# Gem Briefing Note 12/1

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GEM Compliance Consulting

# Transition to the new regulatory structure

## Implementing 'twin peaks' within the FSA

### Introduction

In a speech by Hector Sants, Chief Executive of the FSA, at the British Bankers Association, Mr Sants provided an update on the abolition of the FSA and the transition to the new regulatory structure in the UK, the 'twin peaks' style regulatory model.

### Background

As previously announced, prudential supervision for banks, insurers and major investment firms is due to be transferred from the FSA to a new body called the Prudential Regulation Authority ('PRA'). The FSA will be abolished and will be replaced by the Financial Conduct Authority ('FCA') which will focus on consumer protection and market regulation. All firms not supervised by the PRA will be supervised for both prudential and conduct issues by the FCA. In addition, the FCA will supervise conduct issues of PRA supervised firms.
The intention is that the 'twin peaks' style regulatory model will be up and running in early 2013.

This timetable is dependent upon the successful passage of the proposed new legislation, the Financial Services Bill, to enact these changes. This is currently passing through the legislative process. Until such date, the FSA is still required to operate in principle within the current legal framework of the existing legislation of the Financial Services and Markets Act ('FSMA') 2000.

### Key impact from April 2012

In advance of this, the FSA's supervision model will be undergoing a restructuring to introduce the twin peaks regulatory model internally from 2 April 2012.

Mr Sants confirmed that this will result in a significant change in the way firms are supervised.

Key differences will include:

- There will be two independent groups of supervisors for banks, insurers and major investment firms covering prudential and conduct issues. All other firms will be solely supervised by the conduct supervisors.
- The supervisors will make their own, separate, set of regulatory judgments against different objectives.
- The supervisors will co-ordinate internally to maximise the exchange of information that is relevant to their individual objectives, but firms should be clear that they are acting separately when engaging with firms. This has been termed 'independent but coordinated regulation'.
- The FSA will retain the principle of seeking to ensure that regulatory data is only collected

once, via one common current data infrastructure.

For those firms that are most directly impacted, the key operational change will be that the existing ARROW risk mitigation programme will be split between prudential and conduct issues. From 2 April, the two supervisory units will run their own risk mitigation programmes and firms will have two separate sets of assessments and sets of mitigating actions to address. Each supervisory group may ask apparently similar questions but it should be understood that the purposes will be different.

Going forward, there will not be a consolidated list of the required actions arising from the two supervisory groups.  Therefore, firms will have to ensure that each such process is separately managed.

The FSA has issued a Dear CEO letter to relevant firms outlining these impacts and this is also available from the FSA website.

## Other key messages for all firms

The FSA sees the move to the twin peaks structure as an opportunity to embed the move to forward-looking, proactive and judgment based supervision and a move away from the previous 'reactive' style. This emphasises the importance of boards managing their institutions responsibly. In future, the focus will be on whether a firm's judgments and in particular its business model delivers good outcomes for consumers.

Specifically in relation to conduct supervision, Mr Sants stated that the overarching aim of conduct regulation will be to ensure that markets work well by protecting consumers and protecting and enhancing the integrity of markets. This can be highlighted by three main objectives of:

- ensuring consumers get a fair deal;
- ensuring markets are resilient and fair; and
- ensuring firms minimise the possibility that they may be used for financial crime.

## Next steps

The link below accesses a press release introducing the recent speech, which also contains a link to the full speech itself.

http://www.fsa.gov.uk/library/communication/pr/2012/012.shtml

In preparation for the transition, later this year, two further documents will be published by both the FSA and the Bank of England setting out in more detail how the PRA and FSA regimes will function.  This will also give firms a further opportunity to comment before these regimes go live.

In advance of this, firms should already be considering now what, if any, key impacts they can identify including determining whether they will come under the 'twin peaks' model or whether they will be solely supervised by the Financial Conduct Authority. They should have documented plans on how to manage this transition as the pace of change increases during 2012.

Firms should be ensure that senior management are briefed regularly on the current status of the transition and on any actions required for the firm, its management, the compliance function and/or staff that need to be implemented before the formal 'switchover' in early 2013.

*This briefing note is intended as a summary only and is not full and/or firm specific advice. For further information and assistance on how to manage the transition process to the new regulatory structure, please contact Gillian Gallacher for further guidance.*