

The following Compliance articles are for the week ending 14 August 2009.

COMMENTARY

WIDER IMPLICATIONS REFERRAL: LEHMAN'S-BACKED STRUCTURED PRODUCTS - UPDATE

On 14 August, the Financial Services Authority (FSA) commented that since Lehman Brothers' collapse in September 2008, the FSA and the Financial Ombudsman Service (FOS) have been looking at the potential detriment this has caused for investors in the UK structured products market.

In May, the FSA and FOS agreed that the issues relating to Lehman's backed structured products should be considered under the "Wider Implications" process, in order to allow the FSA to explore all options to achieve the best outcome for consumers.

The FSA committed to update FOS three months into its review, and has now provided this update. Although the FSA has completed several elements of its work, it has asked FOS to continue to defer its consideration of complaints by a further three months to allow the FSA to consider the remaining aspects. The FSA's update, and additional information on this Wider Implications referral, can be found on the Wider Implications website.

[Source: FSA Website](#)

FSA CONFIRMS INTRODUCTION OF REMUNERATION CODE OF PRACTICE

On 12 August the FSA introduced a new code that will require large banks, building societies and broker dealers in the UK to establish, implement and maintain remuneration policies consistent with effective risk management.

The new code is designed to achieve two objectives:

1. That boards focus more closely on ensuring that the total amount distributed by a firm is consistent with good risk management and sustainability
2. That individual compensation practices provide the right incentives

Eight principles have also been added to the FSA's handbook to ensure firms understand how the FSA will assess compliance.

The code makes clear that it is not expected that firms will enter into contracts with individuals which provide guaranteed bonuses for more than one year. It is also expected that for senior employees two-thirds of bonuses will be spread over three years.

Firms are expected to provide the FSA with a remuneration policy statement by the end of October. This will have to be signed off by remuneration committees and will enable the FSA to check compliance with the code. Non-compliant firms could face enforcement action or ultimately, be forced to hold additional capital should they pursue risky processes.

Hector Sants, FSA chief executive, said: "The FSA is determined that banks' remuneration policies should be consistent with, and promote, effective risk management. The new rules and code of practice, which will take effect from January, next year, are aimed at achieving this. Whilst there is general international agreement on the need for supervisory action on remuneration policies and practices we will be the first major financial regulator to take this step. We think that it is important to have rules in place for 2010."

The rule and code are consistent with the recommendations of the Financial Stability Board and with the measures being considered by others such as Switzerland and the EU. International negotiations on common guidelines should be concluded in the first half of 2010.

Source: FSA Website

GUIDANCE ON "GUIDANCE"

In Chapter 2 of the Enforcement Guide, the FSA make clear that their approach to regulation and enforcement involves a combination of high-level principles, detailed rules, guidance and supporting material, with an increasing emphasis on the FSA's Principles for Businesses ('the Principles').

This is because the FSA believe that an approach that is based less on detailed rules and that focuses more on outcomes will allow them to achieve their regulatory objectives in a more efficient and effective way.

When does the FSA issue guidance or supporting material?

The FSA outcomes-focused approach includes encouraging firms to exercise judgement about, and take responsibility for, what the Principles mean for them in terms of how they conduct their business.

To assist firms in this, the FSA recognise that it is important that firms can understand what FSA expects of them. So, in some areas, FSA aim to provide greater clarity about their expectations of firms by using guidance and supporting material (such as case studies, examples of good and bad practice, and FSA speeches) to supplement the Principles and support the rules and guidance in the Handbook.

The emerging regulatory architecture provides practical examples and other material to support firms. Some of this material comes through industry solutions.

Can firms rely on the FSA's guidance and supporting material?

The FSA will not take action against a person for behaviour that it considers to be in line with FSA guidance, supporting material or FSA-confirmed industry guidance which was current at the time of the behaviour in question.

Rights conferred on third parties (such as a firm's clients) are not affected by FSA guidance or supporting material, and it does not bind the courts (e.g. in relation to an action for damages for breach of a rule).

Are guidance and supporting material binding on firms?

Guidance and supporting material are not binding on those to whom the FSA's rules apply. Rather, such materials are intended to illustrate ways (but not the only ways) in which a person can comply with the relevant rules.

Guidance and supporting material do not set out the minimum standard of conduct needed to comply with a rule, nor is there any presumption that departing from guidance indicates a breach of a rule.

If a firm has complied with the Principles and other rules, then it does not matter whether it has also complied with other material the FSA has issued.

FSA guidance and supporting material are potentially relevant to an enforcement case, e.g. to help assess whether it could reasonably have been understood or predicted at the time that the conduct in question fell below the standards required by the Principles or rules. The extent to which FSA may take guidance and supporting material into account when considering a matter will depend on all the circumstances of the case.

