E-Briefing Detailed Version
(Covering the period from 1 Sept – 18 October 2010)

1. Current consultations

1.A. Handbook consultation

The SRA recently released the second handbook consultation "The Architecture of Change Part 2 - the new SRA Handbook - feedback and further consultation" (see http://www.sra.org.uk/sra/consultations/OFR-handbook-October.page for details. The CLLS's Professional Rules and Regulation Committee (PR&RC) is taking the lead in responding to this consultation
)
The consultation period ends on 13 January 2011. The paper states, *inter alia*:

> **1. Executive summary**
>
> 1. This consultation is the last opportunity for comments on the SRA's new Handbook which will underpin the regulation of solicitors and law firms from October 2011. It builds on the foundations laid in "The Architecture of Change: the new SRA Handbook" (the May Consultation). The May Consultation initiated the implementation process for outcomes-focused regulation (OFR). This paper takes that process a step further by providing more detail on the regulatory framework for both traditional law firms and alternative business structures (ABSs) …
>
> …4. In this paper we:
> o report on the feedback which we received to our May Consultation;
> o propose further changes to the new SRA Code of Conduct (the Code) and other sets of rules in the Handbook; and o consult on further sets of rules.
>
> …6...The SRA is undertaking an extensive change programme in order to ensure that both our staff and our operations are able to meet the challenges of implementing OFR. This includes a major IT programme and also assessment and training of our staff. We are also making extensive preparations for communications programme to guide firms and individuals through the transition to the new Handbook and OFR;
>
> …Our approach to information requirements is discussed in this paper and we will shortly be issuing prototypes of forms to illustrate the sort of information that we will be requesting;
>
> …We intend to provide firms with further information generally to enable them to make the transition. We will publish information on our website during the coming months.
>
> …7. Some of the concerns expressed related to our overall approach to supervision and enforcement. We will be giving further information about these in our November 2010 publication.
>
> …8...The cost-benefit analysis on our outcomes-focused regulatory approach will be published in November 2010.
>
> **..2. Introduction**
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> …11. We intend that the new Handbook and our outcomes-focused approach to authorisation, supervision and enforcement, will bring about a culture change in the provision of legal services. One of the key catalysts for this change is the opening up of the legal services market to new entrants. …

…13. In summary, this paper sets out:

- the revised structure of the new SRA Handbook which will contain all our regulatory requirements for both firms and individuals, for in-house[2] and overseas practice, and explains the implementation timeline; o further consultation on revisions to the:
- SRA Principles;
- SRA Code of Conduct; and
- requirements contained in the Specialist Services; Authorisation, and Practising Requirements; Discipline and Costs Recovery and Client Protection sections of the Handbook, based on the responses to the May Consultation;
- final version of rules on which we consulted on in May (e.g. the SRA Accounts Rules);

14. We invite further views on our revised proposals. We have set out some questions throughout this paper upon which we should be particularly grateful for your views. You will find a complete list of the questions at Annex M.

3. A new approach to regulation

Strategic objectives – our evidence-based approach

…16…

- risk-based regulation enables the SRA to focus resources on problem firms, which should enhance public confidence in the delivery of legal services and drive down the costs associated with regulating problem firms;
- OFR benefits are increased flexibility, reduced bureaucracy and better client service.

Alternative business structures

…36…(iii) our ultimate concern is the fragmentation of the legal services market into unregulated firms which provide poor standards of service and put client money at risk, and high quality, professionally run and regulated firms providing reserved legal services.

Multi-disciplinary practices

…38. Our working group involving other regulators and professional bodies will continue to tease out and resolve some difficult issues in relation to MDP ABSs, both in the run up to October 2011 and beyond. These discussions will be reflected in the FMOU which we plan to publish in December 2010 and in other communications.

4. Architecture of the new Handbook - bringing principles and outcomes to the heart of our regime

…40. We are committed to the implementation of a regulatory regime that has at its heart the right outcomes for consumers whilst being proportionate to the risks that we have identified. Outcomes-focused regulation enables us to move away from a "one size fits all" approach, since it introduces greater flexibility and opportunities for innovation, based on clients' requirements.

…46…In relation to the glossary, this is still in the process of development, which reflects the fact that our rules themselves are at different stages of completion. We will be consulting on the new glossary in the second quarter of 2011 in order to finalise it prior to October 2011.

47. The SRA is committed to OFR since we believe that this is the model which most accurately reflects our focus on client protection and service.

Principles and guidance

…61. We remain of the view that the Principles should apply both to firms and to all those who work within firms, and this is confirmed in the application provisions to the Principles.

…62… We have reconsidered our approach to issuing guidance. Throughout the Handbook, where we consider it appropriate to do so, we have provided guidance (for example in the notes to the Accounts Rules and in the Authorisation Rules). In relation to the Code, we wish to avoid the risk of guidance being regarded as mandatory. We have, therefore, reviewed, and where appropriate amended and expanded the non mandatory indicative behaviours, which fulfil a similar function to that of guidance. …We intend to assist users further by publishing material on our website aimed at easing the transition from the current to the new regulatory regime. This will include frequently asked questions, guidance on particular issues that arise, "decision trees" and a user manual that will assist firms and individuals in making the transition to a more outcomes-focused approach to meeting their regulatory obligations. We also agree with the suggestion that we publish anonymised examples of achievement and non-achievement of the outcomes in the Code.

5. Conduct of legal services

(a) SRA Code

…76. We have reviewed the [indicative behaviours (IBs)] for their application to City firms. We would also stress that IBs are not mandatory and that firms have the option to achieve the outcomes in other ways.

…78. … The approach that we are taking also includes:
o publishing for consumers a set of key outcomes that we expect firms to achieve for their clients;

…79. The Introduction to the Code has been revised to make it clear both that IBs are not mandatory and that firms and individuals have choices in terms of how they meet the outcomes. We encourage practitioners to meet the outcomes in a way that is most appropriate for their clients, be they FTSE 100 companies or particularly vulnerable individuals. We also make it clear that non-compliance with IBs will not, of itself, constitute grounds for disciplinary action.

Specific issues
(a) Conflicts of interests

…83. Of the models offered, respondents tended to favour Model 2. However, there was broad support for the retention of requirements similar to the existing rules. This was because the majority of respondents felt that now was not the time for significant change to the conflict of interest provisions, despite the re-drafting of the Code and that the SRA should, therefore, retain both the emphasis in, and form of, the existing provisions.

(b) Separate business rule

…89. We have reviewed the specific drafting comments. We continue to believe, however, that there is a need to restrict regulated firms (and individuals currently providing reserved legal services) from providing non-reserved legal activities through a separate business.

