwide economic recovery, including the risk of a double-dip recession in some European countries, and rising and broadening of European sovereign risk. On derivatives markets, in particular in the sovereign CDS segment, it is likely that markets will continue to "test" countries in difficulties in achieving the announced budget and debt goals. It is worth noting, however, that a sensible reduction in the perception of sovereign risk has been observed recently fuelled by the implementation of tough fiscal adjustment programmes in most European countries and the authorities' commitment to carry out and publish stress tests on the banking sector.

The financial crisis has triggered a process of financial dis-intermediation whereby banks play a diminished role in the financial system and direct finance becomes more important. Such a shift has implications in terms of the risk distribution within the financial system, including systemic risk.

The medium term

Going forward, it remains to be seen to what extent market and regulatory developments will be able to contribute both to developing the positive risk sharing functions and curtailing the possible negative effects of informational asymmetries of financial innovations.

Aside from high asset valuation, two signs which have been identified in the past as conducive to a bubble – rapid growth in private-sector credit and significant investment

flows into particular asset classes – are not currently present. If a low interest rate environment were to persist, a close monitoring of the situation particularly in emerging and commodities markets on the one hand and, within Europe, some local markets (e.g. real estate) on the other, might well be needed.

The evolution of the boundaries between wholesale markets and retail markets needs to be monitored with due attention because of an increasing tendency to shift risks to (possibly unaware) retail investors through new complex financial products.

The findings of this report will inform Europe's securities supervisors in their day-to-day analysis of supervisory priorities and will inform the emphasis and importance of factors as they are weighed in the regulatory development policy which seeks to take steps to protect investors and preserve well functioning markets.

Final Guidelines On Risk Measurement And The Calculation Of Global Exposure And Counterparty Risk For UCITS

CESR has published guidelines (Ref. CESR/10-788) on risk measurement and the calculation of global exposure and counterparty risk for Undertakings for Collective Investments in Transferable Securities (UCITS) and a feedback statement (Ref. CESR/10-798).

The key purpose of CESR's guidelines is to provide both regulators and companies managing UCITS with detailed methodologies to calculate the global exposure and counterparty risk for UCITS, whilst at the same time, fostering a level-playing-field in the area of risk measurement among EU Member States. CESR's guidelines are to accompany the Level 2 implementing measures of the UCITS Directive. This Directive will become applicable from 1 July 2011.

The guidelines set out detailed methodologies that have to be followed by UCITS when they use either the commitment or the more advanced Value-at-Risk (VaR) approach for calculating theirglobal exposure (the VaR approaches are designed for more complex investment strategies). For UCITS using the VaR approach, CESR guidelines also provide additional safeguards which these UCITS should put in place when calculating the global exposure (stress testing and back testing obligations of the VaR model, validation of the model etc.).

In these guidelines, CESR also defines a set of high level principles relating to assets that may be used as collateral and cover rules for transactions in financial derivative instruments.

Guidelines provide calculation methodologies for different investment strategies
CESR wishes to emphasise that the calculation of the global exposure represents only one element of the UCITS overall risk management process. It remains the responsibility of the UCITS to select an appropriate methodology to calculate it.

Concerning the calculation of the global exposure, CESR sets out detailed methodologies to be followed by UCITS when they use the commitment (see paragraph 2, page 7 of the guidelines) or the VaR approaches (see paragraph 3, page 22 of the guidelines). This means that the risk management process of a UCITS should comprise the right procedures which enable the management company to assess the UCITS' exposure to all material risks including market risks, liquidity risks, counterparty risks and operational risks. UCITS must assess their investment strategy and portfolio composition on an ongoing basis to establish where an intra-day calculation may be required. This may be necessary, for example, on a particular day due to increased volatility or might be required more frequently.

Further work on structured UCITS
CESR received 48 responses to a public consultation (Ref. CESR/10-108) held on

the draft guidelines.

The feedback of the consultation was positive with stakeholders largely supporting the draft guidelines proposed by CESR. In the consultation paper, CESR sought stakeholders' views on the most appropriate approach for an optional 'sensitivity'-based regime in relation to interest rate strategies for the calculation of the global exposure. In particular, CESR consulted on two possible methods. The final version of the guidelines retains the option which was favoured by the respondents (Option 2). However, the Committee felt it appropriate to include this option into the standard regime of netting and hedging rules (Box 7 of the Guidelines) under a new section labelled "duration-netting rules".

In the consultation paper (Ref CESR/10-108) (pages 50 and 51), the Committee consulted on its initial views on specific guidelines for structured UCITS for the calculation of the global exposure.

Given market participants' feedback on this issue, CESR will carry out further work to assess whether it might be appropriate for certain types of structured UCITS to use other methodologies than those published today to calculate their global exposure. This work will be finalised in time to give stakeholders the possibility to prepare themselves to apply other methodologies for certain types of structured UCITS, when the UCITS IV Directive comes into force, if the outcome of the work is positive.

The Guidelines can be viewed via a link at: http://www.cesr-eu.org/index.php?page=home_details&id=498

Chair And Vice Chair Of CESR Elected

CESR Members have elected Carlos Tavares, Chairman of the Comissão do Mercado de Valores Mobiliários at the CMVM, as Chair of CESR and Jean Guill, Director General of the Commission de surveillance du secteur financier (CSSF) as Vice Chair of CESR.

The election becomes effective as of 1 August and will ensure a smooth transition for CESR as it prepares to become the European Securities and Markets Authority (ESMA), an EU authority, with increased powers.

Under the CESR Charter, the positions are held for two years, however, it is likely that the creation of ESMA, which is currently anticipated to take effect in January 2011, may result in a shorter term being served on this occasion.

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Council of Mortgage Lenders

CML Responds To FSA Responsible Lending Proposals

In response to the FSA's consultation paper on responsible lending, the Council of Mortgage Lenders (CML) emphasises that the mortgage industry recognises the inevitability of regulatory change – but points out that there may also be unwelcome side effects for consumers from this process.

The FSA proposes to require borrowers' incomes to be verified in all cases – meaning not only that "self-cert" mortgages will no longer exist, but also that lenders will no longer be able to undertake "fast track" mortgage processing. Under the "fast track" process, lenders assess the application and, on low risk cases, may then undertake a lower level of documentary scrutiny than on higher risk cases, although the borrower should be unaware of this. "Fast track" loans, according to CML analysis and the FSA's own, have actually experienced lower levels of default than income-verified loans in the prime market, but are no longer expected to be allowed. This will inevitably mean higher administrative costs in processing loan applications.

In terms of affordability, the FSA plans to require mortgage affordability to be assessed on a capital repayment basis, even where the mortgage is interest-only. Most lenders already calculate affordability on this basis, so this is unlikely to be a concern in its own right. However, the position of borrowers who wish to transfer to interest-only to manage periods of financial difficulty needs careful consideration in terms of regulatory treatment and outcomes for consumers.

The FSA also propose a prescriptive approach to assessing the applicant's available income to support the mortgage application, after taking account of other expenditure. Again, lenders commonly use "affordability" models to do exactly this. Nevertheless, it is important to recognise that the FSA's proposed conservative approach to assessing available income may indeed make borrowing "safer", but may also make it more difficult for households to get a mortgage. This is particularly relevant given that most cases of mortgage arrears and repossession cannot be attributed to failures in the affordability assessment of the original lending decision. Most cases of financial difficulty occur because of changes in the borrower's circumstance, as evidence repeatedly shows. For example, joint research by the three main advice agencies in December 2009 suggested that over-commitment was a feature in only 10% of arrears cases. Job loss, by contrast, was cited as a factor in 40% of cases.

CML director general Michael Coogan said: "There will always be a regulatory trade-off between protecting consumers from over-borrowing, and increasing the barriers to home-ownership. The mortgage market for the time being has already corrected to a degree that the main consumer concern right now is about access to finance, not about risky lending.The risk is that the gain will not match the pain in the short term. The industry and consumers will feel the costs of imposing new regulatory requirements now, in a market where they are not needed, but the potential consumer benefits will only be felt at some unspecified time in the future. We look forward to working with the FSA to ensure that a pragmatic approach to implementation can be adopted as far as possible, to reduce the negative side-effects that may arise from well-intentioned regulation. There is also a need to manage the regulatory burden that may emerge if the UK proceeds with changes just at the time that the European Commission is also due to publish proposals on the same aspects of mortgage regulation."

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European Banks Call For Caution In Light Of Incomplete Reform Picture

The European Banking Federation (EBF) acknowledges the progress achieved by the Group of Governors and Heads of Supervision of the Basel Committee at their meeting of 26 July 2010 in reaching broad agreement on some elements of the new capital and liquidity rules. It however stresses that whilst new rules on the quantity and quality of capital and reform of liquidity regime of banks will be a stepping stone in the regulatory reform to make the financial system more robust and stable, they must not prevent European banks from playing their part in promoting economic recovery.

The Secretary General of the EBF, Guido Ravoet, made clear that "The supervisory community has clearly heard the concerns of the banking industry and other economic leaders. However some decisions on key elements of the Basel package still have to be taken and others are cause for concern. For instance, we fear that there may not be enough flexibility to accommodate the business models that prevail in Europe and that have proved resilient."

At this stage, the Federation remains unable to assess the various elements of the broad agreement reached by the Basel Committee's Group of Governors and Heads of Supervision, as the package is not yet complete:

* crucial components, such as the actual definition and level of capital that will need to be held under the new rules have not been determined;
* the economic impact assessment of the new rules has not been released;
* it is not clear to what extent the level playing field has been preserved, notably regarding the decisions made on the definition of capital.

The EBF welcomes the treatment of minority interests in the banking subsidiaries of a group, but this treatment should also be extended to the minority interests in the insurance subsidiaries of a group. The Federation notes an improved approach to deferred tax assets, but remains concerned over the thresholds proposed and their impact on tier 1 capital considering the different tax laws in force in EU Member States. The extension of the liquidity pool's range of eligible assets is also going in the right direction, but clearly more work needs to be done to accommodate covered bonds, which are an important source of housing finance in Europe. Similarly, the review of the net stable funding ratio, which, as it was previously proposed could have prevented banks undertaking their important role of maturity transformation should be supported. European banks however remain highly concerned with the maintenance of the two buffers – in addition to the tier 1 capital requirements, the leverage ratio and the still strict proposals on deductions.

The non-risk based instrument of a leverage ratio is still very much a central component of the package. The positive side is that banks have received more clarity on the ratio, with a reasonably long phase-in period, but it should remain a supplementary measure for discussion between a bank and its supervisor as part of the supervisory review process.

The full impact of the new proposals cannot be gauged until decisions on the phasing-in and calibration of the proposals have been made and the EBF encourages this to be done quickly and in as transparent a way as possible.

Ravoet added: “There is a range of other measures under consideration alongside these capital and liquidity proposals, such as bank taxes and levies, the impact of which must be looked at holistically to ensure they do not impede our industry’s capacity to sustain lending and economic growth. It is important now that final agreement is reached swiftly so that these new proposals can be implemented in a coordinated way around the world in order to further reinforce the resilience of the global banking system.”

