# THE PRINCIPLES OF AN EFFECTIVE REGULATORY-REVIEW MECHANISM FOR FINANCIAL SERVICES

16 February 2021

# 1. INTRODUCTION AND EXECUTIVE SUMMARY

1. This joint paper from UK Finance and Norton Rose Fulbright LLP reflects views of UK Finance and its members on key principles for the development of a regulatory-review process to enhance the accountability of the UK's financial-services regulators. It supports UK Finance's response to HM Treasury's (HMT) phase-II consultation on the future regulatory framework for financial services.

2. The particular focus of this paper is the ability of firms to challenge the decisions of regulators with regard to rule-making and rule-application, outside the context of the formal enforcement process. As noted when the Government consulted on options for reforming regulatory and competition appeals in June 2013:

   *The right of firms to appeal regulatory and competition decisions is central to ensuring robust decision-making and holding regulators to account in the interests of justice. Where firms are materially affected by regulatory decisions, they should have an effective right of challenge if they consider that the regulator has made a mistake or has not acted reasonably.*[1]

3. While it is acknowledged that existing mechanisms may be regarded as facilitating a degree of challenge, certain current features and limitations may be operating as a barrier to access for some firms. Judicial review, the principal way in which market participants are currently able to challenge regulators' decisions, is regarded in practice as neither a viable nor desirable solution for many firms to pursue. In particular:
   - its focus is generally on the process by which decisions are made rather than the merits of those decisions;
   - the risk of jeopardising the supervisory relationship with a regulator by challenging its decision is a key barrier, with a perception among firms that this would have negative repercussions; and
   - the reputational risk from a challenge also acts as a barrier, even where it is considered to be in consumers' interests. This is exacerbated by the relative rarity of such challenges, which means they are inevitably high profile and attract a level of publicity that may be distracting and counter-productive.

4. A more effective review mechanism, addressing these deficiencies, could be a useful tool for both market participants and regulators. It could support the agility and the responsiveness of the UK's regulatory framework and encourage further rigour in regulators' rule-making processes. Indeed, it has the potential to be an important factor in differentiating the UK from other jurisdictions and enhancing its competitiveness as a destination for banking and finance firms.

5. We have identified seven key principles that might best inform consideration of such a mechanism with the overarching aim of engendering confidence not only in the process itself but in the wider UK regulatory framework. These are set out in section 6.

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1 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/229758/bis-13-876-regulatory-and-competition-appeals-revised.pdf.

# 2. THE CONTEXT FOR THIS PAPER

6. Through its phase-II consultation, HMT proposes to substantially revise the future regulatory framework, remaining faithful to the intended outcomes of the model created by the Financial Services and Markets Act 2000 (FSMA)[2] and recognising this will involve the delegation of a "very substantial level of policy responsibility to the UK financial services regulators." It aims to deliver an agile regulatory regime that is coherent, internationally respected and more user-friendly and will address potential issues created by onshoring.

7. The consultation also reviews the arrangements for accountability, scrutiny and public engagement in financial-services policy-making and regulation. It focuses on two key aspects: Parliamentary scrutiny of the work performed by regulators and engagement with regulators by the full range of public stakeholders, including the industry. It is clear from the scope of possible options under consideration that the population of authorised firms can make a valuable contribution in this regard, enhancing the effectiveness of the regulators' rulebooks and the agility of the framework as a whole given the pace of change.

8. This paper is intended to address one particular element of these future arrangements for increased stakeholder engagement: the ability of firms to challenge the decisions of regulators in connection with their rule-making powers and the application of those rules to firms, outside the context of the formal enforcement process. For the purposes of this paper, we consider as out of scope formal decisions of the regulators imposing supervisory measures on firms such as supervisory notices made by the Prudential Regulation Authority (PRA) or the Financial Conduct Authority (FCA), for which there are established challenge mechanisms.

9. This paper therefore seeks to identify the principles of an effective process through which affected parties, including market participants, can seek a review in respect of or challenge the following.

10. It is accepted that the current legal and regulatory framework provides several mechanisms through which firms can influence policy development by regulators and several different avenues to interact with regulators to advance concerns about the imposition of new rules (through formal consultations) or the application of existing rules (through the work of statutory panels).

2 https://www.legislation.gov.uk/ukpga/2000/8/contents.

11. The principal way in which firms can currently challenge regulators in relation to these matters is through a formal judicial review of decisions made in the course of the exercise of their statutory powers. As set out in section 4, there are a number of features of judicial review in a financial-services context that may be the reason for its having been used very infrequently in recent years.

