



HM Treasury, 1 Horse Guards Road, London, SW1A 2HQ

To: All Peers

25 January 2023

My Lords,

FINANCIAL SERVICES AND MARKETS BILL: MATTERS RAISED AT SECOND READING

Thank you for your contributions during the Second Reading of the Financial Services and Markets Bill on 10 January 2023. In my closing speech, I committed to respond in writing on matters raised in the debate which I was unable to cover in the time available.

Regulators' statutory objectives and regulatory principles

A number of contributions touched on the regulators' objectives and regulatory principles. I therefore want to take this opportunity to reiterate the government's position and outline the clear hierarchy that exists in the Financial Services and Markets Act 2000, and is maintained by this Bill.

The Financial Services and Markets Act 2000 requires the Financial Conduct Authority to advance its operational objectives, in line with its overarching strategic objective of ensuring relevant markets function well. The operational objectives are ensuring that consumers of financial services receive an appropriate degree of protection, that the integrity of the UK financial system is protected and enhanced, and that there is healthy competition in the interests of consumers. The new, secondary, growth and competitiveness objective introduced by Clause 24 of this Bill will sit below these existing

operational objectives, and does not require or permit the Financial Conduct Authority to take action which is inconsistent with these existing objectives.

The Financial Services and Markets Act 2000 requires the PRA to advance its general and insurance-specific objectives. The Prudential Regulation Authority has an existing secondary objective on competition which requires it, when discharging its general functions in line with its general and insurance-specific objective, to facilitate, as a secondary objective, the effective competition in the markets for services provided by persons authorised by the Prudential Regulation Authority in carrying on regulated activities. The new growth and competitiveness objective will sit alongside the Prudential Regulation Authority's existing secondary competition objective in this hierarchy.

The Bill is therefore clear that the Financial Conduct Authority's strategic and operational objectives, and the Prudential Regulation Authority's general and insurance-specific objectives, are prioritised ahead of the secondary objectives in the regulatory framework.

The regulators must advance their objectives whilst also having regard to the regulatory principles, which aim to promote good regulatory practice. This means the objectives sit above the principles in the hierarchy, should they ever be in tension. The Bill also makes changes to the regulatory principles for the Prudential Regulation Authority, the Financial Conduct Authority, the Bank of England and the Payment Services Regulator to incorporate the government's climate change target to achieve a net zero economy by 2050.

Reporting requirements on the needs of mutuals

Turning to the specific questions raised during the debate, Lord Tunnicliffe asked whether the government would be supportive of an amendment to require the Prudential Regulation Authority and the Financial Conduct Authority to report on how they have considered the needs of mutuals in their reporting requirements.

I can reassure Peers that there are already specific duties in place in legislation which require the regulators to consider the mutual model in the exercise of their functions and to report on how they have done this.

Section 138K of the Financial Services and Markets Act 2000 provides a legislative obligation on the Prudential Regulation Authority and the Financial Conduct Authority to consider how any new regulatory rules may impact mutual societies and whether the impact may differ from the impact on non-mutual businesses. The regulators must publish a statement providing their opinion on whether there is a significant difference in impact, and if so, what that difference is.

Both the Prudential Regulation Authority and the Financial Conduct Authority are also required to provide annual reports which must cover how they have considered their regulatory principles under paragraph 11(1)(f) of Schedule 1ZA of the Financial Services and Markets Act 2000. One of the regulatory principles, outlined in section 3B of the Act, requires the regulators to consider, where appropriate, the desirability of exercising its functions in a way that recognises differences in the nature of, and objectives of, businesses carried on by different persons.

The government therefore does not consider that further amendment is necessary to ensure that the regulators are adequately considering mutuals, and reporting on them. I nevertheless look forward to discussing any amendments put forward by Peers in Committee.