Towards a European Retail financial Services Market - An EBF Report

European banks aim to ensure a competitive post-crisis retail banking market. To that effect, the European Banking Federation (EBF) publishes a report outlining its strategic views on the creation of a European retail financial services market.

The report aims to discuss the impact of current initiatives on further integration in a post-crisis environment.

“We firmly believe in traditional banking values.” said Guido Ravoet, Secretary General of the EBF, “It is indeed necessary to focus primarily on priorities that continue to stabilise the markets and restore confidence in the short term, and to do so, we must concentrate on a limited number of well targeted initiatives. But at the same time, we are still convinced that the long term goal remains the creation of a real single market for retail financial services to the benefit of banks and consumers alike.”

“For us”, he continued, “this report is a sound basis for dialogue with policy-makers as well as consumer organisations, with whom we are very eager to discuss the future of the European retail market. This report gives a good overview of the direction taken by the authorities in their current review, and presents the Federation’s policy in the relevant areas of retail banking.”

The report can be found on : http://www.ebf-fbe.eu .

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ECB Reviews Risk Control Measures In Its Collateral Framework

The Governing Council of the European Central Bank (ECB) has reviewed the risk control measures in the framework for assets eligible for use as collateral in Eurosystem market operations. The resulting changes stem from the biennial review of the Eurosystem risk control measures and the Governing Council's decision of 8 April 2010 to introduce graduated valuation haircuts for lower-rated assets.

The new schedule duly graduates haircuts according to differences in maturities, liquidity categories and the credit quality of the assets concerned, based on an updated assessment of risk characteristics of eligible assets and the actual use of eligible assets by counterparties. The new haircuts will not imply an undue decrease in the collateral available to counterparties.

Moreover, the definition of liquidity categories for marketable assets and the application of additional valuation mark-downs for theoretically valued assets have been fine-tuned following the review. In particular, all non-Jumbo covered bonds, including structured covered bonds and multi-issuer covered bonds, together with traditional (UCITS-compliant) covered bonds, will be classified in liquidity category III. The additional valuation mark-down of 5% currently applied to theoretically valued asset-backed securities will be extended to theoretically valued bank bonds (including uncovered as well as covered bank bonds, namely Jumbos, traditional and structured covered bonds and multi-issuer covered bonds).

The new haircut schedule, which will enter into force on 1 January 2011, is annexed to the press release at: http://www.ecb.int/press/pr/date/2010/html/pr100728_1.en.html. It contains the valuation haircuts applied to eligible marketable assets. A separate scheme will apply to inverse floating rate instruments and is also annexed to this press release, together with a new haircut schedule for non-marketable assets.

The Governing Council recalls that, if required, the Eurosystem has the possibility to limit or exclude the use of certain assets as collateral in its credit operations, also at the level of individual counterparties.

Publication Of The Results Of The EU-Wide Stress-Testing Exercise

The Committee of European Banking Supervisors (CEBS), the European Central Bank (ECB) and the European Commission welcome the publication of the results of the EU-wide stress-testing exercise, which was prepared and conducted by the CEBS and national supervisory authorities, in close cooperation with the ECB.

We support, in particular, the transparency of this exercise, given the specific market circumstances under which banks currently operate. We therefore welcome the publication of banks' individual results, particularly their respective capital positions and loss estimates under an adverse scenario, as well as detailed information on banks' exposures to EU/EEA central and local government debt. Such disclosures ensure transparency regarding conditions in the EU banking sector.

The adverse scenarios used in the stress test are designed as "what-if" scenarios reflecting severe assumptions which are therefore not very likely to materialise in practice. Accordingly, the results of the test confirm the overall resilience of the EU banking system to negative macroeconomic and financial shocks, and are an important

step forward in restoring market confidence.

Where the results of the exercise indicate that individual banks require additional capital, these banks should take the necessary steps to reinforce their capital positions through private-sector means and by resorting, if necessary, to facilities set up by Member State governments, in full compliance with EU state-aid rules.

More information can be obtained on the CEBS website: http://www.c-ebs.org.

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Statement By Commissioner Michel Barnier On The Approval By The U.S. Senate Of The Financial Reform Bill

The U.S. has adopted very important reforms to strengthen the international financial system. I welcome this important step which will contribute to making the American and international financial systems stronger.

The U.S. are making progress in the implementation of the G20 commitments, and the U.S. bill will be completed by numerous measures in the coming years in order to be completely effective.

Europe is making equally good progress in the implementation of the G20 roadmap. It is essential that the G20 commitments are translated into practice at the same time at international level.

In Europe, a major reform of prudential and remuneration rules for the banking sector has just been adopted. Key proposals have recently been made by the Commission in order to better protect depositors and investors, as well as to better supervise credit rating agencies. I further hope that, in September, Member States and the European Parliament will conclude the on-going negotiations on supervision and alternative investment fund managers (AIFM). Finally, I would like to recall the on-going work concerning resolution funds as well as the forthcoming proposals on derivatives and short selling, which will be put forward in September.

There are differences between the American approach and the one we are following in Europe. This is normal. The two systems – financial and institutional – are not the same. However, we co-operate closely with the U.S. authorities, in particular to avoid any distortion of competition at international level.

The Commission reaffirms its intention to achieve the reform of the European and international financial systems in order to strengthen stability, to re-establish trust among our citizens and to pave the way towards sustainable growth.

Commission Proposes Package To Boost Consumer Protection And Confidence In Financial Services

As part of its work creating a safer and sounder financial system, preventing a future crisis and restoring consumer confidence, the European Commission has proposed changes to existing European rules to further improve protection for bank account holders and retail investors. Furthermore, the Commission has launched a public consultation on options to improve protection for insurance policy holders, including the possibility of setting up Insurance Guarantee Schemes in all Member States. For bank account holders, the measures adopted mean that in case their bank failed, they would receive their money back faster (within 7 days), increased coverage (up to €100,000) and better information on how and when they are protected. For investors who use investment services, the Commission proposes faster compensation if an investment firm fails to return the investor's assets due to fraud, administrative malpractice or operational errors, while the level of compensation is to go up from €20,000 to €50,000. Investors will also receive better information on when the compensation scheme would apply and get better protection against fraudulent misappropriations where their assets are held by a third party – such as in the recent Madoff affair. The proposals, fully in line with the EU's commitments under the G20, are now passed to the European Parliament and the Council of Ministers for consideration.

Protecting savings

The key elements of the proposal are as follows:

* *Better Coverage*: the upgrade to €100,000 by the end of this year is now confirmed. This means that 95% of all bank account holders in the EU will get all their savings back if their bank fails. Coverage now includes small, medium and large companies as well as all currencies. Excluded are all deposits of financial institutions and public authorities, structured investment products and debt certificates.

* *Faster payouts*: bank account holders will be reimbursed within seven days. This will be a major improvement as today many account holders wait weeks, even months, before getting their money back. In order to facilitate such a short payout, managers of Deposit Guarantee Schemes will have to be informed early about problems at banks by supervisory authorities. Banks will have to specify in their books whether deposits are protected or not.

* *Less red tape*: for example, if you live in Portugal and have your account at a failing bank whose headquarters are based in Sweden, the Portuguese scheme would repay you on its own initiative and act as your contact point. The Swedish scheme would then reimburse the Portuguese scheme. This would be a strong improvement over the current situation, where all correspondence has to be done via the scheme of the country where the bank's headquarters are located. The new approach will mean less bureaucracy and faster payouts.

* *Better information*: bank account holders will be better informed on the coverage and functioning of their scheme by a new easy to understand standard template and on their account statements.

* *Long-term and responsible financing*: concerns have been expressed that existing Deposit Guarantee Schemes are not well funded. These proposals will ensure that they are now more soundly financed following a four-step approach. First, solid ex-ante financing provides for a solid reserve. Second, if necessary, this can be supplemented by additional ex-post contributions. Third, if this is still insufficient, schemes can borrow a limited amount from other schemes ("mutual borrowing"). Fourth, as the last resort, other funding arrangements would have to be made as a contingency. Contributions will, as is currently the case, be borne by banks. However, they will be calculated in a fairer way since they will be adjusted to the risks posed by individual banks.

Not only will Europeans have better protection for their savings, but they can now also choose the best savings product in any EU country without worrying about differences in protection. Banks will benefit from the proposal since they could offer competitive products throughout the EU without being hampered by such differences. Moreover, taxpayers benefit from a better financing of schemes – rendering state intervention much less likely.

Most improvements could already come in effect by 2012 and 2013 and would apply in all EU Member States as well as in Norway, Iceland and Liechtenstein, once incorporated in the European Economic Area Agreement.

See also MEMO/10/318

Protecting investments

Since 1997, the Investor Compensation Scheme Directive (97/9/EC) has protected

investors who use investment services in Europe by providing compensation in cases where an investment firm is unable to return assets belonging to an investor. This might occur for example where there is fraud or negligence at a firm or where there are errors or problems in the firm's systems. It is not a protection against investment risks at such. There are now 39 investor compensation schemes in place in the EU's 27 Member States.

In recent years, the Commission has received numerous complaints about the Directive's application in some Member States. These complaints have concerned issues such as schemes having insufficient funding to pay out claims or lengthy delays in paying out claims.

This proposal is intended to ensure that the rules on investor protection are more efficient, that there is a level playing field concerning the type of financial instruments that are protected and that there is appropriate funding and the necessary arrangements to make sure that investors are compensated.

The key elements of the proposal are as follows:

* *Better coverage*: the current minimum level of compensation for investors is €20,000. Under the Commission's proposal, this will be increased to €50,000 per investor.

* *Faster payouts*: under the current legislation, it can sometimes take up to several years for investors to receive any compensation. This is to change under the Commission's proposal, where investors will receive compensation at the latest 9 months after the investment firm's failure. Such a timeframe is however necessary in order to allow competent authorities to investigate the case and determine the positions of individual investors.

* *Improved information*: investors are to receive clearer and more extensive information about the extent to which their assets are covered. For example: investment risk – an investment losing value due to a declining stock market or bankruptcy of an issuer – is not covered under the Directive.

* *Long-term and responsible financing*: since 1997, there have been a number of cases in Member States where schemes have had inadequate funding to compensate lost assets of investors. Under the Commission's proposal, a minimum target fund level will be introduced which needs to be fully pre-funded. If necessary, schemes can borrow a limited amount from other schemes and other funding arrangements as a last resort ("mutual borrowing"). Contributions are to be borne by investment firms.

* *Wider protection*: currently, investors are not necessarily protected if the investment firm uses a third party custodian to hold the client's assets and the third party defaults without returning the invested assets. Similarly, unit holders in investment funds can suffer loss if there is a failure of a depositary or a sub-custodian of the fund. The Madoff investment fraud case in 2008 is a recent example. The Commission now proposes to also cover such situations.

Most improvements could already come into effect by end 2012 and would apply to all EU Member States as well as Norway, Iceland and Liechtenstein, once incorporated in the European Economic Area Agreement.