12. An effective and appropriately used regulatory-review mechanism is clearly desirable, not only for firms but also for consumers, as poor regulation can hamper competition and stifle innovation. It is not the purpose of this paper to put forward a blueprint for such a review mechanism but instead to explore the potential challenges associated with current structures and identify the principles to which regard should be had in the design of such a mechanism. A new review mechanism could be required to deliver an effective appeals process for in-scope decisions so as to better support the objectives of a dynamic and responsive regulatory framework delivering good outcomes. Equally, innovations to current structures could be made to deliver the principles of an effective review mechanism identified in this paper.

13. It is acknowledged that there are important threshold questions to answer in due course concerning the formulation of any review mechanism. In particular, it will be important to consider the parameters of the mechanism, its jurisdiction and the scope of rules in respect of which it may receive a reference. There is also a range of remedies that any mechanism might afford to market participants and regulators, from an appellate body with powers to vary or remove rules or guidance at one end of the spectrum to a body composed of expert members capable of issuing opinions only at the other. UK Finance looks forward to discussing these considerations as HMT formulates detailed proposals for a second consultation later this year.

14. In considering the principles that should guide the consideration of a review mechanism for new and existing regulatory rules identified above, it is also acknowledged that such a mechanism will form one part of the overall regulatory framework and interact with the other structures and mechanisms through which the regulators are held accountable and engage with firms both during and following policy-making processes. We expand on these relationships and co-dependencies in section 6.

# 3. METHODOLOGY

15. The work conducted to inform the matters set out in this paper included undertaking desktop research into existing financial-services regulatory-review mechanisms in the UK. After identifying a range of observed practices, structured discussions took place with a range of practitioners with regard to other UK sectors, such as water, telecommunications and energy, and with regard to financial-services frameworks in other jurisdictions, including Canada, Hong Kong, Italy, the Netherlands, and the United States. These conversations, in addition to numerous discussions involving UK Finance and its members, formed the basis of this paper. As such, this paper does not contain a full analysis of the law, nor does it constitute an opinion of any Norton Rose Fulbright entity on the points of law or other matters discussed.

# 4. THE CURRENT SYSTEM

## INTRODUCTION

16. To consider a more effective mechanism by which firms can review the regulatory rules to which they are subject, it is useful to set out the wider context within which such a system would sit. This is because the development of the principles to which regard should be had in developing such a mechanism is largely dependent on the role it is intended to serve, and this in turn is informed by evaluating the current arrangements and any gap that is perceived to exist. As set out earlier in this paper, the shape of any mechanism by which firms can review certain rules to which they are subject will be determined by the purpose and effectiveness of these wider processes and arrangements.

17. The PRA and the FCA are established through FSMA, as amended. FSMA sets the statutory framework within which the PRA and the FCA operate and from which they obtain their powers and duties. The Payment Systems Regulator (PSR) was established by the Financial Services (Banking Reform) Act 2013 (FSBRA).[3]

18. Pursuant to FSMA, the PRA has a single, general objective to promote the safety and soundness of PRA-authorised persons. The FCA has a single strategic objective to ensure relevant markets function well. This is supplemented by three operational objectives: the consumer-protection objective, the integrity objective and the competition objective.

19. FSMA is the framework legislation that establishes the system of regulation for the very significant majority of regulated financial-services firms in the UK such as banks, insurers, investment firms and non-bank consumer lenders. UK-incorporated banks and insurers are subject to regulation by both the PRA and the FCA, whilst the remaining population of firms authorised pursuant to FSMA are solo-regulated by the FCA. The FCA also has responsibility for licensing and supervising payment institutions pursuant to the Payment Services Regulations 2017[4] and e-money issuers pursuant to the Electronic Money Regulations 2011.[5]

20. The PSR regulates payment systems designated by HMT. Eight payment systems are currently designated for these purposes, including BACS, CHAPS, Faster Payments and LINK. The PSR has three statutory objectives:
    - to ensure payment systems are operated and developed in a way that considers and promotes the interests of service-users;
    - to promote effective competition in the markets for payment systems and services provided by payments systems, in the interest of service-users; and
    - to promote the development of, and innovation in, payment systems, particularly the infrastructure used to operate those systems, in the interest of service-users.

3 https://www.legislation.gov.uk/ukpga/2013/33/contents.

4 https://www.legislation.gov.uk/uksi/2017/752/contents.

5 https://www.legislation.gov.uk/uksi/2011/99/contents.

