

LIBA

LONDON INVESTMENT BANKING ASSOCIATION

ANNUAL REPORT

2001

LIBA is the principal trade association in the United Kingdom for firms active in the investment banking and securities industry. The Association represents the interests of its Members on all aspects of their business and promotes their views to the authorities in the United Kingdom, the European Union and elsewhere.

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STATEMENT BY THE CHAIRMAN

As your Chairman since March 2002, my first task is to thank my predecessors, Michael Marks of Merrill Lynch and John Nelson of CSFB, for their work for LIBA. Both gave unselfishly of their time and skill. The reports which follow cover the period up to the end of February 2002 for the most part. The Association's very considerable achievements over that period owe much to them.

Where do we stand?

City historians are likely to say that, by the end of 2001 international issues had started to overtake our crowded domestic agenda. That change coincided with the typical end of a bull market, exacerbated by the World Trade Centre attacks last September, which directly affected many of our Members.

The authorities have found themselves under acute pressure at every level – national, European, worldwide – to investigate, reform, and regulate more effectively; and to “tackle”, “address” or “deal with” the various alleged crises, problems, failures or weaknesses which preoccupy public opinion. One result is a torrent of inquiries and policy making, not all sensibly motivated, well informed or wisely conducted, and investment banking is sometimes at or near its centre. Consulting markets and their users is essential in any such policy reviews. Happily in Britain, at least, the authorities often consult the industry thoroughly. This confronts us with invitations we cannot afford to refuse. Where consultation about policy is poor, the danger of bad policy can often be greater – in which circumstances representing our interests effectively to the authorities can be even more important, and is certainly harder. This task stretches major financial service businesses and their associations to the uttermost at the best of times. In a period of falling income, rationalisation, structural change, heightened competition and rising public concern, the challenge is greater still. So organisations like LIBA now have to do more, do it faster and in more places in order to safeguard Members' interests.

Experience in the last year has thrown up many important pointers to our future priorities.

Domestic Regulatory Development

Even after Ministers' belated postponement of N2 to November 2001, implementing the Financial Services and Markets Act (FSMA) challenged all parties to the limit. The 90 or so Statutory Instruments (SIs) needed and the associated FSA provisions were made just in time. However this was only made possible by setting very short deadlines for SI consultations, much less than the 3 month minimum set by the Cabinet Office in its guidance on good consultation practice. The price of cutting corners like this is, inevitably, errors and defects. We have emphasised to the Treasury that it is vital to correct important errors in the SIs quickly and to establish a process for keeping the legislation up to date. There were problems with some of FSA's consultations, too, as is explained in the Report of our Chairman's Committee which follows. We hope that in the future FSA will respond more quickly and sensitively to Members' concerns.

“Project Arrow”, the FSA's new regulatory approach, is still in its infancy. While the first signs are encouraging, its soundness can only be judged when the enforcement regime which complements it has settled down. The omens have been mixed. One important element in the enforcement process is the so-called FINSMAT, the Financial Services and Markets Tribunal which will consider

appeals against FSA disciplinary decisions. The introduction in July of the rules for this Tribunal by the Treasury and Lord Chancellor's Department has established a presumption of public hearings, in contrast with previous practice and despite Ministerial assurances to the contrary during debates in both Houses of Parliament. The serious danger of reputational risk to innocent parties in the financial sector is likely to close this important avenue of appeal to significant numbers of firms and individuals in a most unfair way. LIBA led a sustained and systematic campaign to have the rules modified, culminating in a motion in the House of Lords which was only narrowly defeated.

The FSA is also playing an increasingly important role in the development of international regulatory policies, both by Europe and Basel. Happily the collaboration between FSA officials and LIBA has generally been exemplary in these areas.

EU Developments

The most important event in a year of great activity was the European Union's adoption of the Lamfalussy recommendations. The creation of new European machinery for real transparency and open consultation about policies for the single financial market is an enormous step forward. But it will call for markedly greater efforts by all of us if it is to be exploited properly. To that end we have already collaborated with, and often co-ordinated, an expanding group of European and International associations, in work both on the Lamfalussy machinery and a succession of major policies.

The urgent need for these reforms was all-too vividly demonstrated when, prompted no doubt by the naïve importunities of governments, the European Commission prematurely launched two major directives last summer, on Prospectuses and Market Abuse, each seriously defective. After prolonged representation and negotiations involving many Associations and firms, both directives have been substantially improved. However they are still far from perfect. The one consolation is, perhaps, that this sorry saga has underlined to the wider world more tellingly than any representation or press report how essential consultation can be.

That said, consultation is necessary, but not sufficient. In addition the Commission needs more qualified staff and better access to market expertise to cope with the looming cascade of policy initiatives. I have made offers to Commissioner Bolkestein, on our behalf, to try to provide help with secondments where market experience and skills are needed. The Commission have not responded to these initiatives so far. We must hope that they will recognise their value before long.