See also MEMO/10/319

Improving protection for insurance policy holders
Insurance Guarantee Schemes (IGS) provide last-resort protection to consumers when insurers are unable to fulfil their contract commitment, offering protection against the risk that claims will not be met if an insurance company is closed down. IGS can offer protection by paying compensation to consumers, or by securing the continuation of their insurance contract through, for example, facilitating the transfer of policies to a solvent insurer or the guarantee scheme itself. As opposed to the banking and securities sectors, there is no European legislation on guarantee schemes in the insurance sector today. Currently, 12 Member States operate one or more IGS which cover life and/or non-life insurance policies. They not only vary in terms of protection and eligibility, but also on when they are to intervene or how they are to be funded for example.

In the White Paper now adopted, the Commission sets out different options to ensure a fair and comprehensive level of consumer protection in the EU as well as to guard against the need for taxpayers to foot the bill in case an insurance company is to collapse. In particular, it proposes introducing a directive to ensure insurance guarantee schemes exist in all Member States and comply with a minimum set of requirements. The White Paper on Insurance Guarantee Schemes is up for consultation and all interested parties are invited to submit their comments and further input by 30 November 2010.

See also Memo/10/320

More information:

Deposit Guarantee Schemes:
http://ec.europa.eu/internal_market/bank/guarantee/index_en.htm

Investor Compensation Schemes:
http://ec.europa.eu/internal_market/securities/isd/investor_en.htm

Insurance Guarantee Schemes:
http://ec.europa.eu/internal_market/insurance/guarantee_en.htm .

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FRC Announces Project On Lessons From Credit Crisis And Formation Of Advisory Group

The Financial Reporting Council (FRC) has launched a project to examine the lessons to be learned from the credit crisis and other market developments as they impact corporate reporting, accounting and auditing of non-financial services companies. The FRC expects to publish a discussion document in the Autumn.

To assist the FRC in identifying and evaluating appropriate issues, it has established a senior business and accountancy profession advisory group. The new group will advise the FRC on issues such as narrative reporting and the role of the auditor. The Advisory Group comprises:-

* Mark Armour, Chief Financial Officer, Reed Elsevier PLC
* John Cridland, Deputy Director General, CBI
* Steve Maslin, Partner, Grant Thornton
* Ian Powell, Chairman and Senior Partner, PwC UK
* Keith Skeoch, Chief Executive, Standard Life Investments
* Lindsay Tomlinson, Managing Director, BlackRock

The group met for the first time on Monday 26 July.

Stephen Haddrill, Chief Executive of the FRC and Chair of the Advisory Group, said: “I am delighted that senior individuals from business and the accountancy profession have agreed to serve on this Advisory Group to help the FRC to identify key lessons from the financial crisis and the way markets are now developing.

“Our aim is to apply these lessons to the issues within the FRC’s remit and to consult on proposals for reform. It is time to get into the detail of the auditing, accounting and corporate reporting practices that need to be changed to enhance the relevance and value of information provided to the capital markets and the assurance given by audit.”

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FSA Confirms Measures To Reform PPI Market And Protect Consumers

The Financial Services Authority (FSA) has published a policy statement confirming its package of measures to protect consumers in the Payment Protection Insurance (PPI) market. The package will ensure customers are treated more fairly when complaining about PPI and better when buying the product; it includes:

* new handbook guidance to ensure complaints are handled properly, and redressed fairly where appropriate;

* an explanation of when and why firms should analyse their past complaints to identify if there are serious flaws in sales practices that may have affected complainants and even non-complainants; and

* an open letter setting out common sales failings to help firms identify bad practice.

Firms must implement the measures by 1st December 2010, with the time in between to prepare for implementation such as training staff to a higher level. The FSA will be monitoring firms closely to ensure the new standards are adhered to.

The policy statement follows consultation that saw significant levels of highly detailed feedback from PPI providers, sellers, trade groups and consumer bodies.

The measures follow up on the FSA's commitment to reform the market and build on the agreement the FSA secured from the industry in 2009 to stop selling single premium PPI on unsecured loans. The FSA has also taken action against 24 firms and individuals for PPI failings with fines totalling approximately £13 million.

FSA Consults On Changes To Its Remuneration Code

The FSA has announced plans to update its Remuneration Code to take on board remuneration rules required by the Capital Requirements Directive (CRD 3) and the Financial Services Act 2010 (FS Act). The FSA also reports on the implementation of the Code so far, lessons learned from last year's implementation and discusses progress made in achieving international alignment.

The FSA's current Code applies to the largest banks, building societies and broker dealers. However, CRD3 will bring over 2,500 firms within the scope of the Code. These include all banks and building societies, asset managers, hedge fund managers, UCITS investment firms as well as some firms that engage in corporate finance, venture capital, the provision of financial advice and stockbrokers.

The FSA does not intend the final rules to be super-equivalent to the CRD3 requirements unless required to be so by UK legislation.

The existing Code requires that firms apply 'remuneration policies, practices and procedures that are consistent with and promote effective risk management'. Although the Code is broadly consistent with CRD3 provisions and the FS Act, the FSA is required to make some changes to ensure full alignment. In particular, the Code will be strengthened in the following ways:

* *Scope of the Code* – as the scope of the Code is expanded, the FSA is committed

to applying a proportional approach to implementation and will ensure that 'institutions shall comply with the principles in a way and to the extent that is appropriate to their size, internal organisation and the nature, the scope and the complexity of their activities'.

* *Application* – the FSA is consulting on the group of employees to which the Code applies ('Code staff'). These will include senior management and anyone whose professional activities could have a material impact on a firm's risk profile. The consultation paper sets out examples of the key positions in firms that the FSA believes should be subject to the Code. The onus will be on firms to identify their Code staff in the first instance, but their lists will be subject to review and challenge by the FSA.

* *Deferral* – at least 40% of a bonus must be deferred over a period of at least three years for all 'code staff'. At least 60% must be deferred when the bonus is more than £500,000.

* *Proportion in shares* – at least 50% of any variable remuneration components must be made in shares, share-linked instruments or other equivalent non-cash instruments of the firm. These shares will need to be subject to a minimum retention policy.

* *Guarantees* – firms must not offer guaranteed bonuses of more than one year. Guarantees may only be given in exceptional circumstances to new hires for the first year of service.

* *Strengthening of capital base* – firms must ensure that their total variable remuneration does not limit the ability to strengthen their capital base. Total variable remuneration must be significantly reduced in circumstances where the firm produces a subdued or negative financial performance.

* *Voiding provisions* – a new rule will be introduced which defines instances where breaches of the code may render a contract void and/or require recovery of payments made.

* *Severance payments* – should reflect performance over time and failure must not be rewarded.

* *Pensions* – CRD3 states that enhanced discretionary pension benefits should be held for five years in the form of shares or share-like instruments.

Implementation of the Code so far

Whilst it will take time to assess the full impact of the Code in contributing to effective risk management, all firms within scope that have paid bonuses since 1 January 2010 have adhered to the FSA's Code.

Successful implementation has resulted in more demanding standards in a number of areas and has shifted the composition of remuneration structures to forms more consistent with effective risk management.

More generally, the FSA has seen stronger and more independent remuneration committees and greater recognition of the need to consider risk when setting remuneration policies and signing off bonus policies.

Next steps

The consultation period closes on 8 October 2010. The FSA intends to issue a policy

statement in November 2010 with rules effective from 1 January 2011.

The text of the CRD3 was agreed in early July, and its remuneration provisions will come into force on 1 January 2011. This is a tight timetable, and the FSA is urging all firms within its scope to start preparing for its introduction as soon as possible. The FSA has proposed some transitional provisions to give smaller firms some leeway in implementing certain provisions.

FSA Statement On The Publication Of CEBS Stress Tests

The FSA welcomes the publication of the results of the EU-wide stress test exercise conducted by the Committee of European Banking Supervisors (CEBS). The CEBS exercise shows that the UK banks are well placed to handle further periods of economic stress, as outlined in the macro economic parameters detailed by CEBS, should such stress develop.

The purpose of a stress test is to understand the extent to which banks are prepared, should the economic environment take a turn for the worse. It is not a prediction of what will happen or what banks' results will actually be and the CEBS stress test does not take into account actions a bank might take in response to deteriorating economic conditions. It would be misleading therefore to treat the results of the stress test as a forecast either by the FSA or the individual banks.

CEBS stress testing framework

The objective of the CEBS exercise is to undertake an assessment of the strength of EU banks in a consistent manner across institutions and countries. It focused on three different scenarios; a benchmark stress, a more adverse macro-economic stress and a country-wide stress.

The benchmark stress identifies movements in parameters such as GDP, unemployment and interest rates and charts a mild deviation away from the pathway which the economy is currently on: it then makes conservative assumptions about the loan losses which will result in this macro-economic scenario. This helps to set a benchmark (mildly stressed scenario) against which the more adverse stress is then applied. The adverse stress assumes a 3 percentage point deviation of GDP for the EU compared to the European Commission's forecasts over the two-year time horizon. The method of translating this scenario to loss rates is also conservative.

A further 'sovereign stress' was then applied. This tested the resilience of banks to an increase in the yields of government bonds issued by EU member states. It simulates, (i) the associated medium term uptick in household and corporate sector loan losses in the banking book, and (ii) immediate mark to market losses arising from trading book holdings of government bonds of each country. The actual exposures of each bank to central and local government across the EU have been published by each bank. Results identify the simulated Tier 1 ratios of European banks as well as specific simulations for profit and loss measures. The CEBS results are focused on Tier 1 ratios for comparability across the EU.

As expected the outcomes of the stresses demonstrate the preparedness and resilience of the UK banks under unlikely adverse economic scenarios. The FSA has published the high level results for the UK banks. This resilience is a result of the considerable work that has been undertaken to strengthen UK banks in recent years. The CEBS stress test is different but complementary to the FSA's stress testing regime.

FSA's stress testing regime

The UK banks are required to meet the FSA's interim capital regime introduced in November 2008. This requires them to be able to meet a severe stress over a forward looking period exceeding 4% Core Tier 1 at all times. The UK introduced a tougher

definition of Core Tier 1, including the deduction of intangibles such as goodwill, in 2008 so Core Tier 1 ratios cannot be compared across countries. This takes the UK definition in the direction of current proposals from the Basel Committee (4% is double the existing Basel minimum). Present Core Tier 1 ratios are well in excess of this level. The FSA's stress tests used in this regime are tailored to each individual bank and are embedded in the FSA's ongoing supervisory process on a rolling basis. The FSA published in February 2010 the macro-economic parameters to be used in stress tests conducted during 2010, and will in the future publish each year the updated macro-economic parameters.

Supplementary information regarding the assumptions in the CEBS exercise
The following additional information may be useful in understanding the assumptions and interpreting the CEBS results:

Static balance sheet – a key assumption of the CEBS exercise is that of a static balance sheet. This means that it takes the position of the balance sheet – primarily the size of a bank's loan book – at the 2009 level and assumes it will stay at that level for two years. This assumption limits growth in retail and commercial banking revenue in the benchmark and stress scenarios. There is no allowance for pre-agreed strategies, such as changing the business profile, nor does it take account of the types of actions banks might take in response to a macro economic shock such as reducing risk profiles and shrinking the balance sheet.

