20 years on: is financial services regulation in the UK still fit for purpose?

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On 1 December 2001, the UK adopted a radical new approach to the regulation of financial services. Some nine individual regulators of different parts of the financial services industry were merged into a single regulator – the Financial Services Authority. At the same time, a common Ombudsman and Compensation Scheme were established. The change represented a switch from self-regulation, particularly in the area of personal investments, to a harmonised statutory basis of regulation under the Financial Services and Markets Act 2000 (FSMA), with a single regulator able to oversee the market as a whole.

What has changed in the 20 years since? Well, the scope of regulation has extended beyond recognition. Surprisingly, mortgages and insurance mediation were not part of the FSA's original remit but were brought within scope in 2004 and 2005 respectively. The EU's Financial Services Action Plan changed the European regulatory landscape and heavily shaped the UK rulebook, conflicting to some extent with the original purity and coherence of the FSMA regime. Consumer credit and claims management companies have been brought into the fold, with pre-paid funeral plans due to be added in July 2022. Payment services and e-money sit half in, half out – not covered by FSMA but subject to supervision by the FCA under their own regimes.

The most fundamental structural change came in 2013 with the splitting of the FSA into the Prudential Regulation Authority, a division of the Bank of England, taking responsibility for the authorisation and oversight of banks, insurers and the largest asset managers. This left the FSA (rebranded the FCA) responsible for authorising everything else and regulating the conduct of the firms that the PRA authorises. The benefits of a single regulator were lost in favour of a "twin peaks" model that arguably owed more to a political urge to "do something" in the wake of the financial crisis of 2008 than anything else.

Culturally, we have seen a significant shift in the FCA's approach to regulation since 2015, when it acquired concurrent powers as a competition regulator alongside the Competition and Markets Authority. The way in which the FCA intervenes has become more outcomes-focused and informed by market studies and behavioural economics rather than traditional assumptions about how consumers of financial services should behave. In areas such as insurance the FCA is becoming close to, if not actually, a price regulator. The proposed new consumer duty, on which the FCA is currently consulting, will add a further layer of regulation on top of the existing rulebooks.

Twenty years on, while much of the original architecture is still visible, the effect of all of these changes is that the UK regulatory edifice has come to resemble a house that has been subjected to so many awkward and poorly-designed extensions that perhaps the kindest thing would be to tear it down and rebuild from the ground up. The UK's departure from the EU represents an opportunity to restore some of the original consistency and coherence to the regulatory regime by removing unnecessary complexity which adds to the cost of regulation with little or no benefit to the end user or to UK financial stability. The design concept behind FSMA remains fit for purpose, but the current legal and regulatory architecture is confusing and, more importantly, risks becoming a competitive disadvantage to the UK.

To take one example, the FCA's Senior Management Arrangements, Systems and Controls (SYSC) part of the Handbook contains 31 chapters. No one firm will be subject to all of those chapters, however, and chapter 1 requires 66 pages and over 19,000 words just to explain how the rest of SYSC applies to different types of firm. Even once you have found which rules apply, there are 7 sets of transitional provisions in place which may also need to be considered. There is a clear need to make the FCA Handbook in particular easier to navigate for the 51,000 firms that the FCA regulates, as well as to make engagement with both regulators easier and quicker.

The regime, and the regulators, also need to be able to adapt to new technologies and be accessible to new providers, including those from outside the financial services mainstream. This is vital to enable UK consumers to be able to take advantage of new products and services while maintaining appropriate and proportionate protections to enable a rapid response to emerging risks.

The Treasury's *Future Regulatory Framework Review* published in November represents a welcome move in this direction, but may not go far enough. The need to convert retained EU law into PRA and FCA rules should also be seen as an opportunity to iron out inconsistencies and restore coherence and accessibility to the regulatory landscape. The proposed addition of a new growth and international competitiveness objective as a secondary objective is welcome, but it will need a new mindset on the part of the regulators and a willingness to take bold steps to simplify and improve regulation, in place of the endless accretion of additional layers of text with little apparent thought as to the overall effect.

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