Looking ahead, we can now discern the probable overall consequences of effective consultative and rule-making machinery (at last) and pressures to cut the backlog of pending measures which affect our Members – particularly but not only the remaining policies in the Financial Services Action Plan. Over the coming year and a half, their combination will probably generate *twenty* or more distinct directives, initiatives and measures of European policy. Some will call for work in Brussels; some will necessitate “transposition” into British law and practice; *each* will almost certainly necessitate a great deal of effort. Taken together, these changes will be like a tidal wave. My greatest and most urgent priority is to ensure that this Association and its Members can handle these many challenges effectively!

International Capital Adequacy Proposals

Last year both Basel and the Commission published a second round of consultative and other important policy papers. We responded in close and productive liaison with the British Bankers' Association (BBA) and the International Swaps and Derivatives Association (ISDA), with whom we intend to continue to collaborate. For our Members it is essential to ensure that the policies and procedures Basel and the EU adopt are fair and based on a thorough study and understanding of investment banking and its characteristics.

Business Continuity

As the horrors of September 11th begin to lose their immediacy, there is a risk that we begin to take for granted the extraordinary resilience and skills – and contingency plans – which, despite their imperfections, enabled Wall Street to re-establish activity so quickly and effectively. LIBA Members' New York offices were amongst those most affected. This makes us consider particularly carefully what steps we should take in London to apply the lessons of New York. We have therefore kept in active touch with the FSA, the Bank of England, the Treasury and the City Corporation. Our goal has been to establish channels for effective communication, the *sine qua non* when planning for potentially very large crises whose nature and location is unforeseeable. Some useful progress has been made. Filling the remaining gaps is a high priority.

Better Consultation

At a time when laws, regulations and policies are the object of constant change, full and measured consultation and openness have never been more important. Consultation standards in the UK are generally much higher than elsewhere, and in many areas have been getting better for many years. Latterly the ground rules adopted by the FSA – which Michael Marks rightly commended to you in previous years – have not only remained admirable for the most part, but have generally provided an extensive and compelling example to our partners in Europe even if practice occasionally falls short. The “Code of Consultation” promulgated in 2000 by the British Cabinet Office for Government Departments and (to a lesser and uncertain degree) other public agencies has also set very good if not perfect standards. The Committee of European Securities Regulators (CESR) has also adopted a commendable “Statement of Consultation Practice”.

Unfortunately much more needs to be done. The European Commission and Council of Ministers have a long way to go, even if there is (very belated) promise of reform arising from the important and much neglected Consultation on the European White Paper on Governance. At home, the Treasury has consistently cut short the Cabinet Office guidance on deadlines for consultations on the Statutory Instruments implementing the FSMA as I noted earlier. The record of other major departments is also patchy, if improving. Some agencies – of which the Information Commissioner is the most striking recent example – give the impression that they believe the Consultation Guidelines do not and should not apply to them at all.

Since full adherence to proper consultation procedures is essential if we are to continue to do our job of representing Members' interests, Adam Ridley and I will be devoting special efforts to ensuring that reasonable standards are maintained!

Staff and Administration, Relations with Members

LIBA has always operated with a small staff, and has so far managed to handle the growing burden of work without many extra directors and without sacrificing the high quality of their work. This has of course been possible only because of the very active participation of many members in our Committees and Working Groups. Their expertise and involvement gives our views and representations a combination of expertise and authority which is invaluable. We have also received valuable assistance from Allen & Overy, Mishcon de Reya, Norton Rose and Slaughter and May in our work on the FSA's draft conduct of business and listing rules. That said, there are inevitably policy areas where we have been able to do little work although our Members' interests are potentially at stake, such as the Government's reviews of Company Law and Insolvency. This self-discipline has permitted us to control our spending and keep our fees down. But looking ahead, I do not think we can afford to neglect such major policy areas for much longer. Moreover, from January 2002, we have to meet a substantial increase in the rent we pay for 6 Frederick's Place, reflecting the marked tightening in the property market since the previous rent review. In addition we are only now in a position to start to implement the new regime for our membership fees, which the postponement of N2 by the FSA has unworkably delayed. I shall be writing separately to all Members once we have worked out what the new regime will imply for them.

With the creation of the FSA largely complete but a major European agenda looming, I intend to establish closer contacts with as many of you as I can, in part so that Adam Ridley and I can learn more about your priorities at first hand, and make sure we bring you maximum value for your money.

Collaboration

Some priorities are self-evident. At a time when almost all Members are making important economies in difficult markets, they are looking to their trade associations to reduce duplication, avoid destructive competition, maximise fruitful collaboration; and at the same time, to represent the sectors' concerns as effectively as possible, which now means Europe and elsewhere overseas as well as at home.

