

HM Treasury call for proposals for Measuring Success

UK Finance response to consultation from HM Treasury

4 July 2023

Introduction and executive summary

1. UK Finance is the collective voice for the banking and finance industry. Representing around 300 firms, we act to enhance competitiveness, support customers and facilitate innovation. We welcome the opportunity to respond to HM Treasury's (HMT) call for proposals for Measuring Success.¹
2. We **strongly support the new secondary objective to facilitate economic growth and competitiveness** that the Financial Services and Markets Act 2023 assigns to the Prudential Regulation Authority (PRA) and Financial Conduct Authority (FCA) ('the regulators'). The new objective will send a clear signal that the UK is open for business and open to the world. Knowing that competitiveness will be a consideration in the regulators' decision-making will give businesses the confidence to invest for the future, to back UK plc and help the economy to return to higher levels of growth. A thriving, internationally-competitive financial services sector provides hundreds of thousands of high-quality, well-paid jobs, lends to help businesses grow and contributes tax revenue for the public services we all rely on.
3. It is vital that the regulators, like all public bodies, be accountable for meeting their statutory objectives. This is particularly true of an entirely new objective, such as that on growth and competitiveness. Whichever bodies are given this role cannot conduct their scrutiny effectively unless they are provided with information on the actions the regulators have taken to advance their objectives and the resulting outcomes. We therefore **strongly welcome HM Treasury's focus on metrics with which to gauge the regulators' performance.**
4. We respond in detail to the consultation questions and recommend metrics below. In particular, we would draw attention to the following points:
 - a. The regulators have significant influence over growth and competitiveness through the setting of binding rules on firms. They should **estimate and track the 'regulatory burden' imposed by those rules** and be particularly mindful of the volume of new regulatory requirements that they introduce at a given time. It is also **vitaly important that they compare their implementation of international standards against the rest of the world**, accounting for any discrepancies that could affect the competitive position of firms based in the UK. We would also

¹https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1155085/Financial_Services_Regulation_-_Measuring_Success_-_Call_for_Proposals.pdf

welcome more in-depth analysis of the impact of major interventions on the wider economy.

- b. Just as important to the UK's attractiveness to financial services firms is the ease of interacting with the regulators. We **propose that the regulators measure and report on a number of aspects of operational effectiveness**, including the speed with which they process applications for authorisation and approval, the quality of their supervision of firms and the readability of their rulebooks.
5. It is **critical that the government, parliament and regulators be aligned in their understanding of what the new objective means and entails**, and that they articulate this publicly. We welcomed the PRA's September 2022 discussion paper on its approach to policy,² in which it set out and invited feedback on its interpretation of the new objective and how it plans to embed it into its policy-making and supervisory processes. We would strongly encourage the FCA to undertake a similar exercise.
6. Although not within the scope of this consultation, we continue to believe that the Payment Systems Regulator (PSR) should also have a greater focus on growth and competitiveness. We argued throughout the financial services future regulatory framework review for the new secondary objective to be extended to the PSR, and were disappointed that this was not provided for in the Act. We would welcome more detail on the thinking that led the government to this decision, and on any other steps the government is taking to ensure that growth and competitiveness are not excluded from the PSR's thinking.
7. If you have any questions relating to this response, please contact Daniel Wraith, Manager, Strategic Policy, at daniel.wraith@ukfinance.org.uk.

Consultation questions

Q.1 Do you agree with the government's approach to the exercise of the power of direction in Clause 37 of the FSM Bill?

8. We largely agree with the government's proposed approach to exercising the power of direction in (then) clause 37 of the FSM Bill. It is preferable that the power only be used sparingly and as a last resort, in instances where the government believes – but a regulator disagrees – that the provision of particular information is important to measuring and holding that regulator to account for advancing its new objective. We would expect the regulators to provide such information in most circumstances, and to have good reasons for not wanting to voluntarily provide certain information (for instance, if collecting it is disproportionately costly).
9. To minimise the need for the power to be used, we think the regulators should set out, publicly, the information that they will provide voluntarily and how frequently they will publish it. This will give the bodies scrutinising the regulators certainty about the information at their disposal and allow them to plan effectively, while avoiding the need for *ad hoc* information requests using the powers under clause 37.

² <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/discussion-paper/2022/dp422.pdf>

10. When the government consults a regulator over the potential provision of information under this clause, it should do so through a public exchange of letters. If the government thinks there is a good *prima facie* case for a regulator to publish particular information relating to its performance, and the regulator disagrees, the reasons for that disagreement should be made public. Such transparency would allow others to judge the arguments made on both sides and would be in line with the principles of good public governance.

