

FINANCIAL SERVICES PRACTITIONER PANEL

Second major survey of practitioner views of regulation

The FSA is now one year old. It has made huge progress in knitting together its predecessors and through an ambitious consultation process has gained broad practitioner support and understanding.

The 2002 Financial Services Practitioner Panel Survey is a major, authoritative survey of regulated firms in the UK, and follows a similar survey in 1999.

It is the first since the FSA assumed its full powers in 2001.

It shows that practitioners view as beneficial the effect of the change to the FSA as single regulator. In particular:

practitioner support for:

- strong regulation
- a firm line with persistent offenders
- the FSA's approach to consultation
- the supervisory approach in general

practitioner anxiety over:

- the degree of unremitting change
- a perceived deterioration in regulatory performance
- the balance between consumer and practitioner interests
- regulation of process rather than outputs

practitioner concern about:

- complexity and navigability of the handbook
- costs – excessive and growing
- lack of guidance

It is early days for the FSA and there are strong positives around the openness of the FSA and its approach to consultation.

There are also some storm warnings in the results of this survey. There may be a growing gap between expectations and experience, a growing anxiety of where all this change will lead, and a frustration growing over the difficulties of obtaining clear and consistent guidance.

There are clear worries over the total costs of compliance in the UK and the Panel welcomes the speedy response of the FSA to commence a study of compliance costs to help identify efficient practices for the benefit of all.

Practitioners support the broad principle and risk based approach of the FSA. It will be essential that this approach permeates the whole of the FSA's behaviour.

It is a sign of strength of UK regulation that the Practitioner Panel was created in the FSMA and that the FSA has proved open and responsive to the views of practitioners. It is hoped the results of this survey will further assist with the FSA's development.

[cont.]

“The survey results raise some issues for the FSA's relationship with small firms”, said Roger Sanders, one of the joint chairmen of the FSA's Small Business Practitioner Panel (SBPP). “Smaller businesses are feeling the burden of regulatory pressure and cost. The FSA needs to decide how it can take better account of their views, particularly with the new entrants to regulation from general insurance and mortgage intermediaries being mainly small firms.”

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Notes for editors

The Financial Services Practitioner Panel was formed under the Financial Services and Markets Act 2000 as a statutory body designed to monitor the effectiveness of the FSA, communicate to the FSA general concerns of practitioners, respond with practitioners views to the FSA on specific regulatory matters and contribute a broad industry view on the formulation of FSA policy.

The survey was conducted on behalf of the Panel by BMRB International.

The Panel's membership consists of:

Donald Brydon, Chairman, AXA Investment Managers
Alan Ainsworth, Deputy Chairman, Threadneedle Investments
Jonathan Bloomer, Group Chief Executive, Prudential plc
Matthew Bullock, Group Chief Executive, Norwich and Peterborough Building Society
James Crosby, Chief Executive, HBOS plc
Clara Furse, Chief Executive, London Stock Exchange
David Grigson, Chief Financial Officer, Reuters plc
David Hardy, Chief Executive, London Clearing House
Roy Leighton, UK Chairman, Credit Lyonnais Derivatives
Brendan Nelson, Chairman, Financial Sector, KPMG
Hector Sants, Vice Chairman, CSFB
David Verey, formerly Deputy Chairman, Cazenove
Michael Quicke, Chief Executive, Leopold Joseph) Jt Chairmen, Small Business
Roger Sanders, Principal, Roger Sanders Associates) Practitioner Panel

END

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**2002 Survey of the FSA's
regulatory performance
Report November 2002
Summary and Conclusions**

Prepared for: **Financial Services Practitioner Panel**

Prepared by: **BMRB Social Research
Part of BMRB International Limited**

The full report is being published by FSA on its website (www.fsa.gov.uk) on behalf of the Practitioner Panel, on 29 November 2002.

SUMMARY AND CONCLUSIONS

Second survey of the FSA's regulatory performance

The results reported here are based on a survey of 3,890 senior executives in regulated financial services firms. The survey was carried out using postal self-completion questionnaires. The overall response rate was 42% of individuals, and 50% of firms contacted. The survey results are representative of all regulated firms in the industry.