We are already putting these principles into effect in many areas and can, indeed, claim to be pioneers. For example:

- For some years we have provided leadership and co-ordination for two "City Liaison Groups". One deals with the EU proposed Savings Tax Directive, in which we work with over a dozen other trade associations. A second deals with the development and implementation of the FSMA and associated secondary legislation and embraces six other associations as well as three major law firms: Clifford Chance, Freshfields and Linklaters & Alliance.
- We collaborate actively and exchange views intensively with the Italian, French and Swedish Securities Associations with whom we naturally share an increasing range of interests, particularly over European policies.
- We also work closely with over twenty associations in numerous different international policy areas, perhaps most notably with BBA, ISDA, the International Primary Market Association, the Securities Industry Association and The Bond Market Association.

- We are active members of the International Councils of Securities Associations. This group is an increasingly valuable forum for exchange of views, in which contacts lead naturally to informal coalitions on a wide range of issues, where either policy is becoming very international, or problems and experiences are now very similar in most major market economies. Recent examples include Disaster Recovery and the lessons of the World Trade Centre attacks, taxation of foreign bank branches, regulation of analysts, privacy and personal data transmission and the Krueger proposal for countries in debt crises.

I have been deeply impressed since becoming LIBA's Chairman by the sheer scale and complexity of these many, varied and complex relationships, which are maintained with extraordinary economy of both money and effort by our very modest staff. One important lesson they teach is to be cautious about radical, ambitious proposals for mergers and reorganisations. LIBA will best deliver its Members economical, swift, targeted and effective policy work and representation by being flexible, by remaining small and fleet-footed and employing staff of the highest quality, and being constantly on the lookout for ways of working more effectively with others.

Website and Communication

We hope to put much more material onto our Members' website than has been possible so far; and, more generally, so to develop and improve our communications that this report can be shorter. That remains our ambition but, in the meantime, we have designed the layout and headings of this Report to be user-friendly. We do not, as a rule, seek publicity, believing it to be better to work by quiet persuasion in nearly all circumstances, so this Report is the principal means of displaying the wide range of work that your Association undertakes on your behalf.

Sir David Walker
Chairman

May 2002

REPORT OF THE CHAIRMAN'S COMMITTEE

CORPORATE FINANCE

Amendments to the Takeover Code

The Panel on Takeovers & Mergers ("the Panel") restructured its operations during the year, creating a Code Committee with responsibility for considering new rules and proposed amendments to the Code. It is required to publish the proposed rules and amendments for public consultation; to consider responses arising from the public consultation process; and to publish a statement of its conclusions before it introduces new rules, or amends the existing ones.

The Code Committee issued eight consultation papers in the latter part of 2001, covering:

- the implications for the Takeover Code of the FSA's proposals for disseminating corporate information;
- the need for additional announcements following the announcement of talks which might or might not lead to a bid;
- equality of information to competing offerors;
- disclosure of side agreements relating to offer pre-conditions and conditions;
- electronic acceptances in CREST;
- the consequences of purchases by the offeror of shares in the target in exchange for securities;
- the resolution of competitive situations; and
- the aggregation of dealings requiring disclosure.

Code Committee consultations

The Committee is to be congratulated on its clear papers, thorough response statements and professional approach.

The Corporate Finance Committee responded to all the proposals. We broadly supported some proposals, including electronic acceptances in CREST and the aggregation of dealings requiring disclosure. In one case – the need for 'refresher' announcements – the Code Committee recognised that additional regulation was not required. In another – the consequences of acquiring shares in the target – the proposals were implemented in a modified form. We were disappointed that the Panel did not accept our proposal that both companies in a merger should be treated as offerees for equality of information purposes.

LIBA Response

Changes to the Company Listing rules (CP 100/100a)

In late June, the FSA published Proposed changes to the Listing Rules at N2 (CP100, 126 pages) and Proposed UKLA Guidance Manual (CP100a, 242 pages), with an unrealistic response deadline of 31 August. Nonetheless, assisted by Slaughter and May over the summer holiday period, we prepared a detailed submission.

LIBA submission on amendments to Listing Rules

In its revised proposals, the FSA made material changes in a number of areas which we had criticised, in particular:

- Dropping the proposal to oblige companies to notify breaches of the Code of Dealing and of the Listing Rules more generally.

- Recognising the fact that experience on transactions need not be gained solely in the UK to render a corporate adviser competent.

The FSA also made some changes to eliminate the inconsistency between guidance and commentary on the handling of price-sensitive information.

We still need to press the UKLA to eliminate the micro-regulation of sponsors, which is unnecessary, unworkable and duplicates the work of the FSA. Other criticisms we made of the changes proposed in CP100/100a should be dealt with in the FSA's wider review of the Listing Rules during 2002.

Changes to the arrangements for the dissemination of company news

The new arrangements for disseminating company news to the UK market take effect in mid-April 2002. Initially LIBA urged caution, noting that their complexity might not bring significant operational benefits. While the London Stock Exchange Service has now been relaunched to meet competition from the new entrants approved by the FSA, it is still too early to assess the impact of these changes.