21. The statutory frameworks established by FSMA and FSBRA are quite different, and consequently the structure of regulation and the approach of the PRA and the FCA are quite different from that of the PSR. For example, the PRA Rulebook and the FCA Handbook contain very detailed, granular rules and guidance governing the conduct of a wide range of regulated activities. The PSR has a slightly different regulatory toolkit that reflects the different structure of the market it regulates and its status as an economic regulator. The PSR's toolkit includes powers to make rules (known as general directions and requirements) and issue written guidance but also includes powers to make decisions (known as specific directions and requirements). Perhaps the clearest difference in substance is the PSR's power to issue specific directions and requirements that relate to individual, named industry participants but, in contrast to supervisory measures of the PRA and the FCA, these are subject to wider engagement by persons other than the firm to which the direction or requirements are to be applied and may be formally consulted on.

22. The PRA and FCA rule-making procedures provide some opportunity for firms and other stakeholders to feed into their development and provide scrutiny. The experience of practitioners in other jurisdictions has tended to suggest that the greater the opportunity to meaningfully influence rules development by financial-services regulators so they account for the idiosyncrasies of firms and their various business models, the less likely firms may be to seek to obtain reviews of those rules and their application. Nonetheless, the judgment and decision-making is necessarily reserved to regulators, which will consider points made in light of their policy priorities, statutory objectives and wider legislative responsibilities.

23. It is not the aim of this paper to provide a comprehensive exposition or evaluation of the current regulatory framework and the options presently available to firms with regard to in-scope regulatory rule-making and rule application. However, to provide context to what follows, we set out below an overview on some of the different mechanisms currently available.

## CONSULTATION

### PRA AND FCA

24. FSMA generally requires the PRA and the FCA to consult stakeholders on rule proposals and certain types of FCA guidance.[6] The consultation process for making new rules involves publishing a draft of proposals to bring them to the attention of the public and providing a specified time for feedback to be given. The draft rules must be accompanied by a cost/benefit analysis, an explanation of their purpose and an explanation of the regulator's reasons for believing that making the proposed rules is compatible with its duties and has regard to its regulatory principles. Before making final rules, the PRA and the FCA are required to give an explanation of the feedback received during the consultation and how it has been taken into account.

6 Section 138I sets out the FCA consultation process for making rules. Section 138J sets out the PRA consultation process for making rules. These statutory provisions require that as well as consultation with the public, the PRA and the FCA must consult each other on rule proposals. The FCA has the flexibility not to follow these requirements if a delay would prejudice the interests of consumers, and the PRA has the same flexibility if a delay might be prejudicial to the safety and soundness of PRA-authorised firms.

25. The FCA is also required to consult the public when it proposes to give guidance to FCA-regulated persons generally or a class of FCA-regulated persons in relation to rules to which they are subject and in certain other situations. In such cases, the FCA is required to publish a draft of the proposed guidance and provide the opportunity for feedback to be given during a specified timeframe. It must then take into account the feedback received before issuing the guidance. While it is the case that both the PRA and the FCA give informal guidance to firms through speeches and other communications, challenge and recourse in relation to such guidance is outside the scope of the review process that is the subject of this paper.

26. The extent to which the regulators are incentivised to take account of feedback from firms in the consultation phase can be viewed as related to the effectiveness of the mechanisms available to challenge any rules subsequently implemented. If the regulators perceive that options for challenge are limited, the incentive for them to make changes to proposals in the light of comments received as part of the consultation exercise may be reduced.

## PSR

27. The PSR only uses its regulatory powers in relation to participants in the payment systems that have been designated by HMT. For these purposes, participants include payment-systems operators, infrastructure providers and payment-service providers (i.e. any person who provides services to persons who are not participants in the system for the purposes of enabling the transfer of funds using the designated payment system).

28. Under FSBRA, the PSR has the power to take:
    - regulatory action by way of making directions and imposing requirements; and
    - enforcement action for non-compliance.

29. Directions and requirements can be specific or general. Specific directions and requirements are addressed only to certain participants in regulated payment systems or participants of a specified description (e.g. a named operator of a payment system). General directions are addressed to whole classes of participants (e.g. all merchant acquirers). Failures to comply with the PSR's directions and requirements are enforced by way of its enforcement powers.

30. FSBRA provides that when the PSR exercises any of its general functions (e.g. giving general directions or guidance and determining its general policy principles), it must have regard to eight regulatory principles, which include exercising its functions as transparently as possible.

31. Before giving a general direction or imposing a general rule requirement, the PSR must consult the Bank of England (BoE), the PRA and the FCA about the need for, and potential impact of, the proposed regulatory action. The PSR also generally engages in public consultation, but it is not required to publish a draft direction or rule requirement for consultation if it considers delay would be prejudicial to the interests of service users.