Consistent assumptions – CEBS provided benchmarks for the probabilities of default (PDs) and loss-given default (LGDs) which might occur in stress scenarios. These benchmarks increase the consistency of results, which is an important objective in a large multi-country exercise. But it inevitably means that some relevant specific features of individual bank exposures cannot be reflected in the way which is possible when in-depth individual bank stress-tests are conducted.

Separate assumptions were provided by CEBS for each of the EU member states and the USA; in addition, a single set of assumptions was used to model the scenario impact for the 'Rest of the World'. For some banks this is inevitably a major simplification.

Potential double counting – in order to achieve a conservative and consistent approach some losses may have been double counted. For example, the losses captured by the trading book stress in the adverse scenario may also materialise in reduced income from trading, which is factored into assumptions on earnings.

Interpreting the limitations – the limitations of the static book approach and other simplifying assumptions necessary in this pan EU exercise, mean that the results, whilst informative, are not forecasts and should only be understood as a guide to the resilience of the banks in adverse circumstances.

Tougher Prudential Standards For Credit Unions

The FSA has published its near final rules to strengthen the financial resilience of the credit union sector and reduce the number of credit union failures.

On average, around six credit unions are declared in default each year with customers compensated by the Financial Services Compensation Scheme. The new rules aim to improve the financial soundness of credit unions and therefore maintain consumer choice in the financial services sector. The rules will be contained in a new Credit Union sourcebook (CREDS), which will replace the existing sourcebook CRED.

The new rules will raise prudential standards and the main changes are as follows:

* New credit unions must have adequate initial capital, the amount of which will

be dependent on the nature, scale and complexity of their business. In most cases, smaller credit unions will need to have initial capital of at least £10,000 and larger credit unions at least £50,000;

* Smaller credit unions must have a capital-to-assets ratio of at least 3%; and

* All credit unions must hold liquid assets of at least 5% of total relevant liabilities but not below 10% per cent in two consecutive quarters. This is the current requirement for smaller credit unions but a slight increase for larger credit unions.

The capital-to-assets and liquidity requirements will be phased in, coming into full effect on 30 September 2013, which should give credit unions enough time to comply.

The publication of near final rules is timely as it will also help ensure that credit unions are prepared for new Government legislation, which is currently before Parliament and will allow credit unions to carry out a wider range of financial activities. Confirmation of the final CREDS rules will be published after the Government legislation is made, and CREDS will come into effect at the same time as the legislation.

The FSA will also reduce the submission period for annual financial returns from seven to six months so that more timely financial information is received from credit unions.

FSA Implements New Powers Granted By Financial Services Act 2010

The document includes new rules and guidance covering the following areas:

* Use of the power to impose financial penalties or public censure on those who breach short-selling rules;

* Disclosure of significant net short positions (these will go in a new part of the Handbook covering financial stability and market confidence and the current provisions on short selling in the Code of Market Conduct will be deleted);

* Use of the power to suspend firms or individuals by stopping them undertaking some or all of the activities which they are permitted to carry on for a period of time;

* Use of the power to impose financial penalties on individuals who have carried out controlled functions without the necessary approval from the FSA;

* Our policy on the use of the power to gather information in relation to financial stability from specified categories of both authorised and unauthorised persons to help identify potential threats to the UK financial market;

* Making alterations to the FEES manual to reflect amendments made by the Act in relation to the Financial Services Compensation Scheme's (FSCS) contribution to the costs associated with resolutions under the Banking Act 2009.

The final issue covered in this document covers further consultation on the proposal to allow the FSCS to recover management expenses from FSCS levy payers when it is acting for another scheme.

Moves To Make Sure All Borrowers With A New Mortgage Can Afford It

The FSA has outlined proposals to ensure all mortgages are carefully assessed to make sure borrowers can afford them.

Reflecting the FSA's enhanced consumer protection strategy and intensive day-to-day supervision, the proposed changes aim to ensure all lenders get back to the basics of

responsible lending and that problems are prevented before they can develop or get out of control.

Some of the key proposals include:

* Imposing affordability tests for all mortgages and making lenders ultimately responsible for assessing a consumer's ability to pay;

* Requiring verification of borrowers' income in every case to prevent over inflation of income and to prevent mortgage fraud;

* Extra protection for vulnerable customers with a credit-impaired history.

The tough new proposals, published in the consultation paper, form part of a major review by the FSA into the UK mortgage market and are based on detailed analysis of past lending decisions, looking at the causes of arrears and repossessions since 2005. The FSA found that:

* 46% of households either had no money left, or had a shortfall after mortgage payments and living costs were deducted from their income;

* Almost half of new mortgages between 2007 and the first quarter of 2010 were provided without a customer having to verify their income;

* The share of interest-only mortgages has been increasing. At the peak of the market, over 30% of all mortgages were interest-only;

* Many consumers with no repayment vehicle count on future house price rises or uncertain life events to repay their mortgage and some have no plan at all;

* Borrowers with a credit-impaired history are particularly vulnerable.

This report also includes the key findings from the FSA's review into arrears charges, which indicated significant variation in the level of arrears fees across the market. The mortgage rules require arrears charges to be based on a reasonable estimate of the cost of the additional administration required as a result of the customer being in arrears. The FSA is actively seeking views from consumer groups and industry and invites responses by 16 November 2010.

Building Society Merger Confirmed

The FSA has announced that it has confirmed the proposed transfer of the engagements of the Stroud & Swindon Building Society to the Coventry Building Society.

FSA Fines Royal Bank Of Scotland Group £5.6m For UK Sanctions Controls Failings

The FSA has fined members of the Royal Bank of Scotland Group (RBSG) £5.6m for failing to have adequate systems and controls in place to prevent breaches of UK financial sanctions.

UK firms are prohibited from providing financial services to persons on the HM Treasury sanctions list. The Money Laundering Regulations 2007 (the Regulations) require that firms maintain appropriate policies and procedures in order to prevent funds or financial services being made available to those on the sanctions list.

During 2007, RBSG processed the largest volume of foreign payments of any UK financial institution. However, between 15 December 2007 and 31 December 2008, RBS Plc, NatWest, Ulster Bank and Coutts and Co, which are all members of RBSG, failed to adequately screen both their customers, and the payments they made and received, against the sanctions list. This resulted in an unacceptable risk

that RBSG could have facilitated transactions involving sanctions targets, including terrorist financing. The FSA considers that RBSG's failings in relation to its screening procedures were particularly serious because of the risk they posed to the integrity of the UK financial services sector. This is the biggest fine imposed by the FSA to date in pursuit of its financial crime objective. It is also the first fine imposed by the FSA under the Regulations.

As RBSG agreed to settle at an early stage of the FSA investigation, it qualified for a 30% reduction in penalty. The FSA would have otherwise imposed a financial penalty of £8m.

Garrison Censured For Geared Traded Endowment Policies Advice Failings

The FSA has publicly censured The Garrison Finance Centre Limited (Garrison) for failing to communicate clearly the risks of complex investment products – geared traded endowment policies (GTEPs) – to their customers.

Garrison is in liquidation so the FSA has instructed the liquidator to write to the firm's GTEP customers informing them they may have received unsuitable advice and could be entitled to make a claim. The FSA has waived the £35,000 fine it would have imposed so that the money can be used to meet customer claims.

The FSA's investigation found a number of failings in relation to Garrison's advice and sales to customers. Garrison failed to:

* communicate adequately why a GTEP was suitable for a customer and the risks associated with it;

* demonstrate why its recommendations were suitable as it did not gather and/or document adequate information to support its recommendations; and

* show that customers' attitude to risk was commensurate with the GTEP's risk profile.

The FSA sees the failings as particularly serious because a number of customers re-mortgaged their homes to purchase a GTEP following advice from Garrison. Furthermore, of the files the FSA reviewed, only one customer was warned that further capital injections could be required to support the GTEP should it under-perform.

FSA Censures And Bans Three Directors From Acting As Senior Managers

The FSA has publicly censured and banned Stephen Coles, Luke Ryan and Michael Yamoah, the three directors of Simply Trading Group Limited (STG), from senior management positions for falling short of FSA standards. The FSA's investigation found that Coles, Ryan and Yamoah:

* relied too heavily on an external compliance consultant for advice on how to run their business;

* failed to make sure that STG met regulatory requirements, including capital resource requirements and implementing adequate systems and controls; and

* failed to monitor adequately their two appointed representatives, creating a serious risk that customers may have received unsuitable investment advice. This included a failure to ensure that call monitoring equipment was in place at one of the appointed representatives.

For further information go to: http://www.fsa.gov.uk/pages/Library/Communication/PR/2010/127.shtml .

Former Northern Rock Finance Director Fined £320,000 And Banned For Misreporting Mortgage Arrears Figures

The FSA has fined David Jones, former finance director (FD) of Northern Rock PLC (NR) £320,000 and prohibited him from performing any function in relation to any regulated activity.

Jones's misconduct started in mid January 2007 when he agreed, along with David Baker (former NR Deputy CEO), to allow false mortgage arrears figures to appear in explanatory text published with the 2006 annual accounts. Reporting correct figures would have either increased arrears by over 50% or possessions figures by approximately 300%. For nearly a year, Jones was responsible for the continued misreporting of arrears and possessions figures on a monthly basis to NR's assets & liabilities committee (ALCO) and, on a quarterly basis, to the Council of Mortgage Lenders (CML).

Jones received a 20% discount for settling in Stage 2 of the FSA's executive settlement procedures. Were it not for this discount, Jones would have been fined £400,000.

For further information go to: http://www.fsa.gov.uk/pages/Library/Communication/PR/2010/126.shtml.

FSA Secures Compensation For Victims Of Unauthorised Collective Investment Scheme

The FSA has secured £3.717 million in compensation for investors in an unauthorised collective investment scheme operated by Upton & Co. Accountants Limited (Upton). A High Court ruling earlier has confirmed the immediate distribution of £3.717 million to investors on a pro rata basis. Upton has also agreed to make further monthly payments of £10,000 which will be returned to investors in due course.

The Wakefield based firm, which has never been authorised by the FSA, operated a collective investment scheme known as the "Currency Plan" promising investors high rates of return. The money was to be used to invest in foreign exchange markets. However, limited foreign exchange trading occurred and very little was ever returned in cash. Darren Upton, a member of the Association of Chartered Certified Accountants, owned and controlled the firm.

For further information go to: http://www.fsa.gov.uk/pages/Library/Communication/PR/2010/122.shtml.

FSA Fines Father And Son For Market Abuse

The FSA has fined Jeremy Burley £144,200 and his father, Jeffery Burley, £35,000 for engaging in market abuse in relation to the shares of Tower Resources plc (Tower Resources), an oil and gas exploration company, in June 2009. Jeremy Burley's penalty included disgorgement of the £21,700 financial benefit he made through the market abuse.

For further information go to: http://www.fsa.gov.uk/pages/Library/Communication/PR/2010/121.shtml.

Redstone Mortgages Limited Fined £630,000 For Unfair Treatment Of Some Customers In Arrears

The FSA has fined Redstone Mortgages Limited (Redstone) £630,000 for poor treatment of some customers facing mortgage arrears. The firm has agreed to redress customers who were charged unfair and/or excessive charges while they were in arrears. It is estimated that the redress will cost the firm up to £500,000.