EU Takeover Directive proposal

After thirteen years, the proposed Takeover Directive failed to achieve a majority in the European Parliament in July, and fell. While it was hard to judge whether no EU legislation was better than the proposed Directive, the events surrounding the vote gave cause for concern.

Winter Group report on Company Law

In the autumn, the European Commission appointed a high-level group of experts in company law under Mr Jaap Winter to produce recommendations in a number of areas. The key proposals in the report cover the right of shareholders to a "level playing field", and the ability of the bidder to "break through" to control at a given level of shareholding and to operate a "squeeze out" when opposed by a small minority of shareholders.

"Level playing field" refers in this context to the need to ensure at Community level that it is shareholders who decide the future of the target company. Accordingly, any action proposed by incumbent management which could frustrate a bid must be endorsed by the shareholders in general meeting at the time of the bid.

The "break through" proposal is entirely new. The idea is that, whatever the provisions of the company's constitution, a bidder who acquires a super-majority (at least 75%) of the "risk bearing capital" of the target company should be able to "break through" to control. This proposal is beset by difficulties of definition and has already been the subject of some criticism elsewhere in the European Union, particularly because the Winter report is silent on the question of compensation.

Finally, on "squeeze out", the proposal is to entrench in European law a right for the bidder to acquire a remaining small minority in a target company at an equitable price. The proposal also gives the minority a right to sell their stake to the bidder. There is a rebuttable presumption that, if an offer has been made recently, the offer price is an equitable one.

Broadly, LIBA Members support these proposals, which reflect the policy behind current UK provisions, even though some aspects are unsatisfactory. Thus, the requirement that the holders of 90% of the shares to which the offer relates should assent to the offer can sometimes set an impossibly high threshold.

A good deal of work remains to be done to incorporate the Winter report recommendations in a proposal for a new directive. It will be important to ensure that the key principles of the original are maintained: shareholder protection and equitable price.

European Commission proposals regulating the continuing disclosure obligations of companies

In November the Commission published a consultation document on the continuing disclosure obligations of companies. It asked a number of open questions about the desirability of quarterly reporting of company results, suggested various deadlines by which reports should be filed and discussed whether quarterly reports should be audited. We responded in detail, being broadly in favour of quarterly reporting while noting the attendant risks of pure earnings management and greater market volatility; and of the importance of retaining the general obligation to keep the market informed of all material developments in a timely way.

Disclosure consultation

Prospectus Directive proposal

The proposal for a Directive on Prospectuses was brought forward by the Commission in May 2001. As in other areas, LIBA has worked with other trade associations (British, European and international) to help the Treasury and European Institutions understand the practical difficulties the original proposal caused and why it would not help the single European capital market.

One difficulty was the proposal that each issuer would be uniquely and indefinitely tied to the “competent authority” in a particular Member State. This would make it difficult for Member States to specialise in regulating particular forms of issuance, and would tie issuers from countries outside the European Union to the Member State where they first listed. This proposal has now been amended in the Parliamentary text, to allow bond issuers the choice of competent authority. Other difficult areas include the application of the Directive to small and medium-sized enterprises (SMEs) and specialist secondary markets such as the LSE’s AIM; and the requirement to publish a prospectus when offers are made only to a small group of investors, or to professional investors.

Difficulties with the proposed Prospectus Directive

While the objective of the proposal – to facilitate cross-border or pan-European offerings of securities – is laudable, the text originally proposed has had to be heavily amended by the Parliament in order to preserve existing workable arrangements, in which European and international investors and issuers alike have shown their clear confidence.

Like the Market Abuse Directive proposal – see below – the Prospectus Directive would have been transformed by a proper consultation process such as the Lamfalussy report recommended which was open, transparent and systematic, with clear and sensible deadlines.

Market Abuse: UK and European developments

For the first time in a LIBA Annual Report, UK and European developments are described together. The implementation of the UK market abuse regime now both influences, and is influenced by, European legislative and regulatory developments to a significant degree.

We worked with the British Bankers’ Association (BBA) on our response to the FSA’s Supplement to the Draft Code of Market Conduct consultation (CP 76) and secured some valuable changes to the Code.

Joint work on market abuse

The two associations’ joint Group then explored whether a paper defining a number of acceptable market practices should be developed. Although this

exercise did not reach its primary objective, it produced collateral benefits for those who took part, including a deeper understanding of the issues and valuable experience of the practical problems of implementing the legislation.

Proposed European Directive

Our joint work also provided a sound platform for detailed consideration of the proposed European “Market Abuse” Directive on insider dealing and market manipulation. This was brought forward in May after a flawed consultation exercise on which we also comment in the International and EU Developments section of this Report on page 22.