Q.2 What are the key metrics that the FCA and the PRA should publish in relation to their new secondary growth and competitiveness objectives?

11. We have identified several ways in which the regulators affect growth and competitiveness, and have proposed ways of measuring them. We have limited our suggestions to factors that contribute to growth and/or competitiveness that the regulators have influence over. We would urge HMT and the regulators to consider separately the merits of these factors and the proposed metrics for measuring them, as we recognise that there may be better or more practical metrics than those we suggest.
12. The broad ways in which the regulators affect growth and competitiveness are:
 - a. In their capacity as rule-makers, imposing binding (and often costly) requirements on regulated firms, and supervising firms' adherence to them.
 - b. Through their operational effectiveness, particularly where it affects the ease for firms of interacting with them, both at home and overseas.
13. Both of these factors have a bearing on the role of the financial services sector as a driver of economic growth, and on the attractiveness of the UK as a destination for inward investment and as a place to conduct financial services. This is particularly true for firms seeking to grow their businesses and compete in international markets. They also affect the reputations and standing of the regulators themselves, which in turn affect their ability to influence international standards and the trust that consumers and firms (including those considering establishing in the UK) have in them.

Measuring the regulators' impact as rule-makers

14. **Overall burden of regulation.** The main way regulators affect growth and competitiveness is through the setting of binding regulatory requirements on firms. Regulation imposes costs on firms and constraints on their ability to service their customers. These are often justified by the benefits to financial stability, market integrity, competition and consumer protection. Indeed, the UK's reputation for strong and predictable regulation is an asset, as it gives firms the stability and certainty they need to invest and do business with confidence. However, all things being equal, high regulatory costs will have a detrimental effect on the attractiveness of the UK as a jurisdiction in which to provide financial services. Because firms have finite budgets, the cost of complying with regulation affects their ability to contribute to economic growth, by diverting funds that they could otherwise lend to households and businesses, invest in expanding their business, or use to innovate to improve their products and services.
15. We therefore propose that the regulators measure and report on the overall 'burden of regulation' – the costs to firms imposed by their rulebooks. This could consist of an estimate of the annual, fixed costs for firms of complying with the full body of regulation set by each regulator.

16. To account for the significant diversity among regulated firms, we recommend estimating separately the burden of regulation for different representative, stylised regulated firms, including a representative universal bank, a mid-tier/challenger bank, a financial mutual, a specialist mortgage lender, a UK subsidiary of an international wholesale bank and an e-money institution, as well as trading venues, Approved Publication Arrangements, consolidated tape providers, central counterparties and central securities depositories.
17. Reporting these figures annually would allow for comparisons over time and help policy makers and other stakeholders to better understand the impact of regulation on competitiveness and growth. Ideally, it would also allow for comparisons with the burdens of regulation in rival jurisdictions (particularly on key issues such as capital and liquidity requirements), although these would need to be estimated separately.
18. **Regulatory change.** A significant portion of the cost of regulation to firms comes not from ongoing compliance, but from adapting to new regulations. Depending on the nature of a new regulatory requirement, this can involve setting up dedicated project teams (requiring the hiring of new employees and/or diverting current employees from other roles), identifying and making (often significant) changes to IT systems, training staff, performing a ‘gap analysis’ of existing products and services to ensure that they comply with the new regulation, and setting up new systems to monitor compliance. For instance, the FCA estimated that the total one-off direct costs firms may incur to comply with the Consumer Duty to be in the range of £688.6m to £2.4bn.³ Feedback from our members suggest that this estimate was, if anything, conservative.
19. Regulatory change is particularly costly when several regulations are implemented simultaneously. Firms typically rely on the same scarce resources (e.g. staff and consultancy businesses) to adapt to different regulations. If the volume of regulatory change at one time is too great, it can outstrip a firms’ capacity to adapt, compounding the costs. This is an issue even when the individual regulatory initiatives are worthy in and of themselves. This was one of the main reasons for the establishment of the Financial Services Regulatory Initiatives Forum and Regulatory Initiatives Grid (RIG) in 2020.⁴
20. We think that the costs and volume of regulatory change are important determinants of growth and competitiveness, and therefore recommend that the regulators measure the following:
 - a. **The annual cumulative cost of regulatory change.** At its least sophisticated, this could be estimated by each regulator summing all of the one-off costs estimated in the cost-benefit analyses of all regulatory initiatives introduced in a given year.
 - b. **The volume of regulatory change.** Though a crude metric, we think there is merit in each regulator reporting the number of new regulatory initiatives introduced in a given year, categorised by their indicative impact on firms (“high”, “medium” and “low”, as already indicated in the RIG).

