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cc: Cabinet
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288

10 DOWNING STREET

From the Private Secretary

18 January 1984

Dear Callum,

GOWER REPORT ON INVESTOR PROTECTION

The Prime Minister has seen your letter to John Kerr of 13 January. She is content with the Press Notice which your Secretary of State will be issuing when the Gower Report is published.

I am sending copies of this letter to the other recipients of yours.

Yours sincerely

Andrew Turnbull

Andrew Turnbull

Callum McCarthy, Esq.,
Department of Trade and Industry.

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NBPM
AT
18/1

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

17 January 1984

M C McCarthy Esq
Private Secretary to the Secretary of State
for Trade and Industry
Department of Trade and Industry
1 Victoria Street
LONDON SW1

New Callum,

with AT

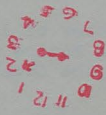
GOWER

Thank you for your letter of 13 January. The Chancellor is content with the Press Notice which your Secretary of State intends to issue when the Gower report is published on 18 January.

Copies of this letter go to the other recipients of yours.

*Yours ever,
J O Kerr*

J O KERR



17 8 JAN 1984



Prime Minister ①
 Agree to Tabbitt's response to
 Gower
 (i) welcoming but
 (ii) not committing HMG?

cc NO
 (without attach)

DEPARTMENT OF TRADE AND INDUSTRY
 1-19 VICTORIA STREET
 LONDON SW1H 0ET
 Telephone (Direct dialling) 01-215 5422
 GTN 215
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AT
 17/11

JU422
 Secretary of State for Trade and Industry

13 January 1984

J Kerr Esq
 HM Treasury
 Parliament Street
 London SW1

Dear John,

GOWER REPORT ON INVESTOR PROTECTION

The Chancellor and other colleagues mainly concerned agreed that the first part of the Gower Report on Investor Protection should be published as a Command Paper. I am accordingly now circulating proof copies together with the preface by my Secretary of State which will be incorporated, a summary compiled by Professor Gower himself and the draft Press Notice which we propose to put out at the time of publication.

2 My Secretary of State is sympathetic to the thrust of the Report but does not propose to commit himself to any further action until we have had the reactions of the interests concerned. His preface accordingly seeks comments by the end of April 1984. The Press Notice does, however, contain an indication of his sympathy for a regime based so far as possible on self regulation within a statutory framework.

3 Publication is planned for January 18.

4 Copies of this letter and attachments go to private secretaries of all Cabinet colleagues, and to Richard Hatfield.

Yours ever,

Callum

CALLUM McCARTHY
 Private Secretary

Encs

DRAFT PRESS NOTICE

PUBLICATION OF GOWER REPORT ON INVESTOR PROTECTION

A new and comprehensive statutory framework within which self regulation would be applied extensively in the securities industry is recommended to the Government in a report by Professor L C B Gower published today in a Command Paper (Cmnd). The intention of the report's recommendations is to provide greater protection for both private and professional investors. This is the first and main part of Professor Gower's Report and gives his analysis and recommendations. Part 2, giving a draft for a Parliamentary Bill which he would propose in order to give effect to his recommendations, is to follow later.

2 Professor Gower proposes a new Investor Protection Act which would provide for the overall regulation of investment business to be undertaken by Government or a Government agency, but with day-to-day supervision undertaken so far as possible by self regulatory bodies recognised for the purpose by Government. Professor Gower also recommends that the marketing of life insurance be made subject to a more extensive degree of regulation than at present; existing insurance supervision, essentially concerned with insurance companies' solvency, would remain unchanged.

3 The Secretary of State for Trade and Industry, Mr Norman Tebbit, MP, said today:

"I call on all concerned to consider Professor Gower's proposals in a constructive and positive spirit, remembering that his present report is already based on extensive consultation with interested parties.

The securities industry in its many ramifications is an important wealth creating sector of our economy. The experience of recent years has shown the need to review, and where necessary, strengthen, arrangements for protection of investors, but this should be done so far as possible in ways consistent

with the liberal and innovative traditions of the City, which have fostered efficiency, enterprise, and competitiveness. Professor Gower's principle of self-regulation within a framework of statutory supervision may well be a way forward. Professor Gower is to be congratulated on providing us with a comprehensive survey, and a coherent set of proposals for consideration which reflect extensive research and discussion. To have done this, as he has, virtually single handed is a prodigious achievement, which deserves the thanks and admiration of all".