The FSA has identified a number of serious failings by Redstone which occurred between 1 January 2007 and 5 August 2009 in relation to its mortgage arrears handling processes and in its dealings with customers in arrears. These include:

* Failing to ensure mortgage servicing staff acting on its behalf had adequate understanding of treating mortgage arrears customers fairly;

* Focusing on reducing arrears to less than two months, regardless of the customer's personal and financial circumstances;

* Having written policies that led, in some cases, to the unnecessary use of litigation to secure arrangements to pay;

* Sending repetitive, excessive and confusing correspondence; and

* Applying four charges to customers' accounts that were unfair and/or excessive. These were:

– A fee for a returned direct debit which was charged regardless of how many times the direct debit had already been returned unpaid;
– Including arrears fees and charges in the balance on which an early repayment charge was calculated;
– Charging for field counsellor visits in full to some customers who had not been properly informed of the timing of the visit and/or of their right to refuse or cancel the visit; or who should have been charged a reduced rate cancellation fee; and
– A fee for litigation activities, which was applied even when such activities were taken by Redstone unnecessarily.

Under FSA rules, a firm must pay due regard to the interests of its customers and ensure they are treated fairly. Redstone was in breach of these rules for a significant period of time. Redstone qualified for a 30% discount under the FSA's settlement discount scheme. Without the discount the fine would have been £900,000. The FSA has taken into account that Redstone worked in an open and co-operative way with the FSA and has made significant improvements to its arrears handling and mortgage litigation procedures.

FSA Fines Network Director For Putting Customers At Risk Of Receiving Unsuitable Advice On PPI

The FSA has fined David Head, director of Essex based mortgage and insurance broker network FT Compliance Services Limited (FTCS), £10,500 for failing to properly supervise insurance brokers who he knew had close links with a firm and individual previously disciplined by the FSA for Payment Protection Insurance (PPI) failings.

FTCS operated as a network and recruited mortgage and insurance brokers as appointed representatives (ARs). Head was solely responsible for ensuring FTCS and its ARs were compliant but he failed to put in place systems and controls to ensure that the ARs made suitable recommendations. Head therefore exposed customers to the risk of purchasing unsuitable PPI.While the number of sales in question was relatively small, the FSA's investigation found that in cases where single premium PPI was sold:

* The ARs were not properly considering customers' eligibility for PPI before making a recommendation;

* The ARs failed to consider whether any medical conditions or existing insurance cover made PPI unsuitable for a customer; and

* There was no evidence to suggest that customers were told that they could buy PPI from other providers which might be more suitable for their needs.

As Head admitted misconduct, agreed to settle at an early stage and was open and cooperative during the FSA investigation, he qualified for a 30% reduction in penalty. The FSA would have otherwise imposed a financial penalty of £15,000.

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Panel Urges Swift Resolution Of PPI Mis-Selling Debacle

Responding to the FSA's announcement on PPI (payment protection insurance), the Financial Services Consumer Panel has urged firms to start handling complaints fairly as soon as possible ahead of the FSA's December 1 deadline. PPI mis-selling and complaints are issues which the Consumer Panel has commented on before, highlighting industry pressure which has delayed the successful resolution of the situation.

Kay Blair, Vice Chairman of the Financial Services Consumer Panel said: "The financial services industry has been dragging its feet over resolving PPI mis-selling and letting down customers by not handling their complaints fairly.

"Consumers with rejected PPI complaints should consider taking them to the Financial Ombudsman Service, where 81% of complaints are currently being upheld. We welcomed the FSA's action in May to suspend the usual six-month time limit for reference to the Ombudsman of rejected complaints and we would urge anyone affected to take action as soon as possible.

"Industry and regulators must learn the lessons of this debacle with further industry action to treat customers fairly and provide simple straightforward products which consumers can compare easily. We have set out our ideas for better financial services in our ten point plan."

Panel Calls For Straightforward Financial Products Ahead Of Government Consultation

The Financial Services Consumer Panel has called for more straightforward financial products ahead of the Government's anticipated review of financial services regulation. The demand follows a round table on the Consumer Panel's fairness research which revealed a consumer perception that financial services compared poorly to the retail sector. Consumers considered financial services less fair, insufficiently competitive and less accessible.

The research found complex products, which include some insurance products, or those with disproportionate charges, such as store cards, particularly unfair. Participants at the round table also highlighted concern over the way banks hide behind phones and documents instead of offering face to face contact, and penalise loyalty in contrast to other sectors.

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FSB Invites Feedback On Risk Disclosure Practices

The Financial Stability Board (FSB) has launched a peer review of the implementation of the recommendations concerning risk disclosures by market participants that were made in the April 2008 Financial Stability Forum Report on Enhancing Market and Institutional Resilience. As part of this review, the FSB invites public input on the implementation of the recommendations.

The financial crisis highlighted the importance to market confidence of reliable valuations and disclosures of the risks that are most relevant to market conditions at the time. The recommendations in the April 2008 report related in large part to disclosures about structured products and certain other risk exposures that were of concern to market participants in 2008. The review will focus on implementation of the recommendations by FSB member jurisdictions and by the major financial institutions located in those jurisdictions.

A template to collect information from national authorities was distributed to FSB members in June 2010, and the responses will be analysed and discussed by the FSB later this year. The review is to be completed by January 2011 and the report will be published.

As part of this review, we welcome feedback from investors, audit firms, financial institutions, industry associations and other stakeholders on their practical experiences as users of the resulting disclosures or in implementing the risk disclosure recommendations. This could include comments on how disclosure practices at financial institutions have changed, areas where implementation has proven to be challenging, or initiatives that have been taken to improve disclosures. Suggestions are also welcome for possible future approaches to enhance the dialogue amongst investors, financial institutions, audit firms, standard setters and regulators about improved principles for disclosure and further improvements in risk disclosure practices.

Feedback should be submitted by 10 September 2010 to fsb@bis.org under the subject heading "FSB Thematic Peer Review on Risk Disclosure." Individual submissions will not be made public.

Unwinding Of Temporary Deposit Insurance Arrangements

A report titled *Update on unwinding Temporary Deposit Insurance Arrangements* can be found at http://www.financialstabilityboard.org/index.htm dated 13 July 2010.

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FOA And EIC Give Qualified Welcome To Commission Consulation On Derivatives And Market Infrastructures – But There Are Concerns

The Futures and Options Association and the FOA European Industry Council have responded jointly to the European Commission's Public Consultation on Derivatives and Market Infrastructures, commending the Commission for its general approach to date, including the degree of industry consultation.

More specifically, the FOA and EIC very much support the intention to exempt non-financial end users from some of the more onerous clearing obligations and to facilitate the continuance of customer choice by not impairing the availability of bilaterally-cleared "bespoke" OTC contracts. The associated capital requirements should not, however, be so disproportionate as to render their use uneconomic for risk management purposes. This calls for a regulatory framework which is effective, proportionate, deliverable and closely correlated with IOSCO's recommendations.

The FOA and EIC do have a number of specific concerns:

One is the Commission's view that, because the authorisation and supervision of CCPs is a "political choice", there is no need for public consultation on who regulates them. "The decision not to consult with stakeholders in the clearing process on who should be responsible for regulating that process and its providers runs entirely against the Principles of Good Regulation," said Anthony Belchambers, FOA Chief Executive. "In particular, we question the ability of the Commission to take 'informed decisions on these markets' without consulting the stakeholders who will be directly affected by that decision."

Secondly, the FOA and EIC are concerned that the Commission's desire to avoid a segmented policy approach to different asset classes in the OTC derivatives market conflicts with their earlier recognition of the need to accommodate market differentiation, particularly in relation to certain commodity markets such as electricity and gas. An unduly standardised approach could distort market functionality and impair the provision of essential dealing and risk-management services for end-users. The FOA and EIC would urge the Commission to deliver on its recognition of market differentiation.

Thirdly, any mandating of interoperability between CCPs should be looked at carefully to ensure that its advantages are not outweighed by undue exacerbation in risk. The FOA and EIC suggest that this may be an issue that would be better addressed outside this proposed legislation.

Steve Sparke, Chairman of the FOA and EIC and COO of Marex Financial, said: "Sustaining the economics that underpin risk-management capability and practice is critical. The Commission's express assurances that it will conduct market impact analysis before implementing its policy decisions have a key part in maintaining a proper balance between establishing safer markets, but also markets that continue to make economic sense for end-users."

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Institute of Chartered Accountants in England and Wales

US Bill Paves Way For Ending Deadlock With EU Over Exchange Of Audit Papers

The US Dodd-Frank Wall Street Reform Act of 21 July is an important step towards solving the deadlock situation between the US and the EU regarding exchange of information between audit firm oversight bodies.

In the aftermath of Enron, the US introduced the Sarbanes-Oxley Act, which required auditors to be registered with, and regularly inspected by, the US Public Company Accounting Oversight Board (PCAOB) if they audited financial reports of US listed companies. The requirement also included inspections of foreign auditors auditing companies listed on US regulated markets.

However, the EU Statutory Audit Directive (Article 47) only allows access to EU auditors' working papers if there is a reciprocal agreement in place regarding the exchange of papers. The Dodd-Frank Act now authorises the PCAOB to share information with foreign auditor oversight authorities.

Michael Izza, ICAEW Chief Executive, commented: "The US Financial Reform Act is a significant step towards putting the deadlock situation between the EU and the US behind us.

"The conflicting US and EU regulations have caused uncertainty to EU-based businesses listed in the US, as they in theory could be required to de-list if audit inspections by the PCAOB were prevented. It has also been challenging for audit firms, as they have been caught in the middle.

"This is a welcome step in the right direction though the long-term aim should be to get to a position of mutual trust between countries, based on knowledge of the counterpart's systems and confidence in each other's audit inspection process, so that sending teams of inspectors to other jurisdictions and exchanging audit working papers are not required at all."

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International Capital Market Association

European Repo Market White Paper Emphasises Importance Of Repo And Urges Reform Of Market Infrastructure

ICMA's European Repo Council (ERC) has published a White Paper on the European repo market, including the role of short-selling, the problem of settlement failures and the need for reform of the market infrastructure. It emphasises the importance of the repo market for the efficiency and stability of the financial system.

The White Paper was commissioned by ICMA's ERC in response to current regulatory considerations which will impact the repo market. There is concern that regulatory initiatives should not constrain the capacity of the repo market in Europe at a time when increasing demands are being made on it, both by the regulators themselves in terms of proposals for enhanced collateral management to reduce risk and by governments in terms of increased debt issuance.

Proposals relating to the restriction of short-selling would have unintended consequences for the securities market, which will increase costs and risks for issuers and investors. There is also an urgent need for action to remove the barriers to the efficient cross-border transfer of securities posed by the settlement infrastructure. The paper highlights infrastructure problems which have caused fails in the system in recent difficult market conditions and suggests solutions.

The White Paper was written by Richard Comotto of the ICMA Centre drawing on extensive interviews with market participants, regulators and clearing systems.