³ <https://www.fca.org.uk/publication/consultation/cp21-36.pdf>

⁴ <https://www.fca.org.uk/news/press-releases/financial-services-regulatory-initiatives-forum-launches-grid>

- c. **The differential impact of regulatory change.** We recommend expanding the RIG to provide a view, for each initiatives, on the expected impact for each of the (relevant) types of representative firm as proposed above. The impact of an initiative can vary significantly depending on the type of firm, so this should be reflected in the RIG.
 - d. **Pace of change.** We would welcome reporting on the average time gap between a new requirement being finalised and the date of its entry into force (“implementation date”). Comparing these against the indicative impacts of initiatives would help in judging whether the regulators are being proportionate by allowing longer implementation periods for higher-impact initiatives.
 - e. **The nature of regulatory initiatives.** It would be useful for the regulators to provide information on the number and percentage of new initiatives that are intended to be clarificatory and/or to reduce regulatory costs.
21. Of course, we recognise that the ongoing and one-off costs involved in complying with regulation are complex and therefore difficult to estimate. They vary from one firm to the next, depending, for instance, on business models and whether a firm operates in multiple jurisdictions. The regulators’ ability to estimate the costs relies partly on the quality of the information available to them – some of which can only be provided by firms themselves. Nonetheless, not all firms will easily be able to meet information requests to inform these estimates, particularly because of the significant reporting burden they already face. We would therefore strongly caution against making surveys or information requests to inform these metrics mandatory.
22. Such estimates would not, in themselves, allow one to judge whether the burden of regulation and the volume of regulatory change are at optimal levels, as such judgements can only be made by comparing the costs with the benefits of regulation. However, we believe it is essential that the regulators and stakeholders assess and track the costs generated by regulatory rules and their impact on growth and competitiveness. The regulators are already required to estimate the costs of new proposed regulations, in the cost-benefit analyses that accompany their consultation papers. We think it is equally important to quantify the costs, not just of new regulations, but also of the “stock” of existing rules.
23. **Proportionality in the aggregate.** The ‘proportionality’ principle⁵ is routinely considered in consultations for individual initiatives. However, there is no structured opportunity to step back and consider the cumulative effects of requirements and whether there are opportunities to rationalise them. If an annual estimate of the burden of regulation is considered too burdensome and/or frequent, an alternative could be to require the regulators to conduct periodic assessments of the aggregate costs and benefits of their rulebooks to inform an assessment of whether they remain proportionate.
24. **Implementation of international standards.** Many of the regulations introduced by the regulators – in particular by the PRA – implement international standards. Some, such as the Basel framework and standards on capital requirements, impose significant costs on firms and have a profound influence on the viability of their businesses. UK

⁵ <https://www.legislation.gov.uk/ukpga/2000/8/section/3B/2018-01-03>

regulators, like other national regulators, have discretion in how they choose to implement these standards. As such, the detailed regulatory requirements originating from international standards – and therefore the costs of complying with them – can vary between jurisdictions. Such divergence can have major implications for the relative attractiveness of the UK as a destination for financial services firms.

25. We believe it is critical to quantify any divergences with key rival jurisdictions in the implementation of international standards. We therefore recommend that both regulators publish estimates of the costs to firms of complying with the UK's versions of international standards, as compared to the original international standards, as well as some analysis of divergence with other key jurisdictions. In circumstances where the regulators choose to require firms to apply UK regulation to business outside the UK (rather than, for instance, permitting UK firms to apply host jurisdiction requirements), this should be quantified separately. These estimates could be updated regularly, to reflect any newly-implemented standards and material changes in circumstances; for instance, when the UK finalises its implementation of international standards before other jurisdictions. We believe the regulators should already be conducting such comparative analysis when deciding their approach to implementing international standards, and we would therefore not expect compiling and publishing such information to be unreasonably onerous.
26. **Regulatory Sandboxes.** The FCA's Regulatory Sandbox is an excellent initiative allowing firms to test new products in a safe environment without being immediately subject to the full extent of regulatory requirements. This supports innovation in financial services, ultimately contributing to the growth of the sector and the wider economy, and helps to ensure that the UK maintains its competitive edge internationally.
27. We propose that the FCA produce and publish metrics allowing stakeholders to judge the success of the sandbox. These could include the number of applications and number of firms accepted to the sandbox in a given year, and the percentage of firms accepted into the sandbox that go on to be authorised.
28. **Economic impact.** As a general comment, we would welcome the regulators conducting more in-depth economic analysis of the impact of large regulatory interventions on growth. Major regulatory interventions, such as the Consumer Duty or Basel 3.1 can arguably have a non-negligible (if still relatively small) impact on the UK's gross domestic product (GDP). We would welcome economic analyses of these interventions, similar to those the government conducts in relation to new cross-border trading arrangements. We recognise, however, that these may be more suitably included within individual cost-benefit analyses than reported as an aggregate metric on regulatory performance.
29. We think there is also merit in tracking the broader health of the sector and its contribution to the rest of the economy. Although regulation is not the only determinant, this would help to judge whether the regulators have struck the right balance, in aggregate, between the costs and benefits of their regulatory requirements. In particular:
 - a. The number of authorised firms in UK markets. Although an imperfect indicator, this would help identify trends over time regarding the UK's attractiveness as a place to do financial services business.

