Financial Services Authority

Business Plan 2012/13

The *Business Plan* covers the financial year 1 April 2012 to 31 March 2013. References to quarters in the body of the text are to the calendar year – for example, 'Q3 2012' is the period July to September 2012.

Business Plan 2012/13

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Adair Lord Turner, FSA Chairman

Foreword by the Chairman

This year's *Business Plan* will be the last for the FSA, and my last as FSA Chairman. Subject to the parliamentary timetable and the legislative process, the FSA will hand over responsibility for prudential regulation to the Prudential Regulation Authority (PRA) and conduct regulation to the Financial Conduct Authority (FCA) in the first half of 2013. Responsibility for macro-prudential oversight of the financial system will be given to the Financial Policy Committee (FPC).

The FSA has radically changed since 2008 and I believe it has become more effective as both a prudential and a conduct regulator. We have also made progress on the international stage, creating a stronger framework for prudential regulation. Over the next year we will need to deliver the structural split of the FSA into its successor bodies, while maintaining a tight control of transitional and ongoing risks and costs. In parallel, we will need to:

- maintain the momentum of prudential reform at the global, European and national level;
- ensure the financial safety and soundness of firms in a still risky macroeconomic context;
- develop further our approach to conduct regulation, on which the FCA will build; and
- maintain the strength of our regulation of wholesale markets and our approach to enforcement.

This *Business Plan* sets out how we will meet these challenges in the coming year.

The CEO's foreword provides a summary; I would like to highlight some key points on the priorities.

Structural change and cost control

The Financial Services Bill has now entered Parliament: it sets out clearly the division of responsibilities between the future successor bodies. But the creation of the PRA and the FCA will require much detailed implementation work. Three key tasks can be distinguished.

- The separation of our supervision function into prudential and conduct elements, moving to a 'twin peaks' structure within the FSA. This will occur on 2 April 2012.

- The precise design of the PRA's structure, headcount and first-year budget, and the planning and implementation of the move into new premises. This task is being led by Hector Sants as CEO designate of the PRA and by Andrew Bailey as his designate deputy, and involves intensive involvement of Bank of England management, and ultimate sign off by the Court of the Bank of England.

- The precise design of the organisation, structure, headcount and first-year budget of the FCA. This task is being led by Martin Wheatley as CEO designate of the FCA, with detailed oversight from the FSA Board, including through a dedicated sub-committee.

These strands of work will enable us to launch the two bodies successfully at the point of 'legal cutover', which we anticipate will occur during the first half of 2013.

Until then, the FSA Board retains ultimate responsibility for the effective execution of the FSA's statutory objectives on both the prudential and conduct side. The Board is therefore very focused on ensuring that the inevitable disruption of major structural change can be managed without any diminution of ongoing effectiveness. It is also very focused on the importance of effective cost control. There are inevitable one-off transition costs which are separately identified in this *Business Plan*. In addition, the Board has approved an IT improvement programme to ensure that the FCA inherits a fit-for-purpose operating platform: these costs too are separately identified.

Financial stability: safety and soundness of firms

Much progress has been made since 2008 in building the resilience of UK banks and other financial firms, with significant improvements in capital and liquidity. But we have not yet reached the levels of capital and liquidity that Basel III prescribed as essential for long- term financial stability, and financial risks remain elevated in the face of difficult macroeconomic conditions in general and eurozone strains in particular.

The interim Financial Policy Committee (FPC), of which both Hector Sants and I are members, has now taken on responsibility for assessing overall financial system risks, with analytical input from both the Bank and the FSA. But the FSA remains ultimately responsible for the prudential regulation and supervision of specific firms, and has a crucial role to play in ensuring the implementation of specific FPC recommendations. Throughout the coming year, therefore, the financial soundness of our major firms will continue to be among our highest priorities.

Reform of prudential regulation

Last year saw important steps in the development of improved prudential standards at global, European and national level. Throughout the coming year, FSA staff will continue to be closely involved in designing and implementing further improvements. This will involve:

- ensuring that global agreements on recovery and resolution planning regimes are translated into robust plans for each of our major banks;

- implementing the policy requirements of the European directives – the Capital Requirements Directive (CRD) IV and Solvency II;

- playing a leading role in developing global approaches to trading book capital, to shadow banking and to ensuring the comparability of capital risk weights;

- assessing and advising the government on the complexities involved in the implementation of the Independent Commission on Banking's proposals for a 'retail ring fence'; and

- producing jointly with the Treasury a Discussion Paper on potential changes to the liabilities and incentives facing senior executive management and non-executive directors of major banks.

Conduct regulation: building a new approach

In the past, the FSA sought to ensure retail consumer protection by focusing on fair disclosure of terms and on the regulation of sales processes. This approach failed to prevent waves of large-scale mis-selling – with the industry subsequently forced to make large compensation payments. The Financial Services Bill commits the FCA to a new approach, with earlier identification of emerging customer detriment risks and earlier intervention to prevent their development.

This year we will need to turn this aspiration into reality – reflecting the new approach in the design of the supervisory and enforcement processes, structure and skills of the FCA. The design will also need to reflect the new responsibilities the Financial Services Bill will give the FCA on competition.

Markets regulation and enforcement: maintaining existing strengths

Organisational responsibility for prudential supervision will change at legal cutover: the approach to retail conduct supervision is being radically reformed. In our Markets and Enforcement Divisions there will be less radical change, but important challenges nevertheless.

In wholesale markets, the role of the European Union is crucial with the European Securities and Markets Authority (ESMA) playing an increasingly powerful role, and with significant policy initiatives in particular in the area of over-the-counter (OTC) derivatives. In the area of enforcement meanwhile, the FSA has continued over the last year to execute a forceful policy of credible deterrence, robustly deploying our civil and criminal prosecution powers. This approach will be taken forward by the FSA and subsequently the FCA, with links being developed between the Enforcement Division and the retail consumer protection agenda.

In total, this is a challenging agenda for the FSA in its final year. But, as the *Business Plan* shows, it is an agenda for which we are well prepared.

Adair Turner

Adair Lord Turner
March 2012

Hector Sants, FSA Chief Executive

Chief Executive Officer's Overview

The FSA's *Business Plan* sets out our work programme for the coming year. The main elements of our plan have been structured to align with our statutory objectives. It is also driven by the risks faced by the firms and markets we regulate and the consumers who use them. As our Chairman sets out in his foreword, these continue to be set against a very difficult macroeconomic environment.

Against this challenging backdrop, the FSA has also been focused on delivering the regulatory reform programme as set out in the government's White Paper published in June last year. The resources required to deliver this programme will increase significantly over the coming year as we set up a 'twin peaks' system within the FSA and complete our preparations for going live in early 2013.

Throughout the life of the FSA one of the greatest challenges facing the organisation, given its four statutory objectives, has been how its success should be judged. Understandably, many commentators have focused on the stability of the banking sector; however, the FSA has a far wider set of responsibilities and only a minority of the staff are engaged in that vital task.

I am a strong supporter of regulators being accountable to Parliament, but this requires clarity and understanding of the agreed objectives and how these objectives are assessed. During my time as CEO we have brought greater clarity to how we measure our performance and this *Business Plan* continues that process.

For the coming year our main focus is on five areas: delivering the regulatory reform programme; influencing the international policy agenda; delivering financial stability; delivering market confidence; and protecting consumers

Successfully delivering the regulatory reform programme is not only a question of establishing the new authorities with effective operational and organisational platforms, it is also a question of ensuring the accumulated knowledge and lessons learned since the financial crisis are passed on to the new regime.

Success, in respect of the international policy agenda, should be measured in how much the outcomes of the policy agenda reflect the UK policy positions, and our ability to smoothly implement while retaining the freedom to address national and firm-specific issues.

In assessing our success in delivering financial stability, our principal objective is to ensure that major firms whose failure would have significant systemic impact ideally do not fail, but if they *do*, do so in an orderly way, therefore minimising their impact on the financial system and preventing the need for an injection of taxpayers' money.

Success in relation to market confidence is assessed by several market-specific measures. Central to this is our evaluation of equity market cleanliness and our credibility as an enforcement organisation in relation to market abuse and insider dealing.

In assessing our success in delivering consumer protection, we seek to avoid major consumer detriment events (defined as above £250m or 50,000 people) That does not mean that the FSA does not seek to reduce the probability of detriment occurring below these levels, rather we accept that, given our limited resources, it is inevitable that detriment will sometimes occur.

Let me now provide an overview of this *Business Plan* for 2012/13, which is organised into eight sections:

- Delivering the regulatory reform programme
- Influencing the international & European policy agendas
- Delivering financial stability
- Delivering market confidence
- Delivering consumer protection
- Financial crime
- Delivering the FSA's operational platform
- The FSA's budget

Regulatory reform

Turning to the first area: the regulatory reform programme. By way of background, the government's plan, set out in its White Paper, is to transfer prudential supervision for banks, building societies, insurers and major investment firms to a subsidiary of the Bank of England, the Prudential Regulation Authority (PRA), and rename the FSA the Financial Conduct Authority (FCA), which will focus on consumer protection and market regulation. This creates a 'twin peaks' structure.

In February this year, I announced the next major milestone in the regulatory reform programme, namely the introduction of a twin-peaks model operating within the FSA from 2 April 2012.

The new model will mean that banks, building societies, insurers and major investment firms will from this date have two groups of supervisors, one focusing on prudential and one focusing on conduct. All other firms (i.e. those not dual regulated) will be solely supervised by the conduct supervisors.

The FSA will not be able to completely replicate the approach proposed by the government in the Financial Services Bill, published on 26 January, but I would like to emphasise that the changes will go as far as possible to ensure that the cutover to the new regulatory structure in early 2013 will be seamless.

Central to achieving the required behavioural changes to supervision are clear objectives, which the regulators need to ensure their actions are aligned with. For the twin-peaks model operating within the FSA from 2 April, the objectives will be closely aligned with those of the PRA and FCA.

The overarching objective of the PRA is to ensure the safety and soundness of firms and to avoid disorderly failure which has systemic consequences. For insurers, it will also seek to ensure that policyholders are protected through sound financial management.

The overarching aim of the FCA is to ensure that markets work well by protecting consumers and protecting and enhancing the integrity of markets. Essentially, this can be distilled into three objectives: i) ensuring consumers get a fair deal; ii) ensuring markets are resilient and fair; and iii) ensuring firms minimise the possibility that they may be used for financial crime.

The new conduct group within the FSA will not, however, be required to take into account the new responsibilities and powers that the Bill is proposing for the FCA. The most noteworthy are the proposed responsibilities for the FCA in relation to competition and the proposal to widen its scope to include consumer credit.

The key characteristics of the model include:

- two independent groups of supervisors for banks, building societies, insurers and major investment firms covering prudential and conduct;
- supervisors making their own, separate, set of regulatory judgements against different objectives;
- 'independent but coordinated regulation' designed to allow internal coordination between both conduct and prudential supervisors to maximise the exchange of information relevant to their individual objectives, but with supervisors making independent decisions and acting separately when engaging with firms; and
- retaining the principle of seeking to ensure that regulatory data is only collected once.

The change will embed the forward-looking, pro-active, judgement-based approach and accelerate the move away from the old reactive style of regulation. The changes must not only be structural, but must also involve behavioural shifts from both supervisors and firms.

Therefore, in my view, the most important change that will occur at twin peaks is not the introduction of a new operational framework, but the opportunity to accelerate the process of behavioural change that the FSA embarked on when we began the reform of the supervisory process in the spring of 2008.

As part of this new approach we must crystallise the change from the 'old style reactive approach' to the 'new style proactive approach' for supervision.

As I have said in the past, the essence of a judgement-based approach is a willingness to intervene when the regulator judges that the outcomes will, in future, be at variance to its mandate, even if the firm does not agree. Such proactive intervention needs to be proportionate and justified, but if we are to improve outcomes and meet the expectation of Parliament and society, such judgements will have to be made.

The key to success in the new judgement-led approach is:

- the ability of supervisors to identify and focus on the big risks to their statutory objectives;
- the capability of supervisors to make the right judgement on how to reduce the probability of risks to their statutory objectives; and
- the decisiveness of supervisors to instruct the firm to execute these actions.

If this new approach is to work effectively firms will also need to change the way they think about regulation. Firms will be expected to do the following:

- Recognise the importance of aligning their goals with those of the supervisors and society as a whole.
- Show a greater willingness to proactively comply with supervisory judgements. We are not asking firms to forgo their right to challenge their supervisor if their decisions have not been properly made. But dragging their feet in complying with requests when it is obvious to all that the outcome is in the best interest of society as a whole, is not a behaviour which should survive in the new world.

- Recognise that this new approach will require greater resources and expertise, and thus costs more than the old reactive model which existed before the crisis.

It is really important that we use this opportunity to accelerate the behavioural and cultural change needed in both regulators and firms.

Influencing the international agenda

While we will, necessarily, have to focus on delivering the regulatory reform programme in the UK, I would like to stress that engaging with the European regulatory process is also important to delivering effective financial regulation in the UK.

It needs to be recognised that currently, for prudential and markets regulation, and increasingly over the longer-term in respect of conduct, the rules will be made by Europe and the roles of both the PRA and the FCA will primarily be supervision and enforcement.

This structural shift for the responsibility for rulemaking has profound consequences. The changes we are making to our supervisory model in the UK to move to a judgement-based approach will not in themselves be enough to significantly improve the soundness of the system. Good supervisory judgements have to be exercised within the framework of effective rules.

As the various FSA reports into the crisis have demonstrated, the principal regulatory deficiency, pre-crisis, was the inadequate capital and liquidity standards. Our Chairman commented in his foreword that significant improvements have been made to the capital and liquidity framework, but we have not yet reached the levels that Basel III prescribed as essential for long-term financial stability. Truly effective reform of the regulatory system will thus only be achieved if Europe delivers on the implementation of the Basel III framework.

The financial crisis also demonstrated that an effective single European market place requires coordinated regulation delivered to a consistent standard across Europe. So the FSA supports the concept behind the European Supervisory Authorities and will continue to give great focus and time over the coming year to working with these bodies and influencing their policy agendas.

On the question of allowing a supervisor flexibility to address firm-specific risks, it is vital that they retain the flexibility to customise the capital and liquidity framework for the individual risk profile of the firm. If Europe harmonised to the point of removing judgement, this will increase risk – not decrease it. It is crucially important that CRD IV and any future regulations are flexible enough to address these concerns.

Delivering financial stability

The FSA is responsible for contributing to the protection and enhancement of the stability of the UK financial system. We do this through ensuring firms are well-supervised, intending to reduce the probability of systemically significant firms failing, and ensuring that if they do fail, they do so in an orderly way and without burdening the taxpayer.

Our role is also to provide support to the wider framework for macroeconomic, fiscal and financial stability in the UK system as a whole. This is principally done through supporting the Bank of England and its Financial Policy Committee (FPC), which has responsibility for overseeing the system as a whole. We also actively participate in a number of European and international fora.

The role for all parties involved in meeting this challenge has been made all the more difficult by the issues being experienced and ongoing fragility in the eurozone economies.

On firm-specific prudential oversight, in addition to our ongoing work to ensure firms have sufficient capital and liquidity, we will also be particularly focused on ensuring they have effective recovery and resolution plans. The UK already has a framework that works effectively for small and medium banking institutions, but it is critical that we complete the work that is already underway for global institutions. This will, however, require the cooperation of overseas regulators and central banks.

We will also continue to develop and strengthen our capability to provide more sophisticated and specialist in-depth risk analytics and stress testing across firms, risk types and all asset classes.

In respect of policy initiatives in the prudential area, it is important to understand that no new discretionary policy initiatives have begun, but a significant – primarily, European-originated – agenda continues.

The key ongoing prudential policy initiatives are:

- CRD IV – The prudential framework for deposit takers and investment banks in Europe is set out in the Capital Requirements Directive (CRD). In 2012/13 we will be preparing to meet the CRD IV deadline of implementation into domestic legislation by 1 January 2013, as well as updating and developing the necessary supervisory and systems changes to allow ongoing compliance with rules. We will consult on the changes to our rules to implement CRD/CRR IV before the legislation comes into force on 1 January 2013.

- Solvency II – The changes under Solvency II aim to protect policyholders by establishing a revised set of EU-wide capital requirements and risk-management standards that will replace the current solvency requirements. This year there will be considerable work undertaken, building up to implementation from January 2014, working up to conducting our consultations to transpose Solvency II by 1 January 2013, with implementation due to begin in January 2014.

- Recommendations of the Independent Commission on Banking – We are working with the Treasury on the official government response to this and on any subsequent White Paper.

Delivering market confidence

On our market confidence objective, we are primarily focused on ensuring that markets are resilient and fair. In general, the policies underpinning the efficient functioning of organised and OTC markets are now set by European regulatory processes. So our role is to influence these and ensure they are effectively applied to markets in the UK, along with continuing the success of our credible deterrence agenda. Currently, there is an extensive global and European policy agenda, including proposals to revise the Markets in Financial Instruments Directive, implement the G20 commitments for OTC derivatives and establish a resolution regime for financial markets infrastructures. We will engage fully with international and European authorities to seek to ensure that these policy initiatives reach the right regulatory outcomes for UK financial markets.

Client assets

In addition to supporting these European initiatives, the protection of client assets will remain a key priority for us. Inadequate records, ineffective segregation of client assets and a low level of awareness of requirements in this area risk causing detriment to clients, creditors and counterparties, with associated reputational damage to confidence in UK markets. In 2012/13 we will further strengthen our intensive regulatory and supervisory approach for firms holding client money and safe custody assets and increase our knowledge and oversight of the UK market.

Furthermore, we will review our client assets regime to see if further changes are required following the lessons learned from ongoing insolvencies, and the recent judgement of the Lehman Brothers International (Europe) client money Supreme Court Appeal. However, it is important to recognise that insolvency law and the Special Administration Regime is determined by primary legislation and not the FSA rules.

Delivering consumer protection

The core of our consumer protection objective is to ensure consumers get a fair deal. In the coming year we will continue to put into practice our new proactive approach in this area, which seeks to combine the traditional reliance on disclosures at the point of sale and delivery of redress, with a greater willingness to intervene earlier, particularly in respect of inappropriate products. In the *Retail Conduct Risk Outlook* we recently published we also set out the 15 highest priority retail conduct risks that we believe require particularly close firm and regulatory focus over the next 12 to 18 months.

Particular areas of focus will be as follows:

- We will be more willing to make our commitment to earlier intervention a reality where we see potential risks to consumer detriment crystallising. We will intervene where we see unsuitable products with a high probability of being mis-sold, as well as where we see firms with poor standards of product design or sales processes.

