

Mr D Lambeth
The Financial System and
Major Operational Disruption FSM Team
Room 4 / 16
HM Treasury
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25th April 2003

Dear Mr Lambeth

HM Treasury's consultation paper: The Financial System and Major Operational Disruption

Our response to the consultation is set out in Sir Adam Ridley's letter dated 3rd April addressed to Mr James Sassoon. Receipt of this letter was acknowledged on 14th April. If you have any difficulty in obtaining a copy of this letter please let me know.

Since preparing our response we have continued to discuss the issues the consultation paper has raised both with our members and others. We remain firmly of the opinion that time needs to be given to undertake the full and complex analysis we outlined in our response before an informed view can be given on whether there is a case for the Government to take additional powers.

I mentioned when we spoke last week that I would send you some additional comment to emphasise the importance we place on the need for the public and private sectors to have a joined up approach to the work being undertaken. The Green Paper sets out at the top of the Executive Summary (on page 3) a key statement and asks two important questions:

"The financial authorities believe that the private sector itself has the main responsibility for promoting order in the financial system in the face of major operational disruption - for example by market co-operation to address problems. Could private sector approaches usefully be strengthened further?

If so, can Treasury, Bank of England and Financial Services Authority help with this?"

The Green Paper clearly sets out that Government view the private sector as being the most important and able to respond rapidly to operational disruption. This is illustrated by reference to the events in the United States following the 11 September

where firms worked closely and co-operatively amongst themselves and with the authorities to ensure a rapid recovery. It is to be noted that the suspension powers available to the United States authorities were not used at this time.

Instead the Federal Reserve Bank of New York worked with the New York State government in developing their declaration that gave New York banks the option (but not the requirement) to close that day (paragraph 3.22 in the Green Paper). Since 11 September the Green Paper states that the US authorities have focused on *market-based approaches*.

This demonstrates that the private sector is best placed to take responsibility for responding to major operational disruptions without the need for government intervention but with government, authorities and private sector working closely together to co-ordinate communications, overcome obstacles and difficulties and generally promote the development of a private sector consensus. We are convinced that the authorities need to concentrate their efforts upon market-based approaches. The authorities have a central role to play as the co-ordinator ensuring that there is a joined up approach to the initiatives being undertaken both now and in the longer term. The authorities must take on the responsibility for ensuring that the work being undertaken and the outcomes are widely and freely communicated to the industry. This will ensure that there is direction to the work and importantly that firms are aware of it.

We all agree that there is a requirement for good communications during a time of crisis. We see a need to establish effective communication protocols to enable market participants to obtain and share reliable information. The process of forming a consensus view as to the appropriate actions necessary will take time and be extremely difficult in such a crisis. We consider that the authorities can greatly assist with the establishment of these communication protocols which will be a significant contribution to making the decision processes more efficient and more widely known. This will add to market confidence during an incident.

We are aware that there are a number of initiatives currently taking place both within the public and private sectors. However, there is the perception, real or otherwise, that there is insufficient information being distributed on them and a lack of co-ordination of effort between them - a distinct lack of the joined up approach to this issue that we strongly advocate. This in turn has given rise to the view that little is taking place and that there is a general lack of knowledge of the situation at senior management level within the industry.

We consider that there is an urgent need to address this situation effectively now. There needs to be an official co-ordinating body for the financial services sector to act as the general overseer to the initiatives being undertaken. The work of the Tripartite Committee does not appear to have included this role to date although it has promoted the need for greater co-operation on these issues within the industry. It may be that the Bank of England with its experience in the field of handling operational disruption is the appropriate body to take on this role.

It would also appear that there is a need to co-ordinate the efforts of the private sector in order to "strengthen it further". This needs to be encouraged through the official co-ordinator and perhaps is an area where the various trade bodies could assist by being asked to take a more active role than has been the case to date.

We consider that the authorities need to commit more resource to co-ordinating the activities of the public and private sectors in this area. This would enable the delivery

of a tested end-to-end plan for handling operational disruption in which all parties could have confidence. Every effort should be made to move forward on the market approaches to provide the solution.

If at the end of this comprehensive exercise areas were identified for Government action, this would be the appropriate time for recommending concise, proportionate and targeted legislation.

If I can be of assistance to you please let me know.

Yours sincerely

Paul Martin
Director