

Future Regulatory Framework Review  
Financial Services Strategy  
HM Treasury  
1 Horse Guards Road  
London  
SW1A 2HQ

Sent by email to [FRF.Review@hmtreasury.gov.uk](mailto:FRF.Review@hmtreasury.gov.uk)

9 February 2022

Dear Future Regulatory Framework Review team,

## **Consultation response: Financial Services Future Regulatory Framework Review**

I am writing to respond to HM Treasury's consultation *Financial Services Future Regulatory Framework Review: Proposals for Reform*, on behalf of ShareAction, a registered charity established to promote transparency and responsible investment practices by pension funds and other institutional investors. We are a member organisation and count amongst our members well-known NGOs and charitable foundations, as well as over 26,000 individual supporters. Among other activities, we work with the financial services sector to promote integration of sustainability factors in investment decisions, long-term stewardship of assets and the consideration of the views of clients, beneficiaries and pension scheme members.

### **1. Do you agree with the government's approach to add new growth and international competitiveness secondary objectives for the PRA and the FCA?**

No, we have significant concerns about this proposal. We are concerned that adding a new secondary objective of competitiveness will eventually lead to rules being weakened to attract business. That would be a cause for concern and potentially undermine the very integrity of the UK market that makes it attractive. For example, an over-focus on competitiveness has been widely acknowledged as a factor in bringing about the 2007/8 financial crisis, including by Andrew Bailey, then head of the FCA and now Governor of the Bank of England.<sup>1</sup> Just as international businesses use the UK's legal system for its high standards and rule of law, we should focus on strong, independent regulators that can ensure well-functioning markets that protect consumers and, ultimately, avoid financial crises that are bad for competitiveness and growth.

Similarly on growth: growth for growth's sake is not desirable. Extensive research suggests that there is an optimum size for a financial sector relative to the rest of an economy, when credit to the private sector is around 90 per cent of GDP, and beyond this point it acts as a drain on human and other resources which could be put to better use elsewhere.<sup>2</sup> The UK far exceeds this point: for example, hitting 192 per cent in 2009.<sup>3</sup> A 2018 research paper found that, from the 1990s to the current period, the cost of 'too much finance' for the UK was in the region of £4,500 billion (approximately 2.5 years of the average GDP across the period).<sup>4</sup> What's more, the cumulative

<sup>1</sup> <https://www.ft.com/content/96517774-a6cc-4e30-a1a4-b82f612c1df3>

<sup>2</sup> Cecchetti and Kharroubi, 2012; Baker, Epstein and Montecino, 2018

<sup>3</sup> <https://data.worldbank.org/indicator/FS.AST.PRVT.GD.ZS?locations=GB>

<sup>4</sup> <http://speri.dept.shef.ac.uk/2018/10/05/uk-finance-curse-report/>

impact of economic growth pursued for its own sake means that we are consistently overshooting the limits of what the Earth can sustain. We are unclear as to how this squares with the Government's ambitions for the UK to be a net-zero financial centre.

Instead, we support the recommendation from the Financial Inclusion Commission and Fair by Design to introduce a cross-cutting “must have regard” to financial inclusion for the FCA.<sup>5</sup> Financial markets do not currently meet the needs of many of those on low incomes or with disabilities. The most vulnerable people are often unable to access necessary products or services because they are defined as “non-standard” and pay extra for services because they are seen as not desirable consumers to serve.

What's more, we are concerned that the proposed new consumer duty could mean that financial services firms would, rather than risk selling products and services to high-risk users and fall foul of the new rules, withdraw from those sections of the market seen as too risky, therefore protecting themselves but resulting in more financial exclusion for the most vulnerable. We would argue that a “must have regard” on financial inclusion is a necessary accompaniment to this new duty.

This “must have regard” should include a statutory duty to report to Parliament annually on:

- the state of financial inclusion in the UK
- measures that the FCA has taken, and is planning to take, in order to advance financial inclusion
- recommended additional measures which could be taken by government and other public bodies to promote financial inclusion.<sup>6</sup>

## **2. Do you agree that the regulatory principle for sustainable growth should be updated to reference climate change and a net zero economy?**

We agree that the regulators' remit should include reference to climate change and the net-zero economy. However, we believe there should be an explicit sustainability-related statutory objective related to the UK's net-zero targets and carbon budgets, and the Paris Agreement (including nature provisions).