- We will continue to intervene to address inappropriate financial incentives, which run the risk of encouraging mis-selling.

- We will continue to focus on the fitness and propriety of those taking up controlled functions and ensure new entrants have appropriate systems and governance in place.

- We will be more willing to use the mechanisms available to achieve efficient redress, in particular the use of section 404 powers, provided by the 2010 Financial Services Act.

- We will continue to take tough enforcement action to deliver credible deterrence where firms or individuals fail to meet the standards expected of them.

To deliver the consumer protection objective, our policy approach seeks, alongside our intrusive supervisory approach, to address a number of deep-rooted market failures and cultural issues that exist in the market. There are no new discretionary initiatives planned for the coming year in relation to these issues, the principal ongoing ones are as follows.

RDR

RDR is due to come into force on 1 January 2013. Our preparatory work will ensure that we can supervise the new regime from then. We will also assess firms' readiness for the new standards.

MMR

We do not plan to implement the proposals before summer 2013. We will consider market conditions and may defer implementation. If there is widespread support for particular proposals, for example in relation to mortgage arrears charges, we may implement some aspects sooner.

Redress

In May 2012, we will publish final proposals aimed at ensuring that consumers are aware of the extent of deposit protection.

Financial crime

In 2012/13, we will focus on our strategic objective of reducing financial crime by:

- ensuring that the regulated community has effective systems and controls in place to prevent financial crime;

- keeping those who lack integrity out of the financial services industry by imposing tough standards at the point of approval and authorisation; and

- warning and educating investors about the dangers they may face from unauthorised business.

In the first half of 2012 we will publish two thematic reports – one on anti-bribery and corruption systems and controls in investment banks, and one on banks' defences, systems and controls, against unauthorised businesses. These reports will be included into updated versions of *Financial Crime: a guide for firms*.

Delivering the FSA's operating platform

An effective and efficient operational platform is crucial to support delivery of the FSA's statutory objectives and we are committed to ensuring that: we have the right people with the right skills; are investing in our infrastructure; and delivering the operational changes required for a safe and smooth transition to new regulatory structure.

In relation to our people, we will place strong emphasis on developing our leadership capabilities, strengthening our core technical competencies through development and recruitment, and engaging our staff. Diversity and equality of opportunity are important to us as an employer and a regulator, and we will continually strive to improve our approaches to this end.

On the question of whether the PRA and the FCA need to make significant changes to the make-up of staff, it is important to reiterate that we have already made significant changes to FSA supervisory staff.

Of the supervisors in the new conduct and prudential groups in the FSA, to be created on 2 April, 78% have joined since July 2007. Furthermore, of the senior supervisory management team at the level of Head of Department and above, 66% have been appointed to their role since July 2007.

We therefore need to focus now on the stability and training of staff so they feel supported in making decisive and assertive judgements.

Next year, we will begin reviewing our IT strategy, focusing on stabilising and enhancing the platform used by our IT and regulatory staff to analyse data and produce reports for supervisors. And we will begin the design phase for the regulatory systems needed to support the work of the FCA.

Budget

As our Chairman said in his foreword, the FSA recognises the difficult economic circumstances for many firms and we are committed to keeping any essential cost increases to a minimum. We will achieve this by capping staff levels for the second year in a row and restricting core operating costs too, broadly in line with inflation.

However, in order to deliver on the plans I have outlined, continue our focus on the quality of our staff, implement the government's regulatory reform programme and invest in the necessary long-term IT infrastructure, the annual funding requirement (AFR) for the FSA will rise this coming year.

A significant part of this increase reflects the costs of implementing the government's reform of the UK regulatory framework. The current £32.5m costs for the restructuring are within the overall estimates set by the Treasury last year, which equates to 28% of the increase in AFR. The AFR will also cover the costs of modernising the IT infrastructure to ensure it is a suitable platform before the transition to the FCA. This will require a £22.4m increase in the AFR, which equates to 29% of the increase.

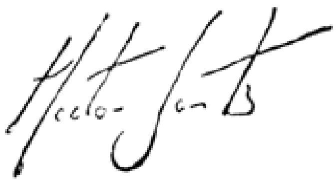
Overall the AFR for 2012/13 is £578.4m, up from £500.5m in 2011/12, a gross increase of 15.6% in overall funding. The increase in fees will be borne mainly by larger firms, reflecting the resources applied to intensive supervision of high-impact firms. Medium-sized firms will see a proportionate increase reflecting the type of business they conduct. However, 42% of the FSA's authorised firms, which only pay the FSA minimum fee will see this unchanged for the third year running at £1,000.

We recognise that the average increase in the FSA's fees for last five years has been around 13%. This rate of growth cannot continue indefinitely, particularly when the financial services industry continues to be under pressure and so we would like to emphasise our commitment to ensuring direct costs of regulation are proportionate.

Conclusion

On the current legislative timetable, this will be the last year for the FSA in its current form and thus the last FSA *Business Plan*.

So the key focus for the next year is to hand over to the new authorities, having demonstrated that we have learned the lessons of the years since the onset of the financial crisis, and that the progress we have made and the benefits that flow from this will continue to felt for the years to come.



Hector Sants
March 2012

Twin peaks regulation within the FSA: what it means for firms

As the *Business Plan* highlights, from 2 April, the FSA will move to a 'twin peaks' model. So, from this date, banks, building societies, insurers and major investment firms will have two groups of supervisors, one group focusing on prudential and the other focusing on conduct. All other firms (i.e. those not 'dual regulated') will be solely supervised by the conduct supervisors.

How the model will work

Two independent groups of supervisors will supervise banks, insurers and major investment firms covering prudential and conduct. All other firms (i.e. those not dual regulated) will be solely supervised by the conduct supervisors.

- The two groups will make their own, separate, set of regulatory judgements against different objectives.
- They will coordinate internally to maximise the exchange of information which is relevant to their individual objectives, but to be clear, they will act separately when engaging with firms. We have termed this 'independent but coordinated regulation'.
- We will retain the principle of seeking to ensure that regulatory data is only collected once. In other words, we will retain our common, current data infrastructure.

These principles reflect the fact that each group of supervisors has a different objective. So they must be able to act independently as they will be pursuing different goals.

These characteristics will be carried over to the FCA and PRA as they are fundamental underpinnings for any twin peaks model, whether operated in a single authority or not.

There may be occasions when the FSA as a whole is required to make judgements that cut across the individual objectives. In these circumstances the judgements will not be made by the individual supervisory groups but rather the overarching FSA executive committees and, where necessary, the FSA board.

Key changes for firms

- We will stop using the existing ARROW risk mitigation programme and will split any outstanding actions between those relevant to the conduct supervisory group's objectives and those relating to the prudential supervisory group.
- From 2 April, the two supervisory units will run their own risk-mitigation programmes and firms will have two separate sets of mitigating actions to address.
- If your firm is due to complete an ARROW assessment before spring 2013, it will still be subject to a supervisory review. But this will consist of two supervisory teams assessing the risks against their new objectives.
- The two supervisory groups may ask an apparently similar question, but the purpose will be different. For example, both groups will ask about the firm's board and governance processes. The prudential supervisors are concerned about the risks to the firm's stability and whether they are being well-managed, while the conduct supervisors are interested in whether the firm's customers are being fairly treated.
- We will not send your firm a consolidated list of the required actions arising from the two supervisory assessments. Central to the concept of genuine twin peaks is that both sets of regulatory objectives are different and determined by Parliament to be of equal importance. So firms must address each set of actions arising from the prudential and conduct reviews with equal focus. To be clear, the two groups of supervisors will not prioritise between prudential and conduct risk.

Key strategic aims and how they will be measured

Regulatory reform

The twin-peaks model within the FSA gives an opportunity to further embed the move towards forward-looking, proactive and judgement-based supervision. Changes should not only be structural, but must also place much more importance on behavioural changes from both supervisors and firms.

Key ways in which we will assess the success of our new judgement-led approach are:

- The ability of supervisors to identify and focus on the big risks to their statutory objectives. This is reflected in our drive to reduce the number of issues recorded in our firm risk management systems, closing or deleting issues where appropriate. Already, this work has delivered a 5% reduction in risks recorded since December 2011. We do not consider it appropriate to set firm targets as risks reflect broader circumstances. Nevertheless, we can reasonably assume further falls in recorded risks.

- The capability of supervisors to make the right judgement about the course of action to reduce the probability of risks to their statutory objectives.

Financial stability

We are responsible for contributing to the protection and enhancement of the stability of the financial system. We do this through ensuring firms are well-supervised and that we identify – and act upon – emerging threats and risks to financial stability.

Our primary objective for financial stability is to make sure that, ideally, firms where failure would have a systemic impact do not fail, but if this does happen, it occurs in an orderly way, minimising the impact on the financial system and cost to the taxpayer.

We measure financial stability through a wide range of capital, funding and liquidity indicators, submitted to the FPC, including for:

- capital, measures including leverage[1] and core tier 1 capital; and

- funding and liquidity, measures including CDS spreads.

Market confidence

Confidence in financial markets can be affected by the stability of the financial system, the degree consumers are protected in financial markets, and the policy settings and supervisory standards relating to the activities on those markets.

It is not possible to have just one metric for the wide range of markets we regulate. We use individual measures for different areas, e.g. for equity markets:

- for market fairness we use measures of market cleanliness, including suspicious trades[2];

1 Typically total assets as reported, divided by common equity less goodwill and intangibles.
2 Despite some methodological drawbacks to this data, it does give us a useful measure.

- for efficiency we use FTSE 100 time-weighted spreads; and
- for resilience we use FTSE volatility measures.

Consumer protection

To secure the appropriate degree of protection for UK consumers, we focus on achieving fair outcomes for consumers. And we seek to ensure that firms adhere to our conduct principles and deliver a forward-looking proportionate supervisory regime through effective risk prioritisation, identification and mitigation.

We seek to avoid events generating consumer detriment above £250m and 50,000 people. This does not mean that we do not aim to reduce the probability of lower levels of detriment occurring, but rather we accept that given our limited resources it is inevitable that detriment to consumers will periodically occur below the £250m level.

Identifying specific metrics is difficult because of the complex sets of factors often involved. However, we recognise the particular importance of consumer detriment and credit metrics, which we measure through:

- redress paid by firms;
- complaints made to firms or the Financial Ombudsman Service; and
- mortgage indicators including arrears and repossessions.

Financial crime

Credible deterrence and enforcement action is an important part of our financial crime strategic objective. However, we recognise that tracking enforcement outcomes does not in itself result in a reliable indication of prevalence. So we do track a range of external measures, including the number of fraud reports reported to CIFAS (Credit Industry Fraud Avoidance System). We set out our supervisory strategy in relation to financial crime in Section 6.

Operations (people)

How we operate, with our people strategy at our heart, underpins the delivery of our statutory objectives. We need high-quality staff with relevant experience and a blend of market and regulatory skills to deliver judgement-based supervision. We measure this through:

- length of service of supervisory staff;
- staff turnover; and
- successful progression of staff through our Training and Competence schemes.

Section 1

Regulatory reform

Introduction

In 2010, the government outlined its proposals for a new regulatory system. It announced that the FSA would be succeeded by two new regulatory authorities – the Prudential Regulation Authority (PRA), responsible for the prudential supervision of banks and insurance, and the Financial Conduct Authority (FCA), focusing on consumer protection and market regulation – creating a 'twin peaks' style regulatory model in the UK.

We have made considerable progress towards establishing the new regulatory structure, setting out the operating philosophies and future vision for the PRA and FCA and working on the detailed design of the two organisations.

During 2012/13, we will achieve two significant milestones towards our transition to the new regulatory system.

- We will move to a 'twin-peaks' regulatory model within the FSA on 2 April 2012. There will be two independent but coordinated groups of supervisors for banks, insurers and major investment firms covering prudential and conduct.
- We will then 'cutover' to the new authorities and legal framework; the point at which the FSA ceases to exist and formally splits into the PRA and FCA. The precise date of this legal cutover depends on the parliamentary timetable and legislative process, but our planning assumption is that it will be early in 2013.

Our transition plans are designed to ensure an orderly and progressive transition to the new regulatory system, together with the opportunity to refine our thinking and processes. During the transition, the FSA will remain as a single regulatory authority and we will continue to deliver against our statutory objectives and business priorities which are outlined further in this *Business Plan*.[3]

Prudential Regulation Authority (PRA)

Operating as part of the Bank of England, the PRA will be a focused prudential regulator, with responsibility for the prudential supervision of banks, building societies, insurers, friendly societies, credit unions, Lloyd's of London and its managing agents, and certain significant investment firms – totalling, we estimate, about 2,200 firms. At the demerger, approximately 1,100 staff will be transferred to the Bank.

3 The 2012/13 *Annual Report* will continue to report on delivery against the FSA's statutory objectives. The timing of its publication may vary, depending on the exact date of legal cutover, and we will provide an update on its timing and content when the 2011/12 Annual Report is published.

The PRA's role will be to contribute to the promotion of the stability of the UK financial system through the micro-prudential regulation of the types of firms set out above. It will have an overall objective to promote the safety and soundness of regulated firms, and will meet this objective primarily by seeking to minimise any adverse effects of firm failure on the UK financial system and by ensuring that firms carry on their business in a way that avoids adverse effects on the system.

For insurance supervision, the PRA will have two complementary objectives – to secure an appropriate degree of protection for policyholders and, as needed, to minimise the adverse impact that the failure of an insurer or the way it carries out its business could have on the stability of the system.

The PRA will achieve this by:
- aiming to avoid failures that are a cost to the economy;
- emphasising resolution planning to permit 'orderly' failure;
- cooperating closely with the FPC and the FCA to ensure macro- and micro-prudential regulation is aligned across the markets; and
- working with the FCA and others to ensure the UK authorities have a strong voice in international – particularly European – policy making.

Financial Conduct Authority (FCA)

The FCA will be a proactive force for enabling the right outcomes for consumers and market participants. It will take a proportionate approach to regulation, adapting to the needs of different consumers and market participants, and set and enforce clear expectations for firms and market participants.

The FCA's role will be to ensure that the relevant markets for financial services in the UK function well. It will achieve this strategic objective by:
- securing an appropriate degree of protection for consumers;
- protecting and enhancing the integrity of the UK financial system; and
- promoting effective competition in the interests of consumers

The FCA will have a duty to promote competition unless this would be incompatible with its strategic and operational objectives. It will also have a separate duty to minimise the extent to which regulated businesses may be used for a purpose connected with financial crime.

As well as its stated objectives, the FCA will:
- focus on the conduct regulation of all firms, covering the range of their dealings with retail customers, through to their activities in wholesale markets (it will regulate about 27,000 firms in total, including those prudentially supervised by the PRA);
- be responsible for the prudential supervision of all firms not prudentially supervised by the PRA (approx 24,500);
- supervise trading infrastructure including the investment exchanges, over-the-counter markets and monitor firms' compliance with the market abuse regime;
- have criminal powers to investigate and prosecute insider dealing;
- take on the FSA's responsibilities as the United Kingdom Listing Authority (UKLA); and
- be responsible for overseeing the Financial Ombudsman Service (FOS), the Money Advice Service (MAS) and, (jointly with the PRA[4]) the Financial Services Compensation Scheme (FSCS).

4 The PRA will be responsible for the oversight and rules of the FSCS relating to deposit taking and insurance provision activities, and the FCA will be responsible for its other activities.

Moving towards the new regulatory system

The legislative timetable for reform

We will continue to work closely with the Treasury on the development of the Financial Services Bill 'the Bill' which is the primary legislation required to enact the changes to the regulatory system. The Bill was introduced to the House of Commons on 26 January 2012, and is currently progressing through the remaining readings and committee stages of Parliament, having already been through pre-legislative scrutiny.

Twin peaks within the FSA

On 2 April 2012, we will move to a 'twin peaks' regulatory model within the FSA, which will allow us to 'road test' some elements of the future 'twin peaks' style of regulation before creating the PRA and FCA.

From 'twin peaks', we will begin to operate two independent, but coordinated supervision teams split between prudential and conduct regulation:

- the Prudential Business Unit (PBU) will be responsible for the prudential supervision of deposit takers, insurers and a small number of significant investment firms and related policy-making; and
- the Conduct Business Unit (CBU) will be responsible for conduct supervision of all firms within the FSA's remit, the prudential supervision of firms outside the PBU's scope (and in the future, the PRA), markets surveillance and oversight, and related policymaking. The CBU will also house the UK Listing Authority and the Client Assets Unit.

The PBU and CBU will, aligned to their clear objectives, develop and operate separate supervisory approaches reflecting their different philosophies and focus on different issues. They will accelerate changes to supervisory behaviours, further embedding the move to forward-looking, proactive and judgement-based supervision that the FSA first started in spring 2008. The focus will be on significant and material risks to their statutory objectives, challenging the underlying causes of the problems that we see, not just the symptoms. There will also be a greater emphasis on the performance of firms' boards and senior management, and an increased appetite to look forward, anticipate problems and willingness to intervene earlier and direct firms when poor performance is identified.

To achieve 'twin peaks', we have split the current integrated approach to supervision, reallocated staff between these two Business Units and made changes to our supervisory risk assessment models. Our supervisory teams will continue to receive training and support on the new approach and processes and we will be reviewing our supervisory training and competency framework during 2012/13.

How different supervisory processes during 'twin peaks' will feel for a regulated firm depends on the nature of its activities. Firms that will be supervised by the PBU and CBU, i.e. those that are 'dual-regulated', will experience a change in the approach and assessment of prudential and conduct matters as they begin working with two independent supervisory teams. These firms will receive a risk assessment from each Business Unit with the respective supervisory decisions and communications to firms clearly identified as prudential or conduct.

While the PBU and CBU will be independent, they will operate in a coordinated manner to avoid unnecessary duplication and ensure that firms are not given contradictory recommendations. Firms that will be solely regulated by the FCA should experience more limited change to supervisory processes as a result of 'twin peaks'. However, they will notice some changes to the supervisory approach, with a more focused approach to prudential and conduct issues and bolder, earlier intervention to tackle potential risks to consumers and market integrity.

We will be contacting firms to ensure that they each understand what 'twin peaks' means for them and who their key supervisory contacts will be from 2 April 2012.

From 'twin peaks' to cutover to the new authorities

'Twin peaks' will continue from 2 April 2012 to cutover, which is expected to be in March 2013 and is the point at which the FSA ceases to exist and the PRA and FCA become separate legal organisations with new statutory objectives. As the FSA, we will continue to carry out our full regulatory obligations during 'twin peaks' and will continue to define risks against our statutory objectives as set out under the Financial Services and Markets Act 2000 (FSMA).