We worked with members of the European Parliament’s Economic and Monetary Affairs Committee (EMAC) to underline the important issues. Over 100 amendments were tabled to a relatively short – 21 Articles – directive proposal, and a number of significant changes were proposed by the Parliament. These included recognition of Chinese walls; recognition that research developed from publicly available data does not constitute insider information; the introduction of the concepts of ‘legitimate reasons’ and ‘accepted methods of operation’; and arrangements for effective co-operation between the “competent authorities” in member states.

The Parliament also underlined the vital point that the Commission should respect the need for high levels of transparency and consultation with all market participants.

In assisting the Parliament in its scrutiny of the Directive, LIBA has worked closely and co-operatively with a wide range of national, European and international organisations. We are optimistic that the broad thrust of our common concerns will be accommodated in the Parliamentary text. The next stage is for the Council of Ministers to take account of the Parliament’s views. The timetable in the Financial Services Action Plan calls for the Directive to be adopted by June 2002 (see page 22).

While the proposed directive on Market Abuse has been brought to the Parliament quickly, its serious defects show vividly how speedy legislation should not become an end in itself. Since updating and amending European legislation is usually challenging, a swift law will often be worse than no law.

SECURITIES TRADING

Market developments

A significant event of 2001 was the acquisition of LIFFE by Euronext, the Dutch company which operates the Amsterdam, Brussels and Paris exchanges. Since the Euronext group already has its own clearing and settlement systems in Clearnet and its partnership with Euroclear, the effect of the acquisition on the London Clearing House could be significant.

Our Securities Trading Committee concerned itself with regulatory developments, in particular transparency and Market Abuse, European market developments, trading technology and settlement issues. It also considered issues surrounding the London Stock Exchange’s proposals for retail access to the SETS public order book.

Meetings with major markets

In March, initiating a programme of meetings with executives from major markets in Europe, the Committee met Mrs Clara Furse, the Chief Executive of the London Stock Exchange, to discuss the challenges it faced, such as the competitive disadvantages caused by Stamp Duty and the structure of the UK’s markets.

The Committee and the LSE recognised and agreed that the major market users wanted a Europe-wide solution to their trade processing needs, offering netting across cash, futures and OTC markets, with collateral posted to one clearing house. However, with the current organisation of post-trade services, this was difficult.

In May the Committee met CRESTCo's Chief Executive, Mr Iain Saville, to review developments and to discuss CRESTCo's European clearing and settlement model.

In September the FSA sought the Committee's view on the reduced transparency regime for high risk trades. Our submission stressed that the role and usefulness of block trading is poorly understood and that special provision should therefore be made for large trades requiring capital commitment. Although a relatively small amount of business was now done with delayed publication, it remained an essential service to institutional investors. Price discovery is very much by reference to the transparent, public market: trades undertaken under a delayed publication regime are priced by reference to publicly available prices, rather than the other way around.

*Reduced
transparency for
high risk trades*

The Committee also considered that changes to the regime risked withdrawal of capital underlying the cash market, which could in turn affect liquidity. Changes to the regime and the perceived risk profile would change the cost of capital for institutions. The Committee recognised that the FSA needed to seek a balance between public interest in transparent markets and liquid markets, and believed that the present balance was about right.

The Myners report

In March, Mr Paul Myners reported at length on pension funds. He believed his report would be the precursor of significant change. Introducing it, he said:

*Abolition of "soft"
commissions?*

"To some the principles may seem surprisingly basic. In a way they are – yet they certainly do not describe the status quo. Were pension funds and other institutions to adhere to them, *substantial change in decision-making behaviour and structures would be implied*" (emphasis added).

He also recommended new fee structures for the industry, which include the effective abolition of soft commissions.

We made a submission to HM Treasury, arguing that implementation of the Myners report should be a step along the road to a single European capital market, rather than the unilateral implementation in the UK of changes which could make a single European market in pensions harder to achieve. Pension reform in Europe represents a substantial opportunity for the UK-based pensions industry, including the investment banks who work with Pension Fund Managers. We stressed that, while supporting the call for more transparency and attention to transaction costs, further thought, research and consultation was needed on how to achieve them. The proposals relating to payments to fund managers and soft commission could well harm not only the financial services industry in the UK but the wider economy.

LIBA on Myners

Trading costs

As foreshadowed in our submission to HM Treasury on the Myners report, we have begun to grapple with the difficult issues surrounding the accurate definition of trading costs. Once these important questions are answered, we hope it will be possible to develop a robust methodology to measure costs across firms, products and markets.

Settlement developments

Central Counterparty for the London Equity Market

LIBA's Settlement Working Party considered the LSE/CREST/LCH proposals for the establishment of a central counterparty for London Stock Exchange order book securities. The Central Counterparty went live as scheduled in June 2001 and has quickly established itself as part of the London-based infrastructure. LIBA Members always recognised that the ultimate object was the facilitation of netting. The LCH netting service for equities is expected to go live in July 2002 and we look forward to its successful introduction and continued development.

