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STATEMENT FOR THE SECRETARY OF STATE

With permission, Mr Speaker, I wish to make a statement about the Government's proposals to establish a new regulatory framework for the financial services industry. These proposals are published in a White Paper which I have today laid before the House and, subject to the Parliamentary timetable, I plan to introduce a Bill in the next Session for their implementation.

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3 A prerequisite for an internationally competitive industry is a clear regulatory framework within which practitioners and customers can deal with confidence, and which safeguards the interests of investors. This regulatory framework must be capable of adjusting to changes in the shape of the markets, and of accommodating rather than stifling innovation.

4 This, the proposals set out in the White Paper are designed to achieve. They will assist enforcement, deter fraud and malpractice, improve disclosure and lay down the principles on which business should be conducted. The

proposals cover both a new regulatory framework and a new institutional structure through which it will work.

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Secretary of State for Trade and Industry

29th January 1985

C Marshall Esq
Private Secretary to the
Lord Privy Seal and Leader
of the Commons
Privy Council Office
Whitehall
London SW1

Dear Charles,

FINANCIAL SERVICES WHITE PAPER

-will request if required.
I wrote to you on 22 January to warn you of my Secretary of State's intention to make a statement introducing this White Paper today. I now attach a copy of the statement my Secretary of State shall make.

2 I am copying this to Tim Flesher (PS/No 10), Murdo Maclean (PS/Chief Whip), Chief Press Secretary (No 10) and Margaret O'Mara (Treasury).

Yours sincerely,

Maureen Dodsworth

MAUREEN DODSWORTH
Private Secretary

JH2AEC

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Ref: 55

29 January 1985

FINANCIAL SERVICES WHITE PAPER PUBLISHED

The Rt Hon Norman Tebbit MP, Secretary of State for Trade and Industry today announced the Government's proposals to establish a new regulatory framework for the financial services industry. These proposals are set out in a White paper "Financial Services in the United Kingdom: A New Framework for Investor Protection" (Cmnd 9432) published today.

The theme is self-regulation within a statutory framework. This will provide for investor protection while at the same time allowing the UK financial services industry to operate efficiently and competitively.

Legislation is planned for the 1985/6 Parliamentary session which will:

- make it a criminal offence for any firm to engage in investment business without being authorised as "fit and proper" to do so. Only those judged "fit and proper" will be authorised to carry on investment businesses.

- define investments and investment business comprehensively, to cover all types of security and to include for the first time financial and commodity futures and options.

- enable the Secretary of State to delegate the power of authorisation to one or more private sector bodies composed of practitioners and users of financial services. The Secretary of State intends to do this.

The White Paper envisages two bodies: a Securities and Investments Board, covering the regulation of securities and investments, and a Marketing of Investments Board, covering the regulation of marketing of pre-packaged investments such as life insurance and unit trusts. If the financial services industry and its customers subsequently prefer a single body, the Government would consider this.

- These boards, and other self-regulatory bodies that they decide to recognise, will be responsible for formulating and enforcing rules of conduct for those they authorise to carry on investment business;

- the boards, which will be financed by the industry, are to be set up in the near future on a voluntary basis, so that the regulatory structure can be in place and operating by the time that the legislation providing the statutory framework is enacted;
- the boards will have the power necessary for them to be effective regulators. There will be safeguards designed to combine the benefits of an effective practitioner-based system with accountability to Government and Parliament including:
 - i) appointments to the Boards will be by or with the agreement of the Secretary of State;
 - ii) the Secretary of State will be empowered to get the bodies to change their rules if, on the advice of the Director General of Fair Trading, he believes that they are anti-competitive, or if they conflict with international obligations;
 - iii) a right of appeal by investment businesses to an independent tribunal appointed by the Secretary of State.

Speaking today in the House of Commons, Mr Tebbit said:

"With permission, Mr Speaker, I wish to make a statement about the Government's proposals to establish a new regulatory framework for the financial services industry. These proposals are published in a White Paper which I have today laid before the House and, subject to the Parliamentary timetable, I plan to introduce a Bill in the next Session for their implementation.

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NOTES TO EDITORS

1. "Financial Services in the United Kingdom. A New Framework for Investor Protection". Cmnd 9432. HMSO £4.65.
2. The framework proposed for City Regulation was outlined by Mr Alex Fletcher, Minister for Corporate and Consumer Affairs in a statement on October 17 1984.
3. "Review of Investor Protection: A Report. Part 1." Professor LCB Gower. Cmnd 9125. HMSO £9.90. Was published in January 1984.