The period between 'twin peaks' and cutover offers the opportunity to refine our thinking and regulatory processes, and to define and build the new PRA and FCA operating models. This will include defining and implementing operational changes and processes, including detailed work on the technology required to support the new supervisory approach. We will also need to ensure that our staff are effectively equipped to deliver the new models and that we have the right mix of industry and regulatory experience.

In addition, the FSA and the Bank of England will publish two further documents setting out in more detail how the PRA and FCA supervisory regimes will function. These will also give firms and other interested parties a further opportunity to comment before the regimes go live.

Cooperation and coordination

While it will be important for the PRA and FCA regulators to pursue their own mandates, they will need to coordinate in some areas and cooperate in others to avoid duplication and conflicting regulatory actions, and to ensure that firms receive consistent messages as they adjust to the new regulatory environment.

The draft Memorandum of Understanding (MoU) between the PRA and the FCA, published in January 2012, defines these arrangements to help ensure they are effective and efficient, and puts in place a high-level framework for how the organisations will work together within the new regulatory structure. The MoU will remain in draft form until the Bill completes its parliamentary process.

During 2012/13, we will continue to work with the Bank and the Treasury to further develop the draft MoU (and supporting documentation such as operating manuals and service level agreements) underpinning this relationship, and also the other formal requirements stipulated in the Bill. While the MoU provides an important framework for effective coordination between the PRA and FCA, it will not be the only thing that drives coordination. The way the people within the organisations work together will be equally important, with the focus on cooperation, openness and transparency.

We will also publish further MoUs between the regulators and other organisations to help ensure effective coordination across the regulatory system.

Competition

As confirmed by the Draft Bill published on 26 January 2012, the FCA's competition objective will go further than FSMA. The FCA will have a specific operational objective to promote effective competition in the interests of consumers. This will enable the FCA to take a more proactive approach in tackling competition issues in financial services markets that cause consumer detriment. This could include looking at behaviours across a market and dealing with issues not often explicitly tackled by the FSA and its predecessors, which could be remedied by measures to promote competition. The FCA will also have to carry out its general functions in a way that promotes effective competition (where compatible with the consumer protection and integrity objectives).

During 2012/13, we will continue with the design of the FCA, including considering how best we can meet this competition objective. We will define how these new powers can be used as a regulatory tool, and how competition can be appropriately embedded into the operational design of the FCA, which will include assessing the resource and skills required to deliver this objective.

In addition, as part of the design of the FCA, we will also need to consider the impact on the organisation of taking on responsibility for consumer credit regulation, plus changes to its supervisory approach, in particular the expectation that it will intervene at an earlier stage.

The cost of regulatory reform

The total cost of creating the PRA, across the Bank, FSA and Treasury, is expected to be in the region of £115m to £150m, which comprises expenditure on accommodation, IT and staff transfer costs. This margin reflects some remaining decisions on the scale and cost of the PRA's IT infrastructure and accommodation although we will continue to work with our colleagues at the Bank to ensure that we have a thorough analysis of current and future infrastructure costs.

The cost of implementing the new regulatory system and creating the PRA and FCA can be split between the FSA and the Bank. The FSA spent £1m in 2010/11, and a further £12m and £32.5m is expected to be spent in 2011/12 and 2012/13 respectively.

Throughout the transition process, the FSA and the Bank will seek to minimise the cost of regulatory reform to firms.

Other regulatory reforms

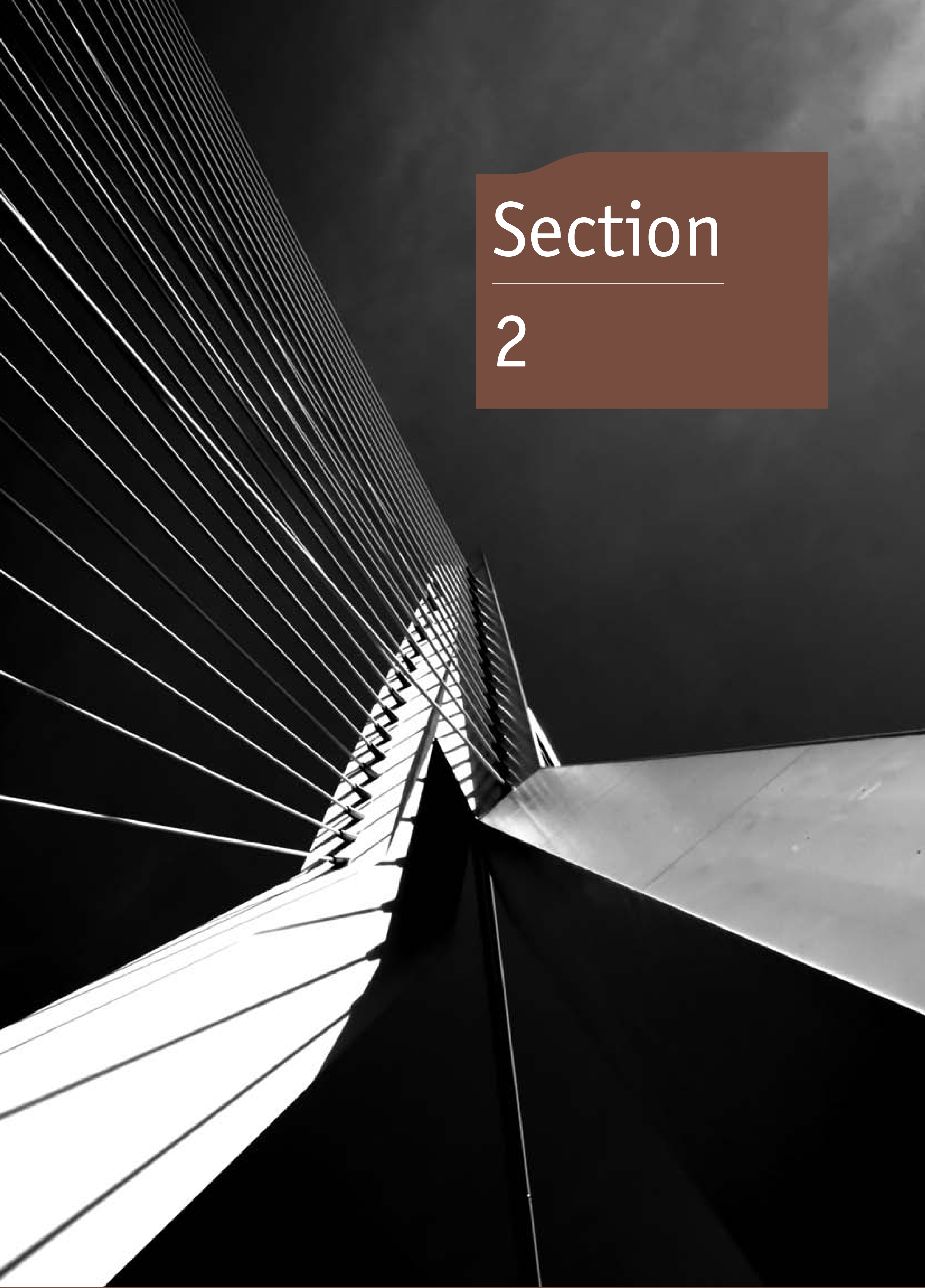
There are a number of separate financial services reforms that may have an impact on the regulatory reform agenda and the scope of the PRA's and FCA's work.

In December 2011, the government published its response to the Independent Commission on Banking's final report on recommended reforms to improve stability and competition in UK banking, which included some recommendations for inclusion in the Bill. The government has confirmed that it will be implementing the main recommendations of the report in full – namely, that high-street banking activities be separated from investment banking activities by a ring-fence, that banks hold a higher capital buffer and that competition in the banking sector be strengthened. Primary and secondary legislation relating to the ring-fence will be completed within this Parliament but separately from the Bill.

We welcome the Treasury's and the Department for Business Innovation and Skills' proposal that in principle, responsibility for consumer credit regulation should be transferred from the Office of Fair Trading to the FCA. This means that, if a proportionate model of regulation can be identified, the FCA could have responsibility for lending and other Consumer Credit Act regulated activities. We will be working with the Treasury and others to design an appropriate regime, which we expect will be implemented one to two years following the formal creation of the FCA.

The international dimension to financial regulation and supervision will increasingly influence the UK regulatory agenda in 2012/13. We will continue to be fully engaged in international financial policy development, particularly in areas of importance to the UK, for example on capital and liquidity standards, such as CRD IV. Further details of the international regulatory agenda can be found in Section 2.

Section 2



International

Introduction

The international dimension to financial regulation and supervision is central to our regulatory agenda, with the majority of the PRA rule book derived from European legislation. Rules are increasingly made by Europe and the role of the PRA and FCA will primarily be one of supervision and enforcement.

Our international priorities for 2012/13 are to:
- deliver effective supervision and crisis planning for cross-border firms and market infrastructures to enhance global financial stability;
- support an effective international regulatory and supervisory architecture; and
- play a key part in developing international standards, to be applied to market participants and supervisory authorities to enhance regulation in the UK.

Effective supervision and crisis planning of cross-border firms

Supervising cross-border firms requires effective cooperation between national supervisory authorities. During 2012/13, we will continue to work closely with other regulators to deliver effective supervision and crisis planning for internationally active firms. We will achieve this by leading supervisory colleges for UK firms that have overseas activities and participating in supervisory colleges for overseas firms active in the UK.

International regulatory architecture

As an active member of each of the European Supervisory Authorities (ESAs) and global standard setting bodies (see Box 1), we will seek to advance UK policy objectives.

Box 1: European Supervisory Authorities and global standard setting bodies

Global standard setting bodies
- Financial Stability Board (FSB)
- Basel Committee on Banking Supervision (BCBS)
- International Association of Insurance Supervisors (IAIS)
- International Organisation of Securities Commissions (IOSCO)
- Financial Action Task Force (FATF)
- Joint Forum

European Supervisory Authorities (ESAs)
- European Banking Authority (EBA)
- European Insurance and Occupational ensions Authority (EIOPA)
- European Securities and Markets Authority (ESMA)

We will work together with the ESAs and global standard-setting bodies to ensure that the international regulatory and supervisory architecture meets the UK's needs. This includes contributing towards reviews of: the governance and structure of standard setting bodies; expanding the IOSCO Multilateral Memorandum of Understanding; and preparing for the UK's input to the review of the ESAs to be undertaken by the European Parliament in 2013. We will also continue to work with international bodies on cross-border enforcement and criminal investigations.

During 2012/13, we will bolster our influential position in international negotiations through effective senior and working-level representation in the international standard setting bodies and the ESAs. Hector Sants and Martin Wheatley are members of the management boards of EIOPA and ESMA respectively, and Hector Sants is a member of the Board of Supervisors of the EBA. We will also continue to second staff to the ESAs, global standard setting bodies, EU institutions and overseas supervisors to enhance skills and promote the sharing of knowledge between international authorities.

Developing international standards

Influencing global financial services policy development is a core part of our International strategy. We will remain heavily involved in negotiations with the ESAs and global standard-setting bodies to develop international rules and standards. These will be binding on many of the firms we regulate and will affect the way we conduct supervision.

Our 2012/13 *Business Plan* reflects the work that will be undertaken on the policy proposals formed at the global level and legislative proposals formed at an EU level, including:

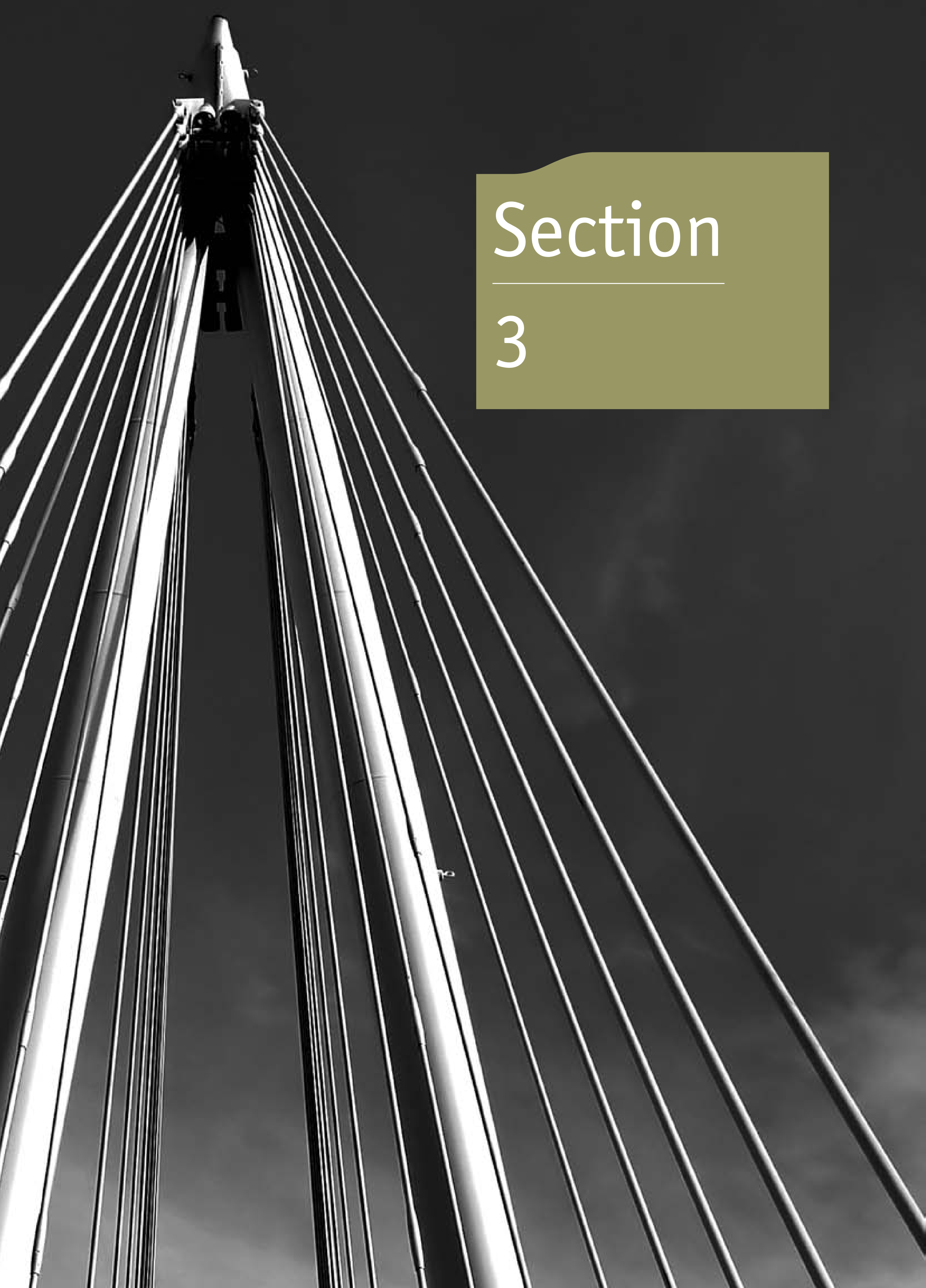
- potential identification of domestic Systemically Important Financial Institutions (SIFIs);
- recovery and resolution plans;
- the Capital Requirements Directive IV;
- the review of the Markets in Financial Instruments Directive;
- the European Market Infrastructure Regulation (EMIR) Directive;
- the review of the Market Abuse Directive (MAD);
- Solvency II; and
- Packaged Retail Investment Products (PRIPs).

Additionally we remain focused on ensuring that the international standards agreed in recent years are fully implemented in the UK – and elsewhere – and that the intended benefits are delivered. At the same time we will ensure that supervisors retain flexibility to customise international frameworks to address firm-specific risks.

We will actively engage in international peer reviews conducted by the IMF, global standard-setting bodies and ESAs to promote robust implementation of international standards globally. We will also incorporate the recommendations made by the IMF following their Financial Services Assessment Programme (2011) into the design of the new UK regulatory architecture and supervisory operating models.

Section

3



Delivering financial stability

Introduction

We are required by statute to 'contribute to the protection and enhancement of the stability of the UK financial system. In carrying this out we aim to ensure the safety and soundness of firms, avoid disorderly failure that has systemic consequences and reduce the cost of orderly failure.

As a micro-prudential regulator we will do this by:
- requiring appropriate capital and liquidity levels and management controls from prospective market entrants;
- implementing international capital and liquidity standards;
- ensuring our firms are well supervised, with strong governance;
- developing and strengthening our supervisory tools;
- requiring firms to strengthen their capital and liquidity regimes, systems and controls, and governance; and
- reducing the impact of any potential failure through our work with firms on their recovery and resolution plans.

We will also support the wider framework for macroeconomic, fiscal and financial stability in the UK and internationally through actively participating in a number of different forums and frameworks, including:
- the Financial Stability Board and other global standard setters;
- the interim FPC, including identifying and monitoring risks and implementing recommendations;
- the EU framework, including ESAs, governing financial regulation and setting out technical standards;
- the UK framework for macro-prudential regulation; and
- the resolution framework, including deposit guarantee schemes.

Summary of our supervisory strategy

Banks

Prudential supervision will continue to focus on forward-looking assessments of the risks to our objectives, including the financial stability objective, from authorised firms. As we prepare for the new UK regulatory framework, changes will be made to anticipate the regulatory framework.

For the largest UK banks and building societies, we will continue to deepen our understanding and assessments of business model sustainability, capital and liquidity stress testing, and governance and risk management effectiveness. Using specialist expertise where appropriate, we will form an overall opinion of major risks to our statutory objectives from each firm, and will devise targeted action plans. Early, proactive interventions will be made to reduce risks to the stability of the system.

Supervisors will continue work on recovery and resolution, including assessing current recovery and resolution planning. This will be extended to a wider population of banks, building societies and investment firms. Supervisors, supported by FSA experts, will work with the Bank of England to assess and improve resolvability.

Regarding banks with foreign operations or that are foreign-owned, we will engage further in international supervisory cooperation through colleges of supervisors and other mechanisms. This will include deeper cooperation with other European supervisors within the new framework of enhanced EU supervision, including processes introduced in 2011 for joint decisions on risk assessments and capital requirements.

Insurers

We will extend our work with the largest firms to deepen our assessments of insurers' business models and their resilience under a range of conditions. We will maintain our focus on understanding the financial impacts of stressed market conditions, including through use of standardised stress testing and reverse stress testing.

As part of our supervisory work on Solvency II, we will continue our assessment of firms' progress towards meeting the new standards, including through detailed reviews of insurers' risk management arrangements and proposed internal models.

