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Ian Price and Janet Brown
Financial Services Authority
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By E-Mail: cp12_26@fsa.gov.uk

14 December 2012

Dear Mr. Price and Ms. Brown

Re: FSA Consultation Paper FSA CP12/26 (Regulatory reform: the PRA and FCA regimes for Approved Persons)

The City of London Law Society represents approximately 15,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi jurisdictional legal issues.

This response to FSA Consultation Paper CP12/26 (Regulatory reform: the PRA and FCA regimes for Approved Persons) has been prepared by the CLLS Regulatory Law Committee (the "**Committee**"). Members of the Committee advise a wide range of firms across Europe who operate in or use the services provided by the financial markets and in particular advise a wide range of credit intermediaries, investment managers, custodians, private equity, debt and other specialist fund managers.

We welcome the efforts made by the FSA to set out the thinking on how matters will transition from the current regime into the prospective PRA and FCA regimes, and note that there is inevitable uncertainty without the benefit of knowing what provision will be made under the Bill currently before Parliament about transitional matters.

However, there are several high-level concerns about the proposals in CP12/26 which the Committee wishes to raise.

1. We are concerned that there is unnecessary complexity in the proposals – particularly in relation to the interaction between the CF2 category for PRA and that for FCA in dual-regulated institutions. The proposals are not easy to grasp, the drafting and the explanations are not clear and consequently give rise to potential difficulties in practice and understanding, which then carries unnecessary risk that regulated institutions and their senior staff will not apply the requirements

accurately. We suggest that this is not consistent with the objectives of either the FSA or the FCA and PRA going forward.

2. We appreciate that the proposed extension of scope of the approved persons regime reflects the FSA's expectation that approved persons should apply the same standards of behaviour in their wider roles, and would to some extent assist in ensuring that the regime is less exposed to unexpected issues such as those which arose in the context of LIBOR setting. However, it raises a number of issues:

2.1 It is disappointing that no case has been made out for such a significant extension of the scope of the APER regime, beyond a reference to clarification of the FSA's expectations, and a statement of the FSA's belief that this will not result in any significant changes for most people. The absence of any further explanation or reasoning is all the more disappointing given some inherent uncertainties in the proposal, coupled with the fact that the current regime already provides a mechanism for taking into account wider issues of fitness and propriety.

2.2 The breadth of the definition of "significant-influence function", once disconnected from specified controlled functions, potentially imports considerable uncertainty into the scope of the regime and the applicability of the SIF Statements of Principle (Principles 5 to 7) to particular functions. Accordingly, greater clarity is needed in respect of both (i) the additional functions the extended APER regime is intended to catch; and (ii) what responsibilities are to be associated with which functions.

The wording of the SIF Statements of Principle appears to relate the duties to be imposed, in connection with the performance of an accountable function, to the business for which the SIF is responsible. However, if the performance of particular functions is to attract regulatory duties beyond the specific controlled functions for which such person is approved, then it is important that the allocation of responsibility for the business or part of the business should be specifically laid down, whether through regulation or guidance, or in firm policies and procedures or by management directive, and in circumstances where the individual knows that he has been tasked with that responsibility.

Given the potentially onerous responsibilities associated with being an approved person (particularly the higher-risk controlled functions), such uncertainty as to the extension of scope of their responsibilities may discourage individuals from agreeing to be registered as an approved person, which in turn might make the UK less attractive to overseas investors. We also consider, that in order for a person properly to understand and be aware of the obligations associated with a function assigned to them, that person should have the opportunity to receive notice of the exact scope of the obligations and responsibilities assigned to them and to acknowledge them before becoming accountable.

"Significant-influence function" is defined as a function that is likely to enable the person responsible for its performance to exercise a significant influence on the

conduct of the authorised person's affairs, in relation to the carrying on of a regulated activity by that authorised person.

"Influence" should flow from the controlled function that the relevant person is appointed to perform and not, as the consultation paper suggests, the characteristics of the relevant person. In this context, "influence" is plainly intended to extend beyond direct decision-making and is, we assume, intended to cover participation in joint-decision making. It would be unfair and disproportionate for persons who should not be within scope to be caught merely because, for example:

- they make recommendations, or give advice, that is generally followed by the firm, or the relevant business within the firm; or
- they express opinions which are viewed as authoritative, or, further, who is viewed as authoritative by virtue of their personal strength, leadership qualities, effectiveness or engagement.

The Regulatory scope and responsibility should not be determined by reference to an individual's personal characteristics, still less by the reactions of others to a particular individual.

If the regulators decline to specify, as controlled functions, those functions which they envisage would be significant influence functions, then the intention must be that the responsibility for so doing should fall to the firm or, perhaps less appropriately, to the individual. In that event, it would be very helpful to provide further guidance about what it is envisaged constitutes "influence" and how, and by reference to what, the significance of such influence is to be measured.

2.3 We assume that the proposals are not intended to bring within the scope of regulation and regulatory scrutiny both the nature and competence of legal advice provided to the firm by in-house lawyers who hold a PRA or FCA SIF function (the FSA has always been very clear in this regard). However, as presently framed, the proposals would have the potential to do so, and Statement of Principle 4 could have the effect of requiring legal advisers to report to the regulator matters on which legal advice had been sought, in circumstances where this would amount to a breach of their professional obligations.

It is of critical importance both for the firm and the regulator that there should be full and open communication between the legal function and the business, and that the legal function should have the ability to provide unbiased and independent advice on financial services law and regulation, and on potential legal issues and risks which may arise in relation to particular activities, products, services and systems.

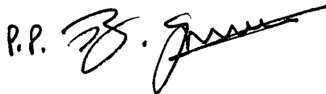
To open such legal advice up to the scrutiny of financial services regulators would represent a significant erosion of the firm's right to legal privilege, a fundamental human right recognised by the English common law, and which the European Court

of Human Rights held in *Campbell v United Kingdom* [1992] 15 EHRR 137 to be part of the right to privacy guaranteed by Article 8 of the European Convention of Human Rights. Indeed, section 413 of FSMA recognises that persons cannot be required to produce or disclose protected items (including communications).

2.4 Finally, the proposals appear to provide that (for dual regulated institutions) an approved person may be at risk of action by either or both of the PRA and FCA for breaches of the Approved Persons Code provisions. This potential for a double jeopardy has not been justified, and appears disproportionate. An individual ought to be able to ascertain which regulator has jurisdiction, and thus what its policies and approach is, beforehand. He ought not to be faced with the prospect that if one regulator begins action and discontinues it, the other may (in effect) be entitled to bring a consecutive action in respect of the same factual matrix. The Memorandum of Understanding (the "**MoU**") between the PRA and FCA should provide that, without fettering their discretion, the PRA and FCA will confer over the taking of regulatory action and that such action should be taken only in relation to the controlled functions for which each such regulator is responsible. Moreover, where there is overlap in the functions specified by them, the PRA and FCA should be required (by the MoU) to determine which regulator will have responsibility for considering (and if justified taking) regulatory action against individuals.

If the FSA would find it helpful to discuss any of these comments then we would be happy to do so. Please contact me in the first instance by telephone on +44 (0) 20 7295 3233 or by email at margaret.chamberlain@traverssmith.com.

Yours sincerely



Margaret Chamberlain
Chair, CLLS Regulatory Law Committee

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THE CITY OF LONDON LAW SOCIETY
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