Godfried De Vidts, Chairman of the ERC commented: "The White Paper will make an important contribution to the debate that is needed amongst policy makers, assisting them to make informed decisions. The support from the market, in the form of the ERC Committee and the ERC Operations Committee, allowed the author to produce this comprehensive document in a comparatively short time, demonstrating the commitment of the repo community of the ERC to continue working on a meaningful debate to solve repo related issues. We welcome more in-depth, constructive discussions with all concerned and trust they will lead to a well-functioning secured funding market that will continue to be an important brick in the building of a more robust financial market environment."

The main issues which the ERC White Paper addresses are:

Role and functioning of the repo market: The White Paper emphasises the important role played by the repo market in providing secure and efficient cash funding, and as a means of borrowing securities, which underpins bond market liquidity. Repo is also a key tool for central bank operations. At a time when governments are depending on markets to distribute large quantities of debt, regulation which affects the repo market could have serious consequences for sovereign debt issuance. It also explains how some of the more arcane features of that market (ie negative repo rates) form a normal part of market operation.

Short selling: In response to the Greek crisis regulators are discussing how to control short-selling and in particular naked short-selling. The repo market provides the borrowing facilities that support short-selling. The paper describes the essential role of short-selling, and outlines the likely costs and risks of regulatory restrictions. The

argument is made that short-selling is not a problem but a necessary and desirable market activity for a well-functioning and liquid securities market, and that "abusive" short-selling is rare and should be tackled through existing market abuse regulations. The paper supports reporting of short positions to regulators to assist them in monitoring short-selling and identifying potential abusive behaviour. The cost of suppressing a normal market activity would be serious unintended consequences for market efficiency and liquidity at a time when governments are seeking to use those markets to issue large amounts of debt. The damage to the repo market would also derail the regulators' proposals to encourage increased collateral management as a means of containing credit risk.

Clearing and settlement: The White Paper proposes that official action is needed by regulators to remove barriers to clearing and settlement in Europe, which may have contributed to problems experienced during recent market turbulence; and suggests reforms. It details interconnectivity barriers between national Clearing and Settlement Depositories in various Eurozone countries and the International Clearing and Settlement Depositories (ICSDs) used by international investors.

The European repo market white paper is available from ICMA's website at: http://www.icmagroup.org.

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International Underwriting Association

IUA Welcomes US Financial Services Reform

New changes to financial services legislation in the US will increase business opportunities for the London market and make it easier for companies to insure American risks. That is the view of International Underwriting Chief Executive Dave Matcham who has welcomed President Barack Obama's signing of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

One important part of the Act is designed to eliminate inefficient regulation of both surplus lines and reinsurance business. It will open up new markets for IUA companies providing surplus lines cover and also paves the way for possible reductions in credit for reinsurance rules that require non-US reinsurers to post collateral of 100% for gross liabilities assumed for American cedents.

Mr Matcham commented: "These reforms represent the most sweeping change to financial regulation in the United States since the Great Depression. Much of the legislation is focussed on the banking industry rather than insurance. But there are a number of measures, due to be implemented in July 2011, which could have very significant and lasting impacts for the London market. In particular, there is excellent news for surplus lines business where the new legislation will make it possible for London companies to offer cover in areas that were simply not possible before. The compliance burden of conducting surplus lines business will also be reduced and a more competitive market should deliver a better service to US customers."

Currently individual states regulate the insurers to which surplus lines brokers may place risks and the levels of regulation vary significantly. The Act will establish uniform standards, barring any state from prohibiting a surplus lines broker placing business with an appropriate non-US insurer.

"This promises to open up both Massachesetts and New Hampshire to IUA members for surplus lines business," declared Mr Matcham.

Secondly the problem of multiples states seeking to regulate and tax the placement of multi-state risks, leading to inconsistent compliance requirements, is tackled by limiting regulatory oversight and insurance premium tax obligations to those set by an insured's home state.

And the current 'diligent search' rules, followed by brokers to determine that a risk cannot be placed in local markets before obtaining surplus lines coverage, no longer apply to large commercial insurance buyers.

Mr Matcham added: "The IUA has campaigned for many years for reforms to deliver a more modern and efficient US regulatory system. The Dodd-Frank Act is designed to restore responsibility and accountability in the US financial systems. It will also introduce some long-awaited improvements to surplus lines supervision."

Another part of the Act will create a Federal Insurance Office (FIO) that will be responsible for monitoring all aspects of the industry. Its authority does not extend to a regulatory role and insurance will continue to be regulated at the state level. But the FIO will also have the power to enter into agreements with foreign governments

and may subsequently override state laws that treat non-US insurers unfavourably.

Furthermore the legislation will limit rules which some states currently use to impose collateral requirements on reinsurance contracts involving ceding insurers licensed in their state – regardless of whether the insurer is actually domiciled there.

Mr Matcham commented: “While the Act does not in itself achieve the sweeping changes to US reinsurance collateral burdens that we have long sought to restrict, it does mean that London market firms will in future only need to worry about requirements in the state where a ceding insurer is domiciled.

“And in one state, Florida, the requirement for non-US reinsurers to post 100% collateral on gross liabilities for American risks has already been relaxed. The Act opens the door for other states to follow suit and I understand that several are now considering such reform.”

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IMA Encourages The FSA To Maintain A Proportionate Approach To Remuneration

Commenting on the FSA's consultation on changes to its remuneration code, Julie Patterson, Director, Authorised Funds and Tax, said: "The new provisions of the Capital Requirements Directive (CRD3) come into effect from 1 January 2011. All EU Member States will have to implement the provisions – the UK is not going it alone.
"The CRD3 provisions allow for a proportionate application of the individual principles, in recognition of the fact that the Directive covers a wide range of types of businesses, including investment managers. Not only may each principle be applied in a proportionate way, but also a principle need not be applied at all where it is not proportionate to do so.

"We welcome the FSA's commitment to adopting a proportionate approach in revising and applying the Code. The FSA suggests that some of the principles should be applied to all firms, some only to certain firms depending on the nature of their businesses, and some on a 'comply or explain' basis. We shall continue our discussions with the FSA on the subset of the principles to be applied to investment managers and the detail of how they will be applied.

"We encourage the FSA in its final code to maintain an approach which makes full use of proportionality."

IMA Comments On New UK Regulatory Structure

* The new structure recognises the role of investment managers as 'agents'
* Good working relationships between regulators will be critical
* Concerns about different retail investment products being regulated differently
* Balance is needed in the regulation of wholesale markets and market infrastructure

Under the structure announced: banks and insurance companies will be prudentially regulated by the new Prudential Regulation Authority (PRA) and all firms will be regulated on conduct of business by the new Consumer Protection and Markets Authority (CPMA), including investment managers. Exchanges, clearing and settlement systems will be supervised by the Bank of England, alongside its existing responsibilities for payment systems. And the Government is to consult separately on whether the UK Listing Authority should be merged with the Financial Reporting Council (FRC), under the Department for Business, Innovation and Skills (BIS).

Commenting on the announcement, Julie Patterson, Director, Authorised Funds & Tax at the IMA said: "We welcome the recognition of the agency role of investment managers, which will be supervised by the Consumer Protection and Markets Authority. Investment managers are different from banks and insurance companies. They act as agents for investors of all types. They are not principal risk-takers, were not a cause of the credit crisis and do not represent a systemic risk.

"There is a rationale for each piece of the proposed re-allocation of responsibilities between statutory bodies, but viewed as a whole we have some concerns. If the regulatory landscape is to be fragmented in this way, there must be close and continuous co-operation between regulators. The objectives of the individual regulators need to be clear and to mesh together. History is persuasive – failures happen when there are gaps in regulatory oversight, when regulators fail to co-operate or when they fail properly to fulfil their obligations. The proposals provide a framework for relationships to work.

"However, the proposals do nothing to level the playing field between retail products. In fact, they risk exacerbating the current differences. Disclosures at the point of sale will all come under the CPMA, but regulation of what is in the products themselves will differ. Authorised funds are subject to detailed and comprehensive rules to protect retail consumers, which we understand will come under the CPMA. Listed, closed-ended investment companies – investment trusts, REITs and VCTs – are subject to special listing rules designed to protect the general interests of investors, which it is proposed will sit with the Financial Reporting Council (FRC). The regulation of insurance products, such as it is, is within the prudential rules for life companies, which will sit with the Prudential Regulation Authority (PRA). And banking products are subject to no real restrictions on the risks of the underlying investments.

"In relation to the regulation of wholesale markets, it is essential that regulators balance sell-side and buy-side interests. Investment managers, as users of the market on the 'buy-side', act on behalf of their clients: pension funds, charities and ordinary investors. There needs to be an efficient and effective mechanism for their voice to be heard. The objectives of the CPMA should allow for that, and we would urge the Bank of England, in its new role as regulator of all exchanges, clearing and settlement systems, to take full heed of buy-side views.

"Given the rescues of banks during the credit crisis and the specially increased compensation arrangements, there is a belief that if anything goes wrong, banks will be bailed out. This is economically untenable – no regulatory regime can be 'zero failure'. The CPMA should not seek to perpetuate this. It is also important that the CPMA, in its regulation of the retail market place, recognises the importance of innovation to meet changing consumer needs and the wider European dimension for funds. Today's proposals will mean fundamental change, which will take a lot or work and will require the focus and attention of many. IMA is committed to helping the Government make it work for our members and for their clients – ordinary investors. It is important that in the process regulators' eyes remain on the ball."

Government Consultation On Annuities Represents A Significant Step Forward

Commenting on the Government's launch of its consultation to remove the effective requirement to annuitise at 75, Jonathan Lipkin, Head of Research at the IMA, said: "The proposed changes represent a significant step forward and will help to create a far more flexible and innovative pensions landscape. In a market where wider options are available, annuities will still have an important role to play, but savers will be able to make decisions that are most appropriate to their specific needs and circumstances. We look forward to engaging with the Government on this consultation and discussing how the reforms can be implemented in a way that both empowers and protects individuals."

IMA Issues Proposals For A Revised Statement Of Recommended Practice For Authorised Funds

The IMA has issued an Exposure Draft of a revised Statement of Recommended Practice for Authorised Funds. The IMA has requested comments on the revisions by 3 September 2010.

The proposal is for a limited scope revision to incorporate amendments made to the Financial Services Authority's rules for Authorised Funds and to UK accounting standards. It is not expected that the changes will have a significant impact.

The invitation to comment and the Exposure Draft are available via links at: http://www.investmentfunds.org.uk/press/2010/20100715.asp. Comments should be sent via email.

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OFT Confirms Scope Of Equity Underwriting Market Study

The OFT has set out the final scope of its market study into equity underwriting and associated services.

The ability to raise equity capital efficiently is important for economic growth and productivity. In 2009, companies raised an estimated £70 billion of equity capital in the UK, paying around £2 billion in fees for equity underwriting and associated services. On 10 June the OFT announced plans to undertake the market study following concerns raised by corporate users of the market, and sought views on its scope.

The responses received from market participants confirmed that they have concerns about this market and have informed the final scope. The study will therefore examine equity underwriting services for the different types of share issue used by listed companies to raise capital in the UK, including rights issues, placings and other types of follow-on offer. The study will be limited to equity issues carried out by FTSE 350 listed firms and will not examine Initial Public Offerings.