For life insurers we will take forward our work on with-profits issues within mutual insurers and begin to organise our separate assessments of the financial and consumer impacts of with-profits issues within the FSA, consistent with the intended future arrangements for the PRA and FCA. For general insurers we will maintain our focus on key financial risks, such as underwriting controls and reserving practices.

Overall, we will make more use of external tools, such as skilled person reviews under s166 of FSMA. Where there are weaknesses in firms' practices we will press for improvements through all tools available to us, including requiring improvements to control frameworks, setting higher capital requirements, requiring senior management changes, and restricting levels of new business. This will ensure supervisory resources are focused on our most significant concerns, with firms' senior management held responsible for resolving other issues that arise through our supervisory work.

Delivering our supervisory capabilities

Background

This will help our supervisors make the right judgements about prioritising risks and the actions that firms should take. In 2012/13 we will develop and strengthen our capability to provide more sophisticated and specialist indepth-risk analytics and stress testing across firms, risk types and all asset classes.

Through our intensive supervision we make judgements on the following:

- the total impact of firm failure;
- business models;
- systems and controls, culture, senior management and governance;
- capital, liquidity and asset quality; and
- resolution planning.

We will continue to use our service standards to measure our performance to ensure that we are processing enquiries and requests efficiently.

Analytics and Risk Technology (ART)

ART is the project to deliver a scalable and agile technology platform to run our stress testing and scenarios analysis framework. There are three key objectives to this project:

1) to capture appropriate data from banks, spanning all asset classes;
2) to provide a risk engine to enable stress testing, including reverse stress, multiple stress and idiosyncratic stress on all portfolios and banks; and
3) to streamline the process.

We have already successfully piloted the process of credit stress testing and have moved the data infrastructure to the Bank of England.

In 2012/13 we will begin to collect 'clean', detailed data for the Very High Impact Firms (VHIFs), and to do this we will have data projects with each of the VHIFs. We will be implementing the collection of data into the electronic data portal in the Bank of England's Monetary and Financial Statistics Division (MFSD) and we will complete further phases of the pilot where we will run Pillar 2b stress tests in multiple banks. Finally, we will look to design the prototype to further the aforementioned pilot into trading and counterparty risk portfolios.

Operational resilience

The main aim of our resilience work is to improve the resilience of the financial system against major operational disruption from any source, including physical events such as terrorist attack, severe weather, pandemic and electronic attack. We work closely with the Bank of England and the Treasury to carry out the following:

- an intensive review of key firms' resilience plans;
- the Market-Wide Exercise (MWE) programme, designed to test the sector's ability to respond collectively in a coordinated way to disruption;
- a benchmarking programme that feeds into our Business Continuity Management Practice Guide, which aims to spread good practice; and
- input into the Finance Sector Resilience Plan (FSRP), submitted to the National Security Council by the Treasury every year, which assesses the resilience of the finance sector.

Our MWE and Benchmarking programmes have given us a good understanding of the operational resilience of the major financial firms and infrastructure providers. To build on this we are rolling out a programme of more intensive reviews of these firms. We aim to complete our reviews by the end of 2012.

We are also implementing a number of lessons learned from previous MWEs and will be undertaking a fresh round of benchmarking to enable us to revise our Business Continuity Management Practice Guide in the second half of the year.

These workstreams will together provide us with the material we need to contribute to the FSRP towards the end of 2012.

Business Model Analysis

In 2012/13 all prudential supervisors will use Business Model Analysis (BMA) as a key part of a judgements-based supervisory approach. BMA looks at the design and execution of a firm's business model, how it makes profits, cash and capital, and what the main threats are to its viability and sustainability, including the external macroeconomic and business environment.

Directors of failed banks

We are examining various options to make it easier to refuse an application for an approved persons status on the basis that the person's previous role as a director of a bank that failed raises fundamental questions about their competence or general suitability to perform a similar role again. We plan to set these out in a Discussion Paper in the first half of 2012.

Internal audit

We are assessing the effectiveness of internal audit functions among the largest deposit takers. We want more effective internal audit functions that supervision can rely on as part of the robust corporate governance at the major firms. This will involve a possible code of practice and guidance on internal audit, to be issued in the second half of 2012.

Additional supervisory responsibility – Northern Ireland Credit Unions (NICUs)

Northern Ireland and Treasury ministers have decided to transfer responsibility for the regulation of NICUs from the Department of Enterprise, Trade and Investment (DETI) to the FSA. The transfer of regulation will take place on 31 March 2012. The transfer is intended to allow NICUs to expand their services, and to provide their members with FSCS protection, which they do not currently have.

Once transferred:

- we will ensure all NICU's are Single Customer View compliant – we expect this to be by September 2012;
- each NICU will operate to a business model with appropriate governance, controls and risk management;
- each NICU will submit accurate regulatory returns, with firms submitting their first quarterly returns in January 2013;
- supervision will apply a risk based approach commensurate with the relative risk of each firm; and
- supervision will be able to deal with any failure of a NI credit union without adverse sector impact.

Policy – Capital and liquidity frameworks

As a national micro-prudential supervisor our main role is to implement international frameworks and European law. However, we also participate in the policy formulation process at both Global and EU levels, and where possible aim to influence the content of new legislation. The following section sets out the major directives on which we will be working.

CRD IV

The prudential framework for deposit takers and investment banks in Europe is set out in the Capital Requirements Directive (CRD). The CRD is updated periodically and the EU Commission published the latest revision for CRD IV in July 2011.

CRD IV implements the international Basel III accord into European law, as well as making a decisive move towards a harmonised EU single rule book. It consolidates the original CRD with subsequent amendments, and places most of the rules in the form of a legally binding regulation (CRR) as well as an implementing directive.

In 2012/13, we will be preparing to meet the deadline of implementing CRD IV into domestic legislation by 1 January 2013, as well as updating and developing the necessary supervisory and systems changes as part of this. We will consult on the resulting changes to our rules before the legislation comes into force.

Solvency II

The changes under the Solvency II Directive for insurance firms aim to protect policyholders by establishing a revised set of EU-wide capital requirements and risk management standards, which will replace the current solvency requirements.

This year, we will:

- continue to work with the Treasury, the European Commission and EIOPA on the negotiation of Omnibus II, Level 2 and Level 3 of the Solvency II directive;
- continue to work with the insurance industry to keep firms up to date with policy developments so they can effectively prepare for implementation;
- conduct our consultations to transpose Solvency II into UK rules and a new draft Handbook by 1 January 2013;
- develop and deliver the design and build of the processes required for implementation on 1 January 2014 and beyond, where policy developments allow us to do this;
- work with firms on the implications of the change from a paper based to an electronic reporting process;
- provide UK-specific regulatory reporting templates, with supporting systems and materials for firms and FSA staff to complement the EU-wide material; and
- deliver the required training and support internally and externally.

We will begin to receive submissions from internal model firms from 30 March 2012 according to their allocated submission slot. For firms intending to use the standard formula, our working assumption is that we will be open to receive applications from 1 January 2013 for all approvals that firms will require from 1 January 2014. We may exercise our discretion to deal earlier with more complex issues.

Throughout this, we will also continue our communication with firms and the industry more widely, to make sure that: various parties know what is expected of them and by when; European policy outcomes are closely aligned with the UK strategy; and there is a clear transition plan from the current regime to Solvency II.

Liquidity

We use our interim liquidity regime as a supervisory framework to assist us in judging if a bank holds sufficient liquidity to maintain its safety and soundness. In judging this we take account of current market conditions. The current circumstances that some banks are facing are those where liquidity buffers are intended to be used.

The Basel III accord included the first global liquidity standards: the Liquidity Coverage Ratio (LCR) – a 30-day stress test – and the Net Stable Funding Ratio (NSFR) – a requirement for banks to ensure they have sufficient stable funding relative to the liquidity of their assets. The planned implementation dates for these ratios are Jan 1, 2015 and Jan 1, 2018 respectively.

In the interim period, we are participating in a review to determine whether there are any unintended consequences of the ratios that would require re-calibration. We will continue to collect data from banks to assess the impact of the new standards which will be analysed by ourselves and both the Basel Committee and the European Banking Authority.

We expect the key elements of the LCR to be finalised during this year to remove market uncertainty. It will then be translated into European law to introduce a binding requirement on UK-domiciled banks, although we do not anticipate this happening during the next 12 months.

Developing the Regulatory framework

Financial Policy Committee (FPC)

The interim FPC is established under the oversight of the Bank of England. It is responsible for the stability and resilience of the financial system as a whole. The government envisages that the FPC will contribute to the Bank's financial stability objective by identifying, monitoring and taking action to remove or reduce systemic risks to protect and enhance the resilience of the UK financial system. It meets quarterly and once it has received statutory footing it will direct bodies, including the PRA and FCA, to act in line with the specified toolkit.

At present, the FPC operates in an interim capacity. It makes recommendations that the FSA needs to consider under its current legal status, which are then implemented in an effective, timely fashion or explains why it is not implementing the recommendations.

During 2012/13 we will continue to support the interim FPC process through briefings on key issues and implementing relevant actions. Our aim is to ensure that it has a clear view of key supervisory, firm-specific and market resilience issues for which the FSA has remit and is fully supported in undertaking its macro-prudential role.

Systemically Important Financial Institutions (SIFIs)

The internationally agreed SIFI policy framework has three key areas:

- a resolution framework;
- more intensive supervision; and
- higher loss-absorbency requirements.

We will work with the relevant international community members to consider extending the higher loss-absorbency requirements to domestic systemically important banks and how this might apply to any globally systemic insurance firms and other SIFIs, such as infrastructure providers. We will also be involved in work to implement the Global SIFI framework in the EU. This work will be carried out with reference to both the outcomes of the Independent Commission on Banking (ICB) proposals and our own recovery and resolution planning mechanisms.

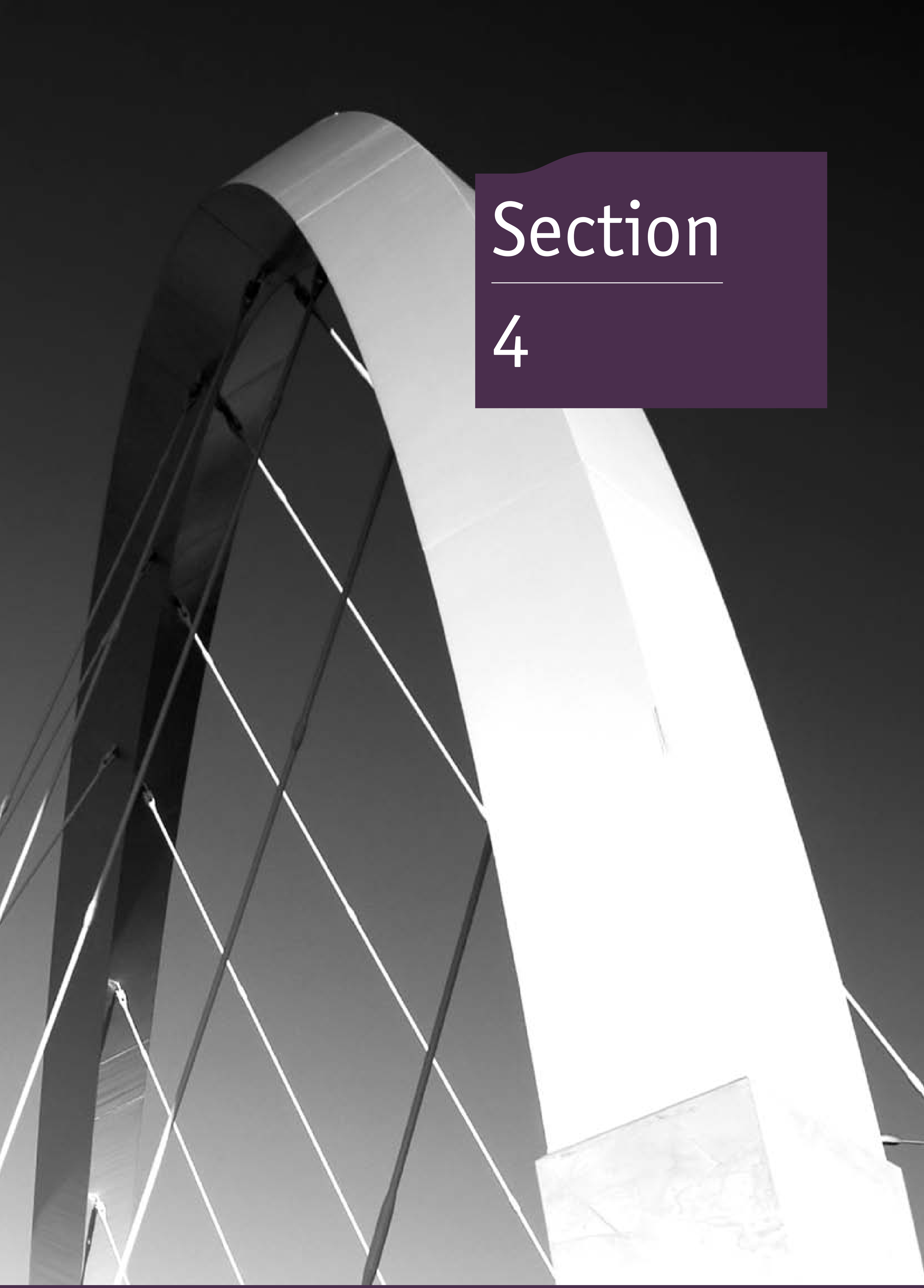
ICB proposals

Following our work with the Treasury on the official government response, we will engage with the Treasury on any White Paper resulting from this. We will also participate in discussions and negotiations on primary and secondary legislative changes and implications of these for our own rules.

Shadow banking

With regulation on banks tightened, it is increasingly important to address systemic risks, such as maturity/liquidity transformation and leverage, arising from the shadow banking sector and its interaction with the regular banking system. We will continue to work with other regulatory bodies in the UK and internationally to better understand and monitor the build up of risks in shadow banking entities and, where appropriate, recommend regulatory changes to mitigate these risks.

Section 4



Delivering market confidence

Introduction

One of our statutory objectives is to maintain confidence in the UK financial system. Central to achieving this objective is that people have confidence in the use of financial markets, and we work towards ensuring markets are efficient, resilient and fair.

Confidence in financial markets can be affected by the stability of the financial system and the degree of protection of consumers in financial markets. Policy setting and supervisory standards relating to the activities in those markets, however, also have a large part to play in this.

We are responsible for formulating the policies underpinning the functioning of organised and over-the-counter (OTC) markets, taking into consideration the wider European and global policy-making framework.

To achieve our market confidence objective during 2012/13 we will:
- deliver an intensive supervisory approach to the markets, including developing our market surveillance systems;
- continue to focus our surveillance and enforcement resources on tackling market abuse, insider dealing and wholesale misconduct within the UK markets;
- operate the UK listing regime;
- further strengthen the protection of client money and assets; and
- operate the UK covered-bond regime.

We also participate fully with the European authorities, particularly the European Securities and Markets Authority (ESMA), to shape the European markets policy agenda to deliver regulatory outcomes.

Delivering supervision to enhance market confidence

Our supervisory approach works towards a market infrastructure that is sound, efficient and resilient, and to ensure the proper conduct of market participants.

Our long-standing policy has been to approach market regulation through a risk-based system, which can assist competition and innovation, including by granting regulatory licences to new entrants who meet the required standards. Our regulatory decisions are made on transparent and objective criteria that respect the freedom of establishment across the EU and encourage fair competition.

During 2012/13, we anticipate significant reconfiguring in the European infrastructure provider environment. We will focus on ensuring that this reconfiguration is within the requirements of our regulatory framework and continues to aid the delivery of efficient, resilient markets so that confidence in those markets is retained. We will work in conjunction with the Treasury and the Bank of England on these issues. The possible European initiative on a resolution regime for CCPs will be an important development in the market infrastructure supervisory environment.

As part of this approach we will continue to conduct thematic assessments based on market developments. Following the publication of ESMA guidelines on systems and controls for highly automated trading, we will undertake a programme of firm visits and desk-based reviews of a selection of market infrastructures and investment firms to assess their organisational arrangements in light of the guidelines.

Maintaining market integrity

During 2012/13 we will continue to use our range of enforcement powers – criminal, regulatory and civil – to take action on market misconduct to support our market confidence objective. We will work on improving standards of conduct in wholesale markets and take tough action against those who commit market abuse and insider dealing. As part of our credible deterrence strategy, we believe that actions against individuals are more likely to lead to a change in behaviour and increase standards of conduct in the industry, so we will continue to focus our efforts in this area in 2012/13.

We will continue to pursue appropriate criminal actions for insider dealing. The criminal cases we are bringing are increasingly large, complex and focused on priority areas, such as abuse by market professionals and insider dealing rings.

In addition to securing prison sentences, we will continue to take action to deprive those found guilty of the proceeds of their crimes through appropriate confiscation proceedings. We have a number of confiscation hearings still due to take place.

Alongside criminal prosecutions, we will continue to take other regulatory action against individuals who commit market abuse, issuing significant fines and banning market abusers from the industry.

Completing the SABRE/ZEN market abuse surveillance system provides an integrated transaction data collection and interrogation tool. During 2012/13 we will continue to develop the interrogation of transaction data and further improve our intelligence-based detection of market risk and market abuse.

Our market surveillance agenda in 2012/13 will take forward our collaborative approach with market infrastructures and other competent authorities. We intend to further build relationships within the Surveillance Practitioners Group (ten major exchanges and trading platforms are represented) to improve the flow of information and enhance engagement of all members. This will include meeting members on an individual and less formal basis, in addition to the bi-monthly meetings to build trust.

During 2012/13 we will collaborate with surveillance teams within Investment Banks to share experiences and provide guidance on our expectations for effective surveillance. All of this work, along with establishing appropriate mechanisms for exchanging information, will allow us to work towards preventing and detecting market abuse in a fragmented trading environment.

As our surveillance and intelligence capabilities improve we are better able to detect and intervene earlier to obtain injunctions to prevent market abuse. We will continue to use our civil powers to apply to the High Court for restitution orders and injunctions to prevent further market abuse.

Together with enforcement action, we remain committed to undertaking a programme of thematic work, including suspicious transaction reports, pre-soundings and subsequent education to industry through issuing guidance. We will also review certain key areas as well as attending firm visits in coordination with firm supervisors to assess firms' market abuse systems and controls.

Despite successful enforcement action against firms for breaches of transaction reporting requirements, compliance remains patchy. During 2012/13, in line with our credible deterrence approach, we will focus on this area. Where firms fail to respond appropriately and improve standards, we will increase penalties.