Examples of international competitiveness objectives around the world

Lord Holmes of Richmond asked whether the government had considered examples of international competitiveness objectives from around the world. Throughout the development of the Future Regulatory Framework Review, the government considered international comparator jurisdictions. As noted by Lord Hill of Oareford in his *UK Listing Review*, other financial services regulators – for example in Australia, Singapore, Hong Kong, and Japan – have growth or competitiveness embedded in their frameworks, as set out in the November 2021 Future Regulatory Framework Review consultation.¹ The government's view is that the successes of these jurisdictions demonstrate the feasibility

¹ *Financial Services Future Regulatory Framework Review: Proposals for Reform*, HM Treasury, November 2021

of embedding competitiveness and growth considerations within a regulatory framework without harming financial stability.

Trade with the European Union

Lord Northbrook asked about the impact of the Bill on trade agreements with the EU, and on boosting exports more generally.

Having left the EU, we have a unique opportunity to take an approach to financial services regulation that better suits our markets. This Bill is a key part of the government's programme to build on our historic strengths as a global financial centre, develop our relationships with jurisdictions around the world, and attract investment and increase opportunities for global cross-border trade. One example is the inclusion provisions to ensure that Mutual Recognition Agreements in financial services can be implemented in a timely way, including the agreement currently being negotiated with Switzerland. The Bill also introduces specific mechanisms to ensure that any potential impact on international trade obligations or deference arrangements to be considered as part of the regulators' rule-making process.

With regard to the EU, the UK already has a Free Trade Agreement with the EU in the form of the Trade and Cooperation Agreement. Following the agreement of the Trade and Cooperation Agreement, the UK negotiated a Memorandum of Understanding for cooperation between the UK and the EU on financial services regulation. Technical discussions on the text concluded in March 2021 and the memorandum, once signed, will establish the Joint UK-EU Financial Regulatory Forum, which will serve as a platform to facilitate dialogue on financial services issues. Whilst the UK government is ready to sign the Memorandum of Understanding, further steps are required on the EU side before the Memorandum of Understanding can come into effect. The government's expectation is that the Memorandum of Understanding, and the Forum it will bring into effect, will help ensure that regulatory developments are well understood on both sides, promoting trade and investment.

This Bill demonstrates that the UK will continue to have high standards of financial services regulation, and will ensure that the UK maintains a coherent, agile and internationally-respected approach to regulation.

Stablecoins

Lord Cromwell asked whether the government was concerned about fluctuations in the value of stablecoins, including those backed by fiat currency, and whether there is a clear definition of stablecoins.

Stablecoins are a particular type of cryptoasset that seeks to maintain a stable value in relation to another asset. There are various ways that a stablecoin can seek to stabilise its value in this way. The government believes that those that are backed 1-to-1 with fiat currency, such as the British Pound, share characteristics with existing forms of payments and so existing regulatory frameworks could be expanded to include such fiat-backed stablecoins. The Bill will provide the government with the powers to do this.

Bringing these stablecoins into the regulatory regime will allow the regulators to set rules, including those aimed at maintaining the value of the stablecoin and those relating to the assets backing the relevant stablecoin.

Separately, recent market events have highlighted risks associated with certain other types of stablecoins that aren't backed by a fiat currency, such as algorithmic stablecoins. As set out in the consultation response in April 2022, the government's position is that algorithmic stablecoins share characteristics with unbacked cryptoassets and are judged to be unsuitable to be used as a means of payment, and therefore the government has no plans to bring them within the scope of payments regulation in the way that it intends to do with fiat-backed stablecoins. The government will consult on a regulatory regime for a broader set of cryptoassets in due course.

Cash and digital payments

Lord Holmes of Richmond asked whether cash should be considered a Critical National Infrastructure. While the designation of critical national infrastructure is sensitive and – as such – is not made public, the government has demonstrated the importance that it places upon access to cash through the inclusion of provisions in this Bill to protect it.