(c) In-house and overseas practice

…94.. Having reviewed the feedback to the consultation, we decided to reintroduce the solicitor-controlled (albeit now recast as "lawyer-controlled") restriction on the application of the Code to overseas practice (note, however, that the Principles do apply to all overseas practice). We have also reviewed the outcomes, and specifically highlighted those that are not applicable (or should apply in a modified form) to overseas practice. We are, however, undertaking a more general review of the regulation of overseas practice in the next 12 months.

Further consultation

…96…Whilst we acknowledge the strong support for the retention of the existing rules to cover conflicts of interests, we believe that the rules needed to be reviewed to ensure consistency and clarity and to emphasise the required outcomes. For this reason we have re-drafted the main rules and the exceptions as outcomes, and clarified the extent of the exceptions;

…97. The Code will come into force for ABSs on the date on which the SRA is designated as a licensing authority and, for recognised bodies and sole practitioners, on 6 October 2011.

(c) Specialist Services

Financial services
…129... ABSs which are authorised and regulated by the SRA would not be able to be treated as an authorised professional firm in the same way as traditional law firms. The FSA has agreed to consult on an amendment to the definition in the FSA Handbook so that ABSs can be treated as authorised professional firms.
…

6. Engaging with the SRA - authorisation and discipline of firms and individuals, and training requirements

Authorisation Rules

…. 153…Further guidance on the authorisation process (including the information to be collected at authorisation) will be included in our November publication concerning the April consultation (''Outcomes-focused regulation - transforming the SRA's regulation of legal services'').

….161…with a view to ensuring that our approach is proportionate, we are considering using self-certification of achievement of given outcomes. We are looking at models of reporting used by other professional regulators and in some other jurisdictions.

SRA Disciplinary Procedure Rules

Specific issues

(a) Financial penalty criteria

206. … By October 2011 the SRA is likely to have powers to levy significantly larger financial penalties under the LSA regime, and will be regulating increasingly diverse business models. The Rules, therefore, set out a new set of financial penalty criteria at Appendix 2 to the Rules.

207. The Rules include new concepts for the SRA, e.g., discounting for early admissions and restitution and suspension of a penalty.

9. Timetable and next steps

Reminder of the timeline

279….The overall timetable is set out below:

Date	Action
November 2010	Report on and response to April 2010 Consultation ("Outcomes-focused regulation - transforming the SRA's regulation of legal services")
13 January 2011	Closing date for written responses to this consultation
April 2011	Publication of final Handbook
August 2011	Anticipated designation of SRA as a Licensing Authority for ABSs
6 October 2011	First ABSs licensed and implementation of new Handbook
April 2013	Special bodies able to apply to be licensed

1.B. European Commission's Green Paper on policy options for progress towards a European Contract Law for consumers and businesses

In July this year, the European Commission launched a Green Paper on policy options for progress towards a European Contract Law for consumers and businesses. (See http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2010:0348:FIN:en:PDF for details.). Comments on the paper are due: on **31st January 2011**. The paper states, *inter alia:*

1. PURPOSE OF THE GREEN PAPER

…The purpose of this Green Paper is to set out the options on how to strengthen the internal market by making progress in the area of European Contract Law, and launch a public consultation on them. Depending on the evaluation of the results of the consultation, the Commission could propose further action by 2012. Any legislative proposal will be accompanied by an appropriate impact assessment.

The Union could fill contract law gaps by adopting effective tools for the removal of market barriers relating to diverging contract laws.

…. the Commission has set up an Expert Group to study the feasibility of a user-friendly instrument of European Contract Law, capable of benefiting consumers and businesses which, at the same time, would provide for legal certainty. The Group will assist the Commission in selecting those parts of the [Draft Common Frame of Reference (DCFR)[1]] which are directly or indirectly related to contract law, and in restructuring, revising and supplementing the selected provisions. It will also take into

[1] Von Bar, C., Clive, E. and Schulte Nölke, H. (eds.), Principles, Definitions and Model Rules of European Private Law. Draft Common Frame of Reference (DCFR), Munich, Sellier, 2009

consideration other relevant sources in this area, as well as the contributions to the present consultation. The Group gathers the expertise from the Union's different legal traditions and stakeholders' interests. Members were selected from among reputable experts in the area of civil law, in particular contract law, and are acting independently and in the public interest. The results of the public consultation launched by this Green Paper will inform the on-going work of the Expert Group….

3. CHALLENGES FOR THE INTERNAL MARKET

3.1. Business-to-consumer contracts….

…Businesses wishing to engage in.. ..cross-border trade may face high legal costs when their contracts are subject to foreign consumer law. In extreme cases, some businesses may even refuse to sell across borders and thus potential consumers of that company may be locked in their national markets and be deprived of the enhanced choice and lower prices offered by the internal market. This may be particularly relevant in e-commerce transactions. Even if the website of a seller could be accessed by consumers from all the Member States, because of the related costs and risks, the seller may refuse to conclude contracts with consumers from other Member States. For example, for 61% of cross-border e-commerce offers, consumers were not able to place an order mainly because businesses refused to serve the consumer's country. Thus, the potential of cross-border e-commerce remains partly unfulfilled, to the detriment of both businesses, in particular SMEs, and consumers.

The Commission's Proposal for a Consumer Rights Directive addresses some of these problems by aiming at simplifying and consolidating the existing legislation in the area of consumer contract law, on the basis of a fully harmonised set of key internal market aspects of consumer contract law. However, even if adopted as proposed, it would not render fully compatible the national contract laws of the Member States in the non-harmonised areas. Also in the areas of fully harmonised provisions, there would be a need to apply them in conjunction with other national provisions of general contract law. Moreover, two years of intense negotiations in the European Parliament and Council have highlighted that there are limits to an approach based on full harmonisation. Consequently, differences between the contract laws of the Member States will remain a reality even after the adoption of the Directive and businesses wishing to sell cross-border will have to comply with them.

….3.2. Business-to-business contracts

… Large companies with strong bargaining power can ensure that their contracts are subject to a particular national law. This may be more difficult for SMEs and therefore raise obstacles to pursuing a uniform commercial policy across the Union, thus preventing businesses from grasping opportunities in the internal market. Furthermore, ensuring compliance with different systems of contract law or obtaining information about the law applicable in another Member State and in another language might increase legal costs.

