

## **FSMA review: problems with the legislation/areas for amendment – issues raised by members of the Financial Services and Markets Legislation City Liaison Group**

### Regulatory objectives and principles of good regulation; structural issues

There are suggestions that the regulatory objectives and principles of good regulation should be amended to oblige FSA to distinguish more clearly between different kinds of business (e.g. in rule-making).

There are a number of concerns about the Ombudsman Scheme (Part XVI FSMA). Amendments which are being discussed include changes to allow firms to appeal against FOS decisions and to allow costs awards to be made against complainants in respect of respondent's costs. As regards "rule-making", it is clear that FOS decisions can have the effect of modifying the meaning of a rule, with the result that the consultation and cost benefit analysis required under the Act are bypassed. We are considering whether legislative amendments are needed to deal with this.

### Particular sections

- Section 21. Implement the Law Society Committee recommendations on amending the financial promotion regime – a number of which the Treasury have already agreed – and consider a more general review of the provisions. (Particular points are whether the exemption of high net worth investors is much use in practice as currently drafted,<sup>1</sup> and the need to reflect FSA guidance on financial promotion in the legislation.)
- Section 104. Repeal the provision dealing with banking business transfers? (It has never been put into force.)
- Market Abuse. Clearly amendments to Part VIII will need to be taken forward as part of MAD implementation, but a particular issue that should be considered at this stage is the need to amend section 122 so that the Code can also provide safe harbours as regards the "requiring or encouraging" offence in section 123(1)(b).
- Section 148. Consider a more flexible modification/waiver provision in emergencies (link to emergency powers?). Also amend 148(4)(a) to allow waivers to be granted in the case where the purpose of a rule can be achieved in another way.
- Section 149. Modify evidential provision so it allows the FSA to create safe harbours (the evidential protection is insufficiently helpful, particularly because the FSA's rules tend to include the provisions referred to in both section 149(2)(a) *and* (2)(b) rather than the latter alone).
- Section 150. Amend to ensure that firms complying with guidance – at least general guidance – cannot be liable in an action for damages based on a rule contravention.
- Section 157. Consider whether modifications can be made to facilitate FSA giving guidance informally. It is also pointed out that FSA should be more conscious of the value of providing general guidance on the application of aspects of the rules for

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<sup>1</sup> Also see Securities Law issues below.

*particular types* of business (although it is not clear that any amendments of the legislation are needed for this).

- Control/close links. *Section 178* – on obligation to notify – consider clarifying to deal with conditional acquisitions; *Section 422(4)(g)*: amendment needed to remove notification obligation in an underwriting of a securities issue for an authorised firm.
- Part XVII - collective investment schemes. Continued concerns about aspects of the CIS definition, in particular as regards whether LLPs are potentially CISs even where they do not have an investment purpose (following amendment to S.I. 2001/1062 made by article 2(4) of 2001/3650)<sup>2</sup>.

### Securities law issues

- Mismatch between concepts of "professional investors" in the FPO, the FSA Handbook and the proposed Prospectus Directive.
- Mismatch between concepts of "professional investors" in the RAO for the purposes of commercial paper and the categories of investors in the US to which commercial paper can be sold without restriction under US securities laws.
- Listing of private companies securities in the UK and in particular the position as regards private companies listing bonds in Luxembourg and the restrictions on "offers to the public" in section 81 Companies Act following the FSMA consequential amendments (see Annex 1).

### Notification requirements under the Directives

We are considering whether some aspects of the implementation of the notification provisions in the Directives are unnecessarily burdensome given the EU requirements.

In particular, and as regards changes in control, there are questions about the application of the Consultation with Competent Authorities Regulations. These appear to require FSA to consult home state regulators *only* where, as a result of an acquisition, the acquirer would become a *parent undertaking* of the UK firm (as defined in Part VII of the Companies Act given section 420). However, we understand that FSA may consider that it needs to consult home state regulators in other cases where a notice of control is required because the acquisition would lead to an increase in control as defined in section 180. The prior consultation procedure obviously takes time, and its use should be limited to the circumstances required in the Directives: if there is ambiguity about the current provisions, the legislation should be amended accordingly.

We are also assessing whether it is necessary to apply the Directive's requirements on notifying changes in a firm's programme of operations to home/host State competent authorities in the case where a subsidiary within a group wishes to deregister because it is no longer undertaking investment business (for example, because its business has been transferred to another firm within the group).

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<sup>2</sup> See Sir Adam Ridley's letter of 7<sup>th</sup> January 2002 to Robin Fellgett.

## Enforcement issues

- The Treasury will recall that members of the Group believed that the Tribunal rules on public hearings would deter firms from disputing decisions taken by the RDC/FSA. We believe that the absence of Tribunal cases so far confirms this concern and that the issues should be reviewed again (as the Treasury undertook to do in the letters of 17<sup>th</sup> August and 16<sup>th</sup> July 2001). Access to the Tribunal was thought to be a fundamental element of the FSMA checks and balances framework, and there is a clear danger that the absence *in practice* of a mechanism to challenge the regulator will raise questions about whether the legislation is ECHR compliant. It may well also have damaging consequences as regards FSA's attitude to the use of its powers. (Annex 2 provides some examples of the kind of issues that we have in mind.)
- Section 391. Notwithstanding the prohibition against publication of a warning or decision notice, there are concerns about the extent to which enforcement matters can be aired in the Press before their time, particularly in high profile cases. This is not only unfair and unattractive but, from a systemic point of view, risks over time undermining the enforcement regime. There is no sanction attached to s.391 and also no basis for preventing newspapers from publishing this information (compare s.348). Thought should be given as to the ways by which the provision could be given some teeth – e.g. criminal sanctions for breach – and applying it also to all those who knowingly publish such information.
- Section 413. This should be amended to make it clear that enforcement proceedings before the RDC constitute "proceedings" for the purposes of section 413(3)(b).
- Section 394. There seems to be some uncertainty in practice about the application of the disclosure rules, and there are concerns that there have been cases where the approach to these has not reflected Parliament's intention. We believe that it should be clear that access will be provided to both the material that the investigation team "relied upon" in deciding to put a case to the RDC – including the recommendations and reasoning – and to the material that the RDC members considering the case actually relied upon at the time.
- The lack of rights of disclosure in the context of the supervisory notice regime has also been raised.

In addition, questions have been raised about whether the RDC arrangements should be changed so that the members which decide on whether a decision notice should be issued in a case are not the same as those that decided to issue the warning notice.

## General

There are concerns in a number of cases about defined terms within FSMA i.e. whether they are used for the purposes of a particular provision, part or more generally.

**Peter Beales**  
**17<sup>th</sup> June 2003**