4 In a foreword to the Command Paper Mr Tebbit invites comments on Professor Gower's recommendations not later than 30 April 1984, after which the Government will decide and make known their intended course of action. Comments should be addressed to the Assistant Secretary (Gower Report), Department of Trade and Industry, Room 504, Sanctuary Buildings, 16-20 Great Smith Street, London SW1P 3DB. Copies of the Report are obtainable from H M Stationery Office, price £

P R E F A C E

I present to Parliament herewith the first and main part of the Report by Professor L C B Gower entitled Review of Investor Protection. Part 2, giving a draft for a Parliamentary Bill which he would propose in order to give effect to his recommendations, is to follow later.

2 The proposals in the Report are Professor Gower's and Ministers will now be considering them. To help in this I invite interested parties to submit comments on Professor Gower's recommendations not later than 30 April 1984 after which the Government will decide and make known their intended course of action. I hope that all those concerned will consider Professor Gower's proposals in a constructive and positive spirit remembering that his present report is already based on extensive consultation with interested parties.

NORMAN TEBBIT

NOTE

Comments should be addressed to the Assistant Secretary (Gower Report), Department of Trade and Industry, Room 504, Sanctuary Buildings, 16-20 Great Smith Street, London SW1P 3DB

REVIEW OF INVESTOR PROTECTION

SUMMARY OF PART I OF PROFESSOR GOWER'S REPORT

Part I of Professor Gower's Report on his independent Review of Investor Protection in Relation to Dealings in Securities and Other Property is published today. It consists of his narrative Report and ninety-two Recommendations. Part II, containing a Draft Bill and notes on its clauses, is in preparation and will be published separately later in the year.

Chapter 1 of the Report describes the procedure adopted in relation to the Review and the philosophy on which the recommendations are based; namely, to provide the essential minimum of regulation needed to protect investors from being made fools of, but not to attempt the impossible task of preventing them from making fools of themselves.

Chapter 2 summarises the basic framework envisaged: see para 2.11. This follows the general lines of the Discussion Document published in January 1982, i.e. regulation of those engaged professionally in investment business under an Act (The Investor Protection Act), replacing, with a wider coverage, the Prevention of Fraud (Investments) Act 1958 and providing for a comprehensive system based, so far as possible, on self-regulatory agencies recognised by, and under the surveillance of, a Government Department or Agency. In the light of the consultations Professor Gower now accepts that, in view of the way in which the investment industry has developed, initially such self-regulatory agencies will have to be based on existing professional institutions rather than on functional criteria and that in consequence there will inevitably be more than the four large agencies envisaged in the Discussion Document, that not all those requiring registration will be members of any of them, and that those who are not will have to be regulated directly by the Government or a Government agency.

Chapter 3 discusses the relative advantages and disadvantages of leaving the Government role wholly to the Department of Trade and Industry or of setting up a self-standing Commission answerable to the Secretary of State. It concludes that if, when legislation is introduced, it is apparent that most firms will secure registration through membership of a recognised agency, so that surveillance of the self-regulatory agencies will be the main Governmental task, it could be undertaken by the Department but that otherwise a self-standing Commission would be preferable.

Chapter 4 deals with the scope of regulation under the Act and recommends that in principle this should cover all marketing activities (including investment advice) relating not only to "securities" but also to other investments such as those in commodity or financial futures, pooling arrangements or contracts linked to life insurance, but not in physical objects over which the investor will secure exclusive control. To give precision, with the necessary flexibility, to this principle, "investments", "securities" and "investment business" would be defined in the Act but with power to add to or subtract from the definitions, either generally or for particular purposes, by Regulations subject to an affirmative resolution of both Houses of Parliament in the event of additions. Employees would not require to be individually registered except for those engaged to advise on, or manage the investments of, pension funds or public investment trust companies. The Chapter also considers the extent to which the same protection should apply to professional as to private investors and recommends that there should be no distinction except for the retention of greater freedom to circulate investment information to "professionals", defined so as to prevent the abuses to which the present "professionals only" exemption has led.

