

The best way to assess the current thinking on PBR is to examine the speeches and press releases from the FSA as MiFID has been implemented and changes made to some of the rules books.

The best way to summarise the approach is “one step forward, two steps back”. In the early days of PBR the statements were all about the benefits of this approach with senior managers taking responsibility and the opportunity to adopt flexible working practices rather than endless processes to meet detailed rules.

Well, let's see what actually happened using the much lauded flexibility that the slimmed down version of the Training & Competence Sourcebook has achieved. The rules were disapplied to Wholesale business. Giving firms the ability to decide what would be a suitable regime for their staff. This has been an area where the regime had been lightly enforced and, with a few exceptions, firms did not feel that this would cause too many issues.

In the area of greatest risk and despite the fact that MiFID does not require anything more than the overriding general competence rule in SYSC 5.1 Skills, knowledge and expertise, the FSA retained the rules relating to advice and investment management for retail clients. In fact, despite the Sourcebook being thinner through the removal of guidance and the Appendices, there is little room for manouvre in terms of greater flexibility to comply with the rules. Indeed the only discernable change is that there is no time limit set for achieving the examination pass needed to be fully competent. At the same time an addition to the definition of competence was made, to include a good standard of ethical behaviour.

There was also an opportunity to radically slim down the Controlled Functions and apportionment rules which the FSA argued strongly should be retained. The merging of customer functions has simplified the approach but again, if the senior management have proper controls in place is this regime necessary at all?

As a long server in the industry I have great sympathy with the dilemma of letting go of detailed rules in areas where history suggests that a compliance culture is not embedded, as did many respondents to the various Consultative Documents. The current half way house does leave the industry searching for where the advantages of the Principles Based approach could lie.

The history of TCF does provide some clues as to how matters may move forward. The process began as long ago as 2004 with a stake in the ground communicated as a way to set a clear target for firms to meet. By focussing on the fairness standard firms would be able to review their products, sales and fulfilment mechanisms to check that they were fair.

Admittedly it took some time to appreciate exactly what was meant by some statements and the FSA responded by explaining what TCF was not. However, since then, there has been no shortage of helpful material from the FSA designed to make clear what they mean. This year has seen two update reports and three specific reports on culture, management information and the relationship between providers and distributors. The quantity of information is easily equal to several new Sourcebooks but more difficult to find.

It is clear that the “rules” in terms of how firms evidence that TCF is being met, monitored and managed are firmly set and are being enforced through themed visits, enforcement action and rhetoric.

There is great support for the “‘win win' situations, where by focusing on higher level principles and outcomes, so better aligning good 'regulatory' practice with good 'business' practice, we can deliver the same or even better outcomes for customers at a lower cost to the firm” as described by John Tiner in his speech in October 2006.

There has to be a way to achieve the real benefits of a principles based regime but to do this will require real effort on the part of senior management to think through how they want to implement such an approach in their own firm. Can cost savings be made, is there a better way to work to evidence that principles are met and can senior management be bothered?

The next article in this series will propose a way forward to see what process for adopting PBR, or even MPBR, could be devised.

So how might the overarching approach to PBR be taken forward? Firstly it is clear and logical that whatever outcomes may be appropriate for each principle will need to be assessed and considered by individual firms. Each firm needs to meet to satisfy itself that it meets the principle

### **Series of three articles: Principles Based Regulation**

1. Whose idea was it anyway and why?
2. The current thinking and clues from TCF
3. HOW to make the shift to principles based compliance

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