We do not think it is sufficient that the Government is proposing to create only a regulatory principle in relation to sustainability, as opposed to a statutory objective (as with the proposed new objectives of growth and competitiveness). As the Government itself says in this consultation paper (giving this as a reason why a regulatory principle of competitiveness would not be sufficient), “the regulators are not required to act to advance their regulatory principles; instead they must take them into account when pursuing their statutory objectives... the government considers that it would not provide the regulators with the appropriate statutory basis required to act to support competitiveness in line with the government's vision for the sector”.<sup>7</sup>

Moreover, this objective should not be tied specifically to economic growth: it is concerning that the only mention of sustainability is in relation to what kind of growth the regulators should pursue. 2021 research found that if the UK's largest financial institutions were a country, they would have the 9<sup>th</sup> largest emissions in the world, at 1.8 times the UK's domestically produced emissions.<sup>8</sup> An objective to promote sustainable growth would not be sufficient to address this problem. We need more planning and direction from the Government if we are to tackle the massive existential threats we face, identifying what outcomes we want to see and how to get there. We need to move away from the traditional approach of the UK's financial regulators, that these systemic issues can only

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<sup>5</sup> <https://financialinclusioncommission.org.uk/blog/author/ficomm/>

<sup>6</sup> [FCA Statutory Duty – Financial Inclusion Commission](#)

<sup>7</sup> [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/1032075/FRF\\_Review\\_Consultation\\_2021\\_-\\_Final\\_.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1032075/FRF_Review_Consultation_2021_-_Final_.pdf), p33

<sup>8</sup> [The-Big-Smoke-the-global-emissions-of-the-UK-financial-sector.pdf \(greenpeace.org.uk\)](#)

be framed in risk terms, to be solved by asking every market participant to come with their own response.<sup>9</sup>

**3. Do you agree that the proposed power for HM Treasury to require the regulators to review their rules offers an appropriate mechanism to review rules when necessary?**

We have concerns that this proposal may affect the independence and transparency of the financial regulators. We believe that a greater role for government is warranted in setting the overall policy direction of financial regulation in relation to looming environmental and societal crises. However, echoing points from the Finance Innovation Lab, it is unclear how the “public interest” or “exceptional circumstances” may be defined, nor the process for appointing the independent person. If HMT has the power to define all three, we believe that this could put undue power in the hands of government and damage the ability of the regulator to function independently.

**4. Do you agree with the proposed approach to resolve the interaction between the regulators’ responsibilities under FSMA and the government’s overseas arrangements and agreements?**

We understand that it is necessary to consider how regulators’ responsibilities will interact with government’s overseas agreements post-Brexit. However, we are concerned that there is a risk that regulatory rules will be watered down to suit trade agreements, rather than trade agreements seeking to reflect and promote the high regulatory standards in the UK. Our view is that financial regulation should always take priority where potential conflicts arise.

**5. Do you agree that these measures require the regulators to provide the necessary information to Parliament on an appropriate statutory basis to conduct its scrutiny?**

We are concerned about the proposed increased powers of HM Treasury and the regulators, post-Brexit, without commensurate increases to transparency and accountability. We support the Civil Society Joint Statement’s recommendation<sup>10</sup> that a new Parliamentary select committee is set up with the purpose of scrutinising the regulators, supported by adequate resourcing. This should have the function of debating new legislation and reviewing the effectiveness of regulatory frameworks.

We agree with HMT that the UK Parliament does not have the time or resources to consider a large volume of highly technical provisions, as ECON does in the EU. We acknowledge that it is proposing to strengthen the engagement mechanisms that exist between HM Treasury and the regulators, and formally requiring the regulators to provide any information requested by Parliament: we are supportive of this. However, we do not agree that the existing Parliamentary scrutiny mechanisms, such as that provided by select committees are sufficient and should continue to be the principal ways in which Parliament holds the regulators to account. The Treasury Select Committee does not have the necessary capacity or resourcing to monitor and hold accountable HMT and the regulators given this enormous transfer of powers.

**6. Do you agree with the proposals to strengthen the role of the panels in providing important and diverse stakeholder input into the development of policy and regulation?**

We agree with HMT that “Panels that have diverse backgrounds, expertise, and thought will be better placed to ensure the regulators receive the most comprehensive appraisal of their policy”. We also welcome the work being done by the regulators to boost diversity on statutory panels, and HMT’s expectation that they will “commit to open and fair recruitment practices to ensure a diverse range of qualified candidates are appointed to panels”. However, we support the Civil Society Joint Statement’s recommendation<sup>11</sup> that HMT instead requires the FCA’s and PRA’s statutory panels to

<sup>9</sup> <https://www.fca.org.uk/firms/climate-change-sustainable-finance>

<sup>10</sup> <https://financeinnovationlab.org/wp-content/uploads/2022/02/FRF-CSO-Joint-Statement-2022.pdf>

<sup>11</sup> Ibid.

consist of a maximum of 50% industry representatives and at least 50% public interest representatives. As part of this, a duty should be placed on the PRA to consult the public, not just firms (amending FSMA s136), including via a new statutory panel. We would further recommend that a set percentage of the statutory panels should be required to have expertise on sustainability-related matters.