Apart from IFAs with less than 10 registered individuals and accountancy and legal firms, one in three of which were randomly selected, all regulated firms were included in the survey. In most cases, two versions of the questionnaire were sent to firms, for separate completion by the chief executive and by the senior person with specific responsibility for compliance. Where the FSA had only one contact (mainly professional firms, smaller IFAs and other small businesses) only the Compliance version of the questionnaire was sent. These smaller organisations are looked at as a separate group.

The survey was carried out in July/ August 2002. The 2002 survey repeats, to a large extent, the similar survey carried out in the summer of 1999; where possible, comparisons are made in this report between the results of the two surveys.

1. Expectations about regulation

In the 1999 survey, there was strong support among all sectors of the financial services industry for the principle of strong regulation. More than eight in ten practitioners thought this was for the benefit of the industry as a whole. Three out of four, however, also agreed that the current system placed too great a burden on the industry, and half that it gave too much weight to the interests of consumers. These views were most strongly expressed by smaller organisations.

Around half of practitioners had already noticed some changes in regulation, in 1999, which they attributed to the creation of the FSA; for most, these changes were only slight. Around three quarters of practitioners were expecting to see further change, and one in three thought there would be a lot more change to come.

When asked whether the new regime would be better, worse, or the same for their own business, about two fifths of practitioners did not expect there would be any difference. One in four expected the new regime to be better, a similar proportion expected things to be worse, and the remainder were unsure.

There were also mixed views on how the switch to the new regulator would affect the financial services industry. About half of practitioners thought the advent of the FSA

would be beneficial to the industry, compared with only one in six who thought it would be harmful, and about a third who did not know or thought it would make no difference. Practitioners in smaller organisations were less likely than others to think the change would be beneficial, and more likely to think it would make no difference.

2. Initial experience

In 2002, there was continuing support in principle for strong regulation - from more than eight in ten practitioners - but chief executives and heads of compliance now felt more strongly than in 1999 that the burden of regulation on the industry was too great. In all practitioner groups, more still agreed than disagreed that too much weight was being given to the interests of consumers. In both surveys, smaller organisations held the most negative views about the burden of regulation and the balance in favour of consumers.

In the 2002 survey, around nine out of ten practitioners had noticed some change in the regulation of their business which they attributed to the creation of the FSA (compared with around half who had noticed any change in the 1999 survey), and around four in ten felt there had been 'a lot' of change. These proportions were similar to the level of change expected by smaller organisations in 1999, but both chief executives and compliance heads had experienced rather more change than their counterparts in the 1999 survey were expecting three years ago.

Asked to comment on the impact of this change on **their own business**, two in five practitioners were unable to express an opinion, with most of these feeling it was 'too early to say'. Those who did give an answer were about twice as likely to say things had got worse than better; this compares with an equal split between positive and negative expectations in 1999. Opinions were similar in both surveys for all three practitioner groups.

When asked about the impact of the change to the FSA upon the **financial services industry as a whole** (as opposed to their own business) chief executives and compliance heads were more positive in their views, being twice as likely to feel the change had been beneficial as harmful for the industry; the balance of opinion was, however, also less positive than expectations in 1999, when the balance between 'beneficial' and 'harmful' had been three to one for chief executives, and four to one for compliance heads. For smaller organisations, opinions also shifted from the 1999 survey, in which practitioners were twice as likely to anticipate the change as being beneficial rather than harmful, to being just as likely to say the change had been harmful as beneficial in 2002.

In both surveys, around one in five practitioners across all industry sectors felt the change to the FSA had made no difference, with one in six saying that they didn't know.

In the 2002 survey, heads of compliance and smaller organisations were also asked to consider the effect on **consumers of financial services**. Around four in ten felt that the change to the FSA had made no difference to consumers, and this opinion was particularly widespread among smaller organisations. Of the remainder, heads of compliance were much more likely to feel the change had been beneficial rather than harmful (by a ratio of four to one) while opinion among smaller organisations was evenly balanced.

3. A widening gap?

The survey was designed to quantify the **relative importance** to practitioners of 15 different criteria for evaluating the effectiveness of the FSA, and then to measure their perceptions of **the performance** of the regulator against these same criteria. Similar questions were asked in the 1999 survey (when 13 criteria were used).