Whereas for certain specialised types of contract having a strong international dimension, such as shipping contracts, businesses may already have become familiar with the laws commonly used for governing this type of transaction, this is not necessarily always the case. In addition, for more general commercial transactions, businesses might benefit from an instrument setting out a uniform set of rules of European Contract Law which would be easily accessible in all official languages. This could provide greater reassurance to businesses engaged in cross-border trade, which might quickly familiarise themselves with such a system by using it in all dealings with businesses in other Member States. In such dealings, it could also come to be seen as an alternative to the Member States national contract laws and a neutral modern contract law regime drawing on the common national law traditions in

a clear and user-friendly manner. Such an option could be particularly attractive for SMEs venturing into new markets for the first time…..

…**4. CHOOSING THE BEST INSTRUMENT FOR EUROPEAN CONTRACT LAW**

…. the instrument should be comprehensive and self-standing, in the sense that references to national laws or international instruments should be as much as possible reduced. Several options have been identified, in respect of the legal nature, the scope of application and the material scope of the future instrument…..

…**4.1. What should be the legal nature of the instrument of European Contract Law?**

…

Option 1: Publication of the results of the Expert Group

The outcome of the work of the Expert Group could be made easily available, by immediate publication on the website of the Commission, without any endorsement at Union level. If the Expert Group produces a practical and user-friendly text, this could be used by European and national legislators as a source of inspiration when drafting legislation and by contractual parties when drafting their standard terms and conditions. It could also be used in higher education or professional training as a compendium drawn from the different contract law traditions of the Member States. Extensive use of this work could contribute, in the long term, to the voluntary convergence of national contract laws.

However, this solution could not address the internal market barriers. Divergences in contract law would not be significantly reduced by a text which has no formal authority or status for courts and legislators.

…Option 2: An official "toolbox" for the legislator

…Option 3: Commission Recommendation on European Contract Law

…Option 4: Regulation setting up an optional instrument of European Contract Law

A Regulation could set up an optional instrument, which would be conceived as a "2nd Regime" in each Member State, thus providing parties with an option between two regimes of domestic contract law.

It would insert into the national laws of the 27 Member States a comprehensive and, as much as possible, self-standing set of contract law rules which could be chosen by the parties as the law regulating their contracts. It would provide parties, primarily those wishing to operate in the internal market, with an alternative set of rules. The instrument could be applicable in cross-border contracts only, or in both cross-border and domestic contracts….

…Option 5: Directive on European Contract Law

… Option 6: Regulation establishing a European Contract Law

… Option 7: Regulation establishing a European Civil Code

…**4.2. What should be the scope of application of the instrument?**

An instrument of contract law could cover several areas of application.

4.2.1. Should the instrument cover both business-to-consumer and business-to-business contracts?

… the instrument could also contain specific provisions, the application of which would only be triggered in certain types of contracts, for example, mandatory

> provisions ensuring a high level of consumer protection. These would come into play when a transaction involves a consumer and a business party[30].
> Separate instruments for business-to-consumer and business-to-business contracts could also be envisaged. In principle, separate instruments could better tackle issues which are specific to these types of contracts and would be easier to elaborate and use.
>
> For reasons of consistency, the instrument of European Contract Law will have to complement the relevant consumer *acquis,* by integrating its requirements, including progress made on consumer protection in the internal market in the Consumer Rights Directive.
>
> …an instrument tailor-made for the online world could be developed. This could be applicable in both cross-border and domestic situations, or only in cross-border situations.

The Ministry of Justice has subsequently launched a "Call for Evidence on the European Commission's Green Paper about European Contract Law". (See http://www.justice.gov.uk/consultations/call-for-evidence-180810.htm for details.) The Call for Evidence exercise runs until **26 November 2010**. Representatives from a number of CLLS Committees have met to consider issues arising from the Call for Evidence and work on preparing the CLLS response is being led by the CLLS Construction Law Committee. The document states, *inter alia:*

> The UK Government, in association with the Scottish Government and Northern Ireland Executive, is seeking evidence and views to inform the UK response to a European Commission public consultation about European contract law.
>
> …Your response is requested by *26 November 2010.* Responses are needed by then to allow adequate time to consider properly all those received and then frame a response in time to meet the Commission's deadline.
>
> … To help frame responses there appears below a framework of questions flowing from the Commission's Green Paper.
>
> … *Background*
>
> Confidence in the system of contract law is essential if trade is to be carried out effectively. Cross-border trade introduces an additional dimension which necessitates the parties agreeing which country's law should apply, and rules on applicable law that would apply if no choice is made.
>
> The Commission has overseen a long-standing project looking at the issue of European contract law.
>
> *…Discussion & Questions*
>
> *The need for and purpose of any European Union work in this sphere*
> The Green Paper assumes throughout that the current divergence of laws of contract and private international law rules present problems for business and consumers alike in cross-border trade, and that this may hinder the smooth operation of the internal market. The Commission puts forward a number of possible factors (e.g. higher transaction costs) which, it argues, suggest action is needed. It goes on to discuss ways that this divergence of laws might somehow be reduced and how that might affect outcomes.
>
> The UK Government will want to be satisfied that there is genuine evidence of a problem for cross-border trade associated with the differences among national laws, before considering whether any EU intervention in the area of contract law is needed

or desirable. Respondents' views and evidence on this question are particularly sought.

Question 1
Does the current regulation of contract law, and in particular divergence of laws at national level, present problems? If problems are present, how significant are they? How can any problems be quantified, and who is affected by them?

Question 2
What are your views on the relative advantages and disadvantages of each of the options and sub-options identified in the Green Paper? In particular, which should be preferred and why?

Question 3
Should any future work/response cover any or all of:

- business-to-business contracts?
- business-to-consumer contracts?
- on-line transactions?

What are the specific points that lead you to conclude this?
Should any solution attempt to regulate both
What would be the priority needs to be addressed for each of these groups and how might that be done? What would be the key features of any solution and why?

Question 4
What should be the preferred "material scope" of any instrument? In particular should it:
(a) have a narrow or a broad scope (see paragraphs 4.3.1 & 2 of the Green Paper)?
(b) Cover all or only specific types of contracts – which ones and why (paragraph 4.3.3)?
(c) If a code is created should it also cover any other issues and what might those be (see paragraph 4.3.4 of the Green Paper which specifically mentions tort, unjustified enrichment and the benevolent intervention in another's affairs as possibilities here)?

Question 5
Are there any other matters not covered in the Commission's Green Paper or this Call for Evidence which you think should be addressed in this exercise and any following work? What are those issues and why should they be covered here?

2. Recent submissions and publications

2.1. Specialist Committees

2.1.1. Company Law

The Company Law Committee and Regulatory Law Committee both responded to the HMT consultation document Cm 7874 "A new approach to financial regulation: judgement, focus and stability". (See http://www.official-documents.gov.uk/document/cm78/7874/7874.pdf for the consultation document and http://www.citysolicitors.org.uk/FileServer.aspx?oID=863&lID=0 for the Company Law Committee's response and http://www.citysolicitors.org.uk/FileServer.aspx?oID=870&lID=0 for the Regulatory Law Committee's response.) The Regulatory Law Committee's response is set out in more detail under heading 2.1.3 below.

