

Annual Report

2016/17



FCA

Markets
Practitioner Panel



Chair's foreword

I am pleased to introduce the fourth FCA Markets Practitioner Panel Annual Report. This is my second and final Annual Report before I step down as Chair of the Panel later this year.

Looking back over the past year, it has been an uncertain and unsettling time for the UK's financial services industry. The implications of the UK's referendum to exit the European Union (Brexit) on 23 June 2016 continue to dominate our work and will do so for some time ahead. We remain committed to doing all that we can to maintain and promote the attractiveness of the UK markets and have worked hard to ensure our key concerns are firmly on the FCA's agenda. Our membership spans a variety of sectors and we are keen to share our practical knowledge and experience with the FCA and the UK Government during the Brexit negotiations.

The industry is also facing the challenge of implementing the final phases of the European Commission's post-crisis regulatory reforms and we have provided constructive challenge to the FCA so that the views of the wholesale market continue to be represented.

Our relationship with the FCA Executive Committee continues to be strong and we have welcomed regular engagement with the FCA Chairman, CEO and other Board Members.

I would like to thank Panel members for their open and constructive contributions and for the interesting and productive discussions we have had – all of which enhances the efficiency of the Panel and our value to the FCA on important market issues.

I have enjoyed my time on the Panel and wish the new Chair, John Trundle, and other Panel members all the very best for the future.

Robert Mass
Chairman, FCA Markets Practitioner Panel

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Introduction

The Markets Practitioner Panel is a statutory panel of the FCA. It is one of a number of panels that the FCA is required to establish and maintain under the Financial Services and Markets Act 2000 (as amended), and represents the interests of practitioners who are likely to be affected by the exercise of the FCA's functions relating to the financial markets.

The Panel benefits from some of its members belonging to other panels, which broadens our understanding and encourages a closer working relationship with them. We have also welcomed FCA Board members attending Panel meetings, who have helped us to understand the FCA's strategy and to give appropriate advice. We have established a constructive relationship with the FCA Chairman, CEO and other members of the FCA's Executive Committee, and also enjoy close engagement with senior representatives from the FCA's Markets Policy team.

The Panel meets formally six times each year, and holds sub-group meetings on specific topics as required, as well as working breakfast meetings and strategy dinners. We held a "Panel Effectiveness" dinner in February 2017, at which we concluded that while our work has a positive impact on the FCA and the FCA Board, we should review the Panel's membership to ensure it continues to reflect different market perspectives, and we should engage more with the other FCA panels, particularly in shared areas of interest. We will also hold our annual

engagement dinner with the FCA Board later this year to discuss our priorities and how we can add further value to the FCA's work.

As part of our aim to provide early and effective industry input into important strategic regulatory issues, we have established a number of strategic priorities:

The UK's exit from the European Union (Brexit)

MiFID II

Liquidity

Negative interest rates

Financial crime, cyber and AML

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The UK's exit from the European Union (Brexit)

Our principal focus has been to ensure that the risk of any disruption to financial markets is minimised. In the run up to the EU Referendum on 23 June 2016, we were interested to hear from the FCA about what work was being done in the event of a 'leave' vote. Following the vote, we held an extraordinary meeting with FCA representatives to discuss our initial views of the impact on markets and potential risks. As a result, we have established a standing agenda item to discuss Brexit-related matters at Panel meetings.

We have encouraged the FCA to engage closely with the relevant UK government departments to ensure that the future of the UK's financial sector is at the centre of the government's negotiating strategy and to provide technical advice on how financial markets operate, including the consequences under different exit scenarios. The FCA should consider potential inconsistencies between EU and UK rules after Brexit, especially extreme cases, where to follow one rule could mean the breach of the corresponding rule in another jurisdiction.

We have also urged the FCA to ensure that it has the necessary resources to deal with the significant Brexit-related work it will be required to undertake.

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MiFID II

MiFID II presents the greatest current regulatory challenge to the industry and we have discussed different aspects of this during the year. We welcomed the European Commission's one-year delay to its implementation, to 3 January 2018, which will give the industry greater time to better prepare itself, but expressed concern about the delays in publishing details about complex issues such as commodity derivatives, ancillary exemptions, the treatment of illiquid instruments and new transparency requirements. We continue to highlight to the FCA the implementation challenges created by MiFID II for firms.

We challenged the FCA's proposals to extend taping requirements to all corporate finance activities (e.g. strategic conversations between corporate finance bankers and corporate executives), as the risk of harm in this particular area did not justify the considerable extra costs and complexities of implementation, noting that other EU regulators had not taken this approach. We welcomed the FCA's decision to consider its approach further in the light of the concerns it had heard.

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Liquidity

Liquidity across all markets continues to be a topic that remains of considerable interest and importance to us. We were reassured to hear that liquidity has also been a focus for the FCA Board and welcomed the opportunity to share our experience in the markets and consider the implications for the regulators. We also suggested that the FCA's thinking should include the trend of "the search for" yield resulting in illiquid investment funds and the consequences of this if there was a market shock.

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Negative interest rate environment

The negative and/or low interest rate environment has continued to be an issue that we have raised with the FCA. In their search for yield, consumers may not understand the impact of negative and/or low interest rates and may take on greater risk than they realise by investing in products they do not fully understand. There are also potentially important structural impacts on pension annuities and what level of provision is appropriate in a prolonged period of low interest rates.