Firms should refer to Chapter 2 of the FSA's Enforcement Guide for further information about the status of Handbook guidance and supporting material.

Source: [FSA Website](#)

ABI RESPONSE TO FSA REMUNERATION GUIDANCE

Responding to the FSA's new Code of Practice on remuneration policies, Peter Montagnon, the ABI's Director of Investment Affairs, said: "This is an important step forward. The FSA has stuck to its principle of linking remuneration to risk, while making the Code less prescriptive and narrowing the scope of the organisations covered. The new version is much more likely to deliver the desired outcome without excessive compliance burdens.

We agree with the FSA that the focus should be on the structure of remuneration, not the size of the package, which companies must be able to determine based on their need to compete. And, as shareholders, we support the proposal that bonus pools should be formed only after taking into account the cost of capital, adjusted for risk.

There is still work to be done so the details do not conflict with the Combined Code and other similar codes, ensuring the FSA proposals are in line with international arrangements.

The FSA has promised further proposals for the wider financial sector in October. We continue to believe that great care needs to be taken to avoid reading across from banks to insurers and asset managers, whose businesses are substantially different in nature and pose much less risk to overall financial stability."

Source: [ABI Website](#)

MORE WORK NEEDED ON RETIREMENT PLANNING

The ABI has published the results of consumer research into the wake-up packs received by defined contribution pension savers six months before retirement.

The packs contain important information on the options for buying an annuity, including the right to shop around using the Open Market Option (OMO).

71% of participants who read the pack said it gave them a better understanding of their options at retirement, and awareness of the right to shop around increased from 62% to 82% after reading it. However, of those participants who remembered receiving the pack, 58% had just skimmed it or hadn't yet read it at all.

The research was designed to measure feedback following improvements made to customer communications in 2008. The survey forms part of a wider industry effort to improve customer engagement with pension savings and retirement planning, including new processes to simplify and speed-up the OMO transfer process.

Maggie Craig, the ABI's Director of Life and Savings, said: "It's encouraging that overall, the wake-up packs are considered to be useful and informative. The fact that the packs informed people about both the right to shop around, and the availability of different types of annuity, shows that the industry is getting better at communicating these important messages to consumers.

The pensions industry is committed to providing clear and helpful information to customers as they approach retirement, and this research will help us make further improvements.

Keeping communications short and simple clearly helps, but the best way to ensure customers get best value from their pension savings is to raise awareness and encourage engagement earlier in their working lives. The ABI is working with members towards this important objective."

[Source: ABI Website](#)

POSSESSIONS FALL AND ARREARS FLATTEN

Statistics published on 14 August by the Council of Mortgage Lenders (CML) show that the number of mortgage possessions fell in the second quarter of the year, while cases of arrears levelled off.

A combination of factors has helped keep mortgage arrears and possessions in check, despite the recession. Most importantly, lenders are showing forbearance to borrowers where customers are trying to resolve their payment problems and have a realistic chance of doing so.

Low interest rates are helping ensure that arrears grow less quickly; giving borrowers a better chance of getting back on track and lenders more scope to extend forbearance. And government schemes are providing some help for borrowers in difficulty by promoting early communication between borrowers, lenders and debt advisers.

But while today's figures reflect the efforts being made to manage mortgage arrears and avoid possession if possible, there can be no complacency about the potential scale of future payment problems.

While the economy remains weak and with unemployment still growing, arrears and possessions are likely to rise in the second half of the year.

[Source: CML Website](#)

BUT TO LET ACTIVITY IN SECOND QUARTER OF 2009

The buy-to-let market showed the first signs of stabilising in the second quarter as arrears improved significantly and the decline in new lending began to slow, according to the CML.

There were 21,600 new buy-to-let loans advanced in the second quarter, a relatively modest 4% decline from 22,400 in the preceding three months. Heavily reliant on wholesale funding, the buy-to-let market has suffered a sharp contraction in the credit crunch.

There are now fewer active lenders in the private rental market, with less money to lend. And therefore seven consecutive quarters of decline have left buy-to-let gross lending at very low levels.

[Source: CML Website](#)

MARKET STABILISING BUT NOT YET "NORMAL"

New data from the CML shows further signs of stabilisation in the mortgage market, but transactions are still weak on a historic basis. Lending for house purchase and remortgaging both increased in June, albeit from very low levels.

There were 45,000 house purchase loans, worth £5.9 billion, up 23% from 36,500 loans in May. However, this is less than half the average number of loans in June over the last seven years.

A total of 116,700 house purchase loans were advanced in the second quarter, a 50% increase from the preceding three months but down 22% from the second quarter of 2008.

Source: CML Website

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