Brooklyn Journal of International Law

Volume 28
Issue 2
SYMPOSIUM: Do Financial Supermarkets Need Super Regulators?

Article 2

2003

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Recommended Citation

Eilis Ferran, *Examining the United Kingdom's Experience in Adopting the Single Financial Regulator Model*, 28 Brook. J. Int'l L. (2003).
Available at: https://brooklynworks.brooklaw.edu/bjil/vol28/iss2/2

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EXAMINING THE UNITED KINGDOM'S EXPERIENCE IN ADOPTING THE SINGLE FINANCIAL REGULATOR MODEL

Eilís Ferran[*]

I. INTRODUCTION

In major markets around the world there has been a growing trend towards unification of responsibility for the regulation of banks, securities markets, and insurance companies.[1] Countries where a unified agency has recently assumed regulatory responsibilities for all financial institutions include the United Kingdom ("U.K."), Japan, and Korea.[2] In May 2002, Germany established a single financial regulator.[3] Ireland and Switzerland are also in the process of moving towards the single regulator model.[4] The increasing popularity of the single regulator model in Europe should be viewed against the background

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I am grateful for comments from Kern Alexander, Chris Bates, Rod Cantrill, James Fanto, Niamh Moloney, Tolek Petch, and participants at the Brooklyn Law School Symposium *Do Financial Supermarkets Need Super Regulators?,* September 20, 2002. This Article reflects the position as of September 2002, but with occasional references to more recent material.

1. Kenneth K. Mwenda & Alex Fleming, International Developments in the Organizational Structure of Financial Services Supervision, Paper Presented at the World Bank Financial Sector Vice-Presidency Seminar, at 1 (Sept. 20, 2001), *available at* http://lnweb18.worldbank.org.

2. NEIL COURTIS, HOW COUNTRIES SUPERVISE THEIR BANKS, INSURERS AND SECURITIES MARKETS xiii (2d ed. 2002). Although Courtis classifies Australia as a single regulator country, its approach is distinctive in that it divides between two agencies responsibility for prudential regulation (Australian Prudential Regulation Authority) and for conduct of business (Australian Securities and Investment Commission). The Netherlands is considering the adoption of a similar cross-sectoral, objective-driven model. *See* Annet Jonk et al., *A New Dutch Model,* 6 FIN. REG. 35 (2001).

3. Hugh Williamson, *Boost for Germany's Financial Role: Federal Agency Three Regulatory Bodies to be Merged into Single Authority from May 1*, FIN. TIMES, Apr. 3, 2002, at 12.

4. Howard Davies, *Foreword — The Importance of Getting Supervision Right*, *in* COURTIS, *supra* note 2, at xi.

of the policy objectives of the European Union ("EU") in the establishment of a fully integrated financial market. The convergence of national regulatory structures of member states has been identified as a necessary step for the achievement of that good.[5]

Scandinavian countries led the way in establishing unitary financial regulators.[6] Norway was the first country to establish an integrated regulatory agency in 1986, followed by Denmark in 1988, and Sweden in 1991.[7] However, as the first major international financial center to adopt the single regulator model,[8] changes made in the U.K. have attracted particular international attention. For countries that are major financial centers,[9] an important argument in favor of the single regulator model is that it matches the nature of their markets — in that the emergence of financial "supermarkets" and increased use of sophisticated techniques, such as securitization and derivatives trading, have broken down the traditional sectoral distinctions.[10] The trend towards the blurring of sectoral boundaries intensified during the 1990s.[11] The overhaul of the U.K.'s regulatory structure thus largely coincided with a period in which

5. THE COMMITTEE OF WISE MEN, FINAL REPORT OF THE COMMITTEE OF WISE MEN ON THE REGULATION OF EUROPEAN SECURITIES MARKETS 42 (2001), *available at* http://europa.eu.int/comm/internal_market/en/finances/general/lamfalussyen.pdf.

6. Giorgio Di Giorgio & Carmine Di Noia, *Financial Market Regulation and Supervision: How Many Peaks for the Euro Area?,* 28 BROOK. J. INT'L L. 463, 469–78 (2002) (providing a general survey of European regulatory frameworks).

7. MICHAEL TAYLOR & ALEX FLEMING, INTEGRATED FINANCIAL SUPERVISION: LESSONS FROM NORTHERN EUROPEAN EXPERIENCE 4–7 (World Bank, Working Paper No. 2223, 1999), *available at* http://econ.worldbank.org/files/950_wps2223.pdf. Banking supervision has never been a central bank function in these countries so the Scandinavian experience has little guidance to offer on this aspect of regulatory consolidation.

8. CLIVE BRIAULT, THE RATIONALE FOR A SINGLE NATIONAL FINANCIAL SERVICES REGULATOR 5 (FSA, Occasional Paper 2, 1999), *available at* http://www.fsa.gov.uk/pubs/occpapers/index-1999.html [hereinafter BRIAULT, THE RATIONALE].

9. This argument may be less significant for countries with smaller or less mature markets. *See* RICHARD K. ABRAMS & MICHAEL W. TAYLOR, ISSUES IN THE UNIFICATION OF FINANCIAL SECTOR SUPERVISION 10–14 (International Monetary Fund, Working Paper No. 00/213, 2000), *available at* http://www.imt.org/external/pubs/ft/wp/2000/wp00213.pdf.

10. BRIAULT, THE RATIONALE, *supra* note 8, at 12–17.

11. *Id.* at 12–14.

the need for changes to national regulatory arrangements, in order to keep pace with the markets, was an issue for public policy debate in many countries.[12]

In addition to trends in the international financial markets, changes to national financial regulatory structures are also driven by country-specific factors.[13] This was certainly true in the U.K., where some of the impetus for change came from local financial scandals and collapses that were attributed, in part, to failings in the old system.[14] Throughout the world, there is wide variety in the existing institutional arrangements and, despite the current interest in the single regulator model, its adoption in practice remains relatively rare.[15] The powerful influence exerted by national historical roots and social, economic, and political traditions[16] means that this situation seems likely to persist. To take the obvious example of the United States, adoption of the single regulator model would face practical and political hurdles that currently appear insurmountable.[17] The recognition that national institutional arrangements evolve under the influence of local factors, as well as global trends in financial markets, suggests that there is no one ideal institutional model that is universally applicable.

While this Article makes no claim as to the superiority of the single regulator model, it considers what other countries may learn from the U.K.'s experience in adopting that structure. A key feature is the extent of fundamental legal change that accompanied the U.K.'s shift to the single regulator model. Unlike some other countries, such as Korea which has a single regulatory agency but separate sectorally-divided legal regimes,[18] the U.K. has sought to match the unitary nature of its

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12. CHARLES GOODHART ET AL., FINANCIAL REGULATION: WHY, HOW AND WHERE NOW? 181 (1998).

13. *Id.*

14. BRIAULT, THE RATIONALE, *supra* note 8, at 8.

15. ABRAMS & TAYLOR, *supra* note 9, at 3. But others see "clear signs" of a trend towards unified supervision, particularly for larger financial markets. *See, e.g.,* COURTIS, *supra* note 2, at xiii.

16. GOODHART ET AL., *supra* note 12, at 145.

17. According to Federal Reserve Chairman Alan Greenspan, the creation of a single regulator would be "highly undesirable on both political and economic grounds." ROSA MARIE LASTRA, CENTRAL BANKING AND BANKING REGULATION 147 (1996).

18. *See generally* Joon Soo Lee, Integrated Financial Supervision: The Korean Experience (Asian Development Bank Project, 2002) *available at*

institutional arrangements for financial regulation with an integrated legal framework. This ambitious approach means that the U.K. should be a particularly rich source of data on using the law to respond to the challenges involved in the process of regulatory consolidation. Part II of this Article sets out the historical background of the transition to the single financial regulator model in the U.K. Part III examines the key events in the transitional period between the announcement of the intended switch and the effectuation of the new unitary regime in December 2001. Part IV looks at the main arguments — for and against — the single regulator model; how the British legislature responded to these arguments in shaping the legislative framework for the new regime; and at early indications of how successfully that framework is beginning to operate in practice. Part V offers one conclusion and some observations.

II. The Background to the Adoption of the Single Regulator Model in the U.K.

The 1980s were a period of regulatory upheaval in the U.K. At that time the U.K. had a fragmented regulatory structure, with different institutional arrangements and legal regimes in place for banking, securities, and insurance business. This historical survey examines key events in the period up to May 1997, when a new Labour government was elected in place of the Conservative government that had been in power since 1979.

In the days immediately following the 1997 election, the new Labour government moved with remarkable swiftness to start the process of switching to the single regulator model. This was one of the new government's first major policy initiatives.[19] This begs the question: What had happened to put regulatory reform so high on the new government's list of priorities?

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www.adb/org/projects/APEC/market_intermediaries/integrated_financial_supervision_kor.pdf.

19. Eva Lomnicka, *Reforming U.K. Financial Services Regulation: The Creation of a Single Regulator*, 1999 J. BUS. L. 480.

A. Banking Regulation[20]

In the 1980s, regulatory responsibility for the U.K. banking sector lay with the central bank — the Bank of England ("the Bank"). Although the Bank's informal involvement in the supervision of banks dates back to the mid-nineteenth century, it was only in 1979 that it acquired formal powers to grant or refuse authorization to carry on a banking business in the U.K.[21] Catalysts for the changes made by the Banking Act 1979 were the secondary banking crisis of 1973–1974 and the Banking Coordination Directive of 1977, which was the first major step towards European harmonization in the banking sector.[22]

Banking failures continued to influence change throughout the following years. In 1984, the collapse of Johnson Matthey Bankers Ltd. exposed defects in the framework established by the Banking Act 1979.[23] As a consequence, that structure was replaced by a new legislative framework.[24] The Banking Act 1987 confirmed the Bank in its role as bank regulator and strengthened its supervisory powers.[25] The 1987 Act introduced a new "Board of Banking Supervision" to assist the Bank in its supervisory functions.[26]

In 1991 another bank failure —the Bank of Credit and Commerce International ("BCCI") — again put the U.K. banking regulatory framework under scrutiny.[27] Although international supervisory action coordinated by the Bank had brought about BCCI's closure in 1991, the Bank was heavily criticized for not intervening sooner to stop BCCI's fraudulent operations.[28] An

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20. This section draws upon chapter 1 of the INQUIRY INTO THE SUPERVISION OF THE BANK OF CREDIT AND COMMERCE INTERNATIONAL (HM Stationary Office, 1992) [hereinafter BINGHAM REPORT], which provides an excellent overview of banking supervision in the U.K. in the period 1972–1992.

21. Banking Act, 1979 (Eng.) (repealed 1987).

22. BINGHAM REPORT, *supra* note 20, ¶ 1.15.

23. *Id.* ¶ 1.38.

24. Banking Act, 1987 (Eng.) (repealed 2001).

25. BINGHAM REPORT, *supra* note 20, ¶ 1.47.

26. *Id.*

27. *See generally* Ray P. Kinsella, *Some Regulatory and Supervisory Lessons of the BCCI Collapse, in* INSTITUTE OF EUROPEAN FINANCE, RESEARCH PAPER NO. 92/10, RESEARCH PAPERS IN BANKING AND FINANCE (1992); PETER TRUELL & LARRY GURWIN, FALSE PROFITS: THE INSIDE STORY OF BCCI, THE WORLD'S MOST CORRUPT FINANCIAL EMPIRE (1992).

28. *See generally* Kinsella, *supra* note 27.

official inquiry, chaired by Lord Justice Bingham, was convened. The inquiry found weaknesses in the Bank's approach to coping with sophisticated fraud. Specifically, it was found that the Bank relied too heavily on informal methods based on trust and frankness.[29] It also identified gaps in the Bank's powers. In response, certain technical changes were made to the Banking Act 1987, as well as changes to the Bank's supervisory practices.[30] On the more radical question — whether a reorganization of regulatory responsibility was required — the inquiry produced a negative response.[31] The option of transferring banking regulatory responsibility from the central bank to an independent body was specifically rejected.[32] The inquiry found nothing in the history of BCCI to invalidate the judgment, made prior to the Banking Act 1987, to continue to entrust this task to the Bank.[33]

The spectacular collapse of Barings in 1995 prompted another official inquiry in the U.K., this time by the Board of Banking Supervision.[34] The Barings crisis had been triggered by massive unauthorized losses incurred by a single derivatives trader employed by the Singaporean arm of the Barings group.[35] The official inquiry found that the main reasons for the collapse of Barings were management failings within Barings and lack of appropriate internal controls.[36] In addition, it also found some failings in the Bank's performance as the lead supervisor of the

29. BINGHAM REPORT, *supra* note 20, ¶ 3.8.

30. MAXIMILIAN J.B. HALL, HANDBOOK OF BANKING REGULATION AND SUPERVISION IN THE UNITED KINGDOM 133–34 (3d ed. 1999).

31. BINGHAM REPORT, *supra* note 20, ¶ 3.3.

32. *Id.* ¶¶ 3.4–3.5.

33. *Id.* ¶¶ 3.4–3.5. This issue had been carefully discussed in the WHITE PAPER ON BANKING SUPERVISION, 1985, Cmnd. 9695, which had preceded the Banking Act 1987. Brian Quinn, *The Influence of the Banking Acts (1979 and 1987) on the Bank of England's Traditional Style of Banking Supervision*, *in* BANK REGULATION AND SUPERVISION IN THE 1990S, at 1 (Joseph J. Norton ed., 1991).

34. *See* REPORT OF THE BOARD OF BANKING SUPERVISION INQUIRY INTO THE CIRCUMSTANCES OF THE COLLAPSE OF BARINGS (HM Stationary Office, 1995) [hereinafter COLLAPSE OF BARINGS REPORT].

35. NICK LEESON & EDWARD WHITLEY, ROGUE TRADER: HOW I BROUGHT DOWN BARINGS BANK AND SHOOK THE FINANCIAL WORLD (1996); LUKE HUNT & KAREN HEINRICH, BARINGS LOST: NICK LEESON AND THE COLLAPSE OF BARINGS PLC (1996).