The executive summary of the consultation document stated:

Introduction

The financial crisis and the failure of the UK regulatory framework

1.1 The UK banking system is emerging from the most serious financial crisis in over a hundred years. In order to avert a total banking collapse, the last Government had to part-nationalise two of the largest banks in the world, and introduce financial sector interventions costing hundreds of billions of pounds.

1.2 Much has been written - in academic journals, in the business press, and in books dedicated to the subject - about the recent financial crisis, and its impact on the global economy. There is now an emerging consensus on the fundamental causes of the crisis, citing factors such as:

- global economic imbalances;
- mispriced and misunderstood risk;
- unsustainable funding and business models for banks;
- excessive build up of debt across the financial system; and
- the growth of an unregulated 'shadow banking' system

1.3 The UK financial system, which is one of the most open, globalised and successful in the world, was impacted by these factors as much as, if not more than, any other. Attempting to explain the crisis purely in terms of global trends, however, is to ignore a fundamentally important point; there were real and significant failings in the UK regulatory framework. This meant that regulators failed in recognising and responding to the problems that were emerging in the financial system.

1.4 The UK's 'tripartite' regulatory system made three authorities - the Bank of England (the Bank), the Financial Services Authority (FSA) and the Treasury - collectively responsible for financial stability, and, as a result, this system failed in a number of important ways. For example, it failed:

- to identify the problems that were building up in the financial system;
- to take steps to mitigate them before they led to significant instability in financial markets; and
- to deal adequately with the crisis when it did break, especially during the first part of the crisis in the summer of 2007.

1.5 These failures arose because the tripartite model contains a number of inherent weaknesses and contradictions. For example:

- it places responsibility for all financial regulation in the hands of a single, monolithic financial regulator, the Financial Services Authority (FSA), which is expected to deal with issues ranging from the safety and soundness of the largest global investment banks to the customer practices of the smallest high-street financial adviser;
- it gives the Bank nominal responsibility - and, since the Banking Act 2009, statutory obligations - for financial stability, but does not provide it with the tools or levers to carry out this role effectively; and
- it gives the Treasury responsibility for maintaining the overall legal and institutional framework, but no clear responsibility for dealing with a crisis which put tens of billions of pounds worth of public funds at risk.

1.6 Perhaps the most obvious failing of the UK system, however, is the fact that no single institution has the responsibility, authority or powers to monitor the system as a whole, identify potentially destabilising trends, and respond to them with concerted action. This is a problem which Lord Turner, the chairman of the FSA, and Paul Tucker, Deputy Governor of the Bank for financial stability, have referred to as 'underlap': a phenomenon whereby macro-prudential risk analysis and mitigation fell between the gaps in the UK regulatory system.

1.7 Lord Turner has also identified, in addition to macro-prudential 'underlap', the fact that the FSA's approach to micro-prudential regulation was flawed. In the run up to the financial crisis, financial supervision relied too much on 'tick-box' compliance with rules and directives at the expense of proper in-depth and strategic risk analysis.

Effective prudential regulation of firms requires an approach based on understanding of their business models, and the ability to make judgements about the risks that firms' activities pose to themselves and to the wider financial system as a whole.

1.8 Under Lord Turner and Hector Sants, the FSA's chief executive, the FSA has made significant progress in identifying and fixing these problems. The Government believes, however, that more fundamental reform than this will be necessary. This is why, as announced by the Chancellor in his Mansion House speech on 16 June 2010, the Government is now embarking on a programme of reform to renew the UK's system of financial regulation, and to make it stronger and more effective for the future.

Reforming the tripartite model

1.9 In addition to dealing with the operational failings of the system introduced between 1997 and 2000, the Government believes that reform to the regulatory framework must address a number of fundamental issues.

Macro-prudential regulation

1.10 First, there must be a dedicated focus on macro-prudential analysis and action, to ensure that risks developing across the financial system as a whole are identified and responded to. That is why the Government will create a new Financial Policy Committee (FPC) in the Bank of England, with primary statutory responsibility for maintaining financial stability. Unlike in the current system, which provides the Bank with responsibility but no tools for financial stability, the Government will provide the FPC with control of macro-prudential tools to ensure that systemic risks to financial stability are dealt with.

1.11 The majority of the FPC's members will be Bank executives, to bring the expertise and understanding of the financial system that only a central bank can provide. The Governor and current Deputy Governors for financial stability and monetary policy will be joined by a new Deputy Governor for prudential regulation, as well as two other Bank executives. But the FPC will also include external members to ensure that wider perspectives - including from other regulatory bodies, and from the markets themselves - are fed into the Committee's work. The FPC will be a transparent and accountable institution, with appropriate lines of accountability into the Court of Directors of the Bank of England and the Treasury, as well as broader accountability to Parliament.

1.12 The Government recognises that in the modern, globalised financial system, macro-prudential action will need to be internationally coordinated to be effective. The FPC will therefore work internationally with similar systemically-focused authorities, such as the G20 Financial Stability Board, and the European Systemic Risk Board, as well as national regulators where appropriate, to coordinate macro-prudential policy.

Prudential regulation of individual firms

1.13 Second, the regulatory architecture has to ensure that macro-prudential regulation of the financial system is coordinated effectively with the prudential regulation of individual firms, and that a new, more judgement-focused approach to regulation of firms is adopted so that business models can be challenged, risks identified and action taken to preserve stability.

1.14 That is why the Government will transfer operational responsibility for prudential regulation from the FSA to a new subsidiary of the Bank of England. This new Prudential Regulation Authority (PRA) will be responsible for prudential regulation of all deposit-taking institutions, insurers and investment banks. The PRA will have a board chaired by the Governor of the Bank, and a chief executive who will also be the newly created Deputy Governor for prudential regulation.

1.15 By placing firm-specific prudential regulation under the auspices of the Bank, the Government will bring together responsibility for macro- and micro-prudential

regulation in a single institution. There will no longer be a gap in which responsibilities are unclear, and regulatory powers uncertain. The FPC will be able, within the remit of macro-prudential policy, to require the PRA to take regulatory action with respect to all firms. For example, the FPC may require an increase in the capital held by firms during an upswing in the credit cycle. The PRA would implement this change and monitor compliance through its supervisory function. The FPC may also suggest amendments to rules to make the system more resilient. And the FPC could have similar macro-prudential controls over the new conduct regulator, the consumer protection and markets authority (CPMA), should conduct-based macro-prudential tools be developed.