The OFT will examine the way that the underwriting market works and assess whether there is potential for improving the way it functions. It will consider:

* how underwriting services are purchased
* how underwriting services are provided, and
* how the regulatory environment affects the provision of these services.

Clive Maxwell, OFT Senior Director of Services, said: “We have had constructive discussions with a number of interested parties on the scope of the study, and will now begin the detailed analysis of the market to identify any potential areas for improvement. The study will also help us to advise the Government in its wider thinking about wholesale financial markets.”

The OFT will issue a public statement on progress before the end of 2010.

The Pensions Regulator

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Regulator Updates Guidance On Transfer Incentives

A strengthened position on transfer incentives has been outlined in guidance published for consultation by The Pensions Regulator. It clarifies the role of the employer and trustee and aims to ensure that trustees become actively involved in managing the risks of such exercises. The guidance is accompanied by a new e-learning module and a joint statement with the FSA, all available on the regulator's website.

The regulator's position is in accordance with that of the FSA and the guidance replaces the 'Inducement Offers' guidance published in 2007. It highlights that trustees should start from the presumption that such exercises and transfers are not in members' interests and should therefore approach any exercise cautiously and actively. Trustees play an important role in ensuring that scheme members are in the best possible position to make the right decision in relation to their benefits. In order for transfer exercises to be conducted in an open, fair and transparent way, the regulator expects:

* members to be provided with clear information that is not misleading;
* members to be provided with impartial and independent advice to ensure they make the right decisions;
* trustees to engage in the offer process and apply a high level of scrutiny to all incentive exercises to ensure members' interests are protected;
* employers to ensure that any offers made are consistent with the principles in the guidance; and
* no pressure of any sort to be placed on members to make a decision to accept the offer.

The regulator's chair David Norgrove said: "As our guidance emphasises, any transfer exercise should be conducted with the highest regard to members' interests. Trustees should start from the presumption that such exercises are not in members' interests and should be approached with caution.

"Since we published our initial guidance in 2007, we have seen behaviour that concerns us. There has been a box-ticking approach that has led to exercises being run without due consideration to scheme members. As a result we will be looking closely at exercises and working with other regulatory bodies to ensure that standards are improved. We expect trustees to play an active role in ensuring that members are able to make informed decisions." Mr Norgrove added: "The Pensions Ombudsman will take this guidance into account to determine whether any complaint is upheld. He can then direct trustees or employers to compensate members accordingly."

The consultation lasts for 12 weeks.Responses should be submitted by 05 Oct. 2010.

Norgrove To Step Down At End Of His Term

The Department for Work and Pensions has announced that David Norgrove, chair of the Pensions Regulator, has said he will be stepping down when his second term in the post comes to an end on 31 December 2010.

The Secretary of State will begin recruitment for a successor in September, to have a new chair in place for the start of January 2011.

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Board Publishes Report To The Secretary Of State For Business Innovation And Skills

The Professional Oversight Board (POB), a part of the Financial Reporting Council, has published its 'Report to the Secretary of State for Business Innovation and Skills for the year to 31 March 2010'. This reports on the Board's responsibilities:

* for statutory independent oversight over the regulation of auditors by recognised professional bodies;
* for monitoring the quality of major audits, through its Audit Inspection Unit;
* for non-statutory oversight of the regulation of actuaries and accountants by their professional bodies;
* for regulation internationally;
* as the Independent Supervisor of Auditors General.

Whilst much has been published previously, the report brings together the results of all the Board's work and specifically summarises the results of our oversight of audit regulation by the professional bodies. The report concludes that, whilst all the recognised bodies devote substantial resources to their regulatory responsibilities, and much regulatory practice is of a high standard, there are aspects of regulatory activity at some recognised bodies that give us significant concerns.

Publication Of AIU 2009/10 Annual Report

The POB has published the Audit Inspection Unit's (AIU) Annual Report for 2009/10. The report provides an overview of the activities and findings of AIU.

The Report emphasises:

* How firms have responded positively to the challenges arising from the economic downturn particularly in relation to the audit of going concern.
* The rigorous nature of the AIU's inspections and their impact on audit quality.
* That firms have policies and procedures in place to support audit quality that are generally appropriate to the size of the firms and the nature of their client base.
* Despite the quality of firms' policies and procedures, the number of audits assessed by the AIU as requiring significant improvements remains too high.
* The findings suggest that firms are not always applying:
    - their procedures consistently on all aspects of individual audits; or
    - sufficient professional scepticism in relation to key audit judgments.
* Firms must embrace the principles underlying the Ethical Standards and accept that they should not provide non-audit services to audit clients where appropriate safeguards do not exist.

Commenting on the report, Dame Barbara Mills, Chair of the Board said: "The AIU's inspection activities continue to result in improvements to firms' policies and procedures which are now generally good. While the number of good quality audits we have seen has increased, I am disappointed that the number of audits assessed as requiring significant improvement remains too high. Firms must make more effort to ensure that the improvements in their procedures are reflected in individual audit engagements. We expect firms to place greater emphasis on achieving behavioural change to ensure this is the case and we will increase our efforts to see that this occurs." Individual reports on the findings from the AIU's inspections at Deloitte, Ernst & Young, KPMG and PricewaterhouseCoopers will be published in September.

Securities and Exchange Commission

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SEC Chairman Schapiro Announces Open Process for Regulatory Reform Rulemaking

Securities and Exchange Commission (SEC) Chairman Mary L. Schapiro has announced that the agency is making it easier for the public to provide comments as the agency sets out to make rules required under the Dodd-Frank Wall Street Reform and Consumer Protection Act.

Under a new process, the public will be able to comment before the agency even proposes its regulatory reform rules and amendments. Additionally, the SEC will provide greater public disclosure of meetings with SEC staff.

For further information go to: http://www.sec.gov/news/press/2010/2010-135.htm.

Public Request for Comment to Inform Study of Obligations of Broker-Dealers and Investment Advisers

The SEC has published a request for public comment to inform its study of the obligations and standards of care of broker-dealers and investment advisers providing personalized investment advice about securities to retail investors. The study is required under the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, which President Obama signed into law on July 21, 2010.

As required by the Dodd-Frank Act, the SEC is requesting public input, comments, and data on issues related to the effectiveness of existing standards of care for brokers-dealers and investment advisers, and whether there are gaps, shortcomings, or overlaps in the current legal or regulatory standards.

The public comment period will remain open for 30 days, following publication of the comment request in the Federal Register.

SEC Approves Disclosure Form Changes to Provide Investors Greater Information About Their Investment Advisers

The SEC has voted unanimously to adopt changes to the principal disclosure document that SEC-registered investment advisers must provide to their clients and prospective clients.

Form ADV, Part 2 — commonly referred to as the "brochure" — explains to the investor an investment adviser's qualifications, investment strategies, and business practices. The brochure in its current format requires advisers to respond to a series of multiple-choice and fill-in-the-blank questions organized in a "check-the-box" format that frequently does not correspond well to an adviser's business. In some cases, the required disclosure may not describe the adviser's business or conflicts in a way that is truly accessible to the investor. The amendments adopted by the SEC will:

* Improve the format and update the requirements of the brochure.

* Expand the content to better include details most relevant to the clients of investment advisers.

* Require brochure "supplements" to be delivered to new and prospective clients to give resume-like information about the individuals at an investment advisory firm who will provide services to the clients.

* Ensure investors have easy access to the brochures as investment advisers are

required to file them electronically for posting on the SEC's website.

The amended rules and forms will be effective 60 days after publication in the Federal Register. Most investment advisers will begin distributing and publicly posting new brochures in the first quarter of 2011.

For further information go to: http://www.sec.gov/news/press/2010/2010-127.htm.

Measures Proposed To Improve Regulation Of Fund Distribution Fees And Provide Better Disclosure For Investors

The SEC has voted unanimously to propose measures aimed to improve the regulation of mutual fund distribution fees and provide better disclosure for investors.

The marketing and selling costs involved with running a mutual fund are commonly referred to as a fund's distribution costs. To cover these costs, the companies that run mutual funds are permitted to charge fees known as 12b-1 fees. These fees are deducted from a mutual fund to compensate securities professionals for sales efforts and services provided to the fund's investors.

12b-1 fees were developed in the late 1970s when funds were losing investor assets faster than they were attracting new assets, and self-distributed funds were emerging in search of ways to pay for necessary marketing expenses. These fees amounted to an aggregate of just a few million dollars in 1980 when they were first permitted, but that total has ballooned as the use of 12b-1 fees has evolved. These fees amounted to $9.5 billion in 2009.

"Despite paying billions of dollars, many investors do not understand what 12b-1 fees are, and it's likely that some don't even know that these fees are being deducted from their funds or who they are ultimately compensating," said SEC Chairman Mary L. Schapiro. "Our proposals would replace rule 12b-1 with new rules designed to enhance clarity, fairness and competition when investors buy mutual funds."

The SEC's proposal would:

* Protect investors by limiting fund sales charges.
* Improve transparency of fees for investors.
* Encourage retail price competition.
* Revise fund director oversight duties.

There will be a 90-day public comment period after the SEC's proposal is published in the Federal Register.

For further information go to: http://www.sec.gov/news/press/2010/2010-126.htm.

SEC Adds Units To Oversee Financial Institutions, Asset-Backed Securities, New Financial Products And Trends

The SEC's division that reviews public company filings is creating three specialized offices to enhance its disclosure review and policy operations. The new offices in the Division of Corporation Finance will focus on large financial institutions, asset-backed securities and other structured products, and securities offering trends.

"These changes will help us focus our resources more sharply on critically important institutions and financial products so we can stay ahead of the curve and better protect investors," said Meredith Cross, Director of the SEC's Division of Corporation Finance.

The three new offices are:

* A disclosure review office that will expand the Division's enhanced reviews of large financial services companies.

* An office focused exclusively on disclosure reviews and policy-making for asset-backed securities and other structured finance products.

* An office that will review new securities products and capital markets trends and develop recommendations for changes to enhance investor protection in securities offerings.

For further information go to: http://www.sec.gov/news/press/2010/2010-124.htm

SEC Votes to Seek Public Comment on U.S. Proxy System

The SEC has voted unanimously to issue a concept release seeking public comment on the U.S. proxy system and asking whether rule revisions should be considered to promote greater efficiency and transparency.

For further information go to: http://www.sec.gov/news/press/2010/2010-122.htm

SEC Charges Citigroup and Two Executives for Misleading Investors About Exposure to Subprime Mortgage Assets

The SEC has charged Citigroup Inc. with misleading investors about the company's exposure to subprime mortgage-related assets. The SEC also charged one current and one former executive for their roles in causing Citigroup to make the misleading statements in an SEC filing.

The SEC alleges that in response to intense investor interest on the topic, Citigroup repeatedly made misleading statements in earnings calls and public filings about the extent of its holdings of assets backed by subprime mortgages. Between July and mid-October 2007, Citigroup represented that subprime exposure in its investment banking unit was $13 billion or less, when in fact it was more than $50 billion.