36. COLLAPSE OF BARINGS REPORT, *supra* note 34, ¶¶ 13.10–13.12.

Barings group.[37] Like the previous BCCI collapse, Barings provided a graphic illustration of the difficult challenges facing national regulators attempting to supervise complex multinational banking groups. It also illustrated the need within a fragmented regulatory system for close contact and cooperation between banking and securities regulators in order to achieve effective supervision of financial supermarkets, whose businesses straddled the fuzzy boundaries between those sectors.[38]

While bank failures were reflecting badly on the Bank in its regulatory role, a growing consensus was emerging among politicians and economists in favor of giving the central bank monetary policy independence.[39] Central bank independence is regarded as a practical consequence of the new economic orthodoxy in which monetary policy is the main instrument for delivering price stability.[40]

The connection between monetary policy independence and the location of regulatory responsibility for the banking sector is that if the two functions are combined, regulatory concerns may create conflicts of interest that undermine policy independence.

37. *Id.* ¶¶ 13.57–13.61.

38. *Id.* ¶ 14.44. The earlier collapse of a smaller bank (British & Commonwealth) in 1990 had also demonstrated the need for close cooperation between relevant regulatory bodies. In the light of subsequent events, Hall's comment on the British & Commonwealth situation was particularly percipient. Hall stated: "one can but wonder if institutional rather than functional regulation would be a better way of dealing with the myriad public interest considerations which arise in connection with the regulation and supervision of highly diversified financial conglomerates." HALL, *supra* note 30, at 189 n.134.

39. *See generally* LASTRA, *supra* note 17, at 10–62. The issue of central bank independence is also partly tied up with the euro-entry debate and entry conditions because Article 108 of the Treaty of Amsterdam requires the member state central banks which, along with the European Central Bank ("ECB"), form the European System of Central Banks ("ESCB") to be independent with regard to Treaty obligations. TREATY OF AMSTERDAM AMENDING THE TREATY ON THE EUROPEAN UNION, THE TREATIES ESTABLISHING THE EUROPEAN COMMUNITIES AND CERTAIN RELATED ACTS, Nov.10, 1997, art. 108, O.J. (C 340) 1 (1997).

40. LASTRA, *supra* note 17, at 13–18; Michael Taylor, *Central Bank Independence: The Policy Background, in* BLACKSTONE'S GUIDE TO THE BANK OF ENGLAND ACT 1998, at 19–20 (Michael Blair et al. eds., 1998); Hossein Samiei & Jan Kees Martijn, *Operational Independence and the Conduct of Monetary Policy in the United Kingdom, in* HOSSEIN SAMIEI ET AL., INTERNATIONAL MONETARY FUND: UNITED KINGDOM EXPERIENCE (IMF Staff Country Report No. 99/44, 1999).

Following Charles Goodhart and Dirk Schoenmaker,[41] Michael Taylor hypothesizes that a central bank might not want to adjust interest rates if to do so might trigger a number of bank failures for which it could be blamed. Separating the monetary policy and regulatory roles would remove this conflict and leave the central bank to determine monetary policy free from extraneous influences. But the arguments for and against separation of functions are finely balanced.[42] This view is not, however, universal. Arguments against separation include: the role of the central bank as lender of last resort; its oversight function in relation to the payment system; the need for consistency between monetary policy and banking supervision; and synergistic advantages in concentration of functions.[43] This debate indicates that a central bank will inevitably have continuing involvement in some aspects of the regulatory process because of its role in ensuring financial stability and, further, that the demarcation of its responsibilities and those of any other body that assumes a banking supervisory role is an issue that must be specifically addressed.

Practical events and the evolution of the public policy economic agenda in the 1980s and early 1990s thus provided various reasons for considering change in banking regulation. It should also be noted that U.K. banking law and regulation was significantly amended during this period in order to implement various new European Community ("EC") measures.[44] These changes — though very significant in their own right in that they removed internal barriers to the free operation of banking activities throughout the EU — did not have a major direct impact on the institutional framework of regulation and so they, and equivalent measures in securities and insurance law, do not require detailed examination here.[45] Their immediate relevance to the present discussion is that piecemeal changes to

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41. Charles A.E. Goodhart & Dirk Schoenmaker, *Institutional Separation Between Supervisory and Monetary Agencies, in* CHARLES A.E. GOODHART, THE EMERGING FRAMEWORK OF FINANCIAL REGULATION 133, 141 (1998).

42. Taylor, *supra* note 40, at 20.

43. LASTRA, *supra* note 17, at 148–49.

44. *See* HALL, *supra* note 30, at 36.

45. *See generally id.* (providing an in-depth view of the evolution of supervisory practice and the structure of banking supervision in the U.K.); CHRISTOS HADJIEMMANUIL, BANKING REGULATION AND THE BANK OF ENGLAND (1996).

existing legislation and the addition of extra layers of regulation, such as those that took place in the 1980s and 1990s to implement EU measures, added to the complexity of the framework and to compliance costs. An advantage of a fundamental root-and-branch reform was that it would provide an opportunity for a thorough, principled assessment of how best to combine domestic and EU requirements into a coherent overall framework.[46]

B. Securities Regulation[47]

The history of the U.K. securities regulation in the 1980s and early 1990s paralleled that of banking regulation; it is the story of a system that was undermined by financial scandals that badly affected consumer confidence. It was also a complex system that exacerbated the problems involved in ensuring effective supervision of multi-function firms. The excessively fragmented regulatory infrastructure of the securities industry meant that firms were often regulated by more than one regulatory agency, with the consequence that the system was heavily dependent upon the quality and effectiveness of communications and cooperation between the regulators. To be sure, there was strong industry dissatisfaction with the system, because the presence of multiple regulators created an uncertainty as to boundaries and created inefficiencies.[48] From its inception, the regulatory regime was the target of persistent criticism. It was seen to be unwieldy and bureaucratic. The extremely detailed, legalistic style of early versions of regulatory rulebooks did little to enhance the reputation of those responsible for the regime.[49] When even the head regulator acknowledged in 1993 that many

46. Alistair Darling, *The Regulation of the U.K. Insurance Industry*, 4 INT'L INS. L. REV. 171, 173 (1996).

47. This section draws upon FINANCIAL SERVICES AND MARKETS BILL (House of Commons Library Research Paper 99/68) June 24, 1999, *available at* http://www.parliament.uk/commons/lib/research/rp99/rp99-068.pdf [hereinafter FINANCIAL SERVICES AND MARKETS BILL].

48. Amelia C. Fawcett, *Examining the Objectives of Financial Regulation — Will the New Regime Succeed? A Practitioner's View, in* REGULATING FINANCIAL SERVICES AND MARKETS IN THE TWENTY FIRST CENTURY 37, 47 (Eilís Ferran & Charles A. E. Goodhart eds., 2001) [hereinafter REGULATING IN THE TWENTY FIRST CENTURY].

49. BEN PETTET, COMPANY LAW 340 (2001); Andrew M. Whittaker, *Legal Technique in City Regulation,* 43 CURRENT LEGAL PROBS. 35, 42 (1990).

of the criticisms were justified,[50] it became indisputable that the U.K.'s defective securities regulation system was in dire need of reform.

The source of the problems was the institutional structure established under the Financial Services Act 1986. Under the Act, ultimate regulatory responsibility for the financial services industry lay with a government department. However, most regulatory powers were delegated to the Securities and Investments Board ("SIB"), a private company limited by guarantee and financed by a levy on market participants.[51] The SIB set the overall framework of regulation but did not itself act as the direct regulator of most investment firms. Second tier regulators — of whom the self-regulatory organizations ("SROs") were the most prominent group — performed that function.[52] SROs were funded, and partly managed, by investment firms. For this reason the style of regulation established by the Financial Services Act 1986, was sometimes described as "self-regulation within a statutory framework."[53] Underlying the emphasis on self-regulation in this description was a political compromise designed to assuage the concerns of market participants. As was noted by Professor Gower, whose studies of U.K. securities regulation in the 1980s powerfully influenced the character of the regime, the intellectually appealing full statutory model could not be pursued at that time because it would have been unacceptable in light of prevailing market conditions.[54] The extent to which the system established under the Financial Services Act 1986 truly retained a self-regulatory character in practice is debatable.[55] That it was presented in this way however, soon had unfortunate repercussions. Many observers

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50. ANDREW LARGE, FINANCIAL SERVICES REGULATION: MAKING THE TWO TIER SYSTEM WORK 10 (1993).

51. Financial Services Act, 1986, c. 60, § 61 (Eng.).

52. LARGE, *supra* note 50, at 22, 45.

53. GUIDE TO FINANCIAL SERVICES REGULATION 27 (Barry A. K. Rider et al. eds., 3d ed. 1997); ALAN C. PAGE & ROBERT B. FERGUSON, INVESTOR PROTECTION 78–105 (1992).

54. LAURENCE CECIL BARTLETT GOWER, REVIEW OF INVESTOR PROTECTION: A DISCUSSION DOCUMENT 75–83 (1982).

55. Laurence Cecil Bartlett Gower, *"Big Bang" and City Regulation*, 51 MOD. L. REV. 1 (1988); Iain MacNeil, *The Future for Financial Regulation: The Financial Services and Markets Bill,* 62 MOD. L. REV. 725 (1999); Eilís Ferran, *Dispute Resolution Mechanisms in the U.K. Financial Sector,* 21 CIV. JUST. Q. 135, 137 (2002).

latched onto the self-regulatory dimension as a key reason why the regime failed to succeed.[56] Yet, while growing mistrust of self-regulation undoubtedly played a part in the events that unfolded over the following years,[57] the more potent seeds of the regime's destruction lay in the complex two-tier structure and in the fragmentation at the SRO level.

At the outset, there were five SROs; however, by 1994, only three remained — the Securities and Futures Authority ("SFA"), the Investment Managers' Regulatory Organisation ("IMRO"), and the Personal Investment Authority ("PIA").[58] Some of the changes to the institutional arrangements at the SRO level can be seen in a positive light, as being the dynamic response of a flexible and market-sensitive system to developments in the industry.[59] But it is also the case that much of the change was driven by dissatisfaction about overlaps and possible gaps in the areas of responsibilities of the original SROs.[60]

There were persistent concerns about the effectiveness of the SROs' efforts to prevent fraud and misconduct. The SROs attracted severe criticism for having failed to protect the interests of consumers in a number of high-profile financial scandals. These included the Maxwell affair, where the IMRO's failure to detect the theft of company pension fund assets by its controller, Robert Maxwell, was the target of particular complaint.[61] Another notorious problem that damaged the reputation of the regulatory agencies in the early 1990s was that of pension mis-selling, whereby investors were sold inappropriate pension investment products.[62] Julia Black and Richard Nobles describe the pensions mis-selling episode as a manifestation of "a critical

56. GOWER, *supra* note 54 at 13–16.

57. Alistair Alcock, *A Regulatory Monster,* 1998 J. BUS. L. 371, 375.

58. Financial Services Act, 1986, c. 60, § 10(2) (Eng.).

59. 4 Fin. Serv. Rep. (Sweet & Maxwell) ¶ 2-650 (Aug. 2000).

60. *Id.*

61. 2 SIR ROGER THOMAS ET AL., MIRROR GROUP NEWSPAPERS PLC. INVESTIGATIONS UNDER SECTION 432 (2) AND 442 OF THE COMPANIES ACT 1985 app. 9 (2001), provides a review of IMRO's work in relation to Maxwell group companies and of changes made at IMRO after the eventual discovery of Maxwell's fraudulent schemes. On the other hand, PETTET, *supra* note 49, at 341, presents a more positive assessment of the effectiveness of SRO disciplinary measures and the hard-hitting nature of their operations.

62. Gerard McMeel, *The Consumer Dimension of Financial Services Law: Lessons from the Pensions Mis-selling Scandal,* 3 COMPANY FIN. & INSOLVENCY L. REV. 29, 29 (1999).

failing in the regulatory structure" involving "regulatory blindness," "lack of awareness," and "lack of communication and cooperation between the different regulators."[63]

In a personal assessment published after the Maxwell affair, the then Chairman of the SIB, Andrew Large, identified a number of problems that were thought to afflict the regime he headed: lack of clarity about regulatory objectives; lack of confidence that self-regulation was anything other than self-interest; doubts about cost-effectiveness; and a feeling that fraud was going undetected.[64] Chairman Large's acknowledgement that many of these criticisms were justified set the agenda for policy discussions and political debate in the following years.[65] By the end of 1995, it was a clearly articulated Labour Party policy, then in opposition, to remove the last remnants of self-regulation and the "unnecessary" distinction between the SIB and the SROs.[66] It seems likely that a Conservative government would have traveled the same route had it remained in power. However, there was no indication at this stage of quite how radical the incoming Labour government would be. The case for a single regulator for the whole of the financial sector did not yet figure prominently in the discussions.

C. Insurance[67]

The regulation of the insurance industry in the 1980s and 1990s was a complex affair, yet it attracted little attention from policymakers (except in relation to the Lloyd's insurance market where there were particular problems). The prudential regulation and authorization of insurance companies were the responsibility of a government department under the Insurance

63. Julia Black & Richard Nobles, *Personal Pensions Misselling: The Causes and Lessons of Regulatory Failure,* 61 MOD. L. REV. 789, 789, 815 (1998).

64. LARGE, *supra* note 50, at 8.

65. *See, e.g.*, TREASURY AND CIVIL SERVICE COMMITTEE, THE SIXTH REPORT, 1995, cmt. 332, at vi.

66. *See* FINANCIAL SERVICES AND MARKETS BILL, *supra* note 47, at 17 (speech by Alistair Darling, the then Labour spokesman on the City). *See also* Darling, *supra* note 46, at 172.

67. *See generally* JOHN BIRDS & NORMA J. HIRD, BIRDS, MODERN INSURANCE LAW ch. 2 (5th ed. 2001); JOHN P. LOWRY & PHILIP RAWLINGS, INSURANCE LAW: DOCTRINES AND PRINCIPLES 348–66 (1999); Darling, *supra* note 46.

Companies Act 1982.[68] Long term insurance policies were treated as investments for the purposes of the Financial Services Act 1986 with the result that these aspects of insurance companies' business also fell within the scope of the regulatory regime established under that Act.[69] Insurance brokers were also subject to another form of self-regulation within a statutory framework[70] operated by a body known as the Insurance Brokers Registration Council. By the 1990s, the continuance of this degree of self-regulation was regarded as anomalous.[71] The Lloyd's insurance market had a special status under the Insurance Companies Act 1982[72] and an exemption under the Financial Services Act 1986.[73] Problems at Lloyd's in the early 1990s resulting from disastrous losses put its special regulatory status under scrutiny. Some observers suggested that by not being within the scope of the Financial Services Act 1986, Lloyd's lost out on access to the latest standards and methods of regulation and that, if it had been better regulated, the impact of the losses might have been less severe.[74] An internal review published in early 1997 recommended that Lloyd's should be

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68. Insurance Companies Act, 1982 c. 50, § 3 (Eng.). *See also* Richard Croly, *The Regulatory Structure in the United Kingdom: The Role of the Department of Trade and Industry,* 1 INT'L INS. L. REV 349 (1993). Responsibility for regulation of the insurance industry was assumed by another government department, HM Treasury, in 1997 as a prelude to its transfer to the Financial Services Authority. Press Release, HM Treasury, Working Towards a Single Financial Regulator (July 30, 1998) *available at* www.hm-treasury.gov.uk/newsroom_and_speeches/press/1998/press_127_98.cfm.