Changes to CREST tariffs

The Settlement Working Party also considered the changes to the CREST tariff. These proposals take account of the impact of netting on CRESTCo. We facilitated an impact analysis which contributed to revised proposals from CREST, working through CREST's Wholesale Markets Liaison Group.

The Working Party is now considering wider European issues, having concentrated on domestic issues in 2001.

Treasury Operations Committee

The Treasury Operations Committee continued to track market developments, including the progress of the Continuous Linked Settlement (CLS) project. The Committee also contributed to LIBA's work following the September 11th terrorist attacks in the United States discussed at greater length on pages 31 and 32.

REGULATORY REFORM

The Financial Services and Markets Act: secondary legislation and regulatory reform

FSMA City Liaison Group

In spite of its length – over 400 sections and 22 schedules – the Financial Services and Markets Act (FSMA) established only general enabling provisions in many areas. Over one hundred Parliamentary Orders have been required to implement the full statutory regime. Assessing and responding to drafts of this material and to the FSA's consultation papers has continued to dominate the work of our Compliance Committee and the various working parties which it has had to establish to consider specific issues. In addition, the informal grouping of trade associations and City law firms which we established in 1998 – the FSMA Legislation City Liaison Group – has continued to act as the primary point of contact between the industry and the Treasury. The other members of this Group are the Association of British Insurers (ABI), the BBA, the Investment Management Association (IMA), the International Primary Market Association (IPMA), the International Swaps and Derivatives Association (ISDA), Clifford Chance, Freshfields Bruckhaus Deringer and Linklaters & Alliance. With its very broad membership, this carefully co-ordinated group has continued to deliver a focused and highly influential City response to the authorities on a wide range of subjects.

During the year we commented on numerous draft Parliamentary Orders covering issues as varied as (*inter alia*):

FSMA secondary legislation

- Financial Promotion (discussed on page 18);
- the Regulated Activities for which authorisation under the FSMA is required;
- Rights of Action (i.e. redress for "private persons" when FSA's rules have been contravened and loss has resulted);

- auditors' communications to the FSA; and
- the transitional and consequential measures designed to allow a smooth introduction of the new regime.

There is no doubt that it was essential to consult the market thoroughly on these measures. For example, the City Liaison Group persuaded the Treasury not only that a large number of technical amendments were needed, but also that the scheme for control of business transfers within the FSMA should not be compulsory for banks; and that the Official Listing of Securities Regulations should be amended without delay to confirm that unlimited companies were able to continue to have their covered warrants listed in the UK. It is a matter of continuing concern that nearly all the consultation deadlines fell well short of the three months minimum period laid down in the Cabinet Office guidelines. On a number of occasions aspects of the legislation were therefore scrutinised less thoroughly than they should have been, leaving important defects.

Responding to Treasury draft Orders

Such defects must be corrected and the FSMA regime will need to be amended regularly if it is not to fall behind market developments. We have therefore started to discuss with the Treasury their approach to amending the Orders, even though the framework nature of the Act itself should mean that further primary legislation will not be needed for some time. The Treasury have indicated that, where possible, amendments should be prepared on a periodic rather than a piecemeal basis, probably on a two-year cycle. They recognise, however, that there will be exceptions to this, not least where new legislation is needed to implement EU Directives. We have stressed that it would be wrong to wait for years to put right defects which have already been identified.

Keeping the legislation up to date

The Treasury have also agreed to consider posting informal consolidated texts of Orders on their website www.hm-treasury.gov.uk as amendments are made and to provide an updated list of all the FSMA Orders section-by-section. These steps should make the legislation much more accessible to Members and their advisers. The City Liaison Group has also stressed that it is essential that the Treasury's Financial Markets team is staffed in a manner that will ensure that the expertise gained over the last five years is maintained as the team's members are moved to other posts.

As the FSA succeeded the previous regulators, the question of the continuity of contracts referring to the former regime was one issue which was resolved without the need for legislation, albeit after a frustratingly drawn-out discussion. Working with the Treasury, the FSA and the Financial Law Panel, the City Liaison Group circulated a paper in July which explained why in the great majority of cases contracts making reference to previous regulators, or to statutory provisions which would be repealed by the FSMA, would probably not need to be amended. The FSA also helped to clarify the position by including a statement on the issue in the transitional rules.