UK Listing Authority (UKLA)

The key aim of the UKLA is that the UK regime for listed issuers raising capital remains efficient and internationally competitive, with high standards of transparency and investor protection.

During 2012/13 we will complete the upgrade of our IT systems. Delivering this will enable a more efficient allocation of resources, and position the UKLA to respond more flexibly to the dynamic market environment.

We will consider responses to our Consultation Paper CP12/2 published in January 2012 including determining whether any specific changes need to be made to the Listing Rules to further enhance the shareholder protections and overall benefits that they currently afford. We will also consult on proposed changes to the Listing Rules to support the implementation of new UKLA IT systems.

Supervising client assets

Our supervisory work shows many firms have inadequate records, ineffective segregation of client assets and a low level of awareness of requirements in this area. This risks causing detriment to clients, creditors and counterparties with associated reputational damage to confidence in UK markets. We seek to ensure that, where necessary, firms exit the market in an orderly manner, with clients' assets returned within a reasonable timeframe, and that the UK market is consequently regarded as a safe place to conduct business.

In 2012/13 we will further strengthen our intensive regulatory and supervisory approach for firms holding client money and safe custody assets and increase our knowledge and oversight of the UK market. We will achieve this through:

- more intensive supervision for firms holding client assets in terms of the number of visits, thematic projects and desk-based reviews;
- further developing our risk assessment methodology through embedding the Client Money and Assets Return (CMAR), which is one of the ways we identify concerns within firms;
- considering our regulatory response following the outcome of the Lehman Brothers International (Europe) (LBIE) Supreme Court client money appeal, expected in the first half of 2012;
- taking forward proposals for a CASS resolution pack to help promote the speedier return of client assets in the event of a firm failure, by ensuring the information and records required by an Insolvency Practitioner to return a client's assets would be readily accessible after a firm's failure;
- considering the next stage of the review of the rules covering client money held by insurance intermediaries (CASS 5); and
- responding, and feeding into various EU directives and regulation.

We will continue to take regulatory action where firm failings are identified. We expect that our increased oversight of firms, through the CMAR and the improving quality of auditors' client assets reports, will provide greater insight and identify issues in firms.

Domestic initiatives

Review of the Client Assets Regime

Following the collapse of MF Global, we have committed to taking a fresh look at our client assets regime. The protection of client assets will continue to be a key regulatory priority, with our specialist Client Asset Unit taking the lead on these issues.

Regulated Covered Bonds (RCB)

In December 2011 we published a Policy Statement reflecting the final amendments to the RCB Sourcebook. This aims to promote transparency and improve investors' understanding of the RCB regime. During 2012/13, we will be preparing for the implementation of amendments to the RCB Regulations and RCB Sourcebook that will come into effect on 1 January 2013.

EU policy

As a national supervisor, our role in this area is primarily to implement EU legislation. However, we also participate in the formulation of new policy, working through

ESMA to improve the overall framework of market regulation.

During 2012/13 we will provide support to the Treasury in the negotiation of five key EU legislative proposals aimed at addressing deficiencies in the efficiency, safety and soundness of markets. These are:

- the European Market Infrastructure Regulation (EMIR), first published in September 2010;
- the review of the Markets in Financial Instruments Directive (MiFID);
- the review of the Market Abuse Directive (MAD);
- the review of the Transparency Directive (TD); and
- further changes to the Credit Rating Agency Regulation (known as CRA 3).

Alongside these high-level legislative proposals we will also work intensively through ESMA, on the development of Technical Standards to progress the full implementation of the European Short Selling Regulation, the Prospectus Directive Amending Directive, and the EMIR by the end of 2012.

During 2012/13, we expect the EU Commission to publish four further legislative proposals covering:

- resolution regime for financial market infrastructures;
- corporate governance for listed issuers;
- a harmonised framework for authorisation and supervision of central securities depositories; and
- legal framework for securities holdings.

Below we outline in more detail some of our key policy priorities for 2012/13, why they are important to our delivery of market confidence and what we plan to achieve during the next year.

Over The Counter (OTC) derivatives

During 2012/13 we are committed to reducing systemic counterparty risk, enabling greater transparency of OTC markets and harmonising standards for clearing houses. Our work in these areas is being taken forward in two broad streams:

- the negotiation and implementation of EMIR; and
- a number of other international initiatives involving regulators and industry participants.

EMIR aims to establish a pan-EU regime for central counterparty clearing houses, risk management of non-centrally cleared trades, and trade repositories.

During 2012, we will continue to support the Treasury in negotiations between the EU Commission, Parliament and Council and work in ESMA on the development of Technical Standards to fully implement the requirements of the regulation by December 2012, in line with G20 commitments. Our aim is to develop robust and proportionate standards that are internationally consistent.

The implementation of EMIR is expected to result in more widespread use of central clearing, therefore increasing the systemic importance of CCPs (central counterparties) and we will adapt our supervision accordingly.

We will also participate in international forums, including the OTC Derivatives Regulators' Forum (ODRF), the International Organisation of Securities Commissions (IOSCO) Task Force on OTC Derivatives and the OTC Derivatives Supervisors Group (ODSG) to develop other industry-led and supervisory reforms of OTC derivative markets.

Resolution mechanism for failing CCPs

During 2012, we expect an EU Commission legislative proposal for Financial Market Infrastructures to be published. We will work closely with the Treasury and other European regulators to ensure that appropriate and internationally consistent standards are proposed regarding the recovery and/or orderly wind down of a Financial Market Infrastructure (FMI – including a CCP). This should include both the tools available to the FMI, and the powers and tools available to the relevant authorities to promote financial stability and market confidence in the case of a FMI failure. This work also contributes to our financial stability objective.

Markets in Financial Instruments Directive and Market Abuse Directive

In October 2011, the Commission published its proposals to amend MiFID and MAD. This included a range of measures influenced by the experience of the financial crisis, such as improving investor protection and enhancing the transparency of markets. In both cases, the proposals will be delivered through two instruments, a regulation and a directive, and will represent a significant package of reforms.

We aim for the proposals to:

- take into account the differences in market structure across different asset classes;
- not unnecessarily restrict access to EU markets for third country firms/investors;
- improve the scope and operation of the anti-market abuse framework; and
- maintain our ability to have access to certain data to support market abuse investigations.

Throughout 2012/13, we will continue to work with the Treasury and through ESMA in the negotiation of the amended directives, regulations and technical standards to implement the resulting legislation, which we expect to be required by mid-2013.

Commodities

Commodities trading markets for the world's key consumables receive considerable political attention due to the significant price volatility of these markets. We will work towards commodities markets remaining efficient and liquid, and regulators having appropriate information and powers to effectively supervise them.

In 2012/13, we have many strands to our work on commodities markets, the most significant workstreams we contribute to include:

- working with the Treasury in G20 and EU negotiations in relation to the commodities related aspects of key EU policy initiatives, Regulation on Energy Market Integrity and Transparency (REMIT) and implementing the Emissions Auctioning Directive;
- as Chair of ESMA's Commodities Task Force, advising the Commission on its legislative proposals and the development of Technical Standards;
- formulating recommendations on the oversight of oil price reporting agencies in IOSCO's Commodities Task Force; and
- thematic work on commodities market surveillance to further develop our relationships with the market.

Transparency Directive

The Commission published proposals for changes to the Transparency Directive in October 2011. The proposals will require companies trading securities on regulated markets in EU member states to publish financial information across Europe. During 2012, we will support the Treasury in the detailed negotiations that are expected to take place until Q3 2012 and we will then implement the resulting legislation. We will also provide assistance to ESMA in drafting Technical Standards as prescribed by amending the directive. We aim to improve the scope and operation of the transparency framework without imposing disproportionate burdens on market participants, and ensuring it is aligned as far as possible with the current UK super-equivalent regime.

CRA's

Due to the influence that CRA's have on market confidence, there is a need for appropriate and consistent regulation of these agencies and activities. Following the agreement of two sets of EU level legislative proposals, there is now a pan-European regime for the registration and supervision of credit rating agencies.

The Commission has published proposals for further amendments to CRA regulation, CRA 3, in November 2011. CRA 3 is focused on trying to inject more competition into the CRA markets, as well as further tightening the regulatory provisions around the rating process. In 2012/13 we will support the Treasury in their negotiations in Europe on the new regulation, with the aim of ensuring that ratings do not have a negative impact on confidence in the markets.

Corporate governance for listed issuers

The EU Commission is expected to publish proposals to strengthen some aspects of corporate governance for listed issuers. This may be done either through changes to existing directives[5] or through a stand-alone measure. We will work with other UK stakeholders, including the Department for Business, Innovation and Skills (BIS) and the Financial Reporting Council on this issue and support the Treasury in negotiations with the EU Commission, Council and Parliament. We seek to ensure that UK interests in the effectiveness of the governance regime for UK listed issuers are identified and protected. We will take an active part in the UK debate on governance issues in the context of the BIS's Kay Review.

5 e.g. Shareholder Rights Directive or the Company Law Directive.

Section

5

Delivering consumer protection

Introduction

It is our statutory objective to secure the appropriate degree of protection for UK consumers.

Delivering consumer protection includes the intensive supervision of firms and intervening earlier in the development of retail products. Within this we recognise the need to avoid or limit consumer detriment. We seek to avoid events generating consumer detriment above £250m or 50,000 people. This does not mean that we should not aim to reduce the probability of lower levels of detriment occurring, but we accept, that given our limited resources, it is inevitable that detriment to consumers will periodically occur below the £250m level.

Because the EU consumer protection regime is less well developed, we have more discretion to make our known rules in this area. However, we will seek to work within the emerging EU policy agenda and not undertake any new discretionary initiatives.

To achieve our consumer protection objective during 2012/13 we will:
- focus on achieving fair outcomes for consumers and seek to ensure that firms adhere to our conduct principles;
- deliver a forward-looking, proportionate supervisory regime through effective risk prioritisation, identification and mitigation;
- ensure an efficient redress mechanism is in place that enables the prompt provision of redress for consumers where necessary;
- continue to focus on the fitness and propriety of those taking up controlled functions and ensure new entrants have appropriate systems and governance in place;
- take tough enforcement action to deliver credible deterrence where firms or individuals fail to meet the standards expected of them;
- take forward the implementation of RDR and the consultation process to agree new policy stemming from MMR; and
- develop our consumer understanding so that we can properly take the consumer’s perspective into account while carrying out our regulatory functions.

We will also participate fully in international regulatory reform and standard-setting by engaging with global standard setters and with the European Supervisory Authorities (ESAs) and other EU institutions to influence the regulatory agenda and outcomes.

We will measure our effectiveness in delivering our consumer protection objective against the following metrics:
- analysis of mortgage indicators including arrears and repossessions;
- redress paid by firms;
- FSA consumer awareness survey; and
- complaints made to firms or the Financial Ombudsman Service.

Retail Conduct Risk Outlook (RCRO) 2012

We published the RCRO on 13 March, which set out our assessment of the 15 highest priority conduct risks that we believe require particularly careful firm and regulatory focus over the next 12-18 months. As well as setting out our highest priority retail conduct risks, the RCRO helps to inform how we set our priorities and deploy our resources.

Summary of our supervision strategy

During 2012/13 we will implement some limited changes to our supervisory conduct approach as we move to the new Financial Conduct Authority. We will start the transition to more intensive supervision where we will be forward looking, proactive and judgement based and where we will be prepared to intervene early. This will include the following.

Larger firms

- For the largest retail deposit takers, we will undertake conduct business model analysis to identify key conduct risks. We are introducing an assessment programme on a module basis focused on product design, governance, effectiveness of sales, and post-sales handling.

- Undertaking peer group business model analysis across our high-impact firm population, identifying outliers that require further supervisory attention.

- Developing integrated sector-based supervision departments. The sector risk assessment is designed to identify cross-firm and product issues that are driving poor outcomes for consumers, the degree of potential detriment involved in these issues and identify appropriate discovery or mitigation work. We expect to roll out the sector-based supervisory teams by the end of June 2012.

- Focusing on fewer key issues to ensure that we are addressing the major conduct issues affecting these firms and we will look at the areas that pose greatest risk to our statutory objectives.

- A greater expectation that firms' senior management and boards have a strategic approach to, and are engaged in, the conduct agenda.

Small firms

- The continued rollout of our revised supervisory approach for small firms. This approach will be proportionate and risk based, and will include a four-year rolling assessment programme, thematic project work and dealing with crystallised risk. The programme incorporates: workshops; face-to-face and paper-based/online reviews; and follow-up work consisting of both verification and supervision visits. For those firms that are not subject to a face-to-face review, an online review tool is being developed and we expect this to go live during the second half of 2012.

- Increased supervision of products looking at whether certain products or class of products can safely be sold to the market for which they are intended. This will involve more intensively looking at the whole product life cycle from design and manufacture to distribution, including looking at products that are designed in wholesale markets but distributed in retail markets. The result of this work could lead to product specific intervention aimed at preventing poorly designed products entering the retail marketplace.

Authorisations

We continue to encourage and provide support for new entrants to financial services through our Authorisations processes, with a view to providing greater choice for consumers and greater competition amongst existing players.

We are conscious of the balance to be struck between ensuring high standards at the gateway, and the importance of allowing innovation and appropriate levels of access for new firms. For example, there has been public debate about the potential advantages of new entrants in the area of small, regional banks focussed on servicing the small and medium enterprise (SME) sector. In such cases we will be proportionate in our approach, and would offer all firms with a viable business model and appropriate levels of resources to a pre-application meeting to help guide them through the application process.

Key policy initiatives

Redress

When financial products or services go wrong, or firms are unable to meet claims against them, consumers should receive prompt and effective redress. We will work closely with the Financial Ombudsman Service (FOS) and the Financial Services Compensation Scheme (FSCS) to take a coordinated approach to redress and ensure that emerging patterns of detriment are identified early and inform supervisory action.

In May, we will publish final proposals aimed at ensuring that consumers are aware of the extent of deposit protection. We will complete thematic work into systems changes by firms to support fast payout if a deposit taker fails. We will change elements of our compensation rules to ensure that consumers are appropriately protected and to facilitate the operation of the FSCS.

During 2012 we aim to complete our review of the FSCS's funding arrangements. Started in October 2009, the review was put on hold 12 months later due to uncertainties around the effect of UK regulatory reform on the FSCS and the ongoing development of EU directives. The review began again in October 2011 amidst high profile defaults and continuing pressure on intermediary classes. It covers the composition of the FSCS funding classes, thresholds and cross-subsidy arrangements, taking into account EU proposals to pre-fund the deposit and investment classes. We will also continue to seek redress for consumers through enforcement action.

PPI Redress

In August 2010 we published Policy Statement 10/12 – *The assessment and redress of payment protection insurance complaints* designed to improve firms' handling of PPI complaints. In April 2011 the High Court decided that the challenges to our proposals from Nemo Personal Finance Limited and the British Bankers' Association by way of judicial review, were unfounded. Our priority now is to ensure that those who were mis-sold PPI receive the redress they are due in a timely manner. We will continue to publish data on PPI redress.

In 2012/13, supervisory activity will test in detail whether firms are actually delivering good outcomes to consumers.

We will also assess how firms are complying with their root cause analysis obligations to identify any systemic issues that drive customer complaints and take proactive steps to contact those customers who may have been affected by such issues but have not yet complained. We will also continue our work with several major firms to deliver appropriate past business reviews of single premium PPI sold face-to-face with unsecured personal loans, which firms voluntarily agreed to after our mystery shopping and early supervisory work.

We are committed to working closely with consumer groups through this period to ensure that the good outcomes that we seek are delivered in practice.

Product intervention

In 2011 we published DP11/1 *Product Intervention* and FS11/3 *Product Intervention: Feedback on DP11/1*.

During 2012/13, we will continue to work on the issues highlighted in FS11/3, namely:

- considering the need for rule changes to give more certainty on our expectations of firms for product governance (i.e. when launching new products and managing them over the product life cycle);

- consulting on rules-based product intervention if we believe that such an approach may effectively mitigate identified risks, including providing necessary clarity to regulated firms;
- continuing to work with the Treasury, the Money Advice Service and firms to see how our work on product intervention can be useful to them, in particular regarding the simple products debate; and
- encouraging changes at EU level, in particular as part of MiFID II, which are consistent with our approach to product intervention.

We currently expect to consult on aspects of our product intervention approach late in 2012/13.

Retail investments

The Retail Distribution Review (RDR) Programme is due for implementation from 1 January 2013. Firms will need to:

- comply with rules designed to clarify the way they describe their services to consumers;
- address the potential for adviser remuneration to distort consumer outcomes; and
- increase the professional standards of retail investment advisers.

The RDR has now moved from its policy development phase to implementation. This means that we will design and implement processes, tools and systems that will enable us to monitor and supervise compliance by the industry with the new rules. These changes will be supported by a comprehensive stakeholder engagement strategy.

Recent research[6] suggests that the majority of individual retail investment advisers (91%) have either qualified or expect to qualify by the end-2012 deadline, so meeting a key part of our professionalism requirements. We will continue to work with accredited bodies in this area. As the end-2012 deadline approaches we may receive waiver applications from firms if they feel unable to meet the deadline. We will ensure that we have a consistent policy in dealing with these applications.

We published PS11/9 *Platforms: Delivering the RDR and other issues for platforms and nominee-related services* in autumn 2011. This made clear our intention to prevent platforms from being funded by payments from product providers and also to stop product providers paying cash rebates to consumers. We have carried out further research to examine platforms' business models, the competition implications of the changes and how consumers interact with platforms. This will inform further policy development and help us to plan a Consultation Paper on rule changes in the first quarter of 2012, with a Policy Statement to follow later in the year.

Markets in Financial Instruments Directive

The Commission's proposal for revising the Markets in Financial Instruments Directive (MiFID II) will be negotiated in 2012. Just as we have sought to tackle issues such as inducements and professionalism through the Retail Distribution Review (RDR) in the UK, we support the Commission's desire to increase consumer protection through MiFID II. We will work with the Treasury to ensure that the Directive delivers effective and proportionate measures, without undermining the RDR.

Packaged Retail Investment Products

We expect that the Commission proposals on PRIPs will be published in the first half of 2012 in multiple pieces of legislation. A regulation will set common product information standards for various different PRIPs, while selling standards akin to those in MiFID will be included in the revised Insurance Mediation Directive (IMD2). During 2012 we will work with the Commission and the ESAs to ensure a good outcome in both areas, delivering consistent investor protection.