69. *See generally* GUIDE TO FINANCIAL SERVICES REGULATION 370–86 (Barry A. K. Rider et al. eds., 3d ed. 1997).

70. Insurance Brokers Registration Act, 1977, c. 46 (Eng.) (repealed 2001).

71. ANDREW MCGEE, THE MODERN LAW OF INSURANCE 21 (2001); Richard Spiller, *Insurance: Broker Regulation*, 6 INT'L INS. L. REV N-67, at N-67 to N-68 (1998).

72. Insurance Companies Act, 1982, c. 50, § 2(2)(a) (Eng.).

73. Financial Services Act, 1986, c. 60, Pt. I, c. IV, § 42 (Eng.).

74. David Gittings, *Lloyd's of London: The Regulation of an International Insurance Market,* 1 J. INT'L FIN. MARKETS 72, 74–75 (1999); Darling, *supra* note 46, at 172. The U.K. government's oversight of the Lloyd's insurance market during the 1980s is the subject of an ongoing investigation by the European Commission. However, the investigation focuses more on whether the system of regulation has been improved by the Financial Services and Markets Act 2000, than on holding the U.K. to account for past mistakes. Andrew Osborn, *Court Hopes Dented for Lloyd's Names,* GUARDIAN (London), Oct. 8, 2002, at 24.

brought within the regulatory jurisdiction of the SIB.[75] The proposal was soon swept up into the radical new approach to financial regulation announced by the new Labour government in May 1997.

D. All Change

The new Labour government was elected on May 1, 1997. On May 6, 1997 the Chancellor of the Exchequer, Gordon Brown, announced that he was giving monetary policy independence to the Bank.[76] This was followed on May 20 by a further announcement from the Chancellor, in which he announced the transfer of responsibility for banking regulation and supervision from the Bank of England to the SIB, as well as reform of the regulatory structure introduced by the Financial Services Act 1986. According to the Chancellor: "SIB will become the single regulator underpinned by statute. The current system of self-regulation will be replaced by a new and fully statutory system, which will put the public interest first, and increase public confidence in the system."[77] The instigation of regulatory reform in itself was no surprise, but that it took the form of a switch to a single regulator was unexpected and politically contentious,[78] not least because the Governor of the Bank had not been consulted about the proposals to strip the Bank of its regulatory role.[79] Previous statements from Labour Party spokesmen had suggested more modest, incremental change concen-

75. *See* Gittings, *supra* note 74, at 75.

76. Gordon Brown, Statement by the Chancellor on the Central Economic Objectives of the New Government (May 6, 1997), *at* http://www.hm-treasury.gov.uk/Newsroom_and_Speeches/speeches/statement/speech_statement_index.cfm? The background to this announcement and its consequences are discussed generally in the House of Lords Select Committee Report, MONETARY POLICY COMMITTEE OF THE BANK OF ENGLAND REPORT, 1999, *available at* http://www.publications.parliament.uk/pa/ld199899/ldselect/ldmon/96/9601.htm (last visited Nov. 12, 2002).

77. Gordon Brown, The Chancellor's Statement to the House of Commons on the Bank of England (May 20, 1997), *at* http://www.hm-treasury.gov.uk/Newsroom_and_Speeches/speeches/statement/speech_statement_index.cfm? [hereinafter Chancellor's Statement on the Bank of England].

78. FINANCIAL SERVICES AND MARKETS BILL, *supra* note 47, at 20–25.

79. On the political fallout of the decision, see ANDREW RAWNSLEY, SERVANTS OF THE PEOPLE: THE INSIDE STORY OF NEW LABOUR 41–44 (2000).

trating, in particular, on dismantling the two-tier structure under the Financial Services Act 1986.[80]

According to the Chancellor's statement, there were three key reasons for the new approach: (1) The existing system was failing to deliver the standards of investor protection and supervision that the industry and the public had the right to expect; (2) The two tier structure under the Financial Services Act 1986 was inefficient, confusing, and lacked accountability and a clear allocation of responsibilities; and (3) The need for a regulatory structure that would reflect the nature of the markets where the old distinctions between banks, securities firms, and insurance companies had become increasingly blurred.[81] The first two reasons were predictable, given the local historical record. The third reason had not previously enjoyed the same degree of prominence. Although matching the nature of the national regulator to the nature of the markets is now the familiar centerpiece of discussions about the institutional framework of regulation, in the political debates on financial regulation in the U.K. in the 1990s it was not an issue that had attracted particular attention.

So why was the single market/single regulator argument raised to such a prominent position by the British Chancellor? The full answer to this question may well remain unknown until current political figures publish their memoirs or until confidential political records are finally released. Mark Boléat, who was the then Director-General of the Association of British Insurers, however, has put forward one plausible theory. Boléat suggests that the decision to opt for a single regulator was driven more by pragmatic considerations relating to pressures on the parliamentary timetable than by principle:

> The Treasury team had failed to secure in the first Queen's Speech legislation to abolish the two tier system under the Financial Services and Markets Act. However, a separate decision had been taken to give the Bank of England independence in respect of conducting monetary policy and this did require legislation. It seems that an opportunist decision was taken at this stage to move towards a single regulator because the legislation to give the Bank of England independence in respect

80. Darling, *supra* note 46, at 172.
81. Chancellor's Statement on the Bank of England, *supra* note 77.

> of monetary policy could be used for any other purpose relevant to the Bank of England.[82]

Initial proposals were very sketchy and important industry sectors, including, for a brief time, insurance,[83] and, for a much longer time, mortgage lending,[84] were not part of the remit originally envisaged for the new regulator.[85] This credits the theory that the switch to a single regulator was a policy decision made "on the hoof" in response to political pressures unconnected to the evolving nature of financial markets.[86] Another theory that has also been suggested is that personal antagonism between the Chancellor of the Exchequer and the Governor of the Bank also played a part in driving the decision to divest the Governor of his institution's regulatory powers.[87]

For observers trying to discover what lessons can be learned from the U.K. experience in adopting the single regulator model, the clearest point that emerges from this brief historical survey up to 1997 is confirmation of the influence of intensely local, country-specific factors in decisions about institutional structures. But May 1997 is too soon to leave the story. Although the decision itself may have been taken opportunisti-

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82. Mark Boléat, The New System of Financial Regulation, Speech at the London Insurance Institute (Nov. 25, 1998).

83. The inclusion of insurance in the new structure was announced in July 1997. Press Release, Department of Trade and Industry, Future Regulation of the Insurance Industry (July 23, 1997), *available at* http://www.newsrelease-archive.net/coi/depts/GTI/coi1035d.ok.

84. JOINT COMMITTEE ON FINANCIAL SERVICES AND MARKETS, DRAFT FINANCIAL SERVICES AND MARKETS BILL: FIRST REPORT ¶ 84 (HL Paper 50-I, HC 328-I, 1999) [hereinafter JOINT COMMITTEE FIRST REPORT], recommended that mortgages should be brought within the scope of the new regime. In response, HM Treasury conducted a consultation exercise with the publication of HM TREASURY, REGULATION OF MORTGAGES: A DISCUSSION DOCUMENT BY HM TREASURY (July 20, 1999). Following this consultation exercise, the decision was made to include mortgages, and power to extend the regime in this way was included in the Financial Services and Markets Act 2000. However, so as not to over burden the FSA in its early days, its assumption of powers in relation to mortgage business was postponed. The FSA currently expects to begin regulating mortgage lenders and advisers by mid-2004. FINANCIAL SERVICES AUTHORITY, TIMETABLE FOR THE REGULATION OF MORTGAGES AND GENERAL INSURANCE (2003), *available at* http://www.fsa.gov.uk/mort_gen_ins/mgi_timetable.pdf.

85. *See also* Alcock, *supra* note 57, at 372, 375.

86. *Id.*

87. RAWNSLEY, *supra* note 79, at 41–44.

cally without full consideration of all of its implications, its announcement was a highly significant event. It intensified debate amongst theorists, inside and outside the U.K., about different institutional structures for financial regulation.[88] At the same time, the challenges involved in turning the single regulator model into practical reality soon became a major preoccupation for industry participants.

III. PUTTING POLICY INTO EFFECT — CREATING A NATIONAL SINGLE REGULATOR [89]

The first stage in the reform process was the renaming of the SIB as the Financial Services Authority ("FSA") in October 1997.[90] Thereafter, most of the existing regulatory agencies collapsed themselves into the FSA structure on a largely informal and ad hoc basis.[91] In effect, the FSA assumed the de facto role of single regulator.[92] But for a transitional period ending on December 1, 2001, the FSA's powers were mostly derived from the old legislation under which the previous fragmented regimes had operated.[93] One important exception was in the banking field, where regulatory and supervisory responsibilities were formally passed to the FSA in June 1998 under the Bank of England Act 1998.[94] However, the 1998 Act merely transferred existing powers without significant amendment. The FSA, as the renamed SIB, was, and still remains, in form, a company limited by guarantee.[95]

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88. For a general survey see GOODHART ET AL., *supra* note 12, at 142–88.

89 Lomnicka, *supra* note 19.

90. See FINANCIAL SERVICES AUTHORITY, CONSUMER INVOLVEMENT (1997), *available at* http://www.fsa.gov.uk/pubs/cp/cp01.pdf, for a summary of enabling legislation and background.

91. Howard Davies, *Law and Regulation,* 3 J. INT'L FIN. MARKETS 169, 169 (2001) [hereinafter Davies, *Law and Regulation*].

92. Formally, the FSA acted as the sub-delegate of existing regulatory agencies. *See* FINANCIAL SERVICES AUTHORITY, CONSUMER INVOLVEMENT app. I (1997), *available at* http://www.fsa.gov.uk/pubs/cp/cp01.pdf.

93. FINANCIAL SERVICES AUTHORITY, *at* http://www.fsa.gov.uk/history (last visited Feb. 19, 2003).

94. Bank of England Act, 1998, § 3, sched. 4 (Eng.). *See also* Davies, *Law and Regulation*, *supra* note 91, at 170; Heidi Mandanis Schooner & Michael Taylor, *Convergence and Competition: The Case of Bank Regulation in Britain and the United States*, 20 MICH. J. INT'L L. 595, 646 (1999).

95. Financial Services and Markets Act, 2000, c. 8, §§ 13–14, 17 (Eng.).

The process of vesting full powers in the FSA as single regulator began in July 1998 with the publication of the Financial Services and Markets Bill in draft form.[96] A period of consultation with industry participants, consumer groups, and other interested parties followed. The most significant part of the public consultation process was the establishment in February 1999 of a Joint Committee of both Houses of Parliament to scrutinize the draft Bill — the first time a Joint Committee had been charged with this task.[97] The Joint Committee, under the Chairmanship of Lord Burns, a former chief civil servant at HM Treasury ("Treasury"), opened paper submission on certain major issues arising from the draft Bill.[98] In addition, the Joint Committee held sessions of oral evidence. The witnesses at these sessions included representatives from the government, the FSA, investment and commercial banks, insurers, consumer groups, and law firms.[99] A novel feature of the oral evidence sessions was that they were run as discussions with fellow panelists allowed to respond to each other's comments and suggestions rather than just responding to questions from members of the Joint Committee. To facilitate discussion, the head of the Treasury Bill team and the Deputy General Counsel of the FSA attended all of the sessions.[100] The Joint Committee's method of conducting its consultation process and the two reports which it produced at the end of its deliberations attracted widespread praise.[101] The Joint Committee was thought to have clarified a number of key issues, in particular the impact of the European Convention on Human Rights on the disciplinary and enforcement procedures of the new regime.[102] This issue was highly

96. Press Release, FSA, Publication of the Draft Bill (July 30, 1998).

97. JOINT COMMITTEE FIRST REPORT, *supra* note 84.

98. Joint Committee on Financial Services and Markets, Press Notice No. 2 of Session 1998–99 (Mar. 10, 1999).

99. JOINT COMMITTEE FIRST REPORT, *supra* note 84, ¶ 6, Minutes of Evidence.

100. Joint Committee on Financial Services and Markets, Press Notice No. 3 of Session 1998–99 (Mar. 19, 1999); JOINT COMMITTEE FIRST REPORT, *supra* note 84, ¶ 6.

101. JOINT COMMITTEE FIRST REPORT, *supra* note 84. *See also* JOINT COMMITTEE ON FINANCIAL SERVICES AND MARKETS, DRAFT FINANCIAL SERVICES AND MARKETS BILL, PARTS V, VI AND XII IN RELATION TO THE EUROPEAN CONVENTION ON HUMAN RIGHTS, SECOND REPORT (1999).

102. Davies, *Law and Regulation*, *supra* note 91, at 170.

topical because the Human Rights Act 1998 was about to bring the Convention more fully into effect under British law.[103]

Although it achieved some notable successes, the Joint Committee sat only for a couple of months and, in the limited time period available, it was able to deal only with selected aspects of the new legislation.[104] The debate then moved into the main chambers of both Houses of Parliament. After a laborious and sometimes controversial passage through Parliament,[105] the Bill finally received Royal Assent in June 2000.[106] However the Financial Services and Markets Act 2000 ("FSMA") provides only the framework of the new regime. The elaborate and extensive details of the regime are contained in secondary legislation, statutory instruments made by the Treasury, and in rules made by the FSA.[107] The process of filling in the details occupied the period from Royal Assent until December 1, 2001 (a date known as "N2"), when the new regime finally came into effect.[108]

Thus, although the FSA has been de facto operational in some form since 1997, it has enjoyed its full powers for only a relatively brief period. This creates an unusual situation. On the one hand, the FSA has had time to establish itself and to begin to build its own identity and methods of operation. Industry, consumers, and the media have had time to experience the reality of dealing with the FSA as a quasi-single regulator and views have formed on how it is shaping up to the task.[109] On

103. Human Rights Act, 1998, c. 42 (Eng.).

104. *See generally* Davies, *Law and Regulation*, *supra* note 91; JOINT COMMITTEE FIRST REPORT, *supra* note 84.