1.16 At the same time, the PRA will also be operationally responsible for the regulation and supervision of individual firms. It will provide firm-specific information to the FPC to illustrate the potential impact of emerging system-level risks on specific types of institution. Its board, chaired by the Governor, and with the Deputy Governor for prudential regulation as chief executive, will have responsibility for all rule-making. Responsibility for significant regulatory decisions affecting firms - for example, on authorisation, supervision, or enforcement of rules or sanctions - will be delegated from the board to an executive committee, which, where conflicts of interest allow, may include non-executive directors on an occasional basis to ensure that they are exposed to the mechanics of firm-specific regulatory and supervisory decision-making.

1.17 A key function of this executive committee will be to rebalance the operations of the prudential regulator away from rules and more towards the exercise of judgements based on supervisory information. The executive committee will thus play an important leadership role in supporting the creation of a new regulatory culture within the PRA.

1.18 As the prudential regulator, the PRA will represent the UK on the new European supervisory authorities for banking and insurance, ensuring that there is a strong and credible voice to promote the UK's interests in these new institutions, and cooperating effectively with European counterparts on the regulation of large, cross-border financial firms.

Consumer protection and markets regulation

1.19 Third, regulation of conduct within the financial system - including the conduct of firms towards their retail customers, and the conduct of participants in wholesale financial markets
will be carried out by a dedicated, specialist body with focused and clear statutory objectives and regulatory functions.

1.20 Prudential and conduct of business regulation require different approaches and cultures, and combining them in the same organisation is difficult. As a result of the combined remit of the FSA, participants in financial services and markets, particularly ordinary consumers of retail products, did not always get the degree of regulatory focus or the protection they may have expected or required.

1.21 The Government will therefore create a dedicated consumer protection and markets authority (CPMA) with a primary statutory responsibility to promote confidence in financial services and markets. This objective will have two important components. First, the protection of consumers through a strong consumer division within the CPMA. And second, through promoting confidence in the integrity and efficiency of the UK's financial markets.

1.22 In its consumer-focused role, the CPMA will therefore take on all the FSA's responsibilities for conduct of business regulation and supervision of all firms, as well as arms-length oversight of the Financial Ombudsman Service, the Consumer Financial Education Body, and the Financial Services Compensation Scheme. The

creation of a regulator with specific responsibility for consumer protection will ensure that the interests of consumers are not forgotten about or subordinated.

1.23 At the same time, a markets division within the CPMA will regulate all aspects of the conduct of participants in wholesale markets, as well as various elements of market infrastructure such as investment exchanges. The CPMA markets division will also represent the UK at the new European Securities and Markets Authority.

1.24 These arrangements will enable the new conduct regulator to develop real focus and specialism in the two areas of its remit, consumer protection and market integrity. This will benefit not only consumers and wholesale markets, but will also enhance financial stability. By identifying potentially significant consumer protection or market integrity issues and bringing them to the attention of the FPC - on which its chief executive will sit - the CPMA will ensure that such risks are not only identified, but dealt with as quickly as possible.

Structure and purpose of this document

1.25 This document sets out the Government's plans in more detail, as follows:

- Chapter 2 describes changes to the Bank of England and the creation of the Financial Policy Committee as the macro-prudential authority;
- Chapters 3 and 4 set out the roles, responsibilities and governance of the PRA and the CPMA;
- Chapter 5 considers the issue of market regulation;
- Chapter 6 considers the coordination of the regulatory bodies in a potential crisis; and
- Chapter 7 sets out the next steps for the reform programme, including public consultation, legislative passage, and operational implementation by the Bank and FSA.

1.26 The document presents a range of issues and questions for consultation. Annex A explains how readers can respond to the consultation process. The Government will, on the basis of this consultation and continuing policy development by the Treasury, present more detailed proposals - including draft legislation - for further consultation early in 2011. As indicated in the Queen's Speech in June, the Government will bring forward legislation to implement its reform programme in the first session of the Parliament, with a view to securing Royal Assent within two years.

The Company Law Committee's response stated, *inter alia:*

By way of background, we think it is important to note that the wider Treasury review is a response to challenges and problems arising out of the financial crisis. However, in our view market regulation in the UK worked well during the financial crisis and on issues such as market abuse and short-selling, the ability of one regulator (the FSA) to consider and address the relevant points (a classic example of an integrated primary/secondary market issue) was very important and contributed to effective and very timely action, where the UK demonstrated that it was at the forefront of the global response. We are concerned that to separate the UKLA from the regulator with primary responsibility for the regulation of the capital markets risks a reduction in the efficiency of UK market regulation and the capacity of the system to respond to future crises.

Anything which makes capital raising in the UK markets for UK companies less effective and less attractive with no compensating regulatory benefit seems to us misguided.

We suggest that any decision on this aspect of the architecture of financial regulation in the UK should be tested against the following objectives:

- to ensure that the UKLA is able to maintain and enhance its reputation as an effective regulator of the primary capital markets in the UK, sensitive to commercial and market realities, while at the same time ensuring that high

standards of behaviour are achieved.
- to ensure that the UK has a strong voice in ESMA on matters of primary market regulation, able to influence future policy and rule making in a way that will allow the capital markets in the UK to retain their leading position.

The Company Law and Regulatory Law Committees also jointly responded with the Law Society to the European Commission consultation paper "Corporate governance in financial institutions and remuneration policies**"**. (See http://ec.europa.eu/internal_market/consultations/2010/governance_en.htm for the consultation paper and http://www.citysolicitors.org.uk/FileServer.aspx?oID=874&lID=0 for the response.)