4. An interim document entitled 'Review of Investor Protection. A discussion document' by Professor Gower was published in January 1982. HMSO £6.60.

5. Professor Gower was commissioned by Mr John Biffen the then Secretary of State for Trade, in July 1981, to carry out an independent review of investor protection.

WHITE PAPER ON FINANCIAL SERVICES IN THE UNITED KINGDOM

- A new Framework for Investor Protection

SUMMARY OF THE MAIN PROPOSALS

Norman Tebbit, the Secretary of State for Trade and Industry, today publishes a White Paper setting out proposals for legislation to reform the regulation of investment business. The main elements of the proposals are as follows:

THE REGULATORY SYSTEM

The new regulatory system will have the following features:

a definition of "investments", which will include in addition to securities covered by the Prevention of Fraud (Investments) Act 1958 (the "PF(I) Act"), the whole range of financial and commodity futures and options contracts, and certain other products. The definition of investments will exclude property which passes under the direct physical control of the investor if purchased (eg commemorative medals). The Department of Trade and Industry will continue to be responsible for the prudential supervision of insurance companies; the marketing of life assurance contracts will be treated as far as possible on the same footing as other similar investments;

a definition of "investment business" which will include, for example, any business which effects transactions in investments with or for others, manages investments (including unit trust schemes) or gives advice about them. There will be various exclusions including companies issuing their own shares, newspapers, and investment clubs. Individuals will not be included unless they propose to carry on investment business as sole traders;

provisions making it an offence to carry on investment business as defined without authorisation; and

provisions giving the Secretary of State authority - which he will be empowered to delegate to regulatory bodies which appear to him to satisfy criteria laid down by the legislation - to grant, vary, make subject to conditions, suspend or revoke such authorisation and to lay down requirements for the conduct of business by those authorised. These requirements will include the application of a "fit and proper" test to all investment businesses: sole traders, partnerships and corporate entities.

Rules for the conduct of business will be based on principles set out in the legislation. These new principles are based largely on existing good market practice in the UK and USA. They are as follows:

i. safeguards against abuses arising from conflicts of interest. For all investment business, this will entail:

- a principle of fair dealing;
- a duty of skill, care and diligence; and
- a duty of disclosure.

For agency business, this will entail in addition:

- a 'best execution' principle; and
- a 'subordination of interest' principle.

ii. protection of clients' assets, whether money or documents of title.

iii. compensation for investors.

iv. investment and dealing recommendations should be adequate and reasonable, having regard to the nature of the investment and the circumstances of the client.

v. disclosure of the terms of business to customers.

vi. the keeping of proper records.

vii. arrangements to ensure the orderly conduct of business.

CRITERIA FOR DELEGATION BY THE SECRETARY OF STATE

The main criteria for delegation will be that:

the body's proposed requirements are such as to ensure that those authorised by it are and remain "fit and proper" to carry on investment business;

its proposed conduct of business rules will afford adequate protection to investors and are consistent with basic principles set out in the legislation; and

all these rules would not impose restrictions on competition greater than are justified for the adequate protection of investors.

INSTITUTIONAL STRUCTURE

The Government favour practitioner-based regulation within a statutory framework. The arrangements recommended by the Governor of the Bank of England after consultation with leaders of City institutions, and by representatives of the life assurance and unit trust industries, envisaged two

practitioner-based regulatory bodies, a "securities and investments board", and a "marketing of investments board" covering in particular life assurance and unit trusts. However, the legislation will in no way prevent delegation to a single practitioner-based regulatory body.

There will be provision for the Boards to recognise membership of self-regulatory organisations such as The Stock Exchange, the National Association of Security Dealers and Investment Managers, the Association of Futures Brokers and Dealers and the Insurance Brokers Registration Council as providing the authorisation required for an investment business.

ACCOUNTABILITY TO GOVERNMENT AND PARLIAMENT

The Government propose the following:

the Chairman and members of the Board or Boards will be appointed by the Secretary of State or with his agreement.