6 www.fsa.gov.uk/pubs/other/rdr-professionalism-research-report.pdf

UCITS Directive

The Commission has proposed developing new Undertakings for Collective Investment in Transferable Securities (UCITS V) legislation as part of their work plan, with publication scheduled for the second quarter of 2012. We expect that this proposal will include material on depositary liability and UCITS managers' remuneration. These changes are likely to be based on aligning UCITS requirements with those required under the Alternative Investment Fund Managers Directive (AIFMD). The Commission has also suggested it may look to widen the scope of the proposals, including material relating to questions concerning UCITS 'eligible assets'. In the meantime, ESMA is working on guidelines relating to Exchange Traded Funds and 'complex UCITS' and will be considering further aspects of the UCITS legislation throughout the year.

Working with the Treasury, we will participate in any negotiations to revise the UCITS Directive, aiming to ensure an appropriate degree of investor protection. In ESMA we will participate actively in producing guidelines and technical standards.

Mortgages

Mortgage Market Review

In December 2011, we published CP11/31, the package of reforms proposed under the Mortgage Market Review (MMR). These aim to ensure that mortgage lenders properly check each applicant's ability to repay their mortgage and that applicants get the right information and advice at the right time during the sales process. We will continue to engage with stakeholders on these proposals, with a view to publishing the feedback statement and final rules this summer.

We do not plan to implement the proposals before summer 2013. We will have regard to market conditions and may defer implementation if necessary. If there is widespread support for particular proposals, for example in relation to mortgage arrears charges, we may implement some aspects sooner. We will start preparing for the successful implementation of the new rules this year, to ensure all firms are aware of and understand the new requirements. We will monitor and take appropriate action in response to any risks we see emerging in the lead-up to implementing the MMR reforms. There will also be changes required to the regulatory reporting requirements in light of the MMR proposals and we will consult on those.

Further mortgage policy reviews

We will review our regulatory approach to Third Party Administrators in the mortgage market. This was announced in the MMR Discussion Paper (DP09/3) and when we complete that work we will publish our wider conclusions and proposals. We will also develop our review of charging practices. MMR work focused on arrears charges, but this wider review will explore whether other charges are fair and fit within our current regulatory requirements.

Mortgage Credit Directive

Consideration of the European Commission's proposal for a directive on mortgage credit is continuing in both the Council of Ministers and in the European Parliament. We will continue to support the government in the negotiations and to help formulate and press the UK position on this proposed directive. If it is agreed before the end of the year, we will begin transposition.

Insurance

Solvency II

We will continue to reform our conduct regulations, where necessary, to implement the requirements of the Solvency II Directive while maintaining appropriate levels of consumer protection. The bulk of this work is expected to be in relation to our rules on permitted links (COBS 21) and on with-profits (COBS 20), with the revised rules intended to be included in the Handbook at the start of 2013. Some aspects are dependent on the completion of work currently being carried out by EIOPA.

Insurance Mediation Directive

The Commission is reviewing the Insurance Mediation Directive (IMD) with an updated proposal expected in the first half of 2012 (IMD2). Once the new text has been adopted we will need to amend the relevant sections of the Handbook. We are committed to supporting the Treasury in its negotiations of the directive so that IMD2 does not present significant implementation challenges for our existing regime, but extends extra protections to consumers as appropriate. As noted earlier, we will continue to press for consistent standards between investment products (PRIPs) subject to MiFID2 and those covered by IMD2.

Referral fees

The government has introduced legislation to ban the payment of referral fees in personal injury cases, through the Legal Aid, Sentencing and Punishment of Offenders Bill, which is currently being considered by Parliament. The Treasury will make regulations to set out our role in ensuring the compliance of regulated firms with the requirements of the new law. We will work closely with the government, other regulators and industry representatives during the implementation stage.

Low value General Insurance

We have identified risks with General Insurance products that offer poor value for customers who have little prospect of claiming and deficiencies in sales practices of these products. They are generally sold as an add-on to other products and often represent poor value in that they replicate other existing rights or free services.

We are committed in 2012/13 to identify these sales and stop them plus deliver redress where appropriate. We will take action against firms that sell products of poor value and mis-sell the products to their customers.

With-profits review

We will continue to engage with firms as necessary to establish that with-profits policyholders and members are treated fairly. We will ensure that firms meet their contractual obligations and manage any conflicts of interest within their with-profits funds appropriately.

Credible deterrence

To further our credible deterrence agenda, specific areas that Enforcement will focus on in 2012/13 will include the fair treatment of customers, insurance fraud, mortgage fraud and the mis-selling of complicated products such as unregulated collective investment schemes. As part of our efforts to address systemic problems across the industry, we will also continue to focus on bringing action where firms breach our client money rules and put consumers' money at risk.

Protecting consumers who are targeted by unauthorised investment businesses, including through share frauds, landbanking and 'get-rich-quick' investment scams will continue to be a high priority and we will bring further criminal and civil proceedings where appropriate.

We will continue to provide guidance to consumers on how to recognise and reduce the risk of falling victim to investment scams

We will increasingly take action in cases where there is a risk of consumer detriment, even if there has been no actual harm to consumers, if we consider it necessary to prevent actual detriment occurring.

Other policy initiatives

Alternative Investment Fund Managers Directive (AIFMD)

Member States are required to implement AIFMD by 2013, so we will be consulting on UK implementing measures, including changes to FSA rules, during the course of 2012. In addition to the 'level 1' Directive, a significant amount of additional material, based on ESMA advice to the Commission, will be adopted by the EU legislators and may also need to be implemented. We will also work within ESMA on a variety of other areas related to AIFMD, such as leverage calculation, remuneration guidelines and relations with third countries.

Payment services and electronic money

The Commission is due to review the closely related Payment Services Directive and second Electronic Money Directive by November 2012. We will take an active role in contributing to this work, taking into account our experience of implementing and supervising these directives.

Compensation and dispute resolution directives

Negotiation on the Deposit Guarantee Scheme Directive is in its final stages. If it is agreed, we will focus on its implementation in 2012. We will work actively to influence any development of standards by the European Banking Authority.

We will continue to support the Treasury in influencing amendments to the Investor Compensation Schemes Directive to ensure that the level of protection for UK consumers is maintained and that funding arrangements are proportionate and practicable. Subject to the EU timetable, we may also consult on implementing the directive in 2012.

The Commission has published proposals for alternative ('out of court') dispute resolution procedures. We will contribute to the development of the UK's response to ensure that the scope of protection the FOS provides to financial services consumers is maintained.

Consumer engagement

In 2011, we established the Consumer Affairs function, who are responsible for further development of our consumer engagement strategy. During 2012/13 we will be focused on developing the consumer agenda by:

- ensuring we are more outward looking and engaged with consumer representative bodies across the UK;
- ensuring that consumer principles are embedded in our culture and decision-making, through enhancements to training to match the processes staff use as part of their everyday work;
- ensuring interaction with consumers is consistent, transparent and appropriate, by developing a more coordinated system of two-way communication between us and consumers, as well as with the Money Advice Service, FOS, FSCS; and
- developing a consumer intelligence capability to gain increased levels of information from a range of sources, including from external consumer bodies, commissioned and existing consumer research, social media and the financial press, which can be used to inform decisions to intervene earlier and more proactively.

Oversight of the Financial Ombudsman Service (FOS), Financial Services Compensation Scheme (FSCS) and the Money Advice Service (MAS)

We have a statutory responsibility for overseeing FOS, FSCS and MAS. All three organisations play a vital role in delivering consumer protection.

The FSA have several responsibilities regarding FOS, FSCS and MAS, including:

- the appointment and removal of the Board (with approval of the Treasury in the case of the chair or chief executive);
- approving the annual budget (in the case of the FSCS approving the management expenses limit);
- approving the annual business plan (in the case of FOS and FSCS consultation during preparation of their annual business plan);
- receiving an annual report in relation to the discharge of their function; and
- in the case of MAS, if the FSA considers it appropriate, the appointment of an independent person to conduct reviews into the economy, efficiency and effectiveness of the use of resources when carrying out their statutory function.

While respecting the independence of FOS, FSCS and MAS in carrying out their statutory function, we have arrangements in place to enable us to monitor the activities of FOS, FSCS and MAS, to ensure each body is capable of exercising their statutory function and enabling the FSA to properly discharge its responsibilities, and we will continue to monitor them to ensure they are fair and proportionate.

We have a programme of regular engagement with FOS, FSCS and MAS, shaping and influencing the relationships to deliver effective consumer outcomes across the shared agenda. We recognise that close cooperation, assistance and communication are essential in the interests of both consumers and the financial services industry.

The FSA remains committed to ensuring the standards of oversight across FOS, FSCS and MAS. In the future regulatory structure, oversight of the FSCS will be assumed jointly with the PRA.

Section

6

Financial crime

Introduction

Credible deterrence and enforcement are at the centre of our strategic objective to reduce financial crime. In 2012/13, we will focus on:

- keeping those who lack integrity out of the financial services industry by imposing tough standards at the point of approval and authorisation;
- warning and educating investors about the dangers they may face from unauthorised business; and
- ensuring that the regulated community has effective systems and controls in place to prevent financial crime.

Our key priorities for 2012/2013 are:

- continuing with our credible deterrence strategy by taking action against those that do not meet our standards;
- encouraging effective systems and controls to prevent financial crime;
- embedding judgement based, intensive and intrusive supervision through thematic reviews and trialling new supervisory models; and
- working with domestic and international partners to influence international standards and increase intelligence sharing.

Systems and controls effectiveness

We will also participate fully in international regulatory reform and standard-setting by engaging with global standard setters and with the European Supervisory Authorities (ESAs) and other EU institutions to influence the regulatory agenda and outcomes.

In the first half of 2012 we will publish two thematic reports: one on anti-bribery and corruption systems and controls in investment banks; and one on banks' defences, systems and controls, against unauthorised businesses. These reports will be included into updated versions of *Financial Crime: a guide for firms*.

We will address financial crime systems and controls issues through our intensive, intrusive supervision of regulated firms, with support from our financial crime and intelligence specialists to ensure that these defences are effective. If firms fail to put safeguards in place to prevent financial crime, we will take robust action, including enforcement action.

Following our anti-money laundering thematic review, *Banks' management of high money laundering risk situations*, published in June 2011, a number of banks were referred for formal investigation to Enforcement that may conclude in 2012. We believe the results of these actions will act as a deterrent to other firms, but we will also continue to conduct visits and engage institutions on anti-money laundering issues during the year.

In 2012, we will trial the Core Financial Crime Programme (CFCP), a new programme of intensive, intrusive supervision to identify money laundering, financial sanctions and terrorist financing risks in the largest banks. We will evaluate the findings from the pilot in mid-2012, when we will decide whether to roll out the programme alongside other financial crime supervision work.

Stakeholder engagement

During 2012/13, we aim to engage with domestic and international policy makers to embed an effective risk-based approach in international anti-money laundering and counter terrorist financing standards.

We will be focused on the European Commission's review of the third Money Laundering Directive, the Financial Action Task Force (FATF)'s revision of its standards and its move towards effective testing of national, legal and regulatory frameworks, and the European Supervisory Authorities (ESAs) work to address European anti-money laundering issues.

Intelligence

We will dedicate resources to maintaining and developing our domestic and international intelligence sources and networks. The intelligence obtained from these gateways is important for enriching our understanding of financial crime risks, assisting our processes and supporting decision-making at the FSA. The information and intelligence collected, shared and used, helps with our enforcement, supervision and authorisation work.

We will continue to collaborate with our law enforcement partners in pursuit of good criminal justice outcomes, as well as crime prevention and disruption.

Section 7

Delivering the FSA's operational platform

Introduction

An effective and efficient operational platform is critical in supporting delivery of our statutory objectives. It will also be key to ensuring a smooth transition to the successor organisations. Many elements of our operations will be inherited by the FCA and will support the delivery of its new approach to regulation.

This section outlines our commitment to:

- ensuring we have the right people and skills required to achieve our objectives;
- investing in our infrastructure;
- delivering the operational changes required for a safe and smooth transition to the new regulatory structure; and
- running our organisation as efficiently and cost effectively as possible.

Our people

Attracting and retaining top talent is essential for us during this time of significant change and we will continue to work to achieve this, enhancing capability for the future.

Our Senior Leadership Team will ensure that our staff have the necessary capability at legal cutover for both regulatory authorities. The approach will be to use the existing FSA performance management framework, together with our training and competency programmes. We will place strong emphasis on developing our leadership capabilities, strengthening our core technical competencies through recruiting, developing and engaging our staff. This will include further developing the skills and knowledge needed for effective supervisors.

We will ensure effective data and knowledge transfer to the PRA and FCA, including determining which roles will transfer to either regulator or to the Bank of England.

Diversity and equal opportunities are important to us as an employer and a regulator and we will continually strive to improve our approaches to this end.

IS investment and transition

A significant investment in our IS systems and capability, over a number of years, is required to ensure that core technology platforms remain supported and able to underpin our key regulatory systems that will be inherited by the FCA. Parts of our IS estate that are currently out-dated need to be modernised and key equipment that has reached the end of its life needs to be upgraded. In conjunction with this, we need to plan for the retendering of our outsourced IS services and, as we move towards the new regulatory system, to develop and design future FCA regulatory systems.

Initial investment over the next year will focus on:

- stabilising and enhancing the platform used to analyse data and produce reports for supervisors;

- starting the process of retendering our outsourced IS services;
- building on progress already made to refresh and stabilise IS systems by completing upgrades of key applications;
- continuing to enhance our IS capability to deliver new and maintain existing systems, by investing in IS tools and methodologies;
- continuing to ensure we retain IS knowledge and reduce our reliance on contractors, building on progress made over the last year; and
- starting the development process for future regulatory systems needed to support the work of the FCA.

This work will not only benefit the FSA but will build the IS development and delivery capabilities needed to provide effective support to the FCA and initially the PRA/Bank of England.

In addition to this investment we will also focus on implementing the changes required to allow relevant systems to be duplicated or migrated to the FCA, PRA or Bank of England, as well as designing and agreeing effective shared services (e.g. certain IS services or processes). We are working closely with counterparts at the Bank of England to ensure we achieve the most cost effective outcomes.

Accommodation

To support our restructure we will need to review and make changes to our accommodation provision.

We will assist the Bank of England with its activities to relocate the PRA to its City location and will reconfigure and restack accommodation for the FCA within the existing FSA estate. We will also continue our work to determine the longer term FCA accommodation strategy.

Olympics business continuity planning

We will ensure that appropriate plans and arrangements are in place to mitigate the risks to our business operations during the Olympic period. This will enable us to remain operational for the duration of the Olympic and Paralympic Games, ensuring we have sufficient staff with access to appropriate resources needed to maintain key activities and to manage the response to any disruption caused during the period.

Section 8

Budget for 2012/13

Introduction

The budget of 2012/13 has been set so we can meet our statutory objectives and deliver on the commitments we have made, using our resources effectively and efficiently. It is shaped by our assessment of the risks posed to our statutory objectives and reflects the risk appetite we have set for different aspects of our work.

We will maintain our delivery of intensive supervision, supported by our philosophy of credible deterrence and our significant profile in Europe and internationally. Internally we continue to maintain our investment in providing an operational platform that is better able to support the needs of our business.

This section explains our budget and funding needs under three headings:
- ongoing regulatory activity (ORA);
- capital expenditure; and
- annual funding requirement (AFR).

In April 2011 we realigned the internal management structure to effect a smooth transition to the Prudential Regulation Authority (PRA) and Financial Conduct Authority (FCA). The Risk and Supervision Business Units were collectively restructured to become the Prudential and Conduct Business Units. We have restated the 2011/12 comparatives accordingly to reflect this and made associated adjustments.

The 2012/13 budget reflects a further separation of supervisory activities as part of internal twin peaks ahead of the legal cutover. This results in staff and associated costs being transferred mainly from the Prudential to the Conduct Business Unit when comparing year-on-year budgets. We have not restated 2011/12 comparatives to take this into account, but the effect is detailed in the following analysis.

Ongoing Regulatory Activity (ORA)

Our budget for 2012/13 is £543.5m, reflecting an increase of £51.5m (10%) compared with the equivalent 2011/12 budget of £492.0m. The increase in budget is because of: a budgeted pay increase of 3.5%[7]; increased depreciation charges resulting from completing key projects associated with maintaining and developing our technology platform; and implementing mandated EU directives. The budgeted pay increase follows a two-year freeze on pay and will be used in a targeted manner. £22.4m (4%) of the ORA budget reflects our commitment to modernise our IT infrastructure to create a suitable platform for the FCA. The rest of the cost base increase mainly reflects an inflationary uplift.

7 Approach to pay is to consider individual skills, experience and contribution and not to award ‘across the board’ increases.

Last year we said we would maintain our headcount at 4,000 FTE until legal cutover. The 2012/13 Budget is based on a headcount of 3,992 FTE as we seek to stabilise headcount in line with our stated objectives.

Cost by business unit

We have set out the planned ORA costs for our business units in Table 8.1, broken down further in Chart 8.2. These figures include specific elements of our operations costs (regular IT costs and other overheads) distributed to the business units based on the number of staff in each unit. This is consistent with our approach in previous years. The costs of Solvency II are not included in this analysis as we recover these costs through a Special Project Fee (SPF).

The Conduct Business Unit budget increase of £36.3m (25%) reflects the movement of staff from the PBU and the annual costs of additional staff hired during 2011/12 to deliver our intensive and intrusive supervisory approach in preparation for the new firm-specific financial regulation regime in the UK. The increased size of the Conduct Business Unit compared to the Prudential Business Unit has resulted in it attracting a greater share of overhead, which has contributed significantly to the increase in its budgeted costs relative to the reduction in PBU.

The Prudential Business Unit budget decrease of £16.5m (10%) reflects the movement of staff into the Conduct Business Unit, while ensuring that the FSA continues to contribute to the protection and enhancement of the stability of the UK financial system.

The £14.8m (33%) budget increase in the Operations Business Unit is mainly due to additional depreciation costs associated with completing key IT projects.

The £12.4m (15%) increase in Central Services is due to an increase in our CEO contingency by £10m to 2.8% of our ORA. The increase recognises that we are undergoing a period of intense change, both internally and in the external environment, and will allow us to remain flexible enough to respond to key challenges that will arise during the year.

Historic comparison of fees by size of firms

In this section we show in more detail how fees are levied by firm and how this has changed. Over time there has been an increase in the proportion of fees paid by the largest firms, shown in Charts 8.3 to 8.5.[8] Between 2008/9 and 2012/13, the top ten firms by size will have seen the proportion of FSA fees they pay increase from 17% to 31%, and the top 100 saw an increase from 24% to 29%. Firms outside the top 100 have generally seen a reduction in the proportion of total FSA fees that they pay.