Citigroup and the two executives agreed to settle the SEC's charges. Citigroup agreed to pay a $75 million penalty. Former chief financial officer Gary Crittenden agreed to pay $100,000, and former head of investor relations Arthur Tildesley, Jr., (currently the head of cross marketing at Citigroup) agreed to pay $80,000.

For further information go to: http://www.sec.gov/news/press/2010/2010-136.htm.

Goldman Sachs To Pay Record $550 Million To Settle SEC Charges Related To Subprime Mortgage CDO

The SEC has announced that Goldman, Sachs & Co. will pay $550 million and reform its business practices to settle SEC charges that Goldman misled investors in a subprime mortgage product just as the U.S. housing market was starting to collapse.

In agreeing to the SEC's largest-ever penalty paid by a Wall Street firm, Goldman also acknowledged that its marketing materials for the subprime product contained incomplete information.

In its April 16 complaint, the SEC alleged that Goldman misstated and omitted key facts regarding a synthetic collateralized debt obligation (CDO) it marketed that hinged on the performance of subprime residential mortgage-backed securities. Goldman failed to disclose to investors vital information about the CDO, known as ABACUS 2007-AC1, particularly the role that hedge fund Paulson & Co. Inc. played in the portfolio selection process and the fact that Paulson had taken a short position against the CDO.

In settlement papers submitted to the U.S. District Court for the Southern District of New York, Goldman made the following acknowledgement:

Goldman acknowledges that the marketing materials for the ABACUS 2007-AC1 transaction contained incomplete information. In particular, it was a mistake for the Goldman marketing materials to state that the reference portfolio was "selected by" ACA Management LLC without disclosing the role of Paulson & Co. Inc. in the portfolio selection process and that Paulson's economic interests were adverse to CDO

investors. Goldman regrets that the marketing materials did not contain that disclosure.

Goldman agreed to settle the SEC's charges without admitting or denying the allegations by consenting to the entry of a final judgment that provides for a permanent injunction from violations of the antifraud provisions of the Securities Act of 1933.

The landmark settlement also requires remedial action by Goldman in its review and approval of offerings of certain mortgage securities. This includes the role and responsibilities of internal legal counsel, compliance personnel, and outside counsel in the review of written marketing materials for such offerings. The settlement also requires additional education and training of Goldman employees in this area of the firm's business. In the settlement, Goldman acknowledged that it is presently conducting a comprehensive, firm-wide review of its business standards, which the SEC has taken into account in connection with the settlement of this matter.

The settlement is subject to approval by the Honorable Barbara S. Jones, United Sates District Judge for the Southern District of New York.

For further information go to: http://www.sec.gov/news/press/2010/2010-123.htm .

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Securities Industry & Financial Markets Association

Dodd-Frank Wall Street Reform And Consumer Protection Act

A regulatory action database, guidance on compliance with the notice requirements of section 929X and other information regarding Dodd-Frank Act is available on the Sifma website at: http://www.sifma.org/Dodd-Frank-Act.html .

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Mr Brian Myerson, Mr Brian Padgett And Mr Daniel Posen 'Cold-Shouldered' For Period Of Three Years For Breaching Takeover Code

On 14 July, the Takeover Appeal Board affirmed the decision of the Hearings Committee of the Takeover Panel that Mr Brian Myerson, Mr Brian Padgett and Mr Daniel Posen should be 'cold-shouldered' for a period of three years. This was the first 'cold-shouldering' by the Takeover Panel since 1992.

The hearing related to purchases of shares in Principle Capital Investment Trust plc ("PCIT") that took place in March 2009 in the context of a battle for control of the PCIT board. The Hearings Committee concluded that:

(i) on 27 March 2009, 6,700,000 shares in PCIT were acquired by an undisclosed concert party comprising Mr Posen and parties acting on the direction of Mr Myerson and Mr Padgett in a deliberate attempt to circumvent the requirement under Rule 9 of the Takeover Code (the "Code") to make an offer to shareholders of PCIT generally;

(ii) in breach of their obligations to assist the Takeover Panel, Mr Myerson, Mr Padgett and Mr Posen subsequently attempted in their dealings with the Takeover Panel Executive (the "Executive") to conceal from the Executive the circumstances relating to the acquisition of those shares, to present a false picture of what happened, to conceal the breaches of the Code involved and, in Mr Posen's case, not to disclose to the Executive the source of the funds used to purchase the shares;

(iii) it should publish a formal Panel Statement in accordance with paragraph 11(b)(v) of the Introduction to the Code indicating that Mr Myerson, Mr Padgett and Mr Posen are persons who in the Hearing Committee's opinion are not likely to comply with the Code; and

(iv) the statement in paragraph (iii) above should remain effective for a period of three years from the date of publication of the decision.

2010 Annual Report

The Panel's 2010 Annual Report was published on 21 July. It can be found on the Panel's website: http://www.thetakeoverpanel.org.uk .

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HM Treasury

Another Step Towards Independence For Northern Rock Plc

A further milestone in Northern Rock plc's return to independence has been reached, with notice that HM Treasury's guarantee arrangements in place for the bank's wholesale liabilities will end in three months time.

This announcement brings forward the end date of wholesale guarantees that, as previously stated, would not extend beyond 31 December 2010. The current beneficiaries under these wholesale guarantees are Northern Rock (Guernsey) and the Northern Rock Foundation, who both have funds on deposit with Northern Rock plc. Fixed term wholesale liabilities in existence at 01 January 2010 continue to be guaranteed until maturity.

This decision was taken following a recommendation from UK Financial Investments (UKFI). The Financial Services Authority (FSA) and the Bank of England have also approved this decision. This announcement does not affect the wholesale guarantee arrangements in place for Northern Rock (Asset Management) plc.

Consultation Launched On The Implementation Of Financial Regulation Reforms Announced At Mansion House

Financial Secretary to the Treasury, Mark Hoban MP, has launched the Government's consultation on the implementation of reforms to financial regulation.The document (which can be viewed at: http://www.hm-treasury.gov.uk/consult_financial_regulation.htm.) sets out detailed proposals for reform of the financial services sector, first announced by the Chancellor in his Mansion House speech on 16th June 2010.

The Chancellor set out plans to overhaul the system of Financial Regulation giving the Bank of England powers over macro prudential regulation through a newly established Financial Policy Committee (FPC), which will be established on an interim basis from Autumn 2010. The consultation invites views on this proposal in addition to plans to create:

* A new prudential regulator under the control of the Bank of England headed by a new Deputy Governor (the first of whom will be current Financial Services Authority Chief Executive, Hector Sants), which will be responsible for supervising the safety and soundness of individual financial firms.

* A new Consumer Protection and Markets Authority (CPMA) to act as a single integrated regulator focussed on conduct in financial markets.

Financial Secretary to the Treasury, Mark Hoban said: "The Coalition Government is delivering on its commitment to reform the financial system, to avoid repeating the mistakes of the recent financial crisis and to ensure that taxpayers are protected. Today is a crucial milestone in our programme of reform. To take this forward, we would welcome the input of everyone who has an interest, including regulators and the regulated community, to ensure that we get the design right."

Equitable Life Bill And Independent Commission Announced

Financial Secretary to the Treasury, Mark Hoban MP has announced that the Coalition Government has introduced a Bill to Parliament, which will enable payments to be made to Equitable Life policyholders.

On May 26, the Government said that it would establish an independent commission

to advise the Government on the best way to allocate payments to policyholders and help develop scheme design, in light of the Ombudsman's recommendation that the payment scheme should be independent of the Government.

Mark Hoban has now announced that Brian Pomeroy, John Tattersall and John Howard have agreed to form the Independent Commission. "The Commission will start work imminently so that we can begin making payments as soon as possible. They are expected to report by the end of January 2011" said Mark Hoban.

Publication Of Sir John Chadwick's Report On Equitable Life

Financial Secretary to the Treasury, Mark Hoban MP has announced that the Coalition Government has published the final report by Sir John Chadwick in relation to losses suffered as a result of Government maladministration in the regulation of Equitable Life.

Mark Hoban said that: "There is a wealth of information in Sir John's report and it is important to consider it all carefully. However, this Government has always made it clear that Sir John's review is just one of the building blocks in resolving what is a complex matter and that there are other judgments to be made in determining the final shape of the scheme."

The Government is also aware that some of his findings are contentious and because of this, and the complexity of the methodology, it will reflect on his report and will listen to representations by interested parties ahead of the Autumn Spending Review. In addition, as the Ombudsman noted in her report, it is appropriate to consider the impact of any scheme on the public purse. The scheme will be a significant spending commitment for this Government and cannot be considered in isolation from the other spending decisions that it will need to make over the coming months, and what is affordable in that context. The Government will therefore be setting out the funding available for the scheme at the Spending Review on 20th October.

The Government Launches A Consultation On Removing The Requirement To Annuitise By Age 75

Financial Secretary to the Treasury, Mark Hoban MP, has announced the start of an 8-week consultation on removing the effective requirement to annuitise by age 75, following the announcement in the June Budget that these rules will end from April 2011.

The consultation document sets out proposals that will simplify the treatment of retirement savings and reduce complexity for individuals as well as for pension and annuity providers.

The reforms will give individuals greater flexibility to choose the retirement options that are best for them, with more choice over how they can provide a retirement income for themselves.

The Government welcomes views from interested parties on how the reforms can best be implemented, in particular the proposed new tax framework, the proposed safeguards against individuals prematurely exhausting savings, and how to minimise unnecessary burdens for individuals and industry.

Consultation Document On Bank Levy

The Government has launched a consultation document on the Bank Levy. The document sets out issues around technical aspects of the design and implementation of the Bank Levy. This consultation exercise will help to ensure that the Levy is designed in a way that best meets its objectives, including ensuring the compliance costs faced by firms are minimised.

It is proposed that draft legislation will be published in the autumn to allow for further comments from stakeholders. Final draft legislation for inclusion in the 2011

Finance Bill will be published towards the end of 2010, ahead of implementation of the Levy. The structure of the Levy is intended to encourage the banks to move away from riskier funding models, reducing systemic risk. Once fully in place, the Levy is expected to generate around £2.5 billion per annum.

Stakeholder views are sought on these proposals by 5th October 2010.

Copies of the consultation document and consultation stage impact assessment have been deposited in the Vote Office and the libraries of both Houses. The documents can also be viewed at: http://www.hm-treasury.gov.uk/consult_bank_levy.htm.

Financial Secretary to the Treasury, Mark Hoban said: "Excessive risk taking in the banking sector was a significant contributory factor in the recent financial crisis. Alongside the wider financial regulatory reform aimed at increasing the resilience of the financial sector, the Levy is intended to ensure that the banking sector makes a fair contribution that reflects the risks it poses to the financial system and the wider economy, and to encourage banks to move away from riskier funding – problems with risky funding led to serious liquidity problems that played a key role in the financial crisis."

The Chancellor of the Exchequer, George Osborne, announced the introduction of a Levy in the June Budget. It will apply to the balance sheets of UK banks and building societies, and to the UK operations of banks from abroad. At the same time, France and Germany also announced that they would introduce a Levy based on banks' balance sheets.