Practitioners were first asked to give each criterion a score between 1 and 10, with high numbers indicating a high level of importance. Of the 15 criteria, 13 were given average scores of 8 or above, indicating they were regarded as very important. Two aspects of the regulatory role stood out as particularly vital for practitioners, 'provide reliable guidance when needed' and 'take a firm line with businesses which persistently break the rules'. 'Listen to consumer views when deciding policies and procedures' and 'Encourage the education of the public about financial products and services' were seen as the least important of the different criteria that practitioners were asked to consider.

Perceptions of importance were relatively unchanged for most criteria from the previous survey. The one exception was 'encourage the education of the public about financial products and services' which all three practitioner groups rated lower in importance in 2002 than in 1999.

Practitioners were then asked to rate the effectiveness of the FSA, on each of the same criteria, by allocating a score from 1 to 10, with high numbers in this case indicating a high level of performance. Although some practitioners felt unable to give a rating on some criteria (the proportion generally ranged between 6% and 20%, depending on the criteria), the proportions were not noticeably higher than in the 1999 survey.

Average effectiveness scores ranged between 4.6 and 6.6 for chief executives (overall average of mean scores 5.4), between 4.7 and 6.8 for heads of compliance (overall average 5.6), and between 4.3 and 6.3 (overall average 4.9) for smaller organisations, suggesting that most practitioners judged the FSA's performance as average rather than

good. Banks, friendly societies and general insurance firms tended to give the highest ratings, and IFAs and firms with life and pensions business the lowest.

Two attributes stood out as having the highest perceived performance scores across all three practitioner groups, 'Take a firm line with businesses which persistently break the rules' and 'Listen to consumer views when deciding policies and procedures'. The former was judged as one of the most important attributes of a regulator at the previous question.

For chief executives and heads of compliance, the attributes which had the lowest performance scores were: 'Provide reliable guidance when needed' and 'Have efficient administrative procedures'. The lowest scores for smaller organisations were: 'Interpret rules in a flexible and common-sense way' and 'Be efficient and economic in use of its resources'.

The largest gaps between importance and performance scores, and therefore the biggest shortfall between expectation and delivery, were (for chief executives and heads of compliance) on the attributes 'Provide reliable guidance when needed', 'Have efficient administrative procedures' and 'Interpret rules in a flexible common-sense way'. The equivalents for smaller organisations were 'Interpret rules in a flexible common-sense way', 'Listen to industry views when deciding policies and procedures' and 'Be efficient and economic in use of its resources'.

It is possible to compare the results of the 2002 and the 1999 surveys, both in terms of importance and perceived performance, with the exception of two criteria which were new for the 2002 survey. It must be remembered that in 1999 practitioners were asked about their current regulator (which only in around a third of cases was the FSA), and in 2002 practitioners were asked about the FSA only. For most practitioners, therefore, the comparison is not between views of the FSA at two points in time, but between views of the FSA in 2002 and their previous regulator in 1999.

In terms of importance, it has already been noted that scores were generally unchanged from 1999; in both surveys, most criteria were judged to be of relatively high importance with mean scores generally between 8 and 9 out of 10. However, when performance scores are compared between the two surveys, it is clear that perceptions of the FSA's performance in 2002 were generally more negative than perceptions of the regulators in 1999. Among chief executives, all except one aspect of performance saw a decrease in mean score (the exception was 'encourage the education of the public') and the overall average score went down from 6.1 to 5.4. Among compliance heads, the result was similar: all except one aspect of performance declined (the exception was again the education of the public) and the overall average score went down from 6.2 to 5.6. The

net result was a widening gap between importance and performance scores and hence between expectation and delivery.

For smaller organisations, the results were rather different. Three aspects of performance saw an improvement in perceptions, against four which saw a decline and eight which remained largely unchanged. The overall average of mean scores increased slightly (but not significantly) between the two surveys, from 4.8 to 4.9. In spite of this improvement, the perceptions of the FSA by smaller organisations in 2002 remained generally more negative than those of chief executives and heads of compliance.

The attributes which showed the largest decrease in mean performance score between the two surveys were 'Provide reliable guidance when needed' and 'Have efficient administrative procedures' for chief executives and heads of compliance, and 'Take a firm line with companies which persistently break the rules' for smaller organisations.

4. Details of experience

Consultation procedure

The general perception among practitioners was that the FSA was making a lot of effort to consult, with around three-quarters of compliance heads and half of smaller organisations agreeing that this was the case.