Board members will include users and other lay members as well as practitioners.

the Secretary of State will be entitled to withdraw regulatory authority if he considers that at any time a Board ceases to conform to the criteria set out in the legislation.

a Board's rules and practices will be subject to initial and continuing scrutiny for anti-competitive elements; the Secretary of State will have power to require the amendment or withdrawal of rules after obtaining the advice of the Director General of Fair Trading.

the Secretary of State will have power to require the amendment or withdrawal of the rules of the Boards if they are contrary to the international obligations of the United Kingdom.

the Boards will report annually to the Secretary of State who will lay their reports before Parliament.

there will be provision for a new and independent tribunal, whose members will be appointed by the Secretary of State, to be the final determinant of any dispute about authorisation decisions or about penalties for breach of the rules.

UNIT TRUSTS

The present controls will be relaxed to allow a greater variety of unit trusts to be made available to the general public and more speculative arrangements to be offered (and promoted) to authorised businesses, and by them to those investors who have appropriate financial resources and experience.

INVESTMENT ADVICE AND THE MARKETING OF INVESTMENTS

Investment advisers, including those who market life assurance or units in unit trusts, will be subject to the conduct of business principles. They will be under a duty to disclose "relevant information" including any material interest they have in a recommendation - for example commissions or other reward which they might receive from other parties. This will enable investors to make more informed decisions.

Under the PF(I) Act it is already a criminal offence to make misleading, false, deceptive or reckless statements or forecasts about investments. The new legislation will extend this provision to cover acts or courses of conduct likely to defraud or deceive investors or potential investors.

PENSIONS

There will be a requirement to disclose comprehensive information about the way pension scheme assets are invested. Any investment manager or adviser involved in the administration of pension schemes as a business (ie other than simply as an employee) will require authorisation. On the regulation of personal pensions the intention is that these should be subject at least to the same safeguards as other forms of investment.

ADVERTISEMENTS AND CIRCULARS

Only authorised investment businesses will have a statutory right to issue advertisements or circulars likely to lead to the sale or purchase of investments. 'Advertisements and circulars' will be defined to include all media. "Cold-calling" will not be banned for the sale of investment products where a cooling off period can be provided.

PUBLIC ISSUES AND TAKE-OVERS

The legislation will provide that all public offers of securities, primary or secondary, including offers made on take-over bids, will be subject to the same statutory regime. All offers to the public will have to comply with requirements regarding their contents, unless specifically exempted. The minimum contents of prospectuses will be set out in regulations made by the Secretary of State.

If the securities market felt that it would be helpful, the Government would be willing to consider providing statutory backing for the City Panel on Take-overs and Mergers.

INSIDER DEALING

The legislation will extend the insider dealing provisions of the Companies Act 1980 to cover all securities, including options and futures contracts based on them, and also to make enforcement more effective.

ENFORCEMENT

The regulatory Board (or Boards) and its recognised self-regulatory organisations will be responsible for enforcing their respective rules. The Department of Trade and Industry and the prosecution authorities will be responsible for enforcing the criminal law. There will be provision for civil law remedies for loss due to breach of the criminal law or of rules of business conduct. Finally, to facilitate the enforcement of these civil law rights, the Government propose powers for the Secretary of State (which he could delegate) to seek injunctions and 'disgorgement orders' against businesses in breach of the criminal law, the rules of the Boards or those of recognised self-regulatory organisations.

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NBPM

AT 281

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

28 January 1985

Mr M C McCarthy
Principal Private Secretary to the
Secretary of State for Trade and Industry
Department of Trade and Industry
1 Victoria Street
London SW1H 0ET

Dear Colman,

WHITE PAPER ON FINANCIAL SERVICES

The Chancellor was grateful for your Secretary of State's letter of 21 January, which reassured him on most of the points raised in his letter of 15 January.

The Chancellor is very concerned that in the event of the two supervisory bodies currently envisaged agreeing to coalesce into one, no further primary legislation would be needed to take account of the change. I understand from previous correspondence that there is no problem on this, but would be grateful for your categorical reassurance.

Secondly, it is not clear from paragraph 7 of your Secretary of State's letter that you do not in fact intend to legislate for 100 per cent compensation. Mr Tebbit may like to know that there is at present no statutory compensation for depositors and shareholders of building societies; the societies are pressing him to make the present 90 per cent voluntary scheme part of the statutory arrangements. Can you clarify this point?

I am copying this letter to Tim Flesher (No.10), the Private Secretaries to other Members of Cabinet, Henry Steel (Law Officer's Department), Murdo MacLean (PS/Chief Whip), Alex Galloway (Paymaster General's Office) and Richard Hatfield (Cabinet Office).

*Yours ever
Lomax.*

MRS R LOMAX
Principal Private Secretary