105. According to *The Sunday Telegraph*: "[T]he Bill to set up the super regulator was one of the most tortuous pieces of legislation in Parliamentary history." Grant Ringshaw, *Crackdown in the City Slapped Wrists or Heads on Spikes?,* SUNDAY TELEGRAPH, Nov. 25, 2001, at 5.

106. Financial Services and Markets Act, 2000, c.8, Enactment Clause (Eng.).

107. *See generally* HM Treasury, *Financial Services*, *at* http://www.hm-treasury.gov.uk/documents/financial_services (last visited Feb. 19, 2003); FSA HANDBOOK, *available at* http://www.fsa.gov.uk/handbook (last modified Mar. 3, 2003).

108. Press Release, Financial Services Authority, FSA Consults on Proposed Fees for New Regime (Sept. 21, 2001), *at* http://www.fsa.gov.uk/pubs/press/2001/120.html; *A Cut-Out-and-Keep Guide to the FSA,* DAILY TELEGRAPH, Dec. 1, 2001, at 35.

109. Howard Davies has described the situation in these terms: "[E]ven before it takes on its new powers, the FSA has acquired a reputation of sorts,

the other hand, views on the performance of the FSA as a single regulator must necessarily be qualified to take account of the fact that it has had its full powers for only a short period of time. The distorting effect of the process of preparing for the new regime must also be considered. The massive task of putting in place the detailed aspects of the regime in the transitional period between 1997 and 2001 undoubtedly diverted resources and attention away from the task of practical delivery of regulation. This means that it would clearly be premature to attempt to say whether the FSA is really delivering in practice the benefits claimed for a single regulator while avoiding the problems that this structure may create. But the U.K.'s experience of living with a quasi-single regulator and, at the same time, making the transition to a formal single regulator is still worth examining further. A remarkable combination of processes were occurring simultaneously: The development of theoretical arguments for and against a single regulator were evolving within the context of a market that was already waking up to the reality of living with a de facto single regulator, and all of these influences were feeding into the political processes through which the new regime was to acquire its legal basis and powers.[110] The U.K. experience between 1997 and 2001 thus provides a valuable case study for testing theoretical arguments about the merits and drawbacks of the single regulator model and for demonstrating how those positive and negative features can be addressed in the legal framework by which the model is introduced.

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built on its performance as a caretaker, rather than as a principal." Davies, *Law and Regulation*, *supra* note 91, at 169.

110. *See, e.g.,* BRIAULT, THE RATIONALE, *supra* note 8, at 6–9; Davies, *Law and Regulation*, *supra* note 91, at 169–70.

IV. HOW IS THE NEW REGIME SHAPING UP? USING THE U.K. EXPERIENCE TO TEST AND EXAMINE THE LEGISLATIVE AND PRACTICAL RESPONSES TO THEORETICAL CONCERNS

A. A Single Financial Regulator is Superior because it Mirrors the Nature of the Participants and Products in Financial Markets

This is a prominent argument in favor of the single regulator model.[111] The proposition that a single regulator is advantageous because it mirrors the nature of modern financial markets, where old distinctions between different sectors and different products have broken down, certainly has logical superficial attraction. However, some commentators have cautioned that the trend towards industry consolidation should not be exaggerated.[112] Although some firms are genuine financial supermarkets with major areas of activity in more than one of the main sectors of banking, securities, and insurance, many others remain dominated by their "core" business, despite some diversification into other sectors.[113] For such firms, the risk that concentration of regulatory responsibility will result in loss of regulatory diversity and valuable sector-specific knowledge and expertise, may not be counterbalanced in practice by a significant reduction in the number of regulatory agencies with which they have to deal.

Was the adoption of the single regulator model interpreted by market participants as simplification of regulation for major financial groups operating across sectors at the expense of more sector-specialized firms and institutions? Or was it viewed by consumer groups as a move driven by the demands of certain sections of the financial services industry for a system of regulation that would be more convenient for them rather than for

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111. *See* Chancellor's Statement on the Bank of England, *supra* note 77; BRIAULT, THE RATIONALE, *supra* note 8, at 12–17.

112. Alcock, *supra* note 57, at 376; GOODHART ET AL., *supra* note 12, at 153.

113. GOODHART ET AL., *supra* note 12, at 153. *See also* Arthur E. Wilmarth, Jr., *The Transformation of the U.S. Financial Services Industry, 1975-2000: Competition, Consolidation and Increased Risks,* 2002 U. ILL. L. REV. 215, 254–55 (pointing out that the U.S. banking industry has separated into two sectors: the global sector involving a small group of very large banks providing the services of financial supermarkets; and the community sector comprising a few thousand smaller banks that provide personalized financial services to small businesses and moderately affluent customers).

the needs of consumers of financial services? It appears not. According to a progress report published by the Treasury in March 1999, the single statutory regulator proposal had attracted almost unanimous support.[114] The influential Joint Committee on Financial Services and Markets supported the principle of a single regulator on the basis of the written and oral evidence presented to it.[115] The proposal also attracted favorable comment from the International Monetary Fund ("IMF").[116] The comparative merits of alternative regulatory structures that had generated some debate[117] were quickly sidelined in the practical and political processes leading up to the adoption of the single regulator model in the U.K.[118]

One key reason why there was no serious objection to the principle of the single regulator may have been that it had the great merit of simplicity. Many of the failings, real or perceived, of the predecessor regimes flowed from their inherent complexity. The switch to a single regulator marked a decisive and radical break with the past. Moreover, in political terms it was clear that adoption of the single regulator was "non-negotiable" and that the Labour government's large majority in Parliament would ensure the safe passage of the relevant legislation.[119] Pragmatically, it made no sense for lobbying groups to direct their efforts at challenging the basic idea of the single regulator since that battle was already lost.[120] From the con-

114. HM TREASURY, FINANCIAL SERVICES AND MARKETS BILL: PROGRESS REPORT ch. 2 (1999), *available at* http://finaserv02.uuhost.uk.uu.net/development/legal/fsma/data/progress_report/progress_report.htm (last visited Nov. 13, 2002).

115. JOINT COMMITTEE FIRST REPORT, *supra* note 84, ¶ 102.

116. IMF Concludes Article IV Consultation with the United Kingdom, IMF Pub. Info. Notice No. 99/17 (Mar. 7, 1999), *at* http://www.imf.org/external/np/sec/pn/1999/pn9917.htm.

117. *See* GOODHART ET AL., *supra* note 12, at 142–88; MICHAEL TAYLOR, CENTRE FOR THE STUDY OF FINANCIAL INNOVATION, TWIN PEAKS: A REGULATORY STRUCTURE FOR THE NEW CENTURY (1995) [hereinafter TAYLOR, TWIN PEAKS]; MICHAEL TAYLOR, CENTRE FOR THE STUDY OF FINANCIAL INNOVATION, PEAK PRACTICE: HOW TO REFORM THE U.K.'S REGULATORY SYSTEM (1996).

118. Howard Davies, *Reforming Financial Regulation: Progress and Priorities, in* REGULATING IN THE TWENTY FIRST CENTURY, *supra* note 48, at 19 [hereinafter Davies, *Reforming Financial Regulation*].

119. *Id.*

120. Secondary battles about the scope of the regime, the powers of the single regulator, and, in particular, the accountability of a single regulator were waiting to be fought. *See infra* notes 145-243 and accompanying text.

sumer perspective, the new system offered the prospect of a "one stop shop" for complaints and redress via a unified financial services ombudsman, and that had strong appeal.[121]

Does adoption of the single regulator model necessarily mean that regulation will actually operate seamlessly unimpeded by old sectoral boundaries? In part, this question is unanswerable at this juncture because it involves an assessment that can only be made with the benefit of data arising from practical experience. However, some observations arise from the processes leading up to the formal establishment of the FSA and relating to the arrangements as now in place.

At the policy level, the FSA has made considerable efforts to establish its credentials as a single regulator in substance, as well as in form, by emphasizing its new integrated approach to regulation.[122] It has adopted a single risk-based approach for use across all regulated sectors, markets, and firms. In this context, "risk" has an unusual interpretation.[123] It used to mean risk that the FSA will fail to achieve its statutory regulatory objectives. The FSA's standard risk assessment process involves scoring the risk against a number of probability and impact factors.[124] The systemic nature of the firm is a relevant factor in the assessment process because maintaining confidence in the financial system, which embraces systemic risk concerns, is one of the statutory objectives.[125] However, the FSA has emphasized the "assessment of all risks has to be coordinated, in order to gauge the overall threat to our objectives."[126]

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121. JOINT COMMITTEE FIRST REPORT, *supra* note 84, ¶¶ 282–96. See Ferran, *supra* note 55, on the implementation of the unified ombudsman scheme and some early assessment of its performance.

122. FINANCIAL SERVICES AUTHORITY, A NEW REGULATOR FOR A NEW MILLENNIUM 29 (2000), *available at* http://www.fsa.gov.uk/pubs/policy/p29.pdf [hereinafter NEW REGULATOR FOR A NEW MILLENNIUM]; FINANCIAL SERVICES AUTHORITY, BUILDING THE NEW REGULATOR: PROGRESS REPORT 2, ¶¶ 59–63 (Feb. 2002), *available at* http://www.fsa.gov.uk/pubs/policy/bnr_progress2.pdf.

123. *See* Howell E. Jackson, *Regulation in a Multi-Sectored Financial Services Industry: An Exploratory Essay,* 77 WASH. U. L.Q. 319, 332–34 (1999) (Part II.A. discusses more common interpretations of "risk" in the context of financial regulation).

124. NEW REGULATOR FOR A NEW MILLENNIUM, *supra* note 122, at 15.

125. *Id.* at 15, 17.

126. *Id.* at 15.

The new risk-based approach to regulation is currently being phased in,[127] so it is obviously too early to gauge whether the FSA has the organizational capacity to deliver an integrated regulatory approach. The signs are good for those financial conglomerates that are regulated by the FSA's Major Financial Groups Division, because that division has been established specifically to "take a coherent and integrated approach to the supervision of these groups."[128] An integrated approach is less obvious in other parts of the FSA's internal departmental structure, which continue to be organized along broadly sectoral lines.[129] The FSA lead regulator model — inherent in the predecessor regimes — is employed to deal with groups that operate predominantly in one sector but with some entities operating in other sectors.[130] This structure is sensible to the extent that, under the single regulator umbrella, it allows for sensitive, differentiated regulation of businesses that are predominantly active only in one sector. In the transitional period, it may have facilitated smooth implementation of the single regulator model because it allowed the staff employed in the previous fragmented structure to continue to work in their area of specialization which, in turn, gave comfort to regulated firms about continuity in practical, day-to-day relationships with

127. The fact that the FSA had not completed the rolling out of its risk based approach was at the center of its dispute with Fitch in June 2002 in which the FSA stated that Fitch's report to the effect that 25% of the U.K.'s insurers had been placed in a higher risk category was a misinterpretation of FSA data. Jill Treanor, *Regulator Calls Fitch "Plain Wrong": FSA Denies Insurers are "Higher Risk,"* GUARDIAN (London), June 14, 2002, at 25.

128. FINANCIAL SERVICES AUTHORITY, INTRODUCTION TO THE FINANCIAL SERVICES AUTHORITY 13 (2001), *available at* http://www.fsa.gov.uk/pubs/other/fsa_intro.pdf [hereinafter INTRODUCTION TO THE FSA]. A report commissioned by the Centre of the Study of Financial Innovation and published in May 2001 indicated that the larger City institutions, particularly those classified as major financial groups, expected to see the greatest benefit of the single regulator structure and that some already were. *See* DAVID LASCELLES, CENTRE FOR THE STUDY OF FINANCIAL INNOVATION, WAKING UP TO THE FSA: HOW THE CITY VIEWS ITS NEW REGULATOR 13 (2001) [hereinafter CSFI, WAKING UP TO THE FSA].

129. *See* INTRODUCTION TO THE FSA, *supra* note 128, at 24 (FSA Organisation Chart).

130. FINANCIAL SERVICES AUTHORITY, LEAD SUPERVISION: THE FSA'S NEW APPROACH TO THE CO-ORDINATION OF ITS SUPERVISION OF GROUPS 5 (1999), *available at* http://www.fsa.gov.uk/pubs/policy/p19.pdf.

their regulators.[131] But it could prove problematic in the longer term, if it facilitates the continuation of ingrained methods and practices that are, in principle, incompatible with the achievement of a truly integrated approach to regulation. Here, again, there are some positive signs coming from FSA pronouncements about insurance regulation, which emphasize that risk-based assessment means a wholly new approach within its insurance division.[132] However, it should be noted that the FSA is under particular pressure to signal a fresh start in insurance regulation because of recent crises in the insurance sector involving both failing firms[133] and defective products,[134] for which the FSA

131. Alcock, *supra* note 57, at 377.

132. FINANCIAL SERVICES AUTHORITY, THE FUTURE REGULATION OF INSURANCE: A PROGRESS REPORT (Oct. 2002) at 19, *available at* http://www.fsa.gov.uk/pubs/policy/bnr_progress3.pdf; FINANCIAL SERVICES AUTHORITY, THE FUTURE REGULATION OF INSURANCE (Nov. 2001), *available at* http://www.fsa.gov.uk/pubs/other/future-reg_insurance.pdf; Alex Brummer, *Spotlight Falls on Insurance*, DAILY MAIL, Dec. 4, 2001, at 67 (reporting the head of the FSA's insurance side as taking the view that a whole new approach to insurance supervision based upon risk assessment is needed); Robert Preston, *City Watchdog Who Bites but Won't Bark*, SUNDAY TIMES (London), Mar. 17, 2002 (reporting Howard Davies, the Chairman of the FSA, as identifying the imperative of modernizing insurance regulation, which was "a generation behind banking supervision and securities regulation").

133. Equitable Life, the world's oldest mutual life assurance company closed to new business in December 2000 following a court case, Equitable Life Assurance Soc'y v. Hyman, [2002] 1 A.C. 408 (H.L.), in which the House of Lords ruled against the company in its interpretation of certain of its pension policies thereby plunging the company into extreme financial difficulties. Independent Insurance, a general insurance company, collapsed in June 2001 after the failure of efforts to raise additional capital. These were headline-grabbing major collapses but according to FSA data, as of January 2002, thirty-nine general insurers were in formal insolvency proceedings in the U.K., with quantified gross insurance liabilities of £12.5 billion. *See generally* Howard Davies, "Rational Expectations" — What Should the Market, and Policyholders, Expect from Insurance Regulation?, AIRMIC Annual Lecture (Jan. 29, 2002), *available at* http://www.fsa.gov.uk/pubs/speeches/sp87.html.