Six in ten compliance heads also agreed there had been sufficient feedback of the results of consultation exercises, compared with one in four who held this opinion in 1999. However, only around half of compliance heads and a quarter of smaller organisations agreed that the reasons for policy decisions following consultation had been explained satisfactorily, and similar proportions felt that the FSA was taking account of industry views

Around eight in ten compliance heads thought FSA consultation papers should be more concise, with a similar proportion of smaller organisations taking this view. With both groups this proportion had increased since the 1999 survey. Similarly, around three-quarters of compliance heads and smaller organisations felt their business did not have time to respond to FSA consultation papers, a significant increase for compliance heads from around two-thirds in 1999 to three-quarters in 2002.

As in 1999, smaller organisations expressed more negative views about consultation procedures on most dimensions.

Among chief executives, opinion was divided as to whether they thought the FSA's consultation process had been effective in collecting the views of their business, with

around 45% saying it had been effective and 45% saying it had been ineffective. Heads of compliance were slightly more positive, but smaller organisations were much less positive, being over twice as likely to say the process was not effective as effective. Other than an understandable decrease in the proportion unable to express an opinion on this issue, results were largely unchanged from 1999.

As in 1999, for both chief executives and heads of compliance, the most popular method of communicating their business's views to the FSA was directly to the FSA, although a substantial proportion preferred to put forward their views via trade associations or via surveys such as this one. For smaller organisations, as in 1999, surveys were the first choice, although a lower proportion chose this option in 2002.

Provision of guidance

Detailed questions about the provision of guidance were asked of heads of compliance and smaller organisations with experience of seeking guidance on rules or regulatory policy from the FSA.

Heads of compliance were positive about some elements of guidance provision, with six in ten feeling that it was possible to be open and frank in discussion with the FSA when seeking guidance, and a similar proportion that the regulator's emphasis was on prevention rather than enforcement.

However, around a half of heads of compliance said it was difficult to work through things informally with the FSA without involving legal people, six in ten felt that FSA staff did not generally provide any informal guidance, and almost as many felt they avoided making decisions altogether. Three quarters of compliance heads disagreed that FSA staff generally give definitive guidance promptly.

Views among smaller organisations were broadly in line with those for compliance heads, with slightly lower proportions feeling that it was possible to be open and frank in discussion with the FSA when seeking guidance and that emphasis was on prevention rather than enforcement.

There was a fall in the perceived clarity of guidance provided between the two surveys. In 2002, around one in ten heads of compliance thought that the guidance received from the FSA was always clear, compared with nearly four in ten who held this view in 1999. Similarly, a quarter of heads of compliance in 2002 thought that guidance received from

the regulator was often unclear, compared with only one in ten in 1999. Practitioners in smaller organisations were more likely than compliance heads to say that guidance was often unclear (four in ten did so), but results were largely unchanged from the previous survey.

There was a similar fall in the perceived consistency of guidance provided, particularly among heads of compliance. In 2002, one fifth of these practitioners said that guidance from the FSA was always consistent, compared with two fifths in 1999 who said this about their regulator at the time. There was a corresponding two-fold increase between the two surveys in the proportion saying that guidance was often inconsistent. Among smaller organisations, there was also a drop in the proportion saying guidance was always consistent, and an increase in those saying it was often inconsistent, although the shift was less pronounced than for compliance heads.

FSA Handbook of Rules and Guidance

Some new questions were included in the 2002 survey about the FSA Handbook of Rules and Guidance. Views on the Handbook were generally negative, particularly so with smaller organisations.

The most pressing issue was finding the rules and guidance needed in the Handbook, with around eight in ten heads of compliance and smaller organisations saying it was difficult to do so. Similarly, around three-quarters of practitioners disagreed that the Handbook was clear and easy to understand. Of those who expressed an opinion, around six in ten also disagreed that the level of detail in the Handbook was about right.

Over half of practitioners who gave an opinion felt that the transition to the new Handbook from SRO rules had not been managed well.