Continuity of contracts

The establishment of the new Financial Services and Markets Tribunal was a less happy episode, however. The City Liaison Group identified serious flaws in the Lord Chancellor's proposal that the general presumption should be that the Tribunal would hear cases in public. We stressed that the potential for reputational damage to firms – and, indeed, individuals – was clear and inevitable, even in a case where the Tribunal did not uphold a FSA decision. Moreover, the proposals appeared to conflict with Ministerial statements, and to undermine one of the key elements in the carefully balanced checks and balances structure built into the FSMA after lengthy Parliamentary debate. The strength of feeling on the issue was such that a motion was moved in the House of Lords in October 2001 against the Statutory Instrument establishing the Tribunal's rules. In the event, the Order was enacted, but by only 140 votes to 129, and Ministers have agreed to review the position if the industry's fears prove to be justified. At this stage it is too early to tell to what extent the change from the

Financial Services and Markets Tribunal

arrangements for private hearings under the Banking and Financial Services Acts will dissuade firms and individuals from taking cases to the Tribunal. It will not be possible for any single observer to identify all those cases where potential appellants have been deterred from applying to the Tribunal by the threat of unacceptable reputational risk. So the harmful impact of the rules may well be very hard to measure.

“N2”, transitional arrangements and FSA consultations

Transitional arrangements after N2

It was not until 12th July 2001 that the Treasury confirmed that the FSMA implementation date – “N2” – would be midnight on 30th November 2001. The City Liaison Group had stressed that this was the earliest possible date, and was only practicable if the FSA allowed firms at least twelve months after N2 to comply with the new provisions of the FSA’s Handbook. The FSA conducted a short consultation on the transitional rules for the Conduct of Business Sourcebook (COBS) in March and April 2001, and in July the rules were “made” by the FSA’s Board. At a general level we supported the structure which the FSA envisaged of three basic types of transitional rule: extra time provisions, technical timing provisions and timeless (saving) provisions. But we had other serious concerns. The rules were far too complicated. Although the FSA agreed to broaden the scope of the transitional provisions in a number of areas, these still did not cover all the cases where modifications had been made. Moreover, the transitional period was only extended modestly to June 2002, although a full year was needed.

FSA’s approach during the transitional period

Such complications obviously exposed firms to the risk of innocent rule breaches, raising the question of how the FSA envisages monitoring and enforcing its rules. Following correspondence over the summer of 2001, the FSA wrote to us to clarify its approach to enforcement during the transitional period. In particular, the FSA explained that disciplinary action against a firm during the transitional period was unlikely

“unless – at the very least – we are satisfied that the firm has breached both the COBS rule and the corresponding rule of its previous regulator (assuming the rule in question is eligible for transitional relief).”

The FSA also emphasised that it would assess pragmatically whether the rules of previous SROs were substantially similar to the new conduct of business rules.

Drafting defects in COBS rules

In addition and in parallel, we discussed with the FSA the drafting of thirty or so provisions in COBS where the requirements did not appear to reflect the way that LIBA Members conduct their business. (In a number of cases we had already raised concerns about the rules in question in our responses to earlier consultation papers.) At the time of writing, the FSA has accepted our arguments that there are drafting difficulties with the rules in the majority of cases which we have raised. These cannot be dealt with simply. Given the procedural requirements in the FSMA, it will be necessary to consult on changes before amendments can be made. However, the transitional period is due to end on 30th June 2002, and in many cases the FSA will not be able to bring forward proposals for amending rules before then even though it has recognised that there are drafting difficulties. We have stressed that in such cases – where rule changes cannot be made in time – the FSA should either extend the transitional provisions or, at the very least, should provide a clear statement highlighting the extent to which its power to grant individual waivers would be of assistance to firms. At the time of writing we are awaiting the FSA’s response.

FSA Consultation and Discussion Papers

During the year the FSA published over 40 Consultation and Discussion papers, and we responded to all the proposals where there were issues of importance to LIBA Members. These ranged from changes in the Listing Rules and the proposed UKLA Guidance Manual; the wide-ranging review of the current Best Execution requirement; further proposals for funding the Financial Services

Compensation Scheme (FSCS), the Financial Ombudsman Service (FOS) and the FSA itself; to proposals for establishing the complaints scheme for independent investigation of maladministration by the FSA and appointing the new Complaints Commissioner. In some cases, given both the volume of consultation and the extensive work which firms were undertaking to prepare for N2, we had to stress to the FSA that they would not receive well considered responses from our Members unless consultation deadlines were extended.

Major themes in our responses were that rules designed to protect retail clients should not be applied to wholesale business, and that over-prescriptive rules which undermine innovation should be avoided. It is still not clear whether the FSA has established a reliable procedure for addressing either concern.

*LIBA responses:
major themes*

These themes also shaped our joint work with the BBA in the first half of the year on the FSA's High Level Standards; on the drafting of the FSA's Inter-professional Conduct chapter (IPC), a part of the Market Conduct section of the Handbook; and on the Bank of England's consultations on the Non-Investment Products (NIPS) Code. A number of changes were made to the proposals following the industry's representations. We particularly welcomed the FSA's agreement to provide clearer statements about the extra-territorial application of the Principles for Businesses and about the application of the IPC to a firm's overseas offices or overseas affiliates.