## STATUTORY PANELS

32. There is also a system of independent panels with which the PRA and the FCA may consult from an early stage in policy development. Generally, the PRA and the FCA are expected to consult with these independent panels on all major policy and regulatory interventions. The panels draw on the experience and views of their members and are intended to provide insight, advice and challenge across the regulators' policy-making functions. For example, the FCA works with four independent statutory panels, including the Practitioner Panel (which represents the interests of regulated firms) and the Smaller Business Practitioner Panel (which represents the interests of smaller regulated firms). The FCA is required to consult these panels on the impact of its work and to consider their views when developing its policies and deciding and implementing other regulatory interventions. The panels are intended to play a role in both advising and challenging the FCA and provide expertise in identifying risks to the market and consumers. However, membership of the panels is necessarily restricted.

33. The PRA works with a statutory industry practitioner panel that represents the interests of firms. The panel is consulted as part of the PRA's arrangements for effective consultation with PRA-authorised persons on the extent to which its general policies and practices are consistent with its general duties. The panel reviews the impact of the PRA's policies insofar as they affect regulated firms, individuals and markets, and it responds and provides feedback to the PRA at an appropriate stage of the policy-development process. As part of the public-consultation process, the PRA ensures effective consultation with the panel and considers any representations it makes.

## MODIFICATIONS AND WAIVERS OF PRA AND FCA RULES

34. Under section 138A of FSMA, firms may apply to the PRA or the FCA for rules that apply to them to be modified or waived. A waiver means a firm does not have to comply with the rule at all. A modification allows a firm to comply with an amended rule that better fits its circumstances. Theoretically any PRA or FCA rule can be waived or modified, with limited exclusions (e.g. rules of conduct made by either regulator under section 64A of FSMA).

35. The PRA and the FCA cannot give a modification or a waiver unless they are satisfied that both the following statutory conditions are met:
    - compliance by the firm with the rules, or with the rules as unmodified, would be unduly burdensome or fail to achieve the purpose for which they were made; and
    - the waiver or modification would not adversely affect the advancement of any of their objectives.

36. Even if these conditions are satisfied, the regulator takes into account other relevant factors when deciding whether to grant the modification or waiver on the merits of the case.

37. The ability of individual firms to apply for a waiver or modification of particular rules is a valuable part of the overall framework within which regulators operate. However, when measured against the principles that might guide the development of a review mechanism, it may be regarded as falling short of the mark. Most clearly, the decision-maker in connection with any waiver or modification remains the regulator. In addition, transparency of decisions could be improved: waivers and modifications granted to particular firms are relatively inaccessible to other firms that might wish to be made aware of them and there is little information available on the circumstances in which regulators refuse requests that might help to inform the approach of other firms with similar issues or concerns.

## PERIODIC REVIEW

38. The principle of reviewing regulation after it has been in operation has been embedded in certain recent legislative initiatives. HMT has set out in the phase-II consultation that it considers more routine use of such provisions might be required to provide enhanced scrutiny of the regulators' exercise of new powers, although it accepts the regulators use reviews in some areas. The consultation also acknowledges the existing process for reviewing regulatory rules is limited and could be improved (e.g. to include more systematic review of rules or make use of independent, expert reviewers to carry out more significant reviews).

## JUDICIAL REVIEW

39. Judicial review is the main way in which the courts supervise bodies exercising public functions to ensure they act lawfully and fairly. It is a mechanism available to firms to challenge the decisions of financial-services regulators. While decisions of the PSR to give general directions or impose general rule requirements may only be judicially reviewed by the courts, any persons affected by decisions to give specific directions or impose specific rule requirements can appeal to the Competition Appeals Tribunal (CAT). In determining the appeal, the CAT must apply the same principles that would be applied by a court on an application for judicial review.

40. Judicial review can be used by individuals and organisations to (effectively) challenge a regulator on the way in which a decision has been reached. While this might, depending on the facts, include policy-related activities, in very broad terms it is necessary to identify a "decision" in respect of which the applicant is seeking judicial review. Firms may consider the identification of such a decision more challenging in the context of the general application of the rules to them by regulator(s) (either individually or collectively).

41. There are three main grounds of judicial review: illegality, procedural unfairness and irrationality. A decision can be overturned on the ground of illegality if the decision-maker did not have the legal power to make that decision, so, in theory, a firm could challenge a regulator's rule-making on the grounds it exceeded its statutory powers when making such a rule. A decision can be overturned on the ground of irrationality if it is so unreasonable that no reasonable person, acting reasonably, could have made it. In theory, a firm could also challenge a regulator's rule-making on such grounds, but the standard to meet is generally considered to be high, and it is rare for courts to grant judicial review on such grounds.

42. Decisions can also be challenged on the ground of a legitimate expectation, either procedural or substantive, which arose as a result of a statement or conduct by a public authority that it would act in a particular way. A legitimate expectation, will, however only arise in a small number of cases, particularly given the need for public authorities to be able to change their policies.