Approach to supervision

Over half of all practitioners described the FSA's application of the rules for Conduct of Business Standards and Prudential Standards as either 'fairly rigid' or 'about right'. Around one in ten described the application as 'highly rigid' and a similar proportion felt it was 'fairly flexible'. Virtually no one described the application as 'highly flexible'. Chief executives were more likely to feel the application was 'about right' or 'fairly rigid', and smaller organisations were more likely to say 'highly rigid', particularly in relation to the rules for Conduct of Business Standards. However, around a quarter of chief executives and four in ten heads of compliance and smaller organisations said they had no experience or didn't know.

Compared with 1999, there was an increase in the proportion of practitioners who were unable to give an opinion about their regulator's approach to supervision. This was presumably due to a relative lack of familiarity with the FSA as a supervisory body, compared with previous regulators who had been operating for many years. .

Opinions of chief executives and compliance heads were generally very similar. Among those who could give an answer, the balance of opinion on the majority of issues was positive. For example, around seven in ten practitioners felt that the FSA applied a reasonable level of supervision for a business of their size and type, and six in ten said the regulator was willing to hold a dialogue with them about compliance issues.

However, there were some less positive opinions as well, with four out of five chief executives and heads of compliance who gave an opinion thinking that the FSA tended to look at processes rather than outcomes, and only one in four agreeing that the FSA gave praise as well as criticism.

In most cases, practitioners who expressed an opinion had less positive views about their regulator than in the 1999 survey.

Smaller organisations were generally more negative than chief executives or heads of compliance with regard to the FSA's supervision, being less likely to agree with positive statements and more likely to agree with negative ones. The exception was 'the FSA applies a reasonable level of supervision', with which they were as likely to agree as other groups. Although results for smaller organisations were less positive than those of other practitioners, they are in some cases more favourable to the FSA than the comparable results for small organisations in 1999

Just over half of compliance heads, and four in ten smaller organisations had direct experience of dealing with FSA supervisory staff. Those who had no experience were not asked to comment on the behaviour of staff, so the results are not directly comparable with the 1999 survey. In 2002, among those who had experience of them, practitioners' views of the FSA's supervisory staff tended to be generally positive. Around eight in ten heads of compliance thought they made site visits at reasonable intervals rather than too frequently, and two-thirds thought they had quite good interpersonal skills, read the information that had been provided about their business, and treated the firm's staff as trustworthy.

However, there were also a number of less favourable impressions, with 45% of heads of compliance feeling that FSA staff followed a checklist rather than concentrating on broad issues of principle and one in six feeling that it was difficult to give feedback to the FSA on their supervisory staff.

As before, the views of practitioners in smaller organisations were less positive. The most positive rating was for frequency of visits, with three-quarters saying that these were at reasonable intervals. Almost two-thirds said that staff tended to just follow a checklist rather than concentrate on broad issues of principle, and that their approach varied depending on the individual.

Enforcement

Only around 5% of practitioners had been subject to any enforcement or disciplinary action either by the FSA or by their previous regulator in the last twelve months. As a result, the questions about enforcement procedures were answered by very small numbers and results can only be described in fairly broad terms.

Opinion was split as to whether practitioners thought their regulator was justified in starting enforcement procedures with similar proportions thinking that they were justified to those who thought they were not justified. Smaller organisations were less

likely than other practitioners to think that their regulator was justified. Heads of compliance were also fairly evenly split on whether the regulator had treated their business fairly during enforcement, although the balance of opinion was negative for chief executives and smaller organisations.

In terms of whether the regulator had imposed a reasonable penalty, completed the investigation and enforcement process within a reasonable time scale, and made clear the rationale for the penalty, there was again some division of opinion between heads of compliance and the other two groups, with the former taking a more positive view.

Costs of compliance

Only about one in seven practitioners (one in 14 smaller organisations) considered the costs of compliance to be reasonable. About four in ten compliance heads, five in ten chief executives and six in ten smaller organisations considered the costs to be 'excessive'. The views of smaller organisations on this issue have not changed from the 1999 survey, but other practitioners were less likely to consider the costs to be reasonable and more likely to consider them excessive than was the case in the previous survey. In 1999 only a third of chief executives and a quarter of compliance heads felt that their compliance costs were excessive.

Smaller organisations were more likely to say that their compliance costs were a high percentage of total costs, compared with other practitioners. Around 45% of chief executives and compliance heads reported that their total compliance costs were less than 5% of total costs, compared with a quarter of smaller organisations. Around a third of smaller organisations said their total compliance costs were 10% or more of total costs, compared with around one in seven chief executives and heads of compliance.