The consultation paper stated, *inter alia:*

> ***GREEN PAPER***
> ***Corporate governance in financial institutions and remuneration policies***
> ***(Text with EEA relevance)***
>
> ***1.*** Introduction
>
> The scale of the financial crisis triggered by the bankruptcy of Lehman Brothers in autumn 2008 and linked to the inappropriate securitisation of US subprime mortgage debt led governments around the world to question the effective strength of financial institutions and the suitability of their regulatory and supervisory systems to deal with financial innovation in a globalised world. The massive injection of public funding in the US and Europe - up to 25% of GDP - was accompanied by a strong political will to learn the lessons of the financial crisis in all its dimensions to prevent such a situation happening again in the future.
>
> In its Communication of 4 March 2009[1], effectively a programme for reforming the regulatory and supervisory framework for financial markets based on the conclusions of the Larosiere report[2], the European Commission announced that it would (i) examine corporate governance rules and practice within financial institutions, particularly banks, in the light of the financial crisis, and (ii) where appropriate, make recommendations, or even propose regulatory measures, in order to remedy any weaknesses in the corporate governance system in this key sector of the economy. Strengthening corporate governance is at the heart of the Commission's programme of financial market reform and crisis prevention. Sustainable growth cannot exist without awareness and healthy management of risks within a company.
> As highlighted by the Larosiere report, it is clear that boards of directors, like supervisory authorities, rarely comprehended either the nature or scale of the risks they were facing. In many cases, the shareholders did not properly perform their role as owners of the companies. Although corporate governance did not directly cause the crisis, the lack of effective control mechanisms contributed significantly to excessive risk-taking on the part of financial institutions. This general observation is all the more worrying because corporate governance has been relied upon as one of the ways of regulating business life. Consequently, there is a need to address the fundamental question of whether the existing corporate governance regime is deficient as far as financial institutions are concerned or whether it has rather been poorly implemented.
>
> In the financial services sector, corporate governance should take account of the interests of other stakeholders (depositors, savers, life insurance policy holders, etc), as well as the stability of the financial system, due to the systemic nature of many players. At the same time, it is important to avoid any moral hazard by not diminishing the responsibility of private stakeholders. It is therefore the responsibility of the board of directors, under the supervision of the shareholders, to set the tone and in particular to define the strategy, risk profile and appetite for risk of the institution it is governing.

> The options outlined in this Green Paper are likely to accompany and supplement the legal provisions implemented or planned for the purpose of strengthening the financial system, in particular in the context of the reform of the European supervisory architecture[3], the Capital Requirements Directive (the 'CRD')[4], the Solvency II Directive[5] for insurance companies, reform of the UCITS system and the regulation of Alternative Investment Fund Managers.
> Corporate governance requirements should also take account of a financial institution's type (retail bank, investment bank) and size. The principles of sound corporate governance referred to in this Green Paper focus primarily on large financial institutions. These principles should be adapted so as to be applied effectively to smaller financial institutions.
>
> This Green Paper should be read in conjunction with the Commission Staff Working Paper (COM(2010) XYZ) **'Corporate governance in financial institutions: the lessons to be learnt from the current financial crisis and possible steps forward.** This document takes stock of the situation.
>
> It is also important to point out that, since its meeting in Washington on 15 November 2008, the G20 has endeavoured to improve, amongst other things, risk management and compensation practices within financial institutions[6].
>
> Lastly, the Commission will soon launch a broader review on corporate governance within listed companies in general and, in particular, on the place and role of shareholders, the distribution of duties between shareholders and boards of directors with regard to supervising senior management teams, the composition of boards of directors, and corporate social responsibility.

The joint response stated, *inter alia:*

> In our view corporate governance is a developing and evolving area and it is particularly ill-suited to legislation and prescription. What is right for one company and set of stakeholders is inappropriate for another and in general the standards of corporate governance expected of or appropriate for companies needs to be proportionate to their size and the risks which they face.
>
> We have benefited in the UK from a best practice Code of Corporate Governance applied on a 'comply or explain' basis. We believe that a comply or explain approach to corporate governance allows the standards to be set higher than would be the case if Member States had to agree on a legislative approach and that the standards can be reviewed and adjusted more frequently than would be the case for legislation. Whilst in the case of banks and financial institutions (BOFIs) corporate governance requirements may be bolstered by supervisors/regulators imposing specific compliance requirements, we still believe that a code of best practice chosen by each Member State is the correct underlying approach.
>
> We should also note that we consider some of the points made in the consultation in relation to BOFIs to be well made, but we do not consider that the same points hold true for companies which are not BOFIs and in particular we consider that it is only in the case of BOFIs that compliance with corporate governance standards may need to be made subject to supervision or regulation by any external bodies in addition to shareholders.
>
> We consider excessive regulation of BOFIs to be a threat to the competitiveness of the EU and its markets. We hope that consideration will be given both to the huge amount of change that has already occurred in relation to the corporate governance of BOFIs and to the cost of compliance with new EU legislation which is imposed over member state practice which is already functioning effectively in most cases.

The response then went on to deal with the specific questions in the consultation document.

2.1.2 Litigation

The Litigation Committee responded to the Civil Justice Council Consultation on a Self Regulatory Code for Third Party Funding (See http://www.civiljusticecouncil.gov.uk/files/TPF_consultation_paper_v1.4_FINAL.doc for the consultation document and http://www.citysolicitors.org.uk/FileServer.aspx?oID=857&lID=0 for the response.). The consultation document states, *inter alia:*

> … Background
> Third Party Funders provide financial support for litigation on the basis that they receive a share of the sums recovered if they succeed, but nothing if the action fails
>
> …. On 25-26 February 2010 , a final stakeholder consultation event was held, to discuss a further draft of the Code of Conduct in the context of Lord Justice Jackson's findings, and to discuss the formation of an Association to promote and oversee self regulation.
>
> Following the event, the Code of Conduct was revised into its final form, and five major funders agreed to take forward the establishment of an Association. A draft Constitution was prepared, and these documents form the basis of this consultation…..
>
> …. The CJC will initially consider the responses to the consultation. After the responses have been considered, it will make recommendations and consult with the Executive of the Council, the full Council and the Ministry of Justice. Recommendations will then be made to the Lord Chancellor and Secretary of State for Justice. …

The response stated, *inter alia:*

> We deal with the four consultation questions in turn:
> **1. Do you consider that the Code of Conduct for the Funding by Third Parties of Litigation in England and Wales, in its current form, should be endorsed by the CJC as best practice for commercial litigation funders? If not, what improvements should be made?**
> As a general point, we agree that, at this early stage of the development of the third party funding market, self-regulation is the way forward. Things are to some degree at an experimental stage and we believe that statutory regulation would risk being too prescriptive and might miss the mark. With self-regulation, there is more chance for sensible rules to evolve. Statutory regulation now might strangle the child at birth. (The response then went on to make detailed comments on the draft code.)
>
> **...2. Do you consider that the Constitution for an Association of Litigation Funders in its current form should be endorsed by the CJC as best practice for commercial litigation funders?**
> Our only comment on this is that the lower limit of £500,000 for membership may present an unjustified barrier to entry for those wishing to enter the litigation funding market. We suggest there should be no lower limit.
>
> **3. Will the Code or Constitution have any impact on your area of business or sector - particularly in terms of benefits or costs?**
> We believe not in the short term. LFAs are still relatively uncommon in high value civil claims (which is the case load of the members of the Committee) and they will remain subject to individual negotiation by the parties in each case. Nevertheless we wanted to give feedback on the Code as we envisage that, over time, elements of the Code

may find their way into industry standard agreements. To that extent, we would like to see the Code get off 'on the right foot'.