43. A number of features of judicial review mean in practice it risks being regarded as neither a viable nor a desirable solution for firms to pursue in connection with the development or application of rules and guidance by regulators. It is therefore rare, in particular in relation to challenging rules or the application of rules; indeed, we are not aware of any authorised firm having successfully challenged a decision of the PRA, the FCA or the PSR by means of judicial review in terms of ultimately achieving the remedy sought. A number of potential issues with judicial review have been raised:
    - narrow and difficult grounds. The focus of judicial review is generally on the process by which decisions are made rather than the merits of those decisions. Ultra vires challenges of the FCA are particularly difficult because its statutory objectives and powers are wide;
    - cost of challenges. The cost of bringing a judicial review is considered relatively high, and this is a barrier that prevent firms from challenging decisions. In addition to its own costs exposure, as a general rule in judicial-review proceedings, the unsuccessful party is required to pay the costs of the successful party;
    - length of process. Judicial-review cases can be relatively lengthy, and timings are dependent on the availability of the relevant court;
    - the supervisory relationship. The risk of jeopardising the supervisory relationship with a regulator by challenging its decision appears to be a key barrier to firms bringing judicial-review proceedings. There is evidence of a perception by certain firms that challenging a regulatory decision by means of judicial review may well have negative repercussions for them in future. This also appears to be a key concern in other jurisdictions, but such a disincentive does not seem to arise to the same extent in other sectors where the regulator does not supervise firms and/or take enforcement action to the same degree;
    - limited time for challenge. Firms must apply for judicial review within three months of the date when grounds for the application first arose. There are circumstances in which issues with a particular rule may only come to light months or even years after that rule has been introduced (e.g. if the regulator applied the rule to a situation none of the parties knew was going to arise). In these instances, firms may face particular challenges in identifying or provoking a decision that is susceptible to judicial review;
    - limited remedy. Even if a firm is successful in a judicial-review challenge, the fact that this may not ultimately produce the outcome a firm desires acts as a disincentive. Commonly a quashing order is sought, with an order requiring the public body to retake the decision in question taking into account the judgment of the court. This may not necessarily result in a different decision being made; and
    - reputational risk. The reputational risk from a challenge may also act as a barrier to seeking judicial review, even where the challenge may be considered to be in the interests of consumers. At present, the relative rarity of such challenges means any that are made will inevitably be high profile, and the firm bringing them may face a distracting and counterproductive level of publicity. If regulatory decisions were challenged more frequently, it might become more publicly acceptable to do so.

44. UK Finance summarised these concerns in its October 2020 response to the call for evidence issued by the Independent Review of Administrative Law Panel.[7]

## COMPLAINTS

45. The PRA and the FCA are required to maintain a complaints scheme to investigate complaints about the exercise of, or failure to exercise, any of their relevant functions. These exclude their legislative functions, including making rules and issuing statements and guidance. As a consequence, firms cannot "complain" about rules or guidance made by the PRA and the FCA.

46. The scope of the scheme notably allows complaints where the regulators have acted or failed to act regarding:
    - mistakes and lack of care;
    - unreasonable delay;
    - unprofessional behaviour;
    - bias; and
    - lack of integrity.

## FINANCIAL OMBUDSMAN SERVICE

47. Complaints about firms (as opposed to the decisions of regulators, with which this paper is primarily concerned) may be made to the Financial Ombudsman Service (FOS), which has a wide power to determine cases by reference to what is, in its opinion, fair and reasonable in all the circumstances of the case. Final determinations by the FOS are binding on firms but not on the complainant. One concern that has arisen is that the FOS may make a decision in relation to the application of a rule on this fair and reasonable basis in circumstances where the options for challenge by firms are very limited.

## CONCLUSIONS

48. The processes and mechanisms described above afford market participants valuable opportunities to influence policy development and rule-making by the regulators. However, there is a limit to the extent to which they provide a mechanism for participants to challenge or otherwise obtain a review of a rule once it has been made or begun to apply to a firm.

49. A more effective mechanism could be a useful tool for both market participants and regulators. It could support the agility of the UK's regulatory framework, further calibrating rules to support stated policy objectives and doing so in a timely manner to ensure rules are as effective as possible.

7 https://www.ukfinance.org.uk/policy-and-guidance/consultation-responses/uk-finance-response-independent-review-administrative-law-call-evidence.