5. Transition or new steady state?

In the 2002 survey, as we have seen, around nine out of ten practitioners reported some change in the regulation of their business which they attributed to the creation of the FSA, and around two in five had experienced a lot of change. This is not surprising, given the transition from sector-based regulation to a much larger single regulator with more wide-ranging objectives and powers.

What is perhaps unexpected is that, six months after N2, the transition is seen by most of the industry as far from complete. When practitioners were asked to gauge the amount of further change in the regulation of their business still to come, almost nine out of ten chief executives and heads of compliance, and eight out of ten smaller organisations, said they expected further change, and two in five thought there would be

'a lot' more change. IFAs and insurance firms were the most likely to expect a lot more change in regulation.

Another indication of the perceived incompleteness of the transition is practitioners' views on the ongoing costs of compliance compared with 1999 i.e. excluding the N2 'bulge'. Around two-thirds of practitioners in all three groups felt the costs of compliance for their business would be higher than in 1999, with most of the remainder either thinking there would be no change or unable to estimate. Of those who felt ongoing costs would be higher, around two-thirds expected them to be more than 10% higher, and one in ten said they expected a cost increase of over 50%. These estimates were similar for all three practitioner groups.

On many of the survey questions about the new regime, a substantial proportion of practitioners indicated that they had no experience of the FSA in that area, could not give an opinion, or that it was 'too early to say'. This applied particularly to questions about guidance, supervision, application of the rules and the overall effect of the change on the firm's own business. So the financial services industry has not, in the 2002 survey, given a final verdict on the FSA's performance as a regulator - the jury is still out.

6. Other views of the new regime

The majority of practitioners who expressed an opinion felt that the FSA was being **as open and responsive as possible** in the way it was currently operating, although two in five smaller organisations took the opposite view. This picture was largely unchanged from the 1999 survey. However, on several other aspects of the regulator's role, the balance of opinion was negative towards the FSA.

The majority with an opinion (two thirds of chief executives and compliance heads, three quarters of smaller organisations) felt that the FSA's powers were too extensive, which matched practitioners' fears about this in 1999). More practitioners disagreed than agreed that there were **sufficient safeguards in place** to ensure that the FSA was accountable for its activities, and the negative balance was particularly marked among smaller organisations. Responses followed a similar pattern for the statement 'The FSA operates independently of the government', with smaller organisations particularly likely to disagree.

Only around a third of chief executives and heads of compliance with an opinion agreed that the government had **listened to industry views** in its decisions about the FSA, falling to one in five smaller organisations. This contrasts with three-quarters of chief executives, two-thirds of compliance heads and six in ten smaller organisations who felt that the government had **listened to consumer** views in its decisions about the FSA.

All practitioners were asked to describe what they saw as the **most important priorities** for the FSA to address as the single regulator for the financial services industry. Most of the issues mentioned in response to this question had been identified in the qualitative interviews, and covered elsewhere in the questionnaire, but this provided an opportunity for practitioners to sum up their priorities overall.

The issues raised were mentioned by lower proportions of practitioners compared with the 1999 survey, when practitioners were being asked to think about the FSA's future agenda. The priorities most frequently mentioned in 2002, by around 8 or 9% of practitioners, were 'promote caveat emptor', 'build consumer confidence', and 'understand the diversity of regulation needed'.

As was the case in the 1999 survey, the main sources of information about the FSA were its own booklets and consultation papers. Compared with 1999, the FSA website has become a far more important source of information, now cited by two-thirds of compliance heads as a main source.

Only around a third of practitioners (a quarter of smaller organisation) had had telephone or face-to-face contact with frontline FSA staff, a lower proportion than in 1999. Practitioners indicated that they had had even less telephone or face-to-face contact with FSA policy makers with seven in ten chief executives and compliance heads and eight in ten smaller organisations having no contact at all.

7. Wider environment issues

Around seven in ten chief executives and heads of compliance and 85% of smaller organisations felt that there were too many regulatory reviews being undertaken of financial services. Two-thirds of practitioners felt that regulatory reviews should be carried out by the FSA and not by other government departments.

