Reforming the framework for Better Regulation

BSA response to BEIS consultation

September 2021

Building Societies Association

Introduction

The BSA - representing all 43 building societies and six large credit unions - supports this move towards better, smarter, more proportionate, and less burdensome regulation. (We also take this opportunity to congratulate the Parliamentarians[1] who led the Taskforce on Innovation, Growth and Regulatory Reform (TIGRR) whose report[2] this consultation principally takes forward – they did an excellent and timely job.) Although much of the specific regulation to which BSA members are subject is covered by the Treasury's Future Regulatory Framework Review, major policy areas that affect us (such as audit, governance and disclosures) do fall under the oversight of BEIS. And BSA members, as businesses, are subject to all the usual range of regulations affecting business across all sectors. So we welcome this consultation initiative both for the direct benefit in certain policy areas, and for the wider signal that it gives to official authorities and regulators as to the desired direction of travel. Not all of the detail is relevant to our members, but the principles involved are so important and necessary that we are submitting a brief formal response on behalf of our membership. This response follows the sequence of the consultation document itself, where possible also answering the specific questions posed.

Chapter One : Overview

We agree that the regulatory system should be smart, proportionate, and consider the needs of business, and we broadly support the other points in the overview chapter. We have only three upfront comments.

First, we urge BEIS to apply the excellent principles and insights in this consultation paper to (at least) one of its projects already under way, namely the recently closed consultation on **audit and governance**. The BSA's view is that, as made clear in our response, some of the proposals and options put forward do not seem consistent with, or connected with, this Better Regulation Framework. This is most clearly the case on the issue of **public interest entities**, where BEIS proposals and omissions seem determined to perpetuate problems inherited from the EU. By contrast, the BSA's comments and counter-proposals are, we think, very much in line with the Better Regulation Framework - particularly as to proportionality. We urge responsible ministers and officials to look again at this matter.

Second, on a less immediate matter, we are concerned that BEIS, HMT and the two regulators PRA/FCA (as well as the pensions regulator) may be minded to mandate climate-related disclosures for all or most businesses following the application so far of obligations based on

[1] Rt Hon Sir Iain Duncan Smith MP (Chair) ; Rt Hon Theresa Villiers MP ; George Freeman MP

[2] Final TIGGR report

the TCFD to large PLCs etc. This was set out in the "Road Map" published in November 2020. That document was, to say the least, light on notions of impact assessment, cost-benefit analysis, proportionality or effectiveness. (These were envisaged for a later stage, but by then the key decision appears to have been taken.) More importantly, it appears totally at variance with the excellent principles put forward in this Better Regulation consultation. So we argue that before any further roll out of mandatory TCFD-based disclosure to - for instance - smaller building societies, the policy case for doing so is robustly examined *de novo* using the admirable tools described in this paper. For instance, since TCFD disclosure will certainly add to our smaller members' compliance burden, what regulatory offsetting (section 3.6) is envisaged ? This whole area needs a pause and re-set before the bandwagon gets out of control.

Finally, on a more minor point, we draw attention to one issue under paragraph 1.11: while it may often be desirable to *"unlock the value of data in the custodianship of regulators"* this should always take account of who owns and supplied the data in the first place, and why it was demanded (usually under compulsion). The prior question, surely, is whether the data individually supplied by businesses is (taking account of proportionality) really necessary for its original purposes. We do not think it would be right in general to continue collecting data without rigorous justification in terms of original purpose, largely so that the aggregated data can be made available to other users, and we consider that the collective beneficial ownership of those required to supply the data in the first place should be recognized.

Chapter Two: The Better Regulation Framework

The principle of ***impact assessments*** is absolutely right: they are an important safeguard against precipitate, knee- jerk regulation in response to high-profile incidents, or the imposition of regulation based on a priori dogmas not necessarily supported by an evidence base. We would welcome any improvement to the existing IA process, as suggested in the chapter, but we think what is most important is that the **principle** of impact assessment in deciding policy is universally respected.

We also support the thinking behind the ***small and micro business assessment (SaMBA)***. While in the financial sphere, it is rare that small businesses can be completely exempt from any regulation, the SaMBA is an important check. We at the BSA express a similar sentiment - **Think Small First** - as a corrective to the usual tendency to design regulation mainly for large firms and then "roll it out" to small firms with a token spray-on of proportionality.