Chapters 5 & 6 discuss matters relating to the suggested self-regulatory agencies. In Chapter 5 it is recommended that, while recognised, their rules and codes of conduct should be immune from competition law, that they should be entitled to apply for subpoenas to compel production of evidence needed in connection with their disciplinary proceedings, and that information interchanged by the agencies in the exercise of their regulatory powers should enjoy specific protection from suits for defamation or breach of confidence. Chapter 6 recommends that bodies might be recognised either as investment exchanges, or as agencies for the regulation of the conduct of their members' investment business, or as both, and that it should be an offence to purport to be carrying on business in the UK as an investment exchange unless recognised as such by the Secretary of State after consultation with the Bank of England. Recommended criteria for recognition, whether as an investment exchange or as an agency, are suggested. They would include satisfying the Department (or Commission) that the agency's rules: did not impose restrictions on competition greater than were needed for the adequate protection of investors and the orderly conduct of the relevant business or market; provided protection for investors at least equal to that afforded by the Rules of the Department (or Commission) applying to those registered directly; and would be adequately monitored and enforced by the agency. If the Government regulator was the Department, an expanded role is envisaged for a strengthened Council for the Securities Industry as co-ordinator of the self-regulatory side of the system and the link between it and the Governmental side.

Chapter 7 deals with direct registration, with the Conduct of Business Rules to which those so registered would be subject, and with the maintenance of a comprehensive computerised register (open to public inspection) of all those registered for investment business, whether directly or through membership of a self-regulatory agency.

Chapter 8 discusses problems relating to the two main types of collective investment undertakings - insurance-linked investments and unit trusts or mutual funds. Among the many recommendations are those designed: to control more effectively the activities of unauthorised life offices and of insurance intermediaries; to relax the present tight Departmental control of the authorisation of unit trusts, delegating this to a recognised self-regulatory agency established by the industry; to permit the incorporation in the UK of mutual funds; and to harmonise the types of underlying investment permissible, whether offered through unit trusts, mutual funds or insurance-linking. Other recommendations are: that the Secretary of State should be empowered to promulgate regulations controlling the maximum commissions payable to tied or independent intermediaries and that this power should be exercised to the extent necessary to enable effective control to be exercised so far as possible through self-regulation by the industry; that unsolicited "cold-calling" for sales of investments should be prohibited by the Act except to the extent allowed by Regulations, which should permit it in respect of authorised life insurance or unit trusts but not otherwise; and that the ten-day "cooling-off" period should be extended to cover sales of single-premium policies and of trust units, but that, in their case, the investor should be entitled to the return only the lesser of what he had paid or would have had to pay had he bought on the day of cancellation.

Chapter 9 deals with public issues of securities, takeovers, and insider-dealing and recommends that the statutory provisions on these matters should be transferred, in a modernised form, from the Companies Acts to the Investor Protection Act. While no substantial amendments are recommended in respect of insider-dealing, a harmonised system is suggested for regulating invitations to the public whether on an issue or a takeover. The case for pre-vetting of prospectuses and for subsequent surveillance of the companies concerned and of any market-makers in the securities is stressed, particularly in the light of

the statistics in paragraph 9.17 which show that some 30% of filed prospectuses relate to securities which are not to be officially listed or dealt in on the USM - a percentage which is likely to increase in the light of the Business Expansion Scheme. A system is recommended whereby supervision would be exercised by The Stock Exchange, in respect of listed or USM securities, and by the CSI and the Takeover Panel in respect of issues undertaken through members of self-regulatory agencies represented on the CSI.

Chapter 10 discusses offences and enforcement. It recommends: substantial changes to the present prohibition on the issue of investment circulars and advertisements; enhanced powers to obtain information, and to control the activities of investment firms in financial difficulties; greater co-ordination between the various authorities, with the primary aim of putting the unfit out of business as rapidly as possible; enhanced civil remedies; and re-consideration of the methods of trial for commercial fraud.

The concluding Chapters 11 and 12 draw attention to various matters which may need attention by others and discuss the geographical coverage of the proposed Act which, it is recommended, should be introduced as a UK Act. Throughout the Report emphasis is laid on the need to tackle effectively the "off-shore" problem and to encourage reciprocal arrangements between countries having effective regulatory systems.