# 5. POINTS OF NOTE FROM OTHER JURISDICTIONS AND SECTORS

50. Although we have not comprehensively surveyed other potentially relevant jurisdictions and sectors, and mapping across into the UK's financial-services regime is potentially problematic, we make the following comments on the basis of our high-level discussions.
    - **Grounds of challenge**. The ability to challenge rule-making and rule application by regulators varies significantly depending on the jurisdiction and sector. We identified a very wide range, from extremely limited options in certain jurisdictions to a much more permissive regime in other sectors, leading potentially to overuse and saturation.
    - **Relationship tensions**. The tension between any challenge to regulatory decisions and any ongoing supervisory relationship appears to be a significant factor in a number of other jurisdictions. Put simply, firms do not want to be seen to "rock the boat" where they are dependent on the regulator's goodwill or good opinion in terms of their fitness and propriety and/or under an obligation to cooperate, particularly in the absence of clear communication from regulators that they welcome challenge and will not regard it as a "black mark" against the challenging firm.
    - **Regulatory deference**. In some jurisdictions, there are indications that the courts have historically tended to defer to regulatory bodies in the context of challenges to regulatory decisions on the basis that regulators are better placed to make those decisions. Such deference may have the effect of undermining confidence in the relevant challenge mechanism.
    - **Length of, and timetable for, appeals.** The length of any challenge process and the perception of how long is too long also varies across sectors and jurisdictions and may depend on the extent to which other, more time-limited mechanisms are available and the extent to which it is possible to suspend the application of a decision pending the outcome of a challenge. A fixed timetable (subject only to appropriate exceptions) may provide greater certainty for those involved.

51. In relation to grounds of challenge, our attention has been drawn in particular to the Australian Administrative Decisions (Judicial Review) Act 1977,[8] which provides for appeals by a person or other parties affected by certain administrative decisions of an Australian federal department or agency of an Australian federal department on the following grounds:
    - a breach of the rules of natural justice occurred in connection with the making of the decision;
    - procedures that were required by law to be observed in connection with the making of the decision were not observed;
    - the person who purported to make the decision did not have jurisdiction to make the decision;
    - the decision was not authorised by the enactment in pursuance of which it was purported to be made;

8 https://www.legislation.gov.au/Details/C2017C00238.

- the making of the decision was an improper exercise of the power conferred by the enactment in pursuance of which it was purported to be made;
- the decision involved an error of law, whether or not the error appeared on the record of the decision;
- the decision was induced or affected by fraud;
- there was no evidence or other material to justify the making of the decision; and
- the decision was otherwise contrary to law.

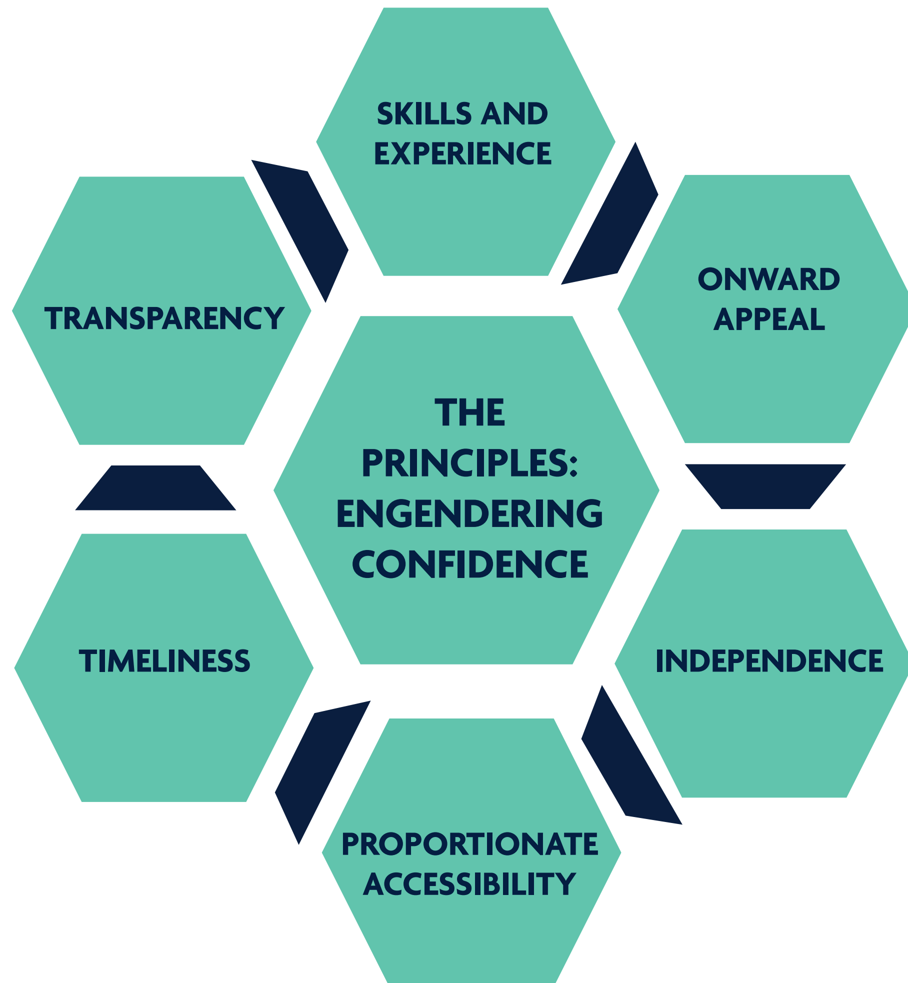
52. We also understand there is precedent in Australia for the Australian Appeals Tribunal (AAT) to consider the application of regulator policy when deciding on a case pertaining to regulatory matters. This has been demonstrated in particular by a case in which the AAT considered the application of a policy statement made by the Australian Securities and Investments Commission (ASIC) and, in its judgement, substituted its own decision for that of ASIC. This decision prompted ASIC to review and amend the policy having regard to its practical application. The precedent appears in a particular setting relating to ASIC's interpretation of certain legislative provisions concerning the registration of liquidators, but it may nonetheless prove a helpful example of an appeal that effectively resulted in a change of the regulator's policy approach in a particular area.