- b. The annual volume of inward financial services foreign direct investment (FDI) and the number of new FDI projects. These are good indicators of the attractiveness of the UK.
 - c. The volume of lending and productive finance provided to businesses by regulated firms. Regulation (in particular prudential regulation) is an important factor in the amount of finance provided to businesses, which is one of the main ways in which the sector supports the wider economy.
30. It might be more appropriate for the government to publish these data, for instance, in HM Treasury's and the City of London Corporation's annual 'State of the Sector' report. Indeed, FDI is already tracked in that report, as are other important metrics such as the UK's strength in providing OTC derivatives trading to the world.

Operational effectiveness

31. The regulators' operational effectiveness influences the ease for firms of interacting with the regulators, which in turn affects the attractiveness of the UK as a destination for financial services firms. Key interactions between regulators and firms include applications for approval to carry out various regulated activities, and the ease for firms of understanding the regulations that apply to them.
32. **Approvals and authorisations.** Before a firm can conduct regulated activities, it must be authorised by the FCA and (depending on the nature of the firm) the PRA. Key activities requiring some form of regulatory approval or authorisation include:
- a. 'New firm authorisation' before a firm can conduct regulated activities. These vary depending on the nature of the firm and the services it provides. (This can also include approval of a parent.)
 - b. The appointment of an individual to a senior manager function under the Senior Managers' Regime.
 - c. Approval of new or changed models across the Internal Rating-Based, Internal Models Approach and Internal Model Method regimes.
 - d. Applications for permissions under the Capital Requirements Regulation.
33. We welcome the FCA's and PRA's recognition of the importance of processing applications in a timely manner, and their commitment to making ongoing improvements to ensure world-class standards of operational effectiveness. We recognise that there can be very sound reasons for a regulator to reject an application for authorisation. However, it is not acceptable for firms to have to wait lengthy periods for their applications to be processed and determined. Firms will be less likely to want to establish in the UK if they expect to face such delays, as these create uncertainty, significantly affecting firms' ability to invest and plan for the future.
34. We recommend that the regulators publish metrics on the timeliness with which they process and determine *all* types of applications for approval or authorisation. While we do not have strong views on the exact metrics that they should publish, we believe they should be:

- a. Reported frequently, allowing for the quick identification of trends. Quarterly reporting, which the FCA and PRA already do, is welcome.
 - b. Broken down by types of firm, thereby providing insights into problems relating to particular business models.
35. **Quality of supervision.** An important factor in a firm's decision to be located in a particular jurisdiction is the quality of supervision by the relevant regulator(s). Being supervised by high quality, internationally-respected regulators can enhance a financial institution's standing with its home or host regulators, customers and investor base. It is therefore essential for the UK regulators to be renowned for world-class supervision.
36. Metrics to measure supervisory quality could include: the average number of supervisory 'touch points' with supervised firms; average time between major reviews; supervisory intensity per type of regulated firm. It would also be useful to conduct an independent industry-wide survey of supervised firms to gather feedback on the regulators' supervision. This could be included in the annual surveys that they already conduct.
37. **Readability of rulebooks.** Another operational determinant of competitiveness is the level of difficulty (or ease) for a firm of identifying the rules and guidance that are relevant to it. This is particularly the case for smaller firms (both domestic and international), which typically do not have large legal and compliance teams. We welcome that both the FCA and PRA have acknowledged this as an important factor, and are undertaking initiatives to make their rulebooks more readable and simple. We suggest it may be worth measuring and reporting on the 'readability' of the regulators' rulebooks. We do not have strong views on how this could be achieved. However, one solution could be to include questions on readability in their annual surveys of firms to understand their experience of navigating and interpreting the rulebooks.
38. **Public engagements.** Less obviously, regulators can also affect ease-of-doing business through regular public engagement, including by appearing and speaking at domestic and international conferences. Speeches by senior regulators help firms to understand the underlying intention of new and existing regulations, and give a useful indication of the regulators' priorities and areas of focus, thereby aiding regulatory certainty. There may therefore be merit in the regulators reporting on the number (broken down by category and audience type) of public engagements they have undertaken.