We are not confident that a clear and transparent process is sufficient on its own to address the imbalances between industry and civil society representation and engagement on issues of financial regulation. In 2015, the FCA required contract-based pension providers to appoint independent governance committees (IGCs) to act in the best interests of scheme members. This followed the Office for Fair Trading (OFT)'s finding that the buy-side in defined contribution pensions was "one of the weakest that [it had] analysed in recent years",<sup>12</sup> causing poor consumer outcomes linked with practice such as routine overcharging by providers. The FCA stated that it believed that "an open and transparent recruitment process is fundamental to the credibility and independence of IGCs. Scheme members must have visibility of the process and confidence in the appointments".<sup>13</sup> However, when we analysed the IGC reports published in 2017, we found that only four of 16 IGCs included a member with experience of representing consumer interests. Only one IGC gave a full description of the process for appointing IGC members.<sup>14</sup> While reviewing the reports and meeting with IGC members, we developed significant concerns that in a few cases, IGC members appeared to be putting the commercial interests of the firm firmly ahead of the interests of members, failing to challenge on issues of substantive consumer detriment.

While we understand that HM Treasury's proposals relate to the regulators' statutory panels rather than the governance arrangements within industry, we believe this example shows the risks inherent in putting faith in supposedly transparent recruitment processes as opposed to setting clear targets for consumer representation. Industry voices have a vital role to play in ensuring regulation works well in practice but they do not have the experience that is needed to represent consumer interests.

**7. Do you agree that the proposed requirement for regulators to publish and maintain frameworks for CBA provides improved transparency for stakeholders?**

We support this proposal.

**8. Should the role of the new CBA Panel be to provide pre-publication comment on CBA, or to provide review of CBA post-publication?**

We believe the CBA Panel should provide pre-publication comment on CBA. We would further recommend that the CBA Panel is tasked with considering how a greater weight can be placed on broader, longer-term, economic, environmental and societal factors in CBA frameworks, such as financial stability, financial inclusion and climate commitments. Our experience of responding to Government consultations indicates that they are often too narrowly focused on short-term concerns such as costs to business.

**9. Do you agree that the proposed requirement for regulators to publish and maintain frameworks for how the regulators review their rules provides improved transparency to stakeholders?**

We agree.

**10. Do you agree with the government's proposal to establish a new Designated Activities Regime to regulate certain activities outside the RAO?**

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<sup>12</sup> [http://webarchive.nationalarchives.gov.uk/20140402194810/http://www.offt.gov.uk/shared\\_offt/market-studies/oft1505](http://webarchive.nationalarchives.gov.uk/20140402194810/http://www.offt.gov.uk/shared_offt/market-studies/oft1505)

<sup>13</sup> <https://www.fca.org.uk/publications/policy-statements/ps15-3-final-rules-independent-governance-committees-including>

<sup>14</sup> Report available on request.

We are broadly supportive of this proposal. However, we would echo the Finance Innovation Lab and recommend that the regulators keep the new regime under review and ensure they are making regulatory interventions where needed. It is important that risky activities and products do not escape regulatory attention, now they fall outside the scope of EU law.

**11. Do you agree with the government’s proposal for HM Treasury to have the ability to apply “have regards” and to place obligations on the regulators to make rules in relation to specific areas of regulation?**

We agree that HMT should be able to place obligations on the regulators to make rules in relation to specific areas of regulation. As we comment in our answer to question 3, we believe that a greater role for government is warranted in setting the overall policy direction of financial regulation in relation to looming environmental and societal crises.

As stated above, we support the recommendation from the Financial Inclusion Commission and Fair by Design to introduce a cross-cutting “must have regard” to financial inclusion for the FCA. Financial markets do not currently meet the needs of many of those on low incomes or with disabilities. The most vulnerable people are often unable to access necessary products or services because they are defined as “non-standard” and pay extra for services because they are seen as not desirable consumers to serve. This “must have regard” should include a statutory duty to report to Parliament annually on:

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Yours sincerely,

Rachel Haworth

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