We have also considered the risk that consumers may not be aware of the impact that a rise in interest rates could have on their investments and their ability to liquidate them, and we have discussed the role of the FCA in relation to investor awareness.

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Financial crime,
cyber and AML

We continued to discuss aspects of financial crime, cyber and AML with the FCA during the year.

We have expressed concern with the evolution of AML rules, as the cost of implementing these rules is expensive and it is often not clear that they serve their intended objective of keeping “dirty” money out of the financial system. Our collective experience suggests that implementation has become largely procedure-driven and we have urged the FCA to take a more principled approach to AML where it is possible to do so, and that it scale back procedures to a more realistic and constructive scale.

Firms’ systems are continually at risk from an increasing volume of sophisticated cyber-attacks. The considerable cost and complexity that is required for just one firm to achieve high levels of cyber resilience suggest that there is a role for cooperation between firms, and with regulators, in sharing information and best practice. We also encouraged the FCA to continue to work closely with the PRA, the Bank of England and the sector to consider how best to engage with suppliers such as software and data vendors, given their integral role in the financial system. We have also urged the FCA to continue work to strengthen its own protection against cyber-attacks and, equally, its ability to respond to and recover from them.

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Other areas of engagement

Senior Managers Regime (SMR)

We have welcomed the introduction of the regime and its objective of assigning accountability clearly at appropriately senior levels within firms. The SMR has been a positive regulatory development which has made a material difference in focusing managers' attention on their responsibilities. However, we have urged the FCA to ensure that accountability appropriately reflects the responsibilities of senior staff to run the business rather than on detailed technical knowledge and compliance processes which inform decision-making, which is typically the responsibility of more junior staff.

We advised the FCA to adopt a proportionate and flexible approach when applying the SMR, that held senior managers to account but did not foster disproportionately risk-adverse behaviour. We were encouraged to hear that the FCA's Supervision Division had established a "centre of excellence" to support a consistent and pragmatic approach when implementing the regime.

We also advised against extending the whole regime to Non-Executive Directors (NEDs) as this risked compromising the role of NEDs as independent of a firm's Executive Committee; and pressed the FCA to consider how the Prudential Regulatory Authority proposed to treat NEDs in their approach to implementing the SMR when deciding their approach.

Asset Management Market Study

We have engaged extensively with the FCA on the asset management market study. We support both the objectives of increasing transparency, ensuring that investors invest with the correct funds for their needs, and many of the measures proposed in the study, although have encouraged the FCA not to inadvertently create additional costs and increased regulatory requirements which have very little or no benefit.

We have focused, in particular, on how to identify and distinguish the true costs of asset investment management from other areas in the value chain such as marketing and distribution. We suggested the FCA clarify the terminology it has used; have greater understanding of the activities at each link of the value chain, focusing on the retail rather than institutional segment of the market; and factoring in all of the associated costs and risks involved when assessing the overall value of a product.

We also advised the FCA to consider any potential Brexit implications, as many asset managers would prefer harmonisation in the products they sell across Europe and not to be required to have a single product for the UK, which would cause further complexity and increase costs.

We will continue to constructively engage with the FCA as it continues to develop its thinking and proposals for the asset management sector.

FCA Strategic Initiatives

We have also drawn on the extensive financial markets experience and detailed technical knowledge among Panel members to advise the FCA on its Mission and Business Plan and provide input to the Sector Views.

We have welcomed these initiatives and applauded the FCA for the pragmatic and risk-based approach it has taken. However, we have encouraged the FCA to take a more holistic and judgment-based approach, and urged cultural change within the FCA to support a fundamental change to the "box-ticking" approach that firms sometimes perceive in the FCA's supervision. We have also encouraged the FCA to ensure its planning is flexible enough to re-prioritise and accommodate any additional Brexit-related pressures that may arise.

Members of FCA Markets Practitioner Panel

1 April 2016 – 31 March 2017

Robert Mass

Head of International Compliance and Global Head of Securities Division Compliance, Goldman Sachs International

Chairman

John Trundle

CEO, Euroclear UK & Ireland

Deputy Chairman

Annemarie Durbin

(joined 1 April 2016 as an ex-officio member of the Panel)

Chair of the FCA's Listing Authority Advisory Panel; Non-Executive Director of WH Smith plc, Santander UK plc and Ladbrokes plc; and member of Standard Chartered Group's Executive Committee.

Suvro Dutta

Partner, Financial Services KPMG

Duncan Ford

Chief Operating Officer, Marshall Wace LLP

Mark Ibbotson

Group CEO, G.H. Financials

Jim Kandunias

Partner and COO, Immersion Capital LLP

Bernard Mensah

Co-Head of Global Fixed Income, Currencies and Commodities (FICC) Trading, Bank of America Merrill Lynch

Abdallah Nauphal

CEO, Insight Investment Management

James Palmer

Senior Partner, Herbert Smith Freehills

Nikhil Rathi

Chief Executive Officer, London Stock Exchange

Paul Swann

President and Managing Director, ICE Clear Europe

Alan Trotter

Group CFO, Invesco

Simon Bragg (until January 2017)

CEO and Chairman, Stifel

Scott Cowling (until January 2017)

Managing Director and Head of EMEA Equity Trade, Blackrock Investment Management (UK) Limited.

FCA Markets Practitioner Panel

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