Chart 8.6 shows that the increase on FSA fees has been predominantly absorbed by larger

Table 8.1: Expenditure by business unit

	12-13 Budget £m	11-12 Budget £m	Change £m	Change %
Conduct	183.8	147.6	36.3	25%
Prudential	156.9	173.4	(16.5)	(10%)
Operations	60.1	45.3	14.8	33%
Other Central Services*	97.5	85.1	12.4	15%
Enforcement & Financial Crime	72.9	68.0	4.8	8%
Sundry Income	(27.7)	(27.4)	(0.3)	1%
Total ORA	543.5	492.0	51.5	10%

*Other Central Services comprises Chairman's and CEO's Offices (including Corporate Services area, Specialist Supervision Unit and Strategy, Planning and Performance), General Counsel's Division, Risk & Financial Stability Division, Communications and Internal Audit. Conduct Business Unit includes the Markets division which has a gross cost budget of £41.4m in 2012/13 (£36.8m in 2011/12). On Chart 8.2, within Central Services we have broken out figures for the Risk and Financial Stability and General Counsel Divisions (covering regulatory legal services).

8 The percentages in Charts 8.4 and 8.5 do not add up to 100%. This is due to rounding.

Chart 8.2: Breakdown of gross costs by business unit

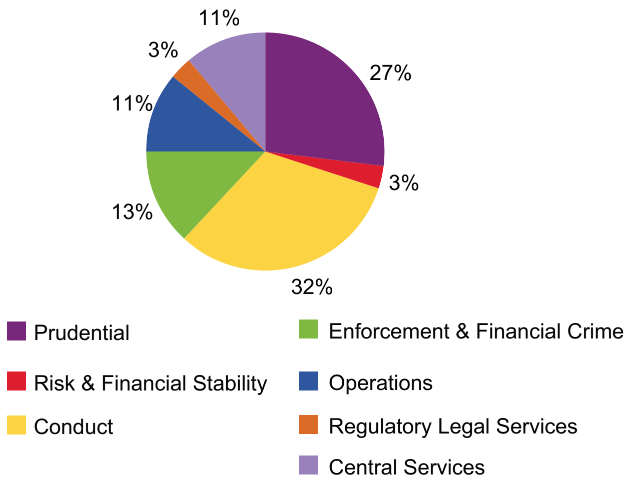


Chart 8.3: Proportion of fees by size of firm – 2012/13

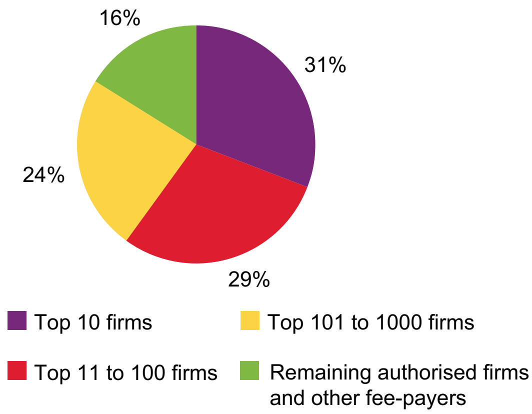


Chart 8.4: Proportion of fees by size of firm – 2010/11

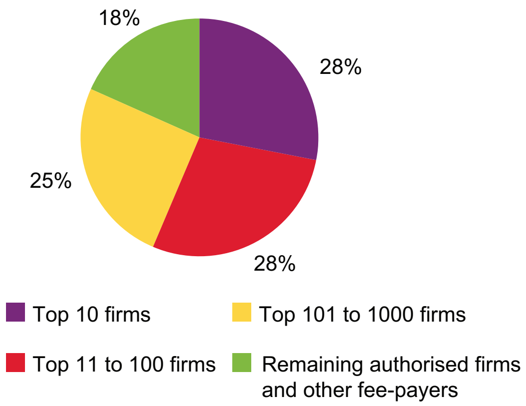


Chart 8.5: Proportion of fees by size of firm – 2008/09

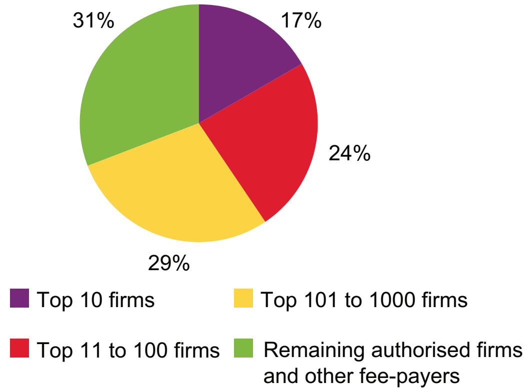
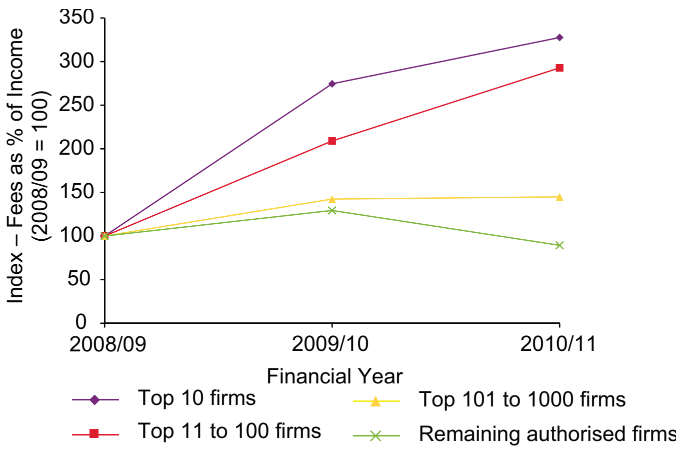


Chart 8.6: Index of Fees as % of income 2008/09 – 2010/11[9]



9 Due to various factors, information held in the FSA on firms' revenues is not comprehensive. Where we did not have income information for a firm, the fees paid by such firm were excluded from the analysis, i.e. the analysis includes fees for firms with income information only. The analysis for 2008/09 is based on 94% of AFR paid by Authorised firms. The analysis for 2009/10 is based on 95% of AFR paid by Authorised firms. The analysis for 2010/11 is based on 94% of AFR paid by Authorised firms. It should also be noted that income is used as a proxy and not all firms' fees are levied on the basis of income.

Table 8.7: Expenditure by type

	12-13 Budget £m	11-12 Budget £m	Change £m	Change %
Staff Costs (incl. Travel, Training, Recruitment & Pension scheme deficit contributions)	371.8	359.5	12.3	3%
Accommodation and Office Services & Depreciation	82.5	65.9	16.6	25%
IT Costs (including IT delivery outsourcing)	73.9	57.9	16.0	28%
Professional Fees	22.6	23.3	(0.7)	(3%)
Other	20.4	12.8	7.6	59%
Sundry Income	(27.7)	(27.4)	(0.3)	1%
Total Income & Expense by Account Type	543.5	492.0	51.5	10%

firms, with the top 100 firms seeing their fees triple as a proportion of revenues between 2008/9 and 2010/11. By comparison firms outside of the 1000 largest have seen fees as a proportion of revenues generally remain static. Please note that 2011/12 data is not available yet, as income figures for some firms have not been produced due to the timing of their financial year-ends.

Cost by type of expenditure

We have set out the planned ORA costs for each type of expenditure in Table 8.7. Budgeted staff costs have increased by £12.3m (3%), which mainly reflects the budgeted general pay increase of 3.5% in 2012/13. Following a two-year salary freeze this reflects a provision to award our staff salary increases up to a maximum of 3.5% of our total payroll. These awards will not be universally applied, but will be targeted to ensure that we incentivise and retain those people whose skills, experience and contribution justify an award.

Accommodation, office services and depreciation cost increase of £16.6m (25%) reflects higher depreciation charges as a result of completing key projects (e.g. Knowledge Infrastructure, SABRE). Our accommodation and office services costs are budgeted to remain stable as we will not be increasing our office space in 2012/13.

IT costs have increased by £16m (28%) as we continue to invest in our technical infrastructure to help meet our statutory objectives. Key elements of the increase are:

- the costs of supporting new business applications implemented in 2011/12 and 2012/13; and
- the cost of modernising our IT infrastructure and IS capability.

Professional fees reflect the external consultancy costs required to secure specific expertise which is not available internally, and should reduce moderately in 2012/13.

Because of a change in budget definitions we have restated the professional fees and IT cost comparatives for 2011/12 to ensure consistency.

Other costs have increased by £7.6m (59%) mainly due to the increase of our CEO contingency fund (2.8% of ORA).

Reducing the deficit in our final salary pension fund

We maintain our commitment to reducing the deficit in our final salary pension fund, which was closed to future accruals from 1 April 2010.

We regularly monitor the funding level of the pension fund and make decisions about the long-term nature of the liabilities and the long-term period over which the pension assets will be held. The last three-yearly scheme specific valuation (SSV) took place on 31 March 2010 and helped form the basis of the new recovery

Chart 8.8: Breakdown of gross costs by account type

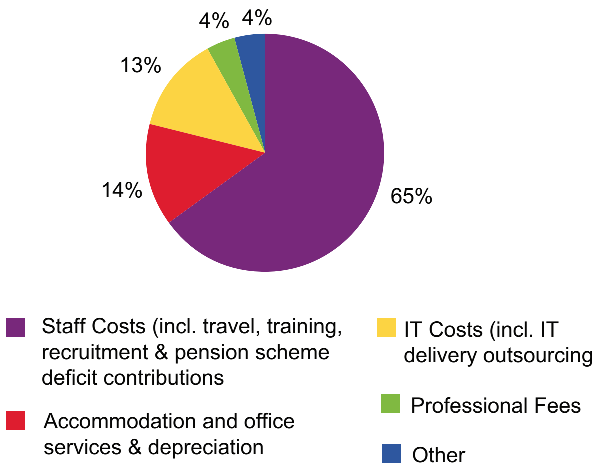


Table 8.9: Capital expenditure

	12-13 Budget £m	11-12 Budget £m	Change £m	Change %
IT Development	26.4	32.2	(5.8)	(18%)
IT Infrastructure	10.8	14.5	(3.7)	(26%)
Accommodation	1.0	0.9	0.1	11%
Total ORA Capital	38.2	47.6	(9.4)	(20%)
Solvency II	8.6	9.4	(0.9)	10%
Total Capital	46.8	57.0	(10.3)	(18%)

plan. In 2012/13 we plan to maintain our total contribution at £19.5m.

Solvency II

Outside our AFR we expect to recover the costs relating to Solvency II from affected firms through an SPF. We currently anticipate that the Solvency II costs will be between £100m and £150m, with an SPF of £25.9m in 2012/13.

Capital expenditure

We are reducing our capital expenditure by 18% from £57m to £46.8m in 2012/13, as shown in Table 8.9. The main reasons for this reduction are the year-on-year movements in the capital requirements of key projects as they move through their project lifecycle and the changing mix of projects within the portfolio.

Annual Funding Requirement (AFR)

In early February, we published our annual fee rates in CP12/3, *Regulatory fees and levies – rates proposals 2012/13*. This followed our annual fees policy CP11/21, *Regulatory Fees and levies policy proposals for 2012/13*, which was published in October 2011.

The total amount required to fund our budgeted costs for 2012/13, as set out in Table 8.10, is £578.4m. This is an increase of 15.6% on the equivalent AFR of £500.5m for 2011/12, This increase reflects the following:

- ORA Budget: An increase of £51.5m (10%). This includes provisions for staff salary increases up to a maximum of 3.5% of total payroll and an additional £22.4m investment in key technology platforms.

Table 8.10: Annual Funding Requirement (AFR)

	12-13 Budget £m	11-12 Budget £m	Change £m	Change %
Budget for ORA	543.5	492.0	51.5	10%
Movement in reserves	0.0	(9.0)	9.0	(100%)
Funding for regulatory reform implementation	32.5	10.9	21.6	198%
Funding the transition to more outcomes-focused regulation	0.0	5.0	(5.0)	(100%)
Recovery of scope change activities	2.4	1.6	0.8	50%
Annual Funding Requirement (AFR)	578.4	500.5	77.9	16%

- Regulatory Reform Programme: An increase of £21.6m (198%) as activity intensifies ahead of the transition to a new legal structure.

- Recovery of scope change costs: An increase of £0.8m (50%). This year we plan to collect £2.4m, mainly due to the final collection for implementing the new regulatory framework applying to credit unions in Northern Ireland.

- Movement in reserves: Any under-spend in 2011/12 it is not expected to be significant, in contrast to last year.

- Transition funding: The Making a Real Difference (MaRD) programme finished in March 2010 and final costs were recovered last year.

Applying financial penalties

Under the Financial Services and Markets Act 2000 (FSMA) we are required to ensure that financial penalties are applied for the benefit of authorised persons. The benefit is applied through discounts to our fees for firms in the 'A' fee-blocks and operators of multi-lateral trading facilities (MTFs) in fee-block B.

The financial penalty discount is applied in the following order:

- firstly, it is allocated to the fee-block(s) paying the enforcement costs of the specific closed cases that gave rise to the penalties, to meet the costs of enforcement action in full, where possible;

- secondly, any remaining money is distributed across fee-blocks to meet the costs of enforcement cases that closed during the year without leading to penalties;

- thirdly, any remaining money is distributed across fee-blocks in proportion to the projected costs of enforcement for the coming year; and

- finally, if any money remains from penalties after all the enforcement costs have been met, it is applied to all authorised firms and MTFs, in proportion to their respective contributions to our AFR.

These distributions are applied in the financial year after we receive the penalty money. If at any stage in this process applying the money from penalties would exceed the total AFR for any particular fee-block, the surplus is returned to the total remaining penalty pot and applied to the other fee-blocks in the same order.

An individual authorised firm should not benefit from deductions generated by a penalty we have imposed on it. We therefore invoice the firm to recover the value of the deduction, provided it exceeds £250.

Financial penalties from enforcement action in 2011/12 are forecast to be lower than in 2010/11. In the 2010/11 financial year these financial penalties were worth £86.2m, equating to a reduction of approximately 16.8% across the fee-blocks for 2011/12 fees. In CP12/3 our forecast of the financial penalties we will receive by the end of March 2012 was £58.7m. This forecast figure is 31.9% lower than last year.

Taking into account the overall affect of the lower anticipated financial penalties discounts, this equates to an increase in chargeable fees of 25.4% for 2012/13 (decrease of 1.7% in 2011/12). We will confirm the final 2012/13 financial penalty discounts to fees in our consolidated Policy Statement, published in May 2012.

Financial management and reporting framework

The scope of activities that fall within our remit is wide and varied. This includes some activities that are intended to be temporary and/or are subject to considerable variation from year to year. We cannot forecast these with the same reliability as regular recurring activities. We will continue to:

- exert sound financial management and budgetary control over all areas of our expenditure and income; and
- seek to manage any unavoidable volatility to minimise the effect on fee payers from year to year.

Our Board believes it is helpful to have a framework within which to manage and report on our costs and funding. So we have identified the following 'streams' of activities, which have distinct cost and funding characteristics.

Ongoing regulatory activity (ORA)

This includes our core operating activities, managed year-on-year as part of our budget process. The ORA is the key figure, along with the explanation for any material movements, which shows how we have met our obligation to be economic and efficient in using our resources.

Changes in scope (increase or decrease)

Sometimes the Treasury legislates to change the scope of activities that we regulate. Any scope changes, as with our other core operating activities, are subject to financial management as part of our budget process. However, until the supervisory process is established, material activities resulting from a scope change are controlled separately so they are individually identifiable. When the supervisory requirements of the scope change have been introduced, we include these activities as an integrated part of our ORA for the following year.

Exceptional items

We have included these costs in the ORA and we will report on material movements each year.

External enforcement costs

Total enforcement costs depend on the number of cases and their complexity. We will continue to manage these costs in total and try to optimise the mix of internal and external enforcement resources when we do this. We have included these costs within the ORA and we will report on any material movements each year.

While we will maintain strong financial management of these costs, the actual amounts may be materially higher or lower than the budgeted level set before the financial year. If this happens, we will review any excess or reduction in costs from the budgeted level and, if appropriate, we will phase the impact on fee payers over a period, as long as we are able to maintain satisfactory reserves.

Panel costs

The Financial Services Consumer Panel and the Practitioner Panel have a status under Financial Services and Markets Act 2000 (FSMA) that guarantees their independence from the FSA. These panels, and the

Smaller Businesses Practitioner Panel, manage their own costs against budgets. They are, however, subject to our approval and are funded through our fees. We have included these costs within our ORA.

Complaints Commissioner

FSMA requires us to have arrangements in place to investigate complaints against us. On 3 September 2001 we introduced our Complaints Scheme to do this. FSMA requires us to ensure the Complaints Commissioner can conduct a full investigation into any complaints. The Complaints Commissioner manages their own costs against their budget, which is subject to our approval and is funded through our fees. These costs are included within our ORA.

Pension scheme deficit reduction

The amounts required to fund our pension liabilities over time are inherently variable, and depend on several variable factors, including current investment values and projected investment return. We intend to eliminate our current deficit over a ten-year period.

Revolving credit facilities

We have two revolving credit facilities, one with Lloyds Banking Group and the other with HSBC for £75m each, to finance the costs of delivering more outcomes-based regulation, overhauling our IT delivery and technical infrastructure and funding our commitments to our final salary pension scheme.

Depending on the timing of our fee collection cycle, there will be times when we may use the borrowing facility to fund such expenditure and other times when we will have surplus funds available for investment. If we use either of our credit facilities, we will repay any borrowings and financing costs incurred using funds we raise as part of the AFR. These credit facilities allow us to manage any volatility in the level and or collection profile of our fees.

In line with our Funding Policy, we maintain the equivalent value of six weeks of our ORA as immediately-available liquid funds. We anticipate that we will have sufficient financial capacity within the revolving credit facilities to meet any expenditure required to address unforeseen events. We plan to keep our reserves at -2% to 2% of ORA.

Appendices

Contents

Appendix 1
FSA independent panels – strategies for 2012

We receive advice and guidance on our policies from three independent Panels – the Financial Services Consumer Panel (FSCP), Financial Services Practitioner Panel (FSPP) and the Smaller Businesses Practitioner Panel (SBPP).

The Panels each develop their own strategic plans to enable them to set their own agendas, as well as responding to the priorities of the FSA.

These plans are reviewed annually in the summer to ensure they are updated and reflect changing events. This section highlights the key points as at the beginning of 2012.

Financial Services Consumer Panel (FSCP)

The FSCP's mission statement is:
'To help to bring about an open, fair, competitive and well-regulated market in which consumers can make good choices, with confidence, from a range of products and services that offer real value to consumers, and to make sure that the interests of consumers are fully taken into account by the FSA and other appropriate audiences.'