Of those who had an opinion, around three quarters of practitioners agreed that the boundaries between complaints handling by the Financial Ombudsman Service and policy setting by the FSA were unclear. There was no clear consensus as to whether the money laundering rules were clear and practical, with similar proportions agreeing and disagreeing.

There was general disagreement with the statement 'The behaviour of the FSA encourages competition to flourish within the UK', particularly so by smaller organisations where nearly seven in ten disagreed.

8. Views of the Financial Services Practitioner Panel

Around one in three chief executives, four in ten heads of compliance and a quarter of smaller organisations had seen or heard something about the Practitioner Panel before they received the letter about the survey. This result was similar to the 1999 survey.

Opinions of the Panel were generally positive; around 90% of practitioners who had seen or heard anything about the Panel thought it had an important role to play on behalf of the industry with the FSA.

Around 70% of practitioners who had seen or heard anything about the Panel felt it was helping the FSA to understand industry views and was independent of the FSA. Around 60% of practitioners felt that the members of the Panel could represent the industry as a whole.

Of those who had an opinion, around two-thirds agreed that the Panel was able to influence FSA policies and decisions. There were more mixed views on the ease with which firms were able to express their views to Panel members, with around half of practitioners who gave an answer agreeing that this was the case.

There were very few differences on these questions between chief executives, heads of compliance and practitioners from smaller organisations.

9. Differences by main area of operation

Generally speaking, practitioners from retail/ personal banks, smaller corporate/ investment banks, investment management firms and general insurance firms were the most positive in their views of the FSA and its performance. This was the case across most aspects of the survey.

Similarly, practitioners from IFAs and firms with life and pensions business were the most negative in their views of the FSA and its performance, almost without exception.

Practitioners from friendly societies and securities and derivatives firms were mixed in their views, being negative about some aspects (particularly in relation to guidance), but more positive on other aspects.

CONCLUSIONS

The 2002 survey of the FSA's regulatory performance was carried out a few months after the FSA assumed full responsibility for the regulation of the industry on 1 December 2001. The survey findings provide authoritative and up-to-date evidence of what the industry thinks of its new regulator. Because it builds on the first survey undertaken three years ago, this second survey is also able to identify how views of the FSA and of the regulatory environment have changed over time.

What firms expect from the FSA

In the 1999 survey, eight in ten practitioners were in favour of strong regulation, and felt that the UK regulatory system needed to change. A substantial proportion believed the new FSA regime would bring change for the industry, and the majority expected the change to be beneficial. They hoped the single regulator would ensure greater consistency and cohesion of regulation across all sectors of the industry, and that this would lead to greater efficiency and lighten the administrative burden. They were also hoping for a more pragmatic, risk-based approach to regulation.

A notable feature of the 2002 survey findings is the continued widespread support in principle for strong regulation, which most practitioners feel is for the benefit of the industry as a whole. In line with this, one of the most important requirements for practitioners is for the FSA to 'take a firm line' with non-compliant firms. An equally key requirement is for the regulator to provide reliable guidance when needed. In both the 1999 and the 2002 surveys, these were identified by practitioners as their two most important requirements.

Expectations versus reality

The overall view of the changes is that they have been beneficial for the financial services industry as a whole (of those expressing a view, approximately 2.5: 1).

Despite expectations remaining high and largely positive, there are signs of a widening gap between the expectation and the experience of regulation. Practitioners now feel more strongly than in 1999 that the burden of regulation on the industry is too great, and the majority think too much weight is being given to the interests of consumers. Views about the impact of the change on the industry as a whole, although still positive, are less so than they were three years ago about the expected change.

When asked about the impact of the change to the FSA on their own business, those who gave an answer were twice as likely to say that things had got worse as to feel they

had got better - again, taking a more negative view about the actual experience than their counterparts predicting the impact of the change in 1999.

There are continuing concerns about the powers and accountability of the FSA, its independence from government and the attention being given by the government to consumer, rather than industry views.

Aspects of firms' experience to date

In the more detailed analysis of firms' experience of regulation, the areas of more specific concern become clear:

Consultation

As in the 1999 survey, the new regulator is given credit for making a lot of effort to consult the industry, and more practitioners now feel there has been sufficient feedback from these exercises. Concerns still remain about the same issues that were felt to be problematic in 1999: the length of the consultation papers, the time needed to consider them, and the general effectiveness of the whole process.