We also mention one important caveat. In presenting to the public the concept of a "proportionate" approach, in the context of financial services in particular, authorities / regulators need to take care that they don't infer/create the perception that adopting different (proportionate) approaches for smaller businesses makes them less secure. Or that consumers have different, inferior rights and protections when dealing with a small business. If that happened, and people felt smaller businesses were more risky/less safe/ less obligated to treat them fairly, there could be market disruption / segmentation and/ or an adverse effect on competition. The PRA has done very well to avoid this trap with its "Strong & Simple" initiative.

While we applaud the spirit of the ***business impact target***, we can see from the example given that it needs some reform – to make it more effective without losing its force through drowning in detail.

We mentioned in passing that in areas- such as financial services - where the EU has asserted competence under the single market philosophy, and attempted micro-managing regulation

through legislation, there has often been no impact assessment at all at a UK specific level. Whereas in future, with the UK making its own laws, this situation should automatically improve.

Chapter Three: Options

We support the general approach outlined in section 3.1 and this is indeed very much in line with what the BSA has advocated, to Government and regulators, since September 2016. BSA member building societies have experienced the defects of EU micro-regulation, and we called early on for adoption of the more flexible approach now outlined. Moreover, we underlined that (in financial services) such a move would be, not a new departure, but a return to the sensible approach set out in the Financial Services and Markets Act 2000 before encroaching EU competence ruled this out in more and more policy areas.

Question 1: What areas of law (particularly retained EU law) would benefit from reform to adopt a less codified, more common law-focused approach?

Question 2: Please provide an explanation for any answers given.

Question 3: Are there any areas of law where the Government should be cautious about adopting this approach?

Our experience primarily relates to financial services regulation where, as we have previously advocated, all regulation should revert to the existing UK model of the Financial Services and Markets Act 2000 with delegated powers to PRA and FCA to make appropriate detailed rules, and away from the EU approach of putting everything in inflexible legislation. We explained in previous advocacy papers how this proved unsuitable in our experience in banking. The priority therefore is to deal with areas of retained EU law.

Again, the Financial Services and Markets Act 2000 provides a good pattern for which areas should still be covered by legislation and not delegated to regulators : these include the overall regulatory architecture, statutory objectives, and safeguards on rulemaking such as consultation and IA, the extent and effect of statutory powers, and anything dealing with offences, penalties and appeals.

Question 5: Should a proportionality principle be mandated at the heart of all UK regulation?

Question 6: Should a proportionality principle be designed to 1) ensure that regulations are proportionate with the level of risk being addressed and 2) focus on reaching the right outcome?

Question 7: If no, please explain alternative suggestions

We support the adoption of a proportionality principle. While true proportionality will benefit all businesses, and is right in principle, it is of particular benefit to smaller market participants as (in our experience) the burden of regulatory compliance falls more heavily on them. Consequently, a failure to regulate proportionately is likely to have anticompetitive effect.

The two approaches outlined in paragraph 3.1.15 need not be seen as mutually exclusive alternatives. We think the first approach is in any case essential : this can be seen simply by considering how the opposite - *that the design etc and cost of regulations should be indifferent to the level of risk being addressed* - is clearly ridiculous. But we also agree that regulation should be outcome focused : compliance with any regulation is not an end in itself but a

means to an identifiable outcome. That being said, we caution against the danger of regulating with hindsight. Sometimes a bad outcome emerges which cannot be attributed to particular failings by the business involved. Nor should remediation be based on who has the deepest pockets.

An example of regulation that is perhaps overdue for review on grounds of proportionality and effectiveness is the attempt to control money laundering through a prescriptive approach to bank account opening and maintenance. The practices considered necessary seem mainly to complicate, or even frustrate, the legitimate banking arrangements of ordinary citizens, and especially of small organisations such as voluntary bodies – and almost certainly have anti-competitive effect. At the same time, this bureaucracy is widely believed to pose at most mild inconvenience to real money launderers. But because this topic area is covered by EU competence, the question of proportionality and effectiveness, and cost benefit analysis, has never been robustly examined for the UK.

Questions 8 and 9 : Should competition be embedded into existing guidance for regulators or embedded into regulators' statutory objectives?

Under the Financial Services and Markets Act, both PRA and FCA have statutory competition objectives. For PRA this is a secondary objective, while the FCA's objective is more prominent. We find this makes for appropriate consideration of competition, and the same approach could work well in other contexts.