134. In particular, the problem of mis-selling endowment policies, which surfaced in the late 1990s (i.e., life assurance policies which were sold in conjunction with mortgages as a mechanism for repayment of mortgage principal at the end of its life but without clear disclosure to customers that there was no guarantee that the policies would in fact generate an amount sufficient to cover the mortgage debt). According to the FSA, by 2000 an estimated 60% of the 11 million existing mortgages were no longer on track to repay the mortgage loan. FINANCIAL SERVICES AUTHORITY, PROGRESS REPORT ON MORTGAGE ENDOWMENTS ¶ 2.18 (Oct., 2000), *available at* http://www.fsa.gov.uk/pubs/policy/p19.pdf.

has had to shoulder some blame[135] as well as attracting significant criticism from politicians and the media.[136]

Mis-selling allegations also surround another underperforming financial product — split capital trusts. *See* FINANCIAL SERVICES AUTHORITY, SPLIT CAPITAL CLOSED END FUNDS ¶¶ 5.11, 5.15 (Dec. 2001), *available at* http://www.fsa.gov.uk/pubs/discussion/dp10.pdf; FINANCIAL SERVICES AUTHORITY, SPLIT CAPITAL INVESTMENT TRUSTS (SPLITS) ¶ 3.7 (May 2002), *available at* http://www.fsa.gov.uk/pubs/policy/pssplits/pdf; Ingrid Mansell, *FSA Launches Investigation into Mis-selling of Splits*, TIMES (London), May 18, 2002, at 43.

135. The FSA's internal audit of the regulator's role in regulating Equitable Life between 1999 and 2000 identified deficiencies in FSA regulation, in particular with regard to communication between prudential and conduct of business regulators. REPORT OF THE FINANCIAL SERVICES AUTHORITY ON THE REVIEW OF THE REGULATION OF THE EQUITABLE LIFE ASSURANCE SOCIETY FROM 1 JANUARY 1999 TO 8 DECEMBER 2000, WHICH HER MAJESTY'S GOVERNMENT IS SUBMITTING AS EVIDENCE TO THE INQUIRY CONDUCTED BY LORD PENROSE ¶ 6.2.5 (2001) [hereinafter BAIRD REPORT]; Press Release No. 57/01, Parliamentary Ombudsman to Investigate Financial Services Authority's Handling of Equitable Life (Oct. 29, 2001), *available at* http://ombudsman.org.uk/pca/press/pn57-01.htm. Following this report, the government established its own independent inquiry. *See* HM Treasury Press Release 113/01, Government Response to FSA Report on the Regulation of Equitable Life, (Oct. 17, 2001), *available at* http://www.hm-treasury.gov.uk/Newsroom_and_Speeches/Press/2001/Press_113.01.cfm. The Parliamentary Ombudsman is also investigating the FSA's handling of the collapse. *See* James Moore, *Ombudsman to Investigate FSA Role at Equitable*, TIMES (London), Oct. 30, 2001, at 24. If the Ombudsman finds the FSA guilty of maladministration, the government could be directed to compensate policyholders.

With regard to the Independent Insurance collapse, press reports indicate that the FSA is to be sued by the company's policyholders for its role in the handling of the collapse. Gary Parkinson, *Independent Holders Sue FSA,* DAILY TELEGRAPH (London), Mar. 13, 2002, at 38.

136. In relation to endowment mis-selling, the FSA was criticized in the press for not launching a full-scale review akin to that which had been conducted previously in relation to pensions mis-selling. In some quarters this was interpreted as the FSA bowing to industry pressure rather than championing consumer interests. The FSA's attempts to diffuse the situation by publishing guidance to firms on dealing with endowment-related complaints and making redress to those with legitimate claims did not stem the flow of critical press coverage. *See, e.g.*, David Prosser & Neasa MacErlean, *Cash: Where's the Rest?: The Endowment Crisis Has Hit Millions Yet Regulators Refuse a Full Review,* OBSERVER, Sept. 2, 2001, at 2. Findings from a yearlong FSA review of the profits industry were also criticized by consumer groups, with suggestions that the FSA had kowtowed to industry in its recommendations. Emma Simon, *The Great With-profits Fudge: The FSA's Report on its Investigation*, SUNDAY TELEGRAPH, June 2, 2002, at 4.

The flip-side of the argument that a single regulator will fail in practice to deliver an integrated regulatory approach, is that it will pursue integration over-enthusiastically thereby failing to make appropriate differentiation between businesses that mainly operate in different sectors, or between businesses within the same sector but which have very different customer bases. A single regulator is obviously vulnerable to attack on this ground but, thus far, criticism of the FSA on the ground that it is attempting to impose a "one-size-fits-all" approach has been muted.[137] The FSA has helped its own cause in this respect by explicitly introducing a differentiated regime, which uses the nature of the counterparty with whom a firm deals as the basis for determining the applicable level of conduct for business regulation.[138] This approach allows for "light touch" regulation of business between market professionals.[139] It has been welcomed as restoring "some of the differentiation that was inherent in the City's old regime."[140]

B. A Single Regulator Should Be Able to Deliver Efficiency Gains

There are several strands to the argument that the single regulator model may be superior to alternative regulatory structures on efficiency grounds.[141] Efficiency in this context

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137. *See* CSFI, WAKING UP TO THE FSA, *supra* note 128, at 4, 14–15 (reporting some fears about the growth of a mono-culture and excessive zeal for harmonization but suggesting that any loss in regulatory diversity has been offset by greater consistency).

138. FSA HANDBOOK, *available at* http://www.fsa.gov.uk/handbook (last modified Mar. 3, 2003); Market Conduct Sourcebook *available at* www.fsa.gov.uk/handbook/legal_instruments/2001/jun21_mar.pdf (last modified Sept. 24, 2002); The Inter-Professionals Code (FSA Consultation Paper 47, 2002) *available at* www.fsa.gov.UK/pubs/CP/47 (last modified July 25, 2002).

139. Edward Black & Emma Radmore, *CP47 — The Inter-professionals Code,* 1 FIN. SERVICES BULL. 11 (2000).

140. CSFI, WAKING UP TO THE FSA, *supra* note 128, at 15.

141. *See generally* BRIAULT, THE RATIONALE, *supra* note 8, at 18–22; CLIVE BRIAULT, REVISITING THE RATIONALE FOR A SINGLE NATIONAL FINANCIAL SERVICES REGULATOR 14–15, 27–31 (FSA Occasional Paper No. 16, 2002), *available at* http://www.fsa.gov.uk/pubs/occpapers/index-2002.html [hereinafter BRIAULT, REVISITING THE RATIONALE]; Leonardo Bartolini, *The Financial Services Authority: Structure, Mandate and Policy Issues, in* HOSSEIN SAMIEI

relates to the manner in which the regulator deploys its own internal resources.[142] This is closely linked to the efficiency of its regulation and supervision, which relates to the wider economic impact of its activities, including compliance costs for regulated firms.[143]

A single regulator's position allows it to look across the entire financial industry and devote regulatory resources to where they are most needed. These include human, as well as financial, resources: the single regulator model should facilitate efficient use of available expertise and experience, a factor that may be particularly significant where such expertise and experience are in short supply. Economies of scale and scope should be possible because the single regulator has a unified management structure; can take advantage of unified central support services; introduce single databases and reporting systems; develop a single set of rules; and adopt consistent policies that are informed by its ability to take a market or industry-wide perspective.[144] A single regulator should, in principle, be able to avoid wasteful duplication and overlap. Economic literature, however, provides plenty of evidence to support counter-arguments about the economics of scale offered by mega-regulators.[145] It is also pointed out in the literature that the direct cost savings available by having a single institutional infrastructure, may be "a comparatively small proportion of the total costs of regulation."[146] With regard to the compliance cost burden on regulated firms, in principle, firms may gain from having to deal with only one regulator and one set of requirements. This is not guaranteed however, because a single regulator's regime might prove to be more burdensome than the combined weight of the applicable parts of a fragmented regime.

The FSA is funded entirely by industry levy.[147] With that in mind, it is unsurprising that the likely efficiency of the new regime was a major concern for industry participants in the pe-

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ET AL., INTERNATIONAL MONETARY FUND: UNITED KINGDOM EXPERIENCE (IMF Staff Country Report No. 99/44, 1999).

142. JOINT COMMITTEE FIRST REPORT, *supra* note 84, ¶ 103.

143. *Id.*

144. GOODHART ET AL., *supra* note 12, at 151–52.

145. For a summary, see GOODHART ET AL., *supra* note 12, at 152–55. *See also* Mwenda & Fleming, *supra* note 1, at 3, 11.

146. GOODHART ET AL., *supra* note 12, at 152.

147. Financial Services and Markets Act, 2000, c. 8, § 12(6) (Eng.).

riod leading up the passing of FSMA. Politically, these were concerns that needed to be explicitly addressed in order to retain industry confidence. Accordingly, clear provisions relating to efficiency were built into the legislative framework.[148] In discharging its general functions, the FSA must have regard to a series of statutory regulatory principles, the first-listed of which is "the need to use its resources in the most efficient and economic way."[149] Another of these principles is that burdens imposed must be "proportionate to the benefits . . . which are expected to result from the imposition."[150] This "proportionality principle" provides a measure against which the FSA must judge whether the costs of regulatory compliance that it imposes on an industry are justifiable.[151] It is supplemented by specific procedural obligations on the FSA to do, and to publish, cost-benefit analysis as part of the process of consultation before it exercises certain of its lawmaking powers.[152] The legal obligation of the FSA to be mindful of the need to run an efficient and economic regulatory regime is further reinforced by other statutory regulatory principles that require it to consider, first, "the international character" of the financial industry and the desirability of maintaining the U.K.'s competitive position and, second, "the need to minimize the adverse effects [of its activities] on competition."[153]

The FSMA gives the government power to commission and publish independent value for money audits of the FSA.[154] However, calls for the National Audit Office to have a direct

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148. *Id.* § 2(2)–(3).

149. *Id.* § 2(3)(a).

150. *Id.* § 2(3)(c).

151. *Id.* § 4(2)(a).

152. In particular, its general rulemaking powers under Financial Services and Markets Act, 2000, c. 8, § 155(1)(2)(a) (Eng.). Whether meaningful cost benefit analysis can actually be achieved by the FSA is an issue that divides commentators. *Compare* ISAAC ALFON & PETER ANDREWS, COST-BENEFIT ANALYSIS IN FINANCIAL REGULATION — HOW TO DO IT AND HOW IT ADDS VALUE (FSA Occasional Paper No. 3, 1999), *with* Charles A. E. Goodhart, *Regulating the Regulator — An Economist's Perspective on Accountability and Control, in* REGULATING IN THE TWENTY-FIRST CENTURY, *supra* note 48, at 151, 156–57. *See also* DAVID SIMPSON ET AL., SOME COST BENEFIT ISSUES IN FINANCIAL REGULATION (FSA Occasional Paper No. 12, 2000), *available at* http://www.fsa.gov.uk/pubs/policy/op12.pdf.

153. Financial Services and Markets Act, 2000, c. 8, § 2(3)(e)–(f) (Eng.).

154. *Id.* § 12.

role in relation to the FSA were resisted.[155] As a company, the FSA is subject to requirements of the companies' legislation with regard to the publication of its annual report and accounts.[156] In addition, under the FSMA it must further make an annual report to the Treasury.[157]

To date, how is the FSA's performance measuring up on efficiency and broader economic grounds? The risk-based approach to regulation is the core of the FSA's strategy for achieving regulatory efficiency. The Chairman of the FSA has claimed that: "It has already led to some significant shifts of resources within the Authority, and to a change of emphasis in line supervisory divisions, towards pro-active work intended to head off emerging risks, and away from routine, box-checking exercises focused on mechanical compliance with rule-based requirements."[158]

The allocation of additional resources to upgrade insurance regulation is the most obvious shift that has taken place. This extra allocation has been achieved by diverting resources out of banking supervision on the basis that banking business appears to pose far fewer risks than insurance business.[159] This approach to the allocation of resources does raise the specter of the FSA being prone to shifting its resources around in response to short-term political pressures — insurance is certainly the obvious current weak link in the regulatory framework but it was not that long ago when banking regulation was in the spotlight as the problem area in the aftermath of various bank failures. However, only time will tell whether this is a real problem.

To date, the FSA has done a reasonable job in keeping its own costs under control. According to an FSA comparative study of the direct costs of regulation, the U.K. ranked second most inexpensive, behind Sweden (another single regulator country), with United States ("U.S.") regulatory costs being some eight-

155. JOINT COMMITTEE FIRST REPORT, *supra* note 84, ¶¶ 108–11.
156. Financial Services and Markets Act, 2000, c. 8, §§ 10(1), 13, sched. 1 (Eng.).
157. *Id.* § 10.
158. Davies, *Law and Regulation*, *supra* note 91, at 172.
159. FINANCIAL SERVICES AUTHORITY, PLAN AND BUDGET 2002/2003, at 5 (2002), *available at* http://www.fsa.gov.uk/pubs/plan/pb2002_03.pdf [hereinafter PLAN AND BUDGET 2002/03].

een times greater than those in the U.K.[160] However, there are concerns that the FSA has only achieved this position at the expense of regulated firms, which have faced a sharp increase in compliance costs,[161] while the brunt of increased compliance costs have been borne disproportionately by smaller firms.[162] Addressing the issue of compliance costs, FSA Chairman Howard Davies has spoken of the aim of the new regime as being to "reduce the overall costs of regulation, especially for well-managed firms."[163] While an increase in compliance costs as industry adapted to the new regime was only to be expected, in the longer term, if the position falls far short of Davies' aim, this would be a major source of industry dissatisfaction. At worst, it could result in firms engaging in "regulatory arbitrage" and shifting their regulatory base to a lower cost jurisdiction.[164] If that were to happen, the FSA would have difficulty convincing observers that it has properly observed the statutory regulatory principles on competitiveness within an international market to which it is supposed to have regard.