The provision of guidance

The largest gap between what practitioners consider important attributes for the FSA to demonstrate and the regulator's perceived performance is in providing reliable guidance. This also gave rise to the largest gap in the 1999 survey, when most practitioners were commenting on their previous regulator, and there were high hopes that the change to a single regulator would result in clear, concise and unambiguous guidance to practitioners, based on broad principles rather than narrow rules.

What has actually happened since the FSA took over is a reduction in the perceived clarity and consistency of the guidance being provided - or, in some cases, guidance not being provided at all. Although the regulator is given some credit for putting the emphasis on prevention rather than enforcement, many practitioners complained about the FSA's apparent inability or unwillingness to provide definitive guidance promptly, or to provide guidance informally without involving legal advisors.

Supervision

Among practitioners who have sufficient experience to comment on the FSA's approach to supervision, the balance of opinion is generally positive, although

less so than in the previous survey when most practitioners were considering their previous regulator. Seven in ten feel the FSA is applying a reasonable level of supervision to their business, and six in ten see the regulator as willing to hold a dialogue with them about compliance issues. On the other hand, over three quarters believe the FSA tends to look at processes rather than outcomes, and less than half feel the regulator has a good understanding of their business. In most cases, practitioners who expressed an opinion had more negative views about their regulator than in the 1999 survey.

The quality of FSA supervisory staff

At the time of the 2002 survey, only around half of practitioners had any direct experience of dealing with FSA supervisory staff. The views of these practitioners about FSA staff are often positive, particularly in relation to the frequency of site visits, the interpersonal skills of FSA staff and the way they treat practitioners' staff. On the debit side, a substantial proportion of practitioners say that FSA staff just tend to follow a checklist rather than broad issues of principle, and that the approach varies depending on the individual.

The Handbook

There is strong criticism of the new FSA Handbook of Rules and Guidance. A large majority find the Handbook difficult both to navigate and to understand. There is a widespread feeling in the industry that the FSA has got it wrong in terms of the level of detail, and that the transition to the new set of rules has not been managed well.

The impact of N2

There is evidence that the impact of N2 has been felt right across the industry with nine in ten practitioners reporting some change in the regulation of their business which they attribute to the creation of the FSA. Practitioners' views on the impact of this change on their business are notable for the sizeable proportion - two in five - who feel it is 'too early to say'. Of the remainder, the general feeling is that things have got worse rather than better. Another area of concern is the increased cost of compliance; more practitioners than in 1999 feel their compliance costs are excessive.

The scale of future change

What is perhaps unexpected is that, six months after N2, the transition is seen by most of the industry as far from complete, with two thirds of practitioners

expecting further changes in regulation. Another indication of the perceived incompleteness of the transition is practitioners' views on the ongoing costs of compliance in the future - two thirds expect ongoing costs to be higher than before the 'N2 bulge'.

Other issues

A large majority of practitioners feel there are too many regulatory reviews being undertaken of financial services, and two-thirds believe such reviews should be carried out solely by the FSA and not by other government departments.

The boundaries between complaints handling by the Financial Ombudsman Service and policy setting by the FSA are generally seen as unclear, with around three quarters of practitioners taking this view.

Overall view of FSA's performance as a regulator

The FSA is given credit for being as open and responsive as possible in the way it is operating. It is also seen as a strong regulator, attracting its highest performance rating for taking a firm line with businesses which persistently break the rules. But on this, as on other aspects, practitioners' assessments of the performance of the FSA are generally less favourable than similar assessments made in the 1999 survey of the financial regulators who were operating at the time. Wider gaps are also opening up between what practitioners identify as important, and how they perceive the FSA's performance, in particular on providing reliable guidance when needed, having efficient administrative procedures, and interpreting rules in a flexible common-sense way - all areas in which hopes of the FSA were particularly high in 1999. The FSA's application of the rules is seen as being rigid rather than flexible.

As already noted, a substantial number of practitioners have had little contact as yet with the FSA and were therefore unable to give an answer to some of the questions, particularly those relating to guidance, supervision, and the overall effect of the change of regulator on their own business. In many respects, it is still 'early days' for the FSA.

It would, therefore, be premature to say that the overall view is turning negative, but there are signs that it could, and this would be in spite of a generally positive attitude by the industry towards the new regulatory regime.