The FSA also made helpful amendments to the draft rules on financing the Compensation and Ombudsman schemes. These should help to prevent firms which have come to the City to transact international business from financing FSA activities undertaken for the benefit of UK retail clients. We hope that the final regime for the FSA's finances will, as we have argued, reflect the need for a fee tariff system which fairly assesses the size of firms' business and the risks that different types of business pose to the FSA's statutory regulatory objectives.

FSA's new regulatory approach: "Project Arrow" and Theme Projects

We have welcomed the FSA's risk-based approach to regulation. A special presentation by FSA staff to members of LIBA committees in March 2001 was particularly helpful, as was a similar meeting to discuss the FSA's work on the "Harnessing Market Forces" theme project.

*FSA's approach
to supervision*

The enforcement powers established by the FSMA are part of the FSA's "tools of supervision" and its approach to disciplinary sanctions has been an issue in several consultation papers. As the regime beds down, it is important that the FSA recognises that resolving issues is more important overall than policing firms' adherence to the letter of each and every rule.

A particular issue has been the status of the Guidance provisions in the FSA's Handbook. We were pleased that the "Reader's Guide" to the Handbook now confirms that general guidance is not binding on those to whom the rules apply although, if a person acts in accordance with general guidance

*Status of FSA
guidance*

"in the circumstances contemplated by that guidance, then the FSA will proceed on the footing that the person has complied with the aspects of the requirement to which the guidance relates".

We also commented on the FSA's proposals for a special regime for Wholesale-only Deposit-takers (Consultation Paper 88). We welcomed the proposal that a light touch regime was appropriate for banks which only accepted wholesale deposits. But, given the FSA's risk-based approach, it was not clear to us why it was thought to be necessary to limit such arrangements to deposit-takers.

Wholesale regime

Integrated Prudential Sourcebook

The FSA published its consultation paper on the Integrated Prudential Sourcebook (IPSB) last June. As with the earlier pre-consultative process, we worked jointly and intensively with the BBA on a response. The IPSB consultation paper showed that the FSA had taken account of industry views. Nevertheless, there were significant issues to emerge, not least continued concern over the need for consistency in the distinction between rules and guidance; the extent to which the FSA intends to encourage firms to seek individual guidance or, indeed, whether waivers must be sought; and the need for consistency of approach. We emphasised the need for “ease of use” to be a guiding principle, stressing the importance of “navigability” and the use of plain English.

Remaining technical issues

Certain technical issues remain under discussion with the FSA, including: deductions from capital for holdings in the capital and subordinated debt of other financial firms; introduction of an additive expenditure-based capital requirement; the treatment of collective investment schemes; underwriting; operational risk; and the extent to which the new requirements incorporate firms’ existing capital buffers. The draft Sourcebook did not cover Liquidity, where work is now in progress but finding a balance between prescription and a proportionate application of the quantitative and qualitative framework envisaged will be difficult.

Implementation to be phased

Introduction of the IPSB had been planned for the start of 2004. But international developments, in particular the Basel and EU capital review and other EU initiatives, prompted the FSA to consult separately on timing and implementation, proposing delay on credit risk, capital, group risk and liquidity. Although all systems and controls requirements are planned to be implemented in 2004, a definitive timetable for the whole Sourcebook is not yet available. We continue to press to ensure the minimum disruption for firms in the eventual implementation of the IPSB.

Using the FSA’s Handbook

Monitoring Handbook amendments

The wide range of activities which the FSA regulates makes it hard for firms to follow changes in the Handbook. We have therefore asked the FSA to consider new ways of ensuring that firms are properly warned of forthcoming amendments to the rules. Similarly, the accessibility and “user friendliness” of FSA’s Handbook is of great importance to firms. The City Liaison Group supported the concerns raised by LIBA Members about revision procedures and submitted a paper to the FSA about the improvements needed. The signs are that many of the proposals that we have made will be accepted.

Answering reasonable questions

A related point is the FSA’s approach to answering reasonable questions by firms about what its rules mean. The FSA will be justified in not responding to some requests for what is tantamount to free consultancy. However regulators must clearly explain to firms what their rules require, particularly given they are now so complicated.

Guidance and Waivers

Our Members have two important related priorities over the provision of waivers. First, there will be cases where rules must be adapted to reflect the different businesses which firms undertake. The FSA has stressed that it accepts the need to avoid a “one-size-fits-all” approach. Nonetheless there is a risk that where a rule does not “fit” for a particular line of business, it will be thought that the problem can be dealt with more or less adequately by providing a waiver or individual guidance to each affected firm. Either would be very time consuming for both firms and the FSA and, in the latter case, would not necessarily provide a defence against an action for breach of a rule. Clearly the right response is, rather, to amend the rule, as we have argued. Second, the FSA must establish a procedure for publicising waivers widely when a waiver is likely to be