Studies on whether the FSA has realized its potential in deploying human resources more efficiently may be forthcoming. Presently, the main concern relating to the FSA's human resources is whether it can attract, and retain in overall terms, a sufficient number of well-qualified staff because of the large

160. Howard Davies, N2 Plus 3, Speech at the Worshipful Company of Chartered Secretaries & Administrators Annual Lecture (Mar. 5, 2002), *available at* http://www.fsa.gov.uk/pubs/speeches/sp93.html [hereinafter Davies, N2 Plus 3]. For further analysis, see FSA, ANNUAL REPORT app. 10 at 133–38 (2001/2002), *available at* http://www.fsa.gov.uk/pubs/annual/ar01_02.pdf; FSA, ANNUAL REPORT app. 5 at 79–83 (2000/2001), *available at* http://www.fsa.gov.uk/pubs/annual/ar00_01.pdf.

161. Using the definition of compliance costs offered by ALFON & ANDREWS, *supra* note 152, at 16, as being: the costs to firms and individuals of those activities required by regulators that would not have been undertaken in the absence of regulation. Davies notes that extensive comparative data on the total costs of regulation is not available and that such data as exists is somewhat impressionistic. Davies, N2 Plus 3, *supra* note 160. *See also* Graham Bannock, *Financial Services Regulation: Controlling the Costs,* 6 FIN. REG. 31, 32–33 (2002).

162. DAVID LASCELLES, CENTRE FOR THE STUDY OF FINANCIAL INNOVATIONS, HOW THE CITY VIEWS ITS NEW REGULATOR 17–19 (2001); Michael Becket, *FSA Red Tape "Hits Small Businesses,"* DAILY TELEGRAPH (London), May 18, 2001, at 34.

163. PLAN AND BUDGET 2002/03, *supra* note 159.

164. JOINT COMMITTEE FIRST REPORT, *supra* note 84, ¶¶ 52–53.

disparity in pay levels between the private and public sectors.[165] Although the FSA has attracted some leading figures from the professions into top-level positions,[166] this is not necessarily indicative of success at all levels within its staffing structure. Senior people who have already fulfilled many of their career ambitions within the private sector are likely already to have achieved a level of financial security that allows them to consider a lifestyle change and/or enables them to appreciate the opportunity to contribute to policy development in areas with strong public interest implications.[167] Young, ambitious, and skilled lawyers, accountants, economists, and other professionals who would be suited to careers in regulation, however, may not (yet) have the luxury of financial security. Furthermore, from their perspective, there is a particular disadvantage that flows directly from the streamlined, unified structure of a single regulator. Put simply, if the management system is unified then there are fewer top positions to which they can aspire. On the other hand, it may be argued that this narrowing of opportunity at the very top is counter-balanced by the greater power, influence, and prestige that should attach to senior positions below the very top level in an agency that is responsible for regulating an entire industry, than to positions of an equivalent level within a fragmented regulatory structure. The impact of the narrowing of career opportunities that may result from the adoption of the single regulator model, and the possible counterbalancing effect of the enhancement in the quality of certain positions just below the very top level, are issues that, to date,

165. This was a concern for the Joint Committee. *Id.* ¶¶ 249–53. There continue to be newspaper reports about the FSA's difficulties in retaining staff. *See, e.g.,* Chris Hughes, *FSA Aims to Stem Staff Exodus with 7.4% Pay Rise,* INDEP., Feb. 1, 2002, at 21.

166. In particular, the FSA has recruited a small team of senior executives recently retired from banks and insurance companies (the "grey panthers") to keep in touch with the markets and advise the FSA staff on transactions. Katherine Griffiths, *FSA "Grey Panthers" to Hunt for Failures*, INDEP., Dec. 4, 2001, at 17.

167. For example, John Tiner, now a managing director at the FSA, was recruited from the private sector (Arthur Andersen) in 2001 with a reported drop of £750,000 in salary. Tiner has been quoted as explaining his switch on the grounds that it gave him the opportunity to help shape a national industry: "I've always known I would go into public service." William Kay, *The Head of the FSA is a Man with a Mission to Succeed. But at What*?, INDEP., May 25, 2002, at 2.

have attracted little attention but they may merit closer examination.

Spending time at the FSA at an early stage in one's career might be attractive to young, skilled professionals if that were to be seen as an especially good route into a lucrative career in the private sector. Although the practice of people building careers in the financial industry in this way is not as well-established in the U.K. as it is assumed to be in the U.S.,[168] there are growing indications of FSA experience being used as a springboard from which to launch a more lucrative private sector career.[169] Therefore, there may be an increasing trend towards this pattern of career development. Such a trend could benefit the FSA because it could increase the size and quality of the human resources available to it. However, there are also potential drawbacks in that it could encourage industry capture because junior regulators might be tempted to adopt lax practices with regard to the firms for which they are responsible in order to enhance their own career opportunities. High turnover of junior-level FSA staff could also prove costly for regulated firms since they would, in effect, have to absorb costs involved in dealing with inexperienced and untested regulators.

Generally speaking, although still a nascent organization, the FSA regime does not show signs of having been captured by industry. Criticisms from industry that the FSA is too consumer-orientated[170] and criticisms from consumer groups that the FSA is too pro-industry, [171] largely balance each other out, which overall, might be thought to be a reasonable state of affairs.[172] The FSA regime has broadly retained the confidence of both industry and consumer associations. Its success in this respect is widely attributed to the FSA's first Chairman, How-

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168. JOINT COMMITTEE FIRST REPORT, *supra* note 84, ¶ 252.

169. *See* Hughes, *supra* note 165.

170. For example, Mary Francis, Director-General of the Association of British Insurers, has been quoted as describing the FSA as "the provisional wing of the Consumers' Association." Liam Halligan, *The FSA Must Put Its Own House in Order,* SUNDAY TELEGRAPH, July 29, 2001, at 4.

171. Particularly with regard to its stance on endowment mortgages and the for profits industry more generally. *See supra* notes 134–37.

172. *See, e.g.*, Chris Hughes, *Three Years On, the FSA Finds Itself Under Attack From All Sides*, INDEP., July 20, 2001, at 21.

ard Davies, who is thought to have had a benign influence on the character of the new regime.[173]

C. The Single Regulator Model May Provide a More Effective System of Regulation

Effectiveness is measured by whether a regulatory system achieves its objectives.[174] Effectiveness overlaps with suitability — a single regulator may be more effective than alternative regulatory models because its structure is better suited to the increasingly integrated nature of financial markets. Employing current popular jargon, the single regulator is likely to be effective because it has a full regulatory "toolkit" at its disposal and is thus ideally placed to select the optimal regulatory responses to any situation.[175] Effectiveness also overlaps with efficiency because inefficient regulation is likely to produce results that are inimical to a properly effective system of regulation.

An argument that merits separate attention is that a single regulator may be more effective because of the coherence and clarity of its mandate. Lack of coherence and clarity about what an agency is supposed to do would be a major weakness of any regulatory system, whether it involves a single regulator or several agencies.[176] But a particular argument for the superiority of the single regulator model in this respect is that the single regulator may be ideally positioned to maintain coherence and clarity of purpose because its unified management structure provides an effective mechanism for resolution of conflicts between different regulatory objectives.[177] However, commentators are sharply divided on this alleged benefit. Charles Goodhart and his co-authors suggest that a single regulator may lack

173. George Trefgarne, *When the FSA Pulls the Strings . . . There is a Refuge from Sir Howard Davies's Red Tape,* DAILY TELEGRAPH, Dec. 1, 2001, at 35.

174. JOINT COMMITTEE FIRST REPORT, *supra* note 84, ¶ 103.

175. NEW REGULATOR FOR A NEW MILLENNIUM, *supra* note 122, at 25–32 (Chapter 3 outlines the FSA's regulatory tools and considers how they may be used in practice).

176. Alan Page, *Regulating the Regulator — A Lawyer's Perspective on Accountability and Control, in* REGULATING IN THE TWENTY-FIRST CENTURY, *supra* note 48, at 127.

177. BRIAULT, THE RATIONALE, *supra* note 8, at 7, 21.

"a clear focus on the objectives and rationale of regulation."[178] So instead of facilitating coherence and clarity, the single regulator model may result in self-contradiction and confusion. Michael Taylor argues that, rather than being a benefit, the ability of a single regulator to resolve disputes about objectives internally is an undesirable feature because such disputes should be resolved at the political level due to their public policy implications.[179] Alternative regulatory models have been put forward by these authors, in which regulatory responsibilities are divided between agencies by reference to different regulatory objectives.[180]

Another theoretical argument for the greater effectiveness of the single regulator model is with regard to consistency, communication, and cooperation at operational levels.[181] Individual regulators may find it easier to communicate and cooperate with each other on matters of common concern when they all work for the same organization rather than when they are scattered between different agencies. Moreover, they should all have a shared cultural approach to their task and operate consistently in accordance with the common policies set at management level.[182] However, success is not guaranteed. Whether these potential gains are realized is obviously dependent on how well separate, specialized divisions within the single regulator actually do cooperate and communicate with each other, and how effectively a consistent cultural approach has permeated throughout the organization.[183]

Law can play a key role in providing a clear and authoritative statement of objectives and in providing an agency with powers to enable it to operate in a consistent manner. The value of establishing a legal framework specifically designed to support the effectiveness of the single regulator model was recognized in the U.K. The "easy" option of simply piecing together the existing sectorally-based legal regimes and vesting all of those exist-

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178. GOODHART ET AL., *supra* note 12, at 153. *See also* DANIEL GROS & KAREL LANNOO, THE EURO CAPITAL MARKET 146–47 (1999) (arguing that regulation by objective could result in excessive regulation of wholesale business because of misplaced concerns about consumer protection).

179. TAYLOR, TWIN PEAKS, *supra* note 117.

180. GOODHART ET AL., *supra* note 12, at 156.

181. *See* BRIAULT, THE RATIONALE, *supra* note 8, at 17–19

182. *Id.*

183. GROS & LANNOO, *supra* note 178, at 145.

ing powers in the FSA was ruled out in favor of the much more ambitious approach of providing a fully integrated common legal framework.[184] Thus, the FSMA gives the FSA broad powers to regulate across the financial sector. The Act also deepens the regulatory regime in key respects including, in particular and most controversially, a new market abuse regime that allows the FSA to impose civil penalties on any person — not just those within the regulated financial industry — who has engaged in abusive conduct.[185]

The cornerstone of the FSMA is the statement of regulatory objectives, which are: maintaining confidence in the financial system; promoting public understanding of the financial system; securing the appropriate degree of protection for consumers; and reducing financial crime.[186] The FSA is under a statutory duty in discharging its general functions to act in a way that is compatible with the regulatory objectives, but only so far as is "reasonably possible."[187] Subject to the same qualification, in the discharge of its general functions the FSA is also required to act in a way that it "considers most appropriate for the purpose of meeting those objectives."[188] These duties are supplemented by the obligation to consider specified regulatory principles, as previously discussed.[189]

The inclusion of a statement of regulatory objectives in the FSMA was generally welcomed during the passage of the legislation, although there was, inevitably, some discussion about whether the right objectives had been specified[190] as well as a more technical legal debate about the drafting of the relevant provisions.[191] The statutory statement of objectives represents a brave attempt to distill the purposes of regulation across sec-

184. Prior to December 2001, the overhaul was not so radical at the second-tier level (i.e., in the rules made by the FSA itself). There, the emphasis was on changes necessary to achieve consistency and simplification, rather than on re-assessment of fundamental principles. Davies, *Law and Regulation*, *supra* note 91, at 169.

185. Financial Services and Markets Act, 2000, c. 8, pt. VIII (Eng.).

186. *Id.* at pt. I, §§ 3–6.

187. *Id.* at pt. I, § 2.

188. *Id.*

189. *See supra* notes 149–53 and accompanying text.

190. In particular whether there should have been a further objective, also requiring the FSA to promote competition.

191. *See* JOINT COMMITTEE FIRST REPORT, *supra* note 84, ¶¶ 18–62 (providing a helpful summary of the main aspects of the debate).

tors that traditionally may have had different focuses.[192] But whether this statement, supplemented by the regulatory principles, actually gives the FSA a clear idea of its purpose and provides it with a workable basis on which to build a coherent and consistent system of effective financial regulation, are major questions that will be best examined through the lens of practical experience. At this stage it would seem sensible to have low expectations — the breadth of the objectives and the FSA's wide discretion with regard to their implementation, may mean that the objectives will prove to have limited value in pinpointing exactly what it is that the FSA is supposed to do and, accordingly, whether it has achieved its mandate.

A key set of issues will be those relating to the objective of maintaining confidence in the financial system and how the FSA's role in this respect relates to the Bank's continuing responsibility for the overall stability of the financial system, especially the stability of the monetary and payment financial systems.[193] Will this arrangement prove to be robust in dealing with systemic risks or will the U.K. model validate those who argue that the ability of a central bank to perform its role as overseer of the financial system is undermined if it is not also the regulator of banks and other institutions that present systemic concerns?[194] For now, these are largely questions for the

192. Jackson, *supra* note 123, at 339–63 (Pt. III explores cross-sectoral variation in U.S. financial regulation).

193. A memorandum of understanding between the FSA, the Bank of England and HM Treasury sets out their respective obligations with regard to financial regulation, details arrangements for Bank of England access to FSA supervisory records and sets outs procedures, in the form of monthly meetings, for cooperation between them. *See* Memorandum of Understanding Between HM Treasury, the Bank of England and the FSA (Oct. 28, 1997), *available at* http://www.hm-treasury.gov.uk/Documents/Financial_Services/Regulating_Financial_Services/fin_rfs_mou.cfm.