2.1.3 Regulatory Law

As above, the Company Law and Regulatory Law Committees also jointly responded to the European Commission consultation paper "Corporate governance in financial institutions and remuneration policies". (See http://ec.europa.eu/internal_market/consultations/2010/governance_en.htm for the consultation paper and [TBA] [R1]for the response.)

The Regulatory Law Committee also responded to FSA Consultation Paper 10/15 "Quarterly consultation No.25"- Chapter 8 ("Client Money and Assets")
. (See http://www.fsa.gov.uk/pages/Library/Policy/CP/2010/10_15.shtml for the consultation document and
http://www.citysolicitors.org.uk/FileServer.aspx?oID=855&lID=0 for the response.).
The relevant chapter of the consultation paper stated, *inter alia:*

> This chapter proposes changes to the Client Assets Sourcebook (CASS) Chapter 6 'Custody rules', and Chapter 7 'Client money rules' in relation to the Title Transfer Collateral Arrangements (TTCA) rules and associated guidance, and guidance associated with the 'Money due and payable to the firm' rules.
>
> 8.2 The changes proposed will apply to all firms to which CASS 6 and 7 apply, and will affect those firms using TTCA to reduce the client money they segregate for their retail clients.

The response stated, *inter alia:*

> ….We have confined our responses to those questions relating to the proposed changes in Chapter 8 in respect of Title Transfer Collateral Arrangements **("TTCA")….**We are concerned that the inability to engage in TTCA with retail clients will in practice deny retail clients access to products in respect of which TTCA are an integral part (for example, stock lending and repos). Where such products are governed by industry standard terms which provide for TTCA, it is unlikely that firms will modify the products to remove TTCA. Accordingly, the result is likely to be that firms will withdraw these products from retail clients. FSA has not indicated that it has identified any problems with TTCA in respect of these products.

The Committee also responded to FSA Consultation Paper "Revising the Remuneration Code" (See
http://www.fsa.gov.uk/pages/Library/Policy/CP/2010/10_19.shtml for the consultation paper and http://www.citysolicitors.org.uk/FileServer.aspx?oID=869&lID=0 for the response. The consultation paper stated, *inter alia:*

> 1.1 This Consultation Paper (CP) proposes, and formally consults on, changes to our 1.1 Remuneration Code (the Code), as set out in the FSA Handbook (see SYSC1 19). Chapter 2 sets out the reasons why these changes are required. These include the passing of the Financial Services Act 2010 in April 2010, and the amendments to the Capital Requirements Directive (CRD3) which come into force on 1 January 2011. As its name implies, CRD3 is principally concerned with revisions to capital requirements, but it also contains important provisions relating to remuneration practices.

As the response stated, *inter alia*

In view of the intervention into individual contractual rights, which includes in some cases rendering or purporting to render contractual provisions void, it is also important to have as much clarity as possible on the applicable requirements. We are very concerned to ensure that the final rules can be understood by and be relevant and fair to the very wide range of firms to which they will apply. Many of these firms will have no direct supervisory relationship within which to raise the host of questions to which the rules give rise, and so the further guidance we request below on a number of provisions will be essential if such firms are to have any chance of understanding and applying the rules to their particular businesses. Limited licence and limited activity firms have not been considered in any detail at all by those who drafted CRD3. Rather the "proportionality" principle has been inserted to deal with them and it is critical that this principle is applied with sensitivity to businesses that are not banks or otherwise systemically relevant.

We set out below our responses to a number of specific consultation questions and comments on certain other areas where we consider that further attention to clarification and proportionate application is needed. We note that there may be changes arising out of the finalisation of the text of CRD3 and/or CEBS guidelines in October and as a result our current views may be modified and we may need to write again.

We appreciate that we have made a lengthy submission, but the issues are very important and many of our comments raise relatively technical matters which are important but which go to clarity of the text rather than anything more substantive.

…. 6.2 As general points:

(a) We believe that the CP and draft rules do not yet fully take account of these CRD3 provisions. While the proportionality proposals made by the FSA are helpful we do not believe they extend as far as is needed in some areas. We trust that the FSA will encourage CEBS also to take full account of these recitals and the general need for proportionality in any guidance it issues. We note that the UK is probably relatively unusual in Europe for having a very substantial number of independent investment firms (asset managers, brokers and others) which are not also banks or part of banking or insurance groups. Proportionate application to such firms is therefore particularly important in the UK.

(b) It will be necessary to incorporate the proportionality guidance fully into the body of the Rules. We agree it is important to have a general provision, such as that in 19.3.3 (and for consistency we suggest the proportionality wording in 19.2.2(3) is also amended to track Recital 4 CRD3) in order to enable the tailoring of the Code to be proportionate to each firm. In addition we believe that the views that the FSA has reached on aspects of the Code which it will not be proportionate to apply to certain types of firm should be set out expressly in guidance to the Rules.

(c) This can be done on a rule by rule basis but the table format used in Annex 5 is also a helpful approach, once it is clearly linked in to the text of the Rules and Guidance.

(d) A number of our comments relating to proportionality appear in our answer to Q5 and elsewhere in our response.

…1. The division of responsibilities and coordination of processes (Questions 5)

Our main concern (a concern which also informs many of the more specific points made below) is that the consultation document underestimates the difficulties of unpicking and dividing up the present legislation (principally FSMA itself, but also including the Regulated Activities Order and the FSA's rules made under FSMA) and distributing responsibilities for the various elements between the PRA and the CPMA; and overestimates the virtues of what is referred to as the "collegiate" solution to the supervision of institutions subject to the jurisdiction of both authorities.

We observe that:

- notwithstanding the assertions in the consultation document that *"prudential and conduct of business regulation require different approaches and cultures"* not suited to be housed in a single regulator, recent experience has [led] both the regulator and the regulated to acknowledge that *"prudentiaf* and *"conduct* labels do not often denote distinct regulatory jurisdictions, but rather different aspects of the same territory (for example, the quality of a firm's management or its systems and controls). Any partition of FSMA, the RAO and the FSA's Handbook will need to take this into account and will, accordingly, be extremely complex - with inevitable implementation difficulties for regulators and firms.
- given the above-quoted major premise as to the necessity to separate conduct from prudential regulation, it is a surprising proposal that the CPMA will become a prudential and conduct regulator of the majority of firms. It will seemingly be both in fact (and, we understand, law) a continuation of the FSA but with a truncated constituency.
- the necessity of establishing collegiate arrangements for major institutions effectively reestablishes a 'shadow' single regulator for such institutions - but without the benefit of a properly unified regulatory organisation and with all the complexities and burdens, for the regulated constituency, of dealing with two formally separate regulators (as to which see the more particular comments below).