53. Overall, our work to date has not identified the existence of a comprehensive process in another jurisdiction or sector that could obviously form the model for a new regulatory-review mechanism for financial services in the UK. Further, as noted above, a number of correspondents in other jurisdictions and sectors shared similar frustrations with current procedures as those described in this paper with respect to the UK's regulatory framework. Consequently, although this would need to be looked into more widely and in more detail, there may be scope for the UK to lead the way if it can introduce a well-respected and effective regulatory-review mechanism in the financial-services sector.

# 6. PRINCIPLES TO INFORM CONSIDERATION OF AN EFFECTIVE REVIEW MECHANISM

54. Through our research and discussions, a number of high-level principles have emerged to inform consideration of an effective review mechanism for the rule-making and rule-application decisions of financial-services regulators. These take into account some of the views expressed concerning the effectiveness of judicial review for such purposes. Before describing those principles, we make the following general comments.
    - Each principle cannot be viewed in isolation, and its individual significance depends on a number of factors including the view taken on prioritisation of the principles and the extent to which other, higher-priority principles are satisfied.
    - There may be tension between certain individual principles and a limit to the extent to which any particular mechanism can embody them all to the same degree. Consideration of any mechanism would need to take into account the overall balance between all the principles.
    - Certain principles may be more or less relevant for particular types of challenge or potential challengers. For this reason, it may be that a sole mechanism or one-size-fits-all approach is not appropriate and both formal and informal routes of challenge or review should be explored, each of which may have a different balance of the principles to cater for different circumstances.
    - A review process does not exist in isolation and should be viewed in the context of the wider regulatory framework, taking into account the specific features of the UK's financial-services sector. For example, any process of review or challenge should complement an effective consultation and enforcement process. An ineffective process puts pressure on these other elements of the regulatory landscape. Indeed, the level of concern regarding the adequacy of a mechanism for challenging rules appears to be directly correlated with the degree of confidence in the consultation process prior to the implementation of new rules. In this regard, there are clear dangers in seeking to identify and transplant wholesale a process from another jurisdiction or sector.

55. With these factors in mind, we set out below the key principles we have identified as being most apposite for informing the consideration of an effective review mechanism and the extent to which it is possible to give greater effect to these principles within a new or adapted mechanism than may currently be the case. In setting out the principles, we are not seeking to be prescriptive but instead to set out elements to which consideration might be given as part of the policy-making process.




## PRINCIPLE 1: ENGENDERING CONFIDENCE

56. Consideration of an effective review process should take into account the degree to which it will engender confidence, not only in the process itself but also in the wider regulatory framework, to the wider benefit of the UK. However, as the Government noted in its June 2013 consultation on options for reforming regulatory and competition appeals:

    *There is a balance to be struck between enabling interested parties to have appropriate rights of appeal and ensuring that the system as a whole functions efficiently and enables the regulator or authority to take decisions in an efficient and timely way, to achieve its duties. A well designed and proportionate appeals process can contribute to the quality, predictability and certainty of the regulatory framework, by exposing regulatory decisions to additional scrutiny and, if necessary, correction. Conversely a poorly designed process can lead to lengthy delays and regulatory uncertainty.*

57. In terms of engendering confidence, while enabling merits-based challenges to the widest possible range of regulatory decisions may be viewed by some as promoting the highest level of confidence in any mechanism, this must be weighed against a potential increase in the length and cost of challenges that might arise from permitting widescale review of all aspects of decisions, which could hinder effective regulation.