194. *See* EUROPEAN CENTRAL BANK, THE ROLE OF CENTRAL BANKS IN PRUDENTIAL SUPERVISION 7 (2001), *available at* http://www.ecb.int/pub/pdf/prudentialsupcbrole_en.pdf [hereinafter ECB, THE ROLE OF CENTRAL BANKS] (providing a recent restatement of the case for preservation of a fundamental role in prudential supervision for national central banks, with particular reference to the eurosystem). *See generally* Leonardo Bartolini, *The Financial Services Authority: Structure, Mandate and Policy Issues, in* HOSSEIN SAMIEI ET AL., INTERNATIONAL MONETARY FUND: UNITED KINGDOM EXPERIENCE (IMF Staff Country Report No. 99/44, 1999); GROS & LANNOO, *supra* note 178, at 140–43.

future,[195] but it is interesting to note that some of those within the U.K.'s financial industry who welcomed the original concept of the single regulator in the U.K. are now beginning to revisit the issue precisely because of concerns about the allocation of responsibilities between the Bank and the FSA.[196] The merits of the U.K. approach with regard to the allocation of responsibilities for financial stability have also been doubted by the European Central Bank.[197]

The FSA has made an inauspicious start concerning claims about the superiority of the single regulator model on the grounds of greater consistency in institutional approach and shorter and simpler lines of communication and cooperation between individual regulators. An FSA internal report on its handling of the crisis affecting a major insurance company in 1999 and 2000 specifically identified poor communication between regulators working within different departments of the FSA as a deficiency in regulation.[198] To date, this remains the most prominent and embarrassing example of the FSA failing to live up to its potential as an effective single regulator; however, there have been others. A more recent example is the criticism by influential bodies within the banking sector of the FSA's proposed prudential rules that, in their view, showed all

195. BRIAULT, REVISITING THE RATIONALE, *supra* note 141, at 14–15, 27–31 (considering the practical operation of this arrangement). Briault suggests that the tripartite arrangement between the Bank, the FSA, and the Treasury works well, although he acknowledges that "the arrangements have not yet been put to the test in a period of massive financial instability, or of the 'failure' of a firm (or firms) posing a significant systemic risk." *Id.* at 15. Others are more skeptical: "The memorandum created the impression they were working together fine, but there's still competition and jealousy of each other's turf. The Bank still considers itself to have some residual authority over the FSA." Faisal Islam, *One of our Governors is Missing: But is the Treasury Looking in the Wrong Place to Fill the Bank of England Job?*, OBSERVER, Sept. 1, 2002, at 5 (quoting Kern Alexander, Senior Fellow in International Law at the Judge Institute, Cambridge).

196. Views of Ian Mullen, Chief Executive of the British Bankers' Association ("BBA"), as reported in *BBA's Unhelpful Criticism Of Financial Services Authority — A Recent Speech By The Head of the British Bankers' Association, In Which He Lambasted The UK's Financial Services Authority, Is Unfair On The Super-regulator*, BANKER, June 1, 2002.

197. *See generally* EUROPEAN CENTRAL BANK, THE ROLE OF CENTRAL BANKS IN PRUDENTIAL SUPERVISION (2001), *available at* http://www.ecb.int/pub/pdf/prudentialsupcbrole_en.pdf.

198. BAIRD REPORT, *supra* note 135, ¶ 6.2.5.

the signs of having been drafted by specialist teams with no one taking overall responsibility to ensure a coherent and consistent approach.[199] In the short term, the FSA can use its youthful status and inexperience as a single regulator as an excuse for this type of regulatory shortcoming, but explanations of that sort will become less convincing as the regime matures.

D. A Single Regulator May be More/Less Accountable

In its simplest terms, the argument for a single regulator case on accountability grounds is that a single regulator has no other regulatory body to which it can transfer blame for regulatory failure.[200] It is suggested that the fact that "the buck stops here" provides the regulator with a strong incentive to establish a clear mandate, to stick to it in its practical operations, and to educate consumers of financial services on what protections they can and cannot reasonably expect from the regulatory system.[201] These features are connected with accountability because the more clearly the regulator's mandate and areas of responsibility are defined, the easier it should be for those who are affected by its operations to hold it accountable.[202] However, commentators also identify major concerns about accountability in relation to single regulators because of the all-embracing nature of their role and their concentrated and potentially draconian powers.[203] Can a single regulator be made properly accountable to an industry while avoiding regulatory capture? Can it be made properly accountable to consumers without creating false perceptions and possible moral hazard concerns about the extent to which the regulatory system will protect them from financial risks? If the single regulator is independent of government, as is the case in the U.K., by what mechanisms can it be held politically accountable in respect of

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199. *See* Press Release, British Bankers' Ass'n, BBA/LIBA Response to Consultation Paper 97 — The Integrated Prudential Sourcebook (Jan. 17, 2002), *available at* http://www.bba.org.uk/public/newsroom/35451/42733/45188?version=1.

200. GOODHART ET AL., *supra* note 12, at 152; Chris Hughes, *The Buck Stops Here*, INDEP., Oct. 3, 2001, at 1.

201. GOODHART ET AL, *supra* note 12, at 151–52

202. LARGE, *supra* note 50, at 82; JOINT COMMITTEE FIRST REPORT, *supra* note 84, ¶¶ 99–146; ROBERT BALDWIN & MARTIN CAVE, UNDERSTANDING REGULATION: THEORY, STRATEGY, PRACTICE ch. 21 (1999).

203. GOODHART ET AL., *supra* note 12, at 153–54.

its public interest functions? These questions are much debated in the literature on regulation and the arguments are often finely balanced. They were also major preoccupations in the public debate in the U.K. leading up to the adoption of the single regulator model.

Industry lobbying groups made extensive use of a nightmarish vision of the FSA as an over-mighty, over-powerful bully in their efforts to influence the content of the legislative framework from which it would derive its powers.[204] Particularly, in relation to its disciplinary and enforcement powers, lurid images of the FSA as legislator, prosecutor, judge, jury, and executioner all rolled into one were frequently invoked.[205] The FSMA, as finally enacted, does give the FSA very extensive powers, but there are also broad legislative control mechanisms which are intended to act as checks and balances against the FSA in the use of these powers.

The regulatory objectives and principles lie at the core of the accountability mechanisms. They are relevant to public accountability (i.e. accountability to industry and consumers), political accountability, and judicial accountability since they provide all interested parties with benchmarks against which to judge the FSA's performance. While the statutory statement of objectives and principles is broadly welcome as an improvement to the accountability framework, some of the more optimistic statements about the significance of the objectives and principles need to be viewed with care. For example, it has been suggested that the regulatory objectives and principles provide the basis for legal accountability because "the FSA could be challenged in the courts on the grounds that it has failed to pursue its objectives or to take the principles into account."[206] While this statement is certainly true, cases where legal challenges against the FSA on these grounds actually succeed are likely to be rare. This is because the FSMA gives the FSA considerable discretion as to how best to meet its objectives. Its duty to act in a way that is compatible with the objectives and, for the purpose of meeting them, extends only "so far as is reasonably pos-

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204. *See* Gary Parkinson, *FSA Bows to Criticisms of Being Judge and Jury in Enforcement Regime*, MONEY MARKETING, July 8, 1999, at 2.

205. Dan Atkinson, *"Judge, Jury and Executioner" Claims Defeat City Super-regulator*, GUARDIAN, July 6, 1999, at 22; Parkinson, *supra* note 204, at 2.

206. BRIAULT, REVISITING THE RATIONALE, *supra* note 141, at 12.

sible."[207] It is for the FSA itself to decide on the "most appropriate" way in which to meet the objectives.[208] Further, the obligations of the FSA with regard to the objectives only arise in relation to its "general functions" — its functions in making rules, issuing codes, and giving general guidance *considered as a whole* and its function of determining general policy and principles.[209] Similarly, the FSA is only required to "have regard" to the regulatory principles and, as with the objectives, this duty only arises in relation to the discharge of its general functions.[210] This careful drafting ensures that there is no mechanism for challenging individual rules or decisions on the grounds that they are incompatible with the objectives or principles. The qualified and self-referential nature of the duties regarding the regulatory objectives and principles appears likely to hamper the effectiveness of judicial review in practice.

Similar caution is appropriate at this stage in relation to other, more detailed, accountability mechanisms provided for in relation to the FSA because they have only been fully operative for a short period of time. Some important aspects are largely untested. For example the Financial Services and Markets Tribunal ("Tribunal"), which is an independent review body to which certain FSA decisions can be referred, has not yet heard a case through to completion. The provisions for the Tribunal in the legislative framework[211] are intended to assuage concerns about the all-embracing role of the FSA as judge, jury, etc, and to meet human rights-related concerns about the availability of independent, fair trials.[212] It has been envisaged that over time this Tribunal will play a key role in relation to FSA accountability.[213] However, the public nature of the Tribunal proceedings may in practice deter people from challenging FSA decisions via this route because of fears about adverse reputational consequences, even if the challenge is successful.

207. Financial Services and Markets Act, 2000, c. 8, § 2 (Eng.).

208. *Id.* § 2(1)(b).

209. *Id.* § 2(4).

210. *Id.* § 2(3)–(4).

211. *Id.* pt. IX.

212. Thomas A. Beazley, *Holding the Balance — Effective Enforcement, Procedural Fairness and Human Rights, in* REGULATING IN THE TWENTY-FIRST CENTURY, *supra* note 48, at 115–26.

213. FRESHFIELDS BRUCKHAUS DERINGER, FINANCIAL SERVICES: INVESTIGATIONS AND ENFORCEMENT 255 (2001). [hereinafter FRESHFIELDS].

The FSA Chairman has claimed that the "prime accountability route" for the FSA will be through Ministers to Parliament,[214] but some commentators have doubted how effective political accountability will be in relation to the FSA.[215] The FSA is an unusual hybrid. It is a private company limited by guarantee and its operations are funded entirely by industry levy.[216] However, the government exercises control in that the Treasury appoints the FSA board,[217] can order independent reviews of its financial affairs,[218] and can commission independent inquiries into regulatory failures.[219] The Treasury, however, cannot intervene directly in the affairs of the FSA, save in very limited circumstances concerned with competition policy.[220] The FSA must make an annual report to the Treasury.[221] The Treasury must put the FSA's report before Parliament.[222] FSA officials can also be ordered to appear before a parliamentary select committee in accordance with the usual procedures of the Houses of Parliament.[223] In practice, the Treasury Select Committee routinely takes evidence from the FSA twice a year, once on its plan and budget for the coming year, and once on its annual report for the previous year. It can also hold inquiries from time to time as it sees fit.[224] Views on whether the system of appearing before the Treasury Select Committee is likely to prove an effective form of accountability to Parliament, are mixed. Although the IMF considers that appearances by financial agency officials before a designated public authority — such as a parliamentary committee — promote accountability, especially when the agencies are granted a high degree of auton-

214. JOINT COMMITTEE FIRST REPORT, *supra* note 84, at Minutes of Evidence ¶ 2 (question 2, reply by Davies, Chairman FSA).
215. *See, e.g.,* Page, *supra* note 176, at 132–33.
216. Financial Services and Markets Act, 2000, c. 8, §§ 13–14, 17 (Eng.).
217. *Id.* § 1.
218. *Id.* § 12.
219. *Id.* § 14.
220. *Id.* § 308.
221. *Id.* sched. 1, § 10. The Treasury can direct the FSA with regard to the contents of the report.
222. *Id.* § 10(3).
223. *Id.* §§ 4–5.
224. *Id.* § 14.

omy,[225] others doubt this.[226] So far, the evidence indicates that appearing before the Treasury Select Committee can be a very uncomfortable short-term experience for FSA officials.[227] But long-term studies will be needed to establish whether this process has meaningful impact.

With regard to public accountability, the FSMA provides for a variety of consultation and disclosure requirements. The FSA is required to engage in public consultations before exercising rulemaking powers, including publication of rules in draft form accompanied by cost-benefit analysis.[228] The FSA has a general obligation to establish and maintain arrangements for consultation with consumers and practitioners.[229] This gives statutory backing to the arrangements that had previously operated in practice, whereby the FSA consulted with a Consumer Panel and a Practitioner Panel.[230] The FSA must have regard to any representations made by either of the panels and, if it disagrees, it must give a written statement of its reasons for doing so.[231]

Again, it is too early to test how well these requirements are working. There are some indications of dissatisfaction with the practical operation of the public consultation requirements,

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225. INTERNATIONAL MONETARY FUND, CODE OF GOOD PRACTICES ON TRANSPARENCY IN MONETARY AND FINANCIAL POLICIES: DECLARATION OF PRINCIPLES 13 (Sept. 1999), *available at* http://www.imf.org/external/np/mae/mft/code/eng/code2e.pdf.

226. Page, *supra* note 176, at 134–35.

227. As this selection of headlines from the press coverage of Davies' appearances before the Select Committee with regard to the Equitable Life crisis illustrates. Katherine Griffiths, *MPs Attack Davies Over Equitable Life Crisis,* INDEP., Oct. 31, 2001, at 17; Nina Montagu-Smith, *FSA Role Puzzles Equitable Inquiry*, DAILY TELEGRAPH, Nov. 14, 2001, at 36; *FSA Denies Collusion with Equitable*, INDEP., Nov. 14, 2001, at 21; *Davies to Face Second Grilling,* DAILY TELEGRAPH, Nov. 12, 2001, at 28.

228. Financial Services and Markets Act, 2000, c. 8, § 65 (Eng.) (guidelines for drafting statements or codes that the Authority may issue describing conduct expected of approved persons); *id.* § 121 (guidelines for drafting codes that the Authority must issue to give guidance for determining whether behavior amounts to market abuse); *id.* § 155 (guidelines for drafting rules under the Authority's general rule-making powers).

229. *Id.* §§ 8–9.

230. *See id.* §§ 9(1), 10(1); Press Release, FSA, Practitioner and Consumer Panels Go Statutory (June 18, 2001), *available at* http://www.fsa.gov.uk/pubs/press/2001/073.html.

231. Financial Services and Markets Act, 2000, c.8, § 11 (Eng.).

largely because of the sheer bulk of consultation material that the FSA has issued in the past few years, and the resources that have gone into responding to it.[232] Given the ambitious nature of the single regulator project in the U.K., it is hard to see how a large and costly consultation process could have been avoided, though it undoubtedly did generate "consultation fatigue."[233] However, if discontent about the burdens on industry and consumers, which are associated with the consultation requirements, does not diminish as the regime becomes more established, this could indicate a serious flaw within the system. The system will also have failed if the FSA develops a reputation for not listening to the criticisms expressed by those who respond to consultation exercises. The FSA will always be vulnerable to this charge, but time and experience will help to distinguish well-founded claims from exaggerated claims made to garner media attention for the self-interested views of a particular group or sector.[234]

Is the independence of the practitioner and consumer panels liable to be compromised because of their position within the formal institutional framework? To be sure, these panels are established by the FSA, the FSA board appoints the members, and it also funds their operation.[235] Moreover, the Consumer Panel, which operates more formally and publicly than the Practitioner Panel, is dependent on FSA staff for its secre-

232. Jill Treanor *FSA "Less Effective" Than Predecessors* GUARDIAN (London), Nov. 29, 2002, at 30; BBC News, *FSA World's "Most Accountable Regulator"* (Dec. 3, 2002), *at* http://news.bbc.co.uk/1/hi/business/2539001.stm.