With the backdrop of changing market conditions and regulatory transformation, the Panel's primary role over the next three years will be to influence how the consumer interest is upheld, and is fundamental, in financial services regulation.

The FSCP currently has six key priorities:

- the shape of future UK regulation;
- EU Regulatory and legislative issues – influencing the development of EU policy to take account of the interests of EU consumers;
- the future regulation of consumer credit;
- the Mortgage Market Review;
- the advice gap; and
- the effective regulation of business conduct.

The Panel will be working closely with the FSA during 2011/12 on each of these priorities to pursue the best possible consumer outcomes.

Financial Services Practitioner Panel (FSPP)

The FSPP aims to provide early and effective practitioner input into our policy development. Its priorities in 2012 will continue to focus on the areas of regulatory change that have the greatest effect on financial services firms. This particularly guides the first two of the Panel's four priorities as follows:

Restructuring UK regulation – the Panel will continue to engage actively in the debate on the Financial Services Bill and in discussions with the FSA and the Bank of England on plans for the FCA, PRA and FPC.

EU and international regulatory developments – the Panel is committed to working more effectively to ensure the voice of UK practitioners is heard and considered in the discussions that decide the direction of regulatory policies before they reach the UK, by increasing its engagement, particularly on EU issues during 2012.

UK competitiveness – the Panel will continue to highlight the importance of maintaining UK competitiveness in financial services at a time of significant increase in regulations and will look to identify and highlight to regulators and the government when UK competitiveness is threatened or where greater proportionality is needed.

FSA business as usual – the Panel will continue to engage actively in debate with the FSA on its business plan and budget, and major UK regulatory initiatives, such as the Retail Distribution Review, the Mortgage Market Review, Recovery and Resolution plans and implementation of Independent Commission on Banking (ICB) proposals, as well as policy and funding needs for the Money Advice Service and FSCS.

Smaller Businesses Practitioner Panel (SBPP)

The SBPP's overall objective continues to be to work to ensure the regulatory environment enables smaller firms to be commercially viable and to flourish, so contributing to the wider economy and providing a broader choice and access for consumers.

The SBPP's key priorities for 2012 are as follows:

1) Restructuring UK regulation – pressing for consideration of smaller firm needs across the planned sector-based structures in the PRA and the FCA, with diversity and proportionality in both regulators' activities.

2) Minimising the cost and burden of regulation for smaller firms – helping to make the FSA budget process more transparent, and developing the concept of cost equality in the split to two regulators.

3) Providing a smaller firms' voice in major UK regulatory developments – particularly looking at the Retail Distribution Review and clarifying policies towards simplified advice and platforms, the implementation of Solvency II and the development of product intervention.

4) Highlighting smaller firms' concerns in EU initiatives – working on getting the smaller firm voice heard within the EU debates, and that any additional UK requirements on EU initiatives are properly justified for smaller firms.

5) Suggesting improvements for FSA smaller firms supervision – working to assist the FSA in improving communications with small firms and in planning for future supervision of smaller firms in the new regulatory structure.

Appendix 2

The Board of the Financial Services Authority at 31 March 2012

Adair Turner	Chairman, the FSA
Hector Sants	Chief Executive, the FSA
Martin Wheatley	Managing Director, Conduct Business Unit, the FSA
Amanda Davidson	Director, Baigrie Davies Governor, Channing School
Sandra Dawson	Director, Judge Business School, University of Cambridge Deputy Vice Chancellor, University of Cambridge Master, Sidney Sussex College Chair, Executive Steering Committee, ESRC Advanced Institute of Management Non-executive Director, Data and Research Services plc Non-executive member, Oxfam Member, The Aga Khan University Advisory Group to establish a new Business School Member, Social Science Research Council, USA Member, Advisory Board, UK Indian Business Council Member, The UK-India Round Table Member, Potanin Foundation Board of Advisers
Peter Fisher	Senior Managing Director, BlackRock Inc
Brian Flanagan	Non-executive director, Bettys and Taylors of Harrogate Adviser, Jet Environmental Ltd
Karin Forseke	Chairman, Alliance Trust Non-executive Director, Royal Opera in Stockholm Non-executive Director, Wallenius Lines Non-executive Director, Eniro AB Board and Council Member, European Council on Foreign Relations (ECFR)
Mick McAteer	Founder and Director, The Financial Inclusion Centre Chairman, the European Commissions Financial Services User Group (FSUG) Board member, The Financial Reporting Council's Professional Oversight Board Board member, CARITAS (Westminster) Advisory Board

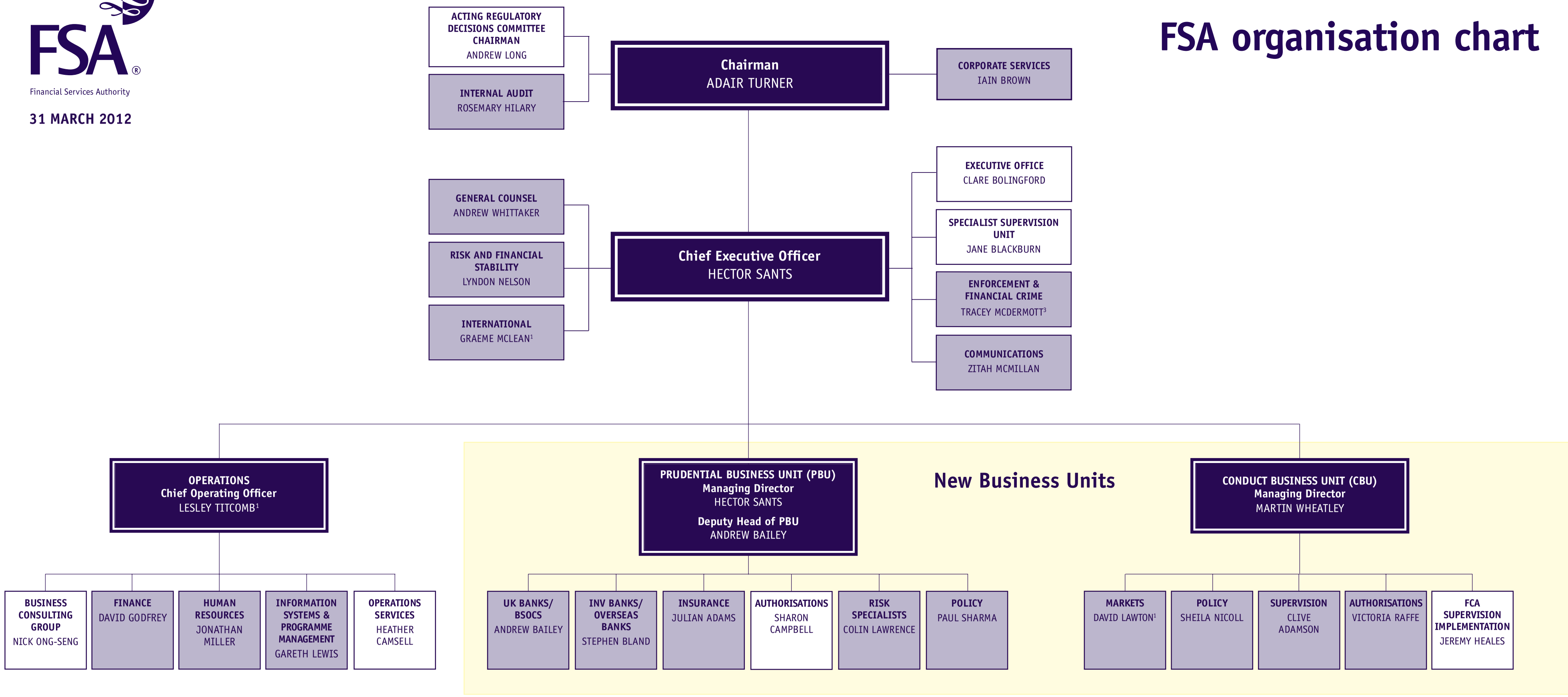
Brian Pomeroy	Chairman, Responsible Gambling Stretegy Board Chairman, The FSA Pension Plan Trustee Ltd Chairman, the Photographer's Gallery Deputy Chairman, QBE Insurance Europe Ltd and QBE Underwriting Ltd Member, Financial Reporting Review Panel Director, The Social Market Foundation
Andrew Scott	Non-executive director, Global Economics Ltd Professor of Economics and Deputy Dean, London Business School Fellow, Centre of Economic Policy Research Scientific Chair, the Euro Area Business Cycle Network
James Strachan	Vice Preseident, RNID Non-executive Director, Welsh Water Ltd Non-executive Director, Sarasin & Partners LLP Non-executive Director, JP Morgan Asian Investment Trust Plc Non-executive Director, Social Finance Ltd Non-executive Director, Towergate Partnership Senior visiting Senior Fellow in risk and regulation, London School of Economics (LSE)
Paul Tucker	Deputy Governor (Financial Stability), Bank of England Member, the Bank's Monetary Policy Committee Member, the Financial Policy Committee

Appendix 3

FSA organisation chart

Financial Services Authority

31 MARCH 2012



1 Acting
2 Interim
3 Acting
4 Team

VERSION 117BP

Appendix 4
Principal European legislation

The principal European legislation that the FSA will be working to influence during 2012/13 is:

EU Legislation	Action	Detail	Statutory Objective
Payment Services Directive	Commission Review	Report on the implementation and impact of the directive required by 1 November 2012	CP
Second Electronic Money Directive	Commission Review	Report on the implementation and impact of the directive required by 1 November 2012	CP
Unfair Commercial Practices Directive	Commission Review	Report on implementation expected in Q2 2012	CP
European Market Infrastructure Regulation	Support negotiation of level 1 and development of technical standards	Level 1 framework legislation expected to be completed and enter into force Q2 2012. Level 2 technical standards expected to be developed, approved and become binding by Q1 2013	MC
Prospectus Directive Amending Directive	Implementation of changes already agreed	Policy Statement to be issued in Q2 2012 following Consultation Paper CP11/28 of December 2011. Work in ESMA on advice to Commission on possible changes to Prospectus Regulation	MC
Solvency II	Preparation for implementation and ongoing negotiation of text at levels 2 and 3	FSA consultation, finalisation of level 2 delegated acts by the Commission and work on technical standards and guidelines by EIOPA	FS, MC
Capital Requirements Directive IV	Negotiation on revisions to the CRD in line with Basel agreement	Ongoing	FS, MC
Venture capital and social entrepreneurship funds	Negotiation of new legislation	Negotiations expected to be completed Q2 2012	CP
Short Selling Regulation	Development of technical standards to progress the full implementation	ESMA to consult on delegated acts and binding technical standards in Q2 2012 with regime to be in force by November 2012	MC
Credit Rating Agency Regulation	Negotiation of third set of regulations	Negotiations for level 1 are expected to be completed by Q3 2012	MC
Markets in Financial Instruments Directive	Negotiation of revised legislation	Negotiations for level 1 are expected to be completed by Q4 2012	FS, MC, CP

EU Legislation	Action	Detail	Statutory Objective
Market Abuse Directive	Negotiation of revised legislation	Negotiations for level 1 are expected to be completed by Q4 2012	MC
Transparency Directive	Negotiation of revised legislation	Negotiations for level 1 are expected to be completed by Q4 2012	MC
Deposit Guarantee Schemes Directive	Negotiation of revised legislation	Negotiations expected to be completed mid-2012	FS, MC, CP
Omnibus II Directive	Negotiation of new legislation	Negotiations expected to be completed 2012	FS, MC
Mortgage Credit Directive	Negotiation of new legislation	Negotiations expected to be completed in 2012	CP
Alternative Investment Fund Managers Directive	Negotiation of implementing measures, preparation for implementation	Negotiations continue through 2012, Consultation Paper in Q3 2012	CP, FS
Central Securities Depositaries Legislation	Negotiation of new legislation	Commission legislative proposal expected during Q1 2012	MC, FS
Insurance Mediation Directive	Negotiation of revised legislation	Draft legislation expected Q1 2012	CP
Packaged Retail Investment Products	Negotiation of new legislation	Draft legislation expected Q1 2012	CP
Resolution regime for financial market infrastructures	Negotiation of new legislation	Commission legislative proposal expected in 2012. Builds on work of FSB and CPSS-IOSCO	FS, MC, CP
Undertakings for Collective Investment in Transferable Securities (UCITS V)	Negotiation of revised legislation and implementing measures	Draft legislation expected Q2 2012	CP
Institutions for Occupational Retirement Provision Directive	Negotiation of revised legislation	Draft legislation expected in Q3 2012	CP, MC
Corporate governance for listed issuers	Negotiation of new legislation	Commission legislative proposals expected in 2012	MC
Securities Law Directive	Negotiation of new legislation	Commission legislative proposals expected in 2012	MC
Insurance Guarantee Schemes Directive	Commission legislative proposals expected	Draft legislation expected Q1 2013	CP
Money Laundering Directive III	Negotiation of revised legislation	Negotiations expected to be completed Q4 2012	FC
Recovery and Resolution Directive	Negotiation of new legislation	Awaiting publication of legislative proposal	FS
EU Commission White Paper on Adequate, Safe and Sustainable Pensions	Input into ongoing work on this topic which could result in new or revised legislation	EU Commission White Paper expected in the first half of 2012	CP, MC

EU Legislation	Action	Detail	Statutory Objective
Investor Compensation Schemes Directive	Negotiation of proposed amendments at trialogue level discussions, with a view to finalising the amendments to the directive	Q3 2012 and ongoing	CP
Proposal for a Directive on alternative dispute resolution and a Regulation on online dispute resolution	Negotiation of new legislation	Negotiations expected to be completed in 2013	CP
Recommendation on access to a basic payment account	Commission Review	Commission to review 2011 Recommendation on access to a basic payment account, and possibly propose legislation after that	CP

Key for statutory objectives:
FS – Financial Stability
MC – Market Confidence
CP – Consumer Protection
FC – Financial Crime

Appendix 5
Milestones for 2012/13

DELIVERING REGULATORY REFORM – PREPARING FOR THE NEW FIRM-SPECIFIC FINANCIAL REGULATION REGIME IN THE UK

	2012 Q2: April-June	2012 Q3: July-September	2012 Q4: October-December	2013 Q1: January-March
PRA	Internal Twin Peaks	*	*	*
FCA	Internal Twin Peaks	*	*	*

DELIVERING FINANCIAL STABILITY – CONTRIBUTING TO THE PROTECTION AND ENHANCEMENT OF THE STABILITY OF THE FINANCIAL SYSTEM

	2012 Q2: April-June	2012 Q3: July-September	2012 Q4: October-December	2013 Q1: January-March
Solvency II	Consultation Paper		Policy Statement	

DELIVERING MARKET CONFIDENCE – MAINTAINING CONFIDENCE IN FINANCIAL MARKETS

	2012 Q2: April-June	2012 Q3: July-September	2012 Q4: October-December	2013 Q1: January-March
Regulated Covered Bonds				Amendments to RCB regulations and sourcebook

*Publications/timings to be confirmed before Board.

DELIVERING CONSUMER PROTECTION – SECURING THE APPROPRIATE DEGREE OF PROTECTION FOR CONSUMERS

	2012 Q2: April-June	2012 Q3: July-September	2012 Q4: October-December	2013 Q1: January-March
FSCS funding model review		Policy Statement		Consultation Paper
Mortgage Market Review – review of charging practices		Consultation Paper		
Mortgage Market Review – Third party administrator TCF		Consultation Paper		
Mortgage Market Review – Changes to regulatory reporting requirements				Consultation Paper
PSD/E-money directive review		Consultation Paper		
RDR – Platforms and nominee services		Policy Statement		
Insurance Mediation Directive	Consultation Paper			
Platform charging and remuneration	Consultation Paper	Policy Statement		
UCITS V			Consultation Paper	
AIFMD		Consultation Paper		

DELIVERING A REDUCTION OF FINANCIAL CRIME – REDUCING THE EXTENT TO WHICH IT IS POSSIBLE FOR A BUSINESS TO BE USED FOR A PURPOSE CONNECTED WITH FINANCIAL CRIME

	2012 Q2: April-June	2012 Q3: July-September	2012 Q4: October-December	2013 Q1: January-March
Anti-bribery and corruption	Thematic Report			
Banks' systems/controls against unauthorised business	Thematic Report			

DELIVERING THE FSA'S OPERATIONAL PLATFORM

	2012 Q2: April-June	2012 Q3: July-September	2012 Q4: October-December	2013 Q1: January-March
Annual Fees Consultation	Policy Statement		Consultation Paper – Policy	Consultation Paper – Rates

Appendix 6
Corporate responsibility

Introduction

We play a key role in protecting and enhancing the integrity and stability of the UK financial system. Corporate citizenship is a vital part of this and we will lead by example to influence positive change, not only within the FSA but also among our peers.

To provide the best service to the public and the financial sector, we need to support our staff to understand, represent and have close links with both the marketplace and the wider community. In this way we can be in the strongest position to fulfill our obligations and role, as well as to play our part in sustaining the environment and being a positive contributor to community improvement.

Diversity and corporate citizenship in the FSA

In 2012/13, internally we will ensure that we continue to recruit, develop and retain the most talented, engaged and diverse workforce that we can. We will develop training packages specifically tailored for our supervisors to enable them to engage with firms on this issue and equip our line managers to ensure all staff feel valued and respected.

We will measure progress by the nine 'protected characteristics' in equality law:

- age;
- disability;
- gender reassignment;
- marriage and civil partnerships;
- pregnancy and maternity;
- race;
- religion or belief;
- sex; and
- sexual orientation.

And for each of the protected characteristics we will measure these against metrics including:

- staff profile;
- employment applications and success rates;
- internal promotions;
- training;
- appraisals (including performance ratings); and
- leavers (voluntary and involuntary).

We will provide an update on progress against our metrics in our Annual Diversity Report.

We are also revisiting our community volunteering program to ensure we are giving our staff the best opportunity to engage meaningfully in the community and to gain skills and understanding that will benefit our role as a regulator.

We are working with our supply chain to ensure that the high corporate responsibility expectations we have of ourselves are reflected in how we do business with others.

Diversity in financial services

We will measure progress on diversity within financial services. We will do this by building on last year's initial work of gathering the diversity statistics of firms in the financial sector. This will enable us to understand sector trends and work with firms to:

- support and encourage firms to have robust and challenging strategies in place to ensure that they are drawing on the broadest pool of talent, helping them to maintain a competitive edge in terms of human capital;
- understand and discuss with firms the barriers to people gaining employment in the sector or developing their full potential; and
- support firms in understanding the implications of boardroom composition on governance and risk.

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