Lord Holmes of Richmond also asked whether the government has plans to undertake a review of digital payments in the context of financial inclusion. As acknowledged in the debate, digital payments are already bringing opportunities – for example through

convenience, security, and speed – to millions of people across the UK, including those who may be in vulnerable groups. Non-cash transactions accounted for about 85% of UK payments in 2021, according to UK Finance. The government wants to ensure that people have access to appropriate financial services, and welcomes evidence and reflections for future policy in relation to payment services through the Call for Evidence on the Payment Services Regulations, published on 13 January.²

Authorised Push Payment fraud

Lord Vaux of Harrowden raised a number of questions relating to authorised push payment fraud. I have also noted the recent report from the Fraud Act 2006 and Digital Fraud Committee, which relates to the reimbursement of authorised push payment scams, to which the government will respond in due course.

On the role of other sectors beyond the financial sector in relation to fraud, the government recognises that many sectors have a role to play in preventing fraud, as evidenced by the inclusion of the fraudulent advertising duty in the Online Safety Bill currently making its way through Parliament. Departments across government will continue to work together to ensure that other sectors play their part in tackling this important issue. However, payment service providers are responsible for ensuring that their anti-fraud systems are effective, and that they are diligent when providing payment accounts knowing such services could be exploited for criminal gain.

Beyond reimbursement by the financial sector, we continue to work with all industries, including the telecommunications and tech sectors, to ensure that protections are in place to protect consumers from losing their hard-earned money and to ensure that every company does what it can to support victims.

Regarding the split in apportioning costs of reimbursement between sending and receiving banks for reimbursement, the Payment Systems Regulator is empowered to determine the right regulatory approach, subject to public consultation in the usual way. The Payment Systems Regulator has the relevant expertise, powers and objectives to work

² <https://www.gov.uk/government/consultations/payment-services-regulations-review-and-call-for-evidence>

with payment systems and providers. The Payment Systems Regulator consulted on its approach to reimbursement in Faster Payments in Autumn 2022, and proposed to allocate the costs of reimbursement equally between sending and receiving providers, with a default 50:50 split. Banks, or other payment service providers, can use a dispute management process to adjust the allocation, to better reflect the steps each provider took to prevent the scam. The Payment Systems Regulator will confirm its final approach and issue a reimbursement requirement for Faster Payments within 6 months of the Financial Services and Markets Bill coming into force.

On the slowing down payments in certain circumstances, many banks already delay and refuse payments where they suspect fraud. The government, financial regulators and industry are working together to ensure that banks can identify suspicious payments in real-time, and intervene where necessary. The government is progressing discussions with the payments industry on what more might be done to support banks to take a more consistent risk-based approach to payments.

Strategic Lawsuits Against Public Participation (“SLAPPs”)

Lord Cromwell raised his concerns over Strategic Lawsuits Against Public Participation, or “SLAPPs”. SLAPPS represent an abuse of the legal system, as they rely upon threatening tactics to silence free speech advocates who act in the public interest.

The government ran a call for evidence on SLAPPS and libel reform from March to May 2022. The government published its response to the Call for Evidence on 20 July 2022, having closely analysed 120 responses from media, legal and civil society professionals. Targeted anti-SLAPP reforms will include a statutory definition of SLAPPs, an early dismissal process and costs protection for SLAPPs cases. The government has committed to primary legislation to make these reforms a reality as soon as parliamentary time allows. However, the government does not consider this Bill to be the appropriate vehicle. If interested Peers wish to discuss this further, knowing the government’s position, then I would be happy to meet with them.

Consolidation of financial services legislation

Finally, Baroness Noakes asked about the potential consolidation of financial services legislation. The government does not currently intend to bring forward a consolidation bill in this area. The Financial Services and Markets Bill will simplify the regulatory landscape by revoking Retained EU Law relating to financial services and allowing it to be replaced with rules made specifically for the UK in regulator rulebooks.

I look forward to further discussing these issues throughout the passage of the Bill. I am also depositing a copy of this letter in the Library of the House.

Yours sincerely,

A handwritten signature in black ink, appearing to be 'PENN', with a long horizontal flourish extending to the right.

BARONESS PENN