233. INQUIRY INTO THE FINANCIAL SERVICES ASSOCIATION'S PRACTITIONER PANEL BEFORE THE SELECT COMMITTEE ON TREASURY (2002), *at* http://www.parliament.the-stationery-office.co.uk/pa/cm200102/cmselect/cmtreasy/600/2020503.htm (statement of Donald Brydon, Chairman of the Practitioner Panel & Chairman and Chief Executive of AXA Investment Managers) [hereinafter INQUIRY INTO THE FSA'S PRACTITIONER PANEL].

234. CSFI, WAKING UP TO THE FSA, *supra* note 128, at 13 (noting complaints from industry participants that their comments have been ignored by the FSA but suggests that this criticism is not altogether fair). The Consumers Association has also accused the FSA of failing to listen to objections about FSA proposals for new rules on the way financial products are sold to investors. Teresa Hunter, *Consumer Group Savages FSA Plans: CA Says Adviser Reforms will be Confusing and Add to Costs,* SUNDAY TELEGRAPH, Apr. 28, 2002, at 4; William Kay, *Consumers Rip into FSA Proposals*, INDEP., Apr. 27, 2002, at 1.

235. Financial Services and Markets Act, 2000, c. 8, § 1(9)–(10) (Eng.).

tariat.[236] All of these features suggest that the panels may struggle to achieve and maintain independence.[237] A report in *The Observer* on the Consumer Panel's annual report encapsulates the issue neatly with the comment: "Brown [chair of the Consumer Panel] remains confident and hopeful that the FSA can clean up the financial services industry. His own job depends on it, after all."[238] The counterargument is that the close links should facilitate constructive and better-informed dialogue between the FSA and the panels. The structure is, then, best viewed as a compromise between true arms-length independence, and privileged access to FSA information and personnel. Whether the optimal trade-offs have been made will be a question for future study.

V. A CONCLUSION AND SOME OBSERVATIONS

The U.K. embraced the single regulator concept in an ambitious way. It decided to bring many different regulatory agencies together into one single institution. Moreover, it decided to place its single regulator within a new, properly-integrated, legal framework, rather than simply giving it the powers that had been previously enjoyed by former regimes, which were divided by sector through a process of stitching together or consolidating existing legislation. Creating the new integrated legal framework was a massive, complex, and time-consuming exercise. Moreover, it was often highly controversial. But, in the end, it was done[239] and when the new system finally became fully operational, it happened smoothly without disruption to the markets.

Accordingly, one definite conclusion that can be drawn from the U.K. experience is that, if the political will is present, major reform of this type can actually be accomplished and effectuated

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236. *Id.* ¶ 1(10).

237. The Treasury Select Committee has expressed some concerns about the panel's lack of financial independence and the FSA's control over the selection processes. INQUIRY INTO THE FSA'S PRACTITIONER PANEL, *supra* note 233 (Question by Mr. Tyrie, Question 15; Question by Mr. Mudie, Questions 45–48; Question by Mr. Laws, Questions 89–90).

238. Maria Scott, *Cash: Incredible: "This Reckless Greed": Watchdog Attacks Industry Where "Consumer is a Dirty Word,"* OBSERVER, May 19, 2002, at 2.

239. Although details of the new legal regime at the level of the FSA Handbook are still to be overhauled. Davies, *Law and Regulation*, *supra* note 91, at 171–72.

within a mature, major international financial center. The U.K. experience also provides support for the intuitive assessment that political support for change will be greater where the existing system is, or is perceived to be, malfunctioning. Beyond this, it is impossible to draw firm conclusions, because the new regime is still in its infancy. Yet there are certainly many positive signs, in particular, the emphasis on an integrated approach to regulation across all parts of the financial services industry.

One interesting feature of the recent British experience with financial regulation is the extent to which the character of its new regime has been associated with its first Chairman, Howard Davies. It is hard to tell whether, or to what extent, the degree of identification of the new regime with a single individual is related to the unitary structure of the FSA, but there may be a significant connection. Arguments for the adoption of the single regulator model include economies of scale through unified management and staffing, and greater effectiveness through the development of a single, institutionalized approach to regulation. A corollary of these arguments is that managerial power will be concentrated in relatively few individuals. Thus, those at the very top of the structure should be in a particularly strong position to dominate the culture and institution. Questions about governance and structure are particularly important because the single regulator model is characterized by a regulatory regime vulnerable to the personal influence of a few individuals. Whether the FSA should have a separate chairman and chief executive is an issue that was sidestepped in relation to Davies because he was already in office by the time the question became a topic for public debate.[240] However, in a broad sense, the FSMA now requires the FSA to have regard to corporate governance principles.[241] Although the significance of the FSA's status as a company should not be taken too far, principles developed in the corporate sector to avoid the potential adverse effects of domination by one individual could, with suitable adaptation for the regulatory context, be useful as

240. JOINT COMMITTEE FIRST REPORT, *supra* note 84, ¶¶ 112–13.

241. Financial Services and Markets Act, 2000, c. 8, § 7 (Eng.). The duty is to have regard to such principles "as it is reasonable to regard as applicable to it." *Id.*

a way of addressing the potential problem of concentration of influence within the unitary FSA regime.

A potentially worrying sign emanating from the top of the FSA is the continuing enthusiasm for further legal change. Rather than giving its own staff, and everyone else, breathing space in which to work with the new regime, the FSA has declared itself to be a "reforming authority" and has announced "a considerable programme of reform to many parts of our rulebook."[242] This reforming zeal can be defended on the grounds that the process of fundamental legal reform that began in 1997 with the announcement of the proposal to adopt the single regulator model, is still incomplete because the review of the lower-tier rules, i.e. those in the FSA Handbook, that took place in the transitional period, was intended to achieve consistency and simplification rather than to re-think fundamental principles. Furthermore, standing still for a long time is not a sensible strategy in financial regulation because the system needs to evolve if it is not to lag too far behind developments in the market. But, while ossification of the system clearly would be in no-one's interests, the FSA needs to be careful not to act excessively in the pursuit of the goal of integrated regulation.

In the sometimes-fevered debate that surrounded the enactment of the FSMA, the prospect of the FSA using its disciplinary and enforcement powers excessively tended to attract the most attention. Those fears have receded, partly, but not exclusively,[243] because of legal intervention in the form of procedural safeguards and, in particular, the establishment of the Financial Services and Markets Tribunal. At present, there appears to be a reasonable degree of confidence in the robustness of these controls on the FSA's disciplinary powers,[244] although this confidence has not yet been properly tested under the pressure of practical, and perhaps controversial, experience. As a law-maker, the FSA is subject to looser forms of control, principally in the form of consultation and disclosure requirements, includ-

242. FINANCIAL SERVICES AUTHORITY, ANNUAL REPORT 5 (2001/2002), *available at* http://www.fsa.gov.uk/pubs/annual/ar01_02.pdf.

243. Changes in personnel at the top of the FSA enforcement division have also been thought to have played a part. In 2001, the head of the FSA's enforcement division was switched to a different position within the organization.

244. *See, e.g.,* FRESHFIELDS, *supra* note 213, at 255.

ing cost-benefit analysis, underpinned by its obligations with regard to statutory regulatory principles and objectives. How effective these controls will be is open to speculation, but it seems unlikely that they would prevent a drift towards a more legalistic and bureaucratic approach if that is the direction in which those in charge of the maturing FSA choose to take it.

But how much freedom will the FSA actually have to shape its own destiny as a rule-maker? A powerful constraint on the FSA's rule-making discretion is its obligation to give effect to EC law.[245] Significant parts of the FSA Handbook already reflect EC rules on banking, insurance, and securities regulation.[246] And the EC influence is increasing as central EC institutions vigorously pursue the goal of full financial integration.[247] There is a trend away from the established approach of minimum harmonization — where the minimum requirements are set at central EC level, but with discretion for member states to impose stricter requirements (sometimes known as "super-equivalence") towards maximum harmonization, where no deviation from the rules set by the central EC authorities is permitted.[248] Current trends suggest that national regulatory authorities of the EC member states will increasingly find their autonomy with regard to rulemaking eroded by obligations to give effect to requirements that have been set at EC level. Their role seems likely to shift from that of direct legislator to that of participant in the process whereby rules are developed at EC level.[249] The goal of ensuring consistency across member

245. Financial Services and Markets Act, 2000, c. 8, §§ 148, 410 (Eng.).

246. *See* FSA HANDBOOK, *available at* http://www.fsa.gov.uk/handbook (last modified Mar. 3, 2003)

247. H. Onno Ruding, Vice Chairman, Citibank, Remarks at the Sixth European Financial Markets Convention in Brussels (May 31, 2002), *available at* http://www.fese.be/initiatives/speeches/2002/efmc2002_ruding_speech.htm.

248. FINANCIAL SERVICES AUTHORITY, REVIEW OF THE LISTING REGIME ¶¶ 3.5–3.25 (July 2002) (discussing European developments and the controversy that the switch towards maximum harmonization has provoked with reference to the ability of national regulatory authorities to impose corporate governance or other qualitative standards beyond those that have been mandated at the European level).

249. Under the Lamfalussy principles national regulators are involved in standard-setting at Level 2 — i.e., filling in the technical details of framework legislation that has been agreed (at Level 1) by the main EC legislative organs. For an overview of the Lamfalussy principles, see Guido Ferrarini, *Pan-*

states would suggest that the EC rules are likely to be increasingly prescriptive with little interpretative discretion or waiver powers being allowed to individual national regulators.[250] So, even though the direct focus of the increasing EC activity is on standard-setting, it seems also likely to affect the day-to-day supervisory relationships between national regulators and regulated firms with regard, for example, to questions of interpretation of particular rules, and/or their application to particular facts, or to applications for rule-waivers in particular circumstances.

Some commentators go further and suggest that the EC is moving inexorably towards the establishment of new pan-European regulatory agencies that would perform the full range of regulatory and supervisory functions, including enforcement.[251] This debate has been particularly active in the securities field where the prospect of a European-Securities and Exchange Commission ("Euro-SEC") is much discussed.[252] It might be said that a shift of regulatory and supervisory powers from national to regional agencies is the logical next stage beyond regulatory consolidation at the national level, as a step in a process that would lead ultimately to the establishment of a single worldwide regulator. Even within Europe, which leads the world in the process of regional financial integration, it seems unlikely in the short-to-medium term that the FSA, or other national regulators, will be replaced by a single Euro-regulator or even (since EC regulation is still largely constructed along sectoral lines) by a group of sectorally-divided Euro-regulators. Banking might look like the most obvious candidate for the assumption of a full regulatory and supervisory role by European institutions but the European Central Bank, which is responsible for monetary policy within the euro

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European Securities Markets: Policy Issues and Regulatory Responses, 3 EUR. BUS. ORG. L. REV. § 2.3 (2002).

250. Level 3 of the Lamfalussy principles aims to encourage cooperation and networking between national regulators to ensure consistent and equivalent application of the rules. The recently-established Committee of European Securities Regulators (CESR) is to play a key role in issuing guidelines, joint interpretative guidance and so forth. *See id.*

251. NIAMH MOLONEY, EC SECURITIES REGULATION 896–97 (Francis G. Jacobs ed., 2002). Chapter 15 provides an admirable summary of the arguments for and against EC centralized regulation and supervision.

252. *Id.* at 843–97.

area, has recently affirmed that the division of responsibilities between itself and national authorities "would seem appropriate to tackle the changes triggered by the introduction of the euro."[253] Public policy debate on fundamental questions about the efficiency, effectiveness, and accountability of super-European regulatory and supervisory agencies is starting but, as yet, it is at an early stage.[254]

However things develop, it seems beyond doubt that in the short-to-medium term, the drive for further regulatory changes affecting the financial sector will come from Europe. It remains to be seen whether the U.K. will be in a strong position to influence change at that level because it has already been through radical upheaval domestically, or whether the U.K. will be found to have made a major strategic mistake by being inward-looking at a time when major reform initiatives were beginning to take shape at the European level. Domestically, although political challenges to the existence of the FSA are always possible, no major political party is likely to espouse the case for further radical, expensive, and disruptive change unless either the FSA fails to deliver the benefits claimed for the single regulator model or that model becomes wholly inappropriate because of changing market conditions. The latter point has particular current relevance because the general economic climate and specific events such as WorldCom and Enron have highlighted the particularly acute conflict of interest problems that can arise within financial supermarkets. These events have added an extra dimension to the debate about the advantages of the "universal banking" business model.[255] "Deconglomeration"

253. ECB, THE ROLE OF CENTRAL BANKS, *supra* note 194, at 7.

254. *See, e.g.,* Chris Bates, *Models for European Regulation: Euro-SEC, Euro-FSA or Lamfalussy?,* 17 J. INT'L BANKING & FIN. LAW 151 (2002); Jeroen Kremers et al., *Does Europe Need a Euro-wide Supervisor?,* 6 FIN. REG. 50 (2001).

255. *Thanks a Bundle — The Model of a Vast, Integrated Financial Firm is Fast Going Out of Favour,* ECONOMIST, Aug. 22, 2002, at 12; Wilmarth, *supra* note 113, at 272–312, 437–44 (discussing disappointing results achieved by banks resulting from big bank mergers). Wilmarth doubts the ability of big, complex financial institutions to produce positive synergies of scale or scope. *Id.* at 438. Further he suggests that arguments used in relation to disenchantment with conglomeration in the industrial sector (e.g., that managers are motivated to build large companies for self interested reasons rather than in pursuit of better returns for investors) are also applicable to the financial sector. *Id.* at 284–85.

within the financial sector could occur as it did previously in the industrial sector. If firms were to retreat back to the safety of traditional sectorally-divided business, claims about the good "fit" of the single regulator model to the nature of regulated markets and firms would become increasingly hollow.

Time and experience should provide some answers to questions and concerns about the single regulator model that have been raised in this article. The U.K. will now be a valuable source of data on whether, or in what ways, the single regulator model is superior to alternative models of regulation, in terms of suitability, efficiency, effectiveness, and accountability. Practical operation of the new regime will also shed light on the robustness of an ambitious, tailor-made, legislative framework that was designed expressly to help secure the potential benefits of the single regulator model and avoid its possible drawbacks.[256]

256. *See* BRIAULT, REVISITING THE RATIONALE, *supra* note 141, at 11 (identifying the U.K.'s integrated legislative framework as being a particular advantage).