As above, the Company Law Committee and Regulatory Law Committee both responded to the HMT consultation document Cm 7874 “A new approach to financial regulation: judgement, focus and stability”. (See http://www.official-documents.gov.uk/document/cm78/7874/7874.pdf for the consultation document and http://www.citysolicitors.org.uk/FileServer.aspx?oID=863&lID=0 for the Company Law Committee’s response and http://www.citysolicitors.org.uk/FileServer.aspx?oID=870&lID=0 for the Regulatory Law Committee’s response.)

The Regulatory Law Committee’s response stated, *inter alia:*

> The Committee would like to comment on certain issues and questions raised in the Government's consultation on reforming the UK's financial regulatory architecture.
> We start (somewhat reluctantly, as will be apparent from our more detailed comments following) from the premise that the high level structural reforms which have been proposed by the Government, namely the creation of the FPC and the transfer of the FSA's existing regulatory functions and responsibilities to, principally, two new regulatory authorities, is a fait accompli in the sense that it reflects a political policy decision taken in the run-up to the recent election and re-affirmed shortly thereafter. This premise is reflected by the nature of the questions posed in Annex A to the consultation document.
>
> We shall not therefore comment further on that 'macro' aspect of the proposals.

The response went on to provide detailed comments under the following headings:

1. The division of responsibilities and coordination of processes (Questions 5)
2. Statutory objectives (Questions 4 and 10)
3. Rule-making powers and accountability (Questions 4, 6, 7 and 9)
4. Authorisation, approval and passporting processes (Question 5)
5. Enforcement, including market abuse
6. Regulation of markets (Question 17 and 18)
7. Crisis management (Questions 19 to 21)
8. International influence
9. Implementation

2.1.4 Revenue Law

The Revenue Law Committee responded to the HMT discussion document on Foreign Branch Taxation (see http://www.hm-treasury.gov.uk/consult_taxation_of_foreign_branches.htm for the discussion document and http://www.citysolicitors.org.uk/FileServer.aspx?oID=858&lID=0 for the response.). As the discussion document stated, *inter alia:*

> This discussion document contains options for reforming the taxation of the foreign branches of UK companies.
>
> This consultation deals with the taxation of foreign branches of UK companies. The Government is not looking to reform the taxation of the UK branches of foreign companies.
>
> The Impact Assessment for the options set out in this discussion document can be found at: http://www.hm-treasury.gov.uk/consult_taxation_of_foreign_branches.htm The Government would like to hear the views of business, as well as the views of representative bodies and tax advisers, on the options set out in this discussion document and the questions posed.
>
> **Introduction**
>
> 1.1 The Government is committed to delivering a more territorial approach to corporation tax and is considering the case for exempting the profits of foreign branches (sometimes known as "permanent establishments") of UK companies. Broadly, a foreign branch is established by a UK company if it carries on part of its trade in another jurisdiction without establishing a separate trading subsidiary company there.
>
> 1.2 The Government recognises that developments in the regulation of financial services companies have made the issue of taxing foreign branch profits a pressing matter for affected companies. At the same time, the Government is aware that the choice of regime for foreign branch taxation could have an impact on companies in other sectors, such as the oil and gas sector.
>
> 1.3 The Government is consulting on the form of an exemption regime for foreign branch profits, to enhance the UK's competitiveness and to achieve greater consistency of tax treatment between foreign branches and subsidiaries of UK companies. It will be necessary to give careful consideration to the treatment of losses incurred in foreign branches, and this discussion document includes options on this issue. The consultation will consider the impact on the UK's competitiveness for all sectors. In considering the options for a new regime, the Government will also balance a number of other factors, including simplicity, fairness and affordability.
>
> 1.4 The Government has established a working group of interested parties.[1] The working group will hold meetings over the summer and autumn to discuss the questions and options in this discussion document. Together with the written responses received to this discussion document, the working group will help inform the Government's decision on the shape of the new regime. Detailed proposals and draft legislation will then be published later in 2010. Consultation will continue over the winter, with legislation to be included in [the] Finance Bill 2011
>
> …1.6 Chapter 2 of this discussion document sets out the context for reform, including the principles against which the Government will assess policy options, international comparisons of branch exemption regimes and an outline of the sectors likely to be most affected by changes to the rules.

> …2.4 The Government is also committed to achieving fairness and simplicity in the tax system, and will assess the options for reform in the context of these principles.

The submission responded to the questions listed in Chapter 5 of the consultation document.

The Revenue Law Committee also responded to the joint HMRC/HMT/BIS consultation document "Modernisation of the tax rules for investment trust companies and Modernisation of company law rules on distributions by investment companies". (See http://customs.hmrc.gov.uk/channelsPortalWebApp/channelsPortalWebApp.portal?_nfpb=true&_pageLabel=pageLibrary_ConsultationDocuments&propertyType=document&columns=1&id=HMCE_PROD1_030622 for the consultation document and http://www.citysolicitors.org.uk/FileServer.aspx?oID=860&lID=0 for the response.) As the consultation document stated:

> **Subject of this consultation:** Views are invited on the proposed changes to the tax rules that provide an exemption from Corporation Tax (CT) on chargeable gains of investment trust companies and on possible amendments to the Companies Act 2006 in respect of investment companies.
>
> **Scope of this consultation:** This is a joint consultation being undertaken by HM Revenue & Customs (HMRC), HM Treasury (HMT) and the Department for Business, Innovation and Skills (BIS).
> HMRC and HMT invite views on possible modernisation of the tax rules for investment trust companies.
> BIS invites views on possible changes to the provisions on distributions by investment companies in the Companies Act 2006.
> Comments on the points raised in this document will be taken into account in proposals for legislative and procedural rules for investment trust companies and investment companies

The response stated, *inter alia:*

- We welcome the proposals to modernise the investment trust rules for the first time since their introduction. As stated in the consultation document the marketplace has changed significantly since 1965.
- We believe it is vital that the UK is able to offer a tax efficient closed-ended investment vehicle as otherwise funds will continue to be established offshore.
- We generally welcome the proposal to set out the conditions and administrative rules in secondary legislation so that changes can be made more quickly to adapt the rules to reflect market changes etc. We hope that this will be accompanied by detailed HMRC guidance on the rules and regulations which we would want to be finalised before the new regime is introduced (as opposed to the position under the offshore funds reform where the final HMRC guidance was only published some six months after the new regime came into effect).
- We have seen a draft of the proposed submission by the Association of Investment Companies which we support subject to our comments below.

The Committee then went on to make a series of specific comments in relation to the consultation paper.

Robert Leeder
Policy & Committees Coordinator