Similarly, under FSMA, innovation was originally embedded into statutory considerations for the former FSA – old section 2 (3) provided that *"In discharging its general functions the Authority must have regard to—[ ] (d)the desirability of facilitating innovation in connection with regulated activities;".* Somehow this innovation principle lost prominence in the break-up of the FSA. FCA has some consideration of innovation as an aspect of its competition remit, while PRA seems to have lost it. We think the original formulation in FSMA 2000 was adequate.

Question 10: Are there any other factors that should be embedded into framework conditions for regulators?

Yes, the need to have regard to diversity of corporate form. Much, perhaps most, Governmental activity towards business, including aspects of regulation, tends to take the proprietary limited company as the normative form of business organisation, with an occasional nod – in the context of small business – towards sole proprietors. The extensive world of mutual and cooperative business is sometimes ignored entirely, sometimes treated as an afterthought, or an exotic variation. The end results are that mutual and cooperative businesses often have to operate under outdated legislation , lack legal facilitations that are made for companies , or are subjected to intrinsically inappropriate regulation based on the company mindset. **We call for parity of esteem for mutual and cooperative business.**

A step in the right direction was secured by the BSA's advocacy : both the PRA and FCA are now legally obligated to recognise the differences in nature and objectives between different corporate forms and specifically for mutual societies (FSMA section 3B (f)). **Similar provisions to recognise corporate diversity and push back against the PLC mindset may be needed in other fields to allow mutual and cooperatives to reach their full potential.**

Question 11: Should the Government delegate greater flexibility to regulators to put the principles of agile regulation into practice, allowing more to be done through decisions, guidance and rules, rather than legislation?

Yes, again we have advocated this in relation to areas of former EU competence since 2016. The FSMA architecture delegates extensively to (now) the two regulators PRA and FCA but within a strict framework of statutory objectives, regulatory principles, and procedural obligations and safeguards and an enhanced accountability regime. While we may not always agree with the actions of either regulator, we regard the basic structure as fit for purpose and the idea could be copied for major regulators elsewhere.

Questions 12/13 – Although we have not directly used the FCA Regulatory Sandbox, we support the concept and consider it could have wider application.

Questions 14/15 – The current arrangements under FSMA as amended provide a suitable form of enhanced accountability for the two regulators, and that model could be adopted elsewhere. We attach especial importance to the involvement of statutory panels representing stakeholder interests, and the BSA has, through its nominees, actively supported the PRA and FCA practitioner panels.

Questions 16/17 – While there should always be scope both for feedback, and for outside scrutiny, effective day to day regulation requires an element of stability. Too many, or too frequent surveys or deep dives risk detracting from the quality and focus of the core regulatory activity.

Questions 18 to 23 : We support both early scrutiny, at outline or in-principle level, and a streamlining of impact assessment. But we would also suggest more widespread adoption of an existing regulatory tool – the **Table of Eleven** – to help officials be clearer on : what form the optimal intervention should take; the complex interactions between regulation, knowledge/awareness, incentives and enforcement ; and the understanding that the required outcome is a particular set of circumstances or modified behaviours, not the creation of a new regulation per se. The Table of Eleven will particularly help with two related bugbears : extending or creating new regulation instead of addressing compliance with and enforcement of existing regulation ; and "performative regulation" – regulation that is hailed as "making a statement" or "sending a message" but often with little focus on actual compliance or enforcement. The proliferation of performative regulation with little compliance or enforcement risks undermining the status of and effectiveness of good regulation as all regulation is thereby brought into disrepute.

The Table of Eleven (T-11) is an analysis tool developed by the Ministry of Justice in the Netherlands in the 1990s to aid effective policy making and regulatory compliance. It was later cited by the OECD as widely influential across advanced economies in improving regulatory effectiveness, but does not feature, we think, in either the TIGRR report or the BEIS consultation. The distinctive insight of T-11 is the breakdown of the intermediate behavioural steps between the input (a piece of regulation) and the outcome constituted by a defined target state of affairs. Wider use of T-11 would reduce the temptation towards "performative regulation".

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The Building Societies Association (BSA) is the voice of the UK's building societies and also represents a number of credit unions.

We fulfil two key roles. We provide our members with information to help them run their businesses. We also represent their interests to audiences including the Financial Conduct Authority, Prudential Regulation Authority and other regulators, the Government and Parliament, the Bank of England, the media and other opinion formers, and the general public.

Our members have total assets of over £435 billion, and account for 23% of the UK mortgage market and 17% of the UK savings market.