58. Achieving a high degree of confidence may be viewed as a central principle that is to some degree dependent on the extent to which other principles are accommodated and seen and experienced as being met.

## PRINCIPLE 2: SKILLS AND EXPERIENCE

59. Confidence will be enhanced through the review mechanism having the requisite skills and experience to provide effective challenge to regulatory decisions and by establishing clear grounds for review and decision-making criteria (to which careful consideration will need to be given).

60. The design of the review mechanism will also be informed by consideration of the extent to which it may be required to effectively overrule the regulator. It would need to be both confident and capable of engendering confidence.

## PRINCIPLE 3: ONWARD APPEAL

61. Confidence in the mechanism may also be affected by the availability and extent of any onward appeal to another decision-maker at a more senior level, and so consideration should be given to how any mechanism fits within the overall justice system.

## PRINCIPLE 4: INDEPENDENCE

62. Consideration of an effective review mechanism should take into account the need for it to be demonstrably free of any conflicts of interest, perceived or actual, so that its decisions are not tainted by factors such as bias and firms have confidence in the process as well as the outcome the process delivers.

63. In the context of the financial-services industry, a process allowing review of certain regulatory decisions by an independent body could also help to address any potential tension that arises from the nature of the supervisory relationship between firms and regulators.

64. While a process involving an "in-house" mechanism may score highly in terms of accessibility and timeliness (discussed below), it may suffer from at least a perception of a lack of independence and increased risk of damage to the supervisory relationship. (For example, in an enforcement context, some market participants may have historically perceived a referral to the Upper Tribunal as preferable to making representations to the FCA's Regulatory Decisions Committee.)

## PRINCIPLE 5: PROPORTIONATE ACCESSIBILITY

65. Consideration of an effective review process should take into account the degree to which it will be accessible to all firms, not just those falling within a particular category (e.g. those with the greatest resources). It should also have regard to minimising inappropriate barriers to access while recognising some level of disincentive may be appropriate to avoid a disproportionate level of potentially unmeritorious challenge that could lead to saturation, delay and increased cost and constitute a drain on regulatory resource to the detriment of the wider financial industry.

66. Potential barriers to access that have been raised in our discussions include:
    - a narrow scope in terms of decisions that can be challenged, the grounds on which a challenge can be brought or the type of person who can bring a challenge;
    - a wide scope in terms of regulators' powers/discretion (and consequent impact on ability to bring an ultra vires challenge);
    - cost and exposure to adverse costs;
    - the nature of the supervisory relationship, which is less of a factor in other sectors, and the extent of the powers available to supervisors and potential impact of these on those whom they regulate;
    - the nature of the remedies available and likelihood of securing an improved outcome; and
    - competition concerns for firms considering collaborating or joining forced with peers for the purpose of challenging regulatory decisions.

67. Consideration of any mechanism will need to take into account the extent to which it is possible and appropriate to minimise these barriers.

68. In meeting the principle of accessibility, it may be appropriate to consider including a mechanism to challenge particularly important issues by representative bodies. An example of this on the consumer side is the super-complaints regime under section 11 of the Enterprise Act 2002,[9] which allows a designated consumer body to make a complaint to the Competition and Markets Authority (CMA) that certain features of a market are or appear to be significantly harming the interests of consumers and requires the CMA to publish a response within 90 days stating how it proposes to deal with the complaint.

## PRINCIPLE 6: TIMELINESS

69. Consideration of an effective review process should take into account the need to deliver a decision within a reasonable period of time. Long delays act as a disincentive to appeals, creating a high management time cost in addition to a high monetary cost. They also create regulatory uncertainty.

70. Timeliness is an important principle in view of the potentially significant impact that regulatory rule changes can have on firms and their business models. Consideration should be given to measures that minimise the potentially adverse impact of rules or rule application while being subject to review. Given the recognised need for the regulatory framework to respond nimbly to the fast pace of change in the financial-services sector, it is important for challenge mechanisms through which regulators' in-scope decisions are reviewed to be equally equipped to deliver findings in a timely manner.

9 https://www.legislation.gov.uk/ukpga/2002/40/section/11.

71. While timeliness and cost are clearly correlated, there is also a tension between timeliness and quality of decision-making/confidence. For example, a simpler and shorter process may give rise to concerns regarding matters such as the sufficiency of the consideration of the issues and evidence and the fairness of the process. On the other hand, as noted above, key barriers to entry to the current process include a perception of high cost.

### PRINCIPLE 7: TRANSPARENCY

72. Any consideration of an effective review process should take into account the appropriate level of transparency required to meet its objectives, including the extent to which detailed decisions should be published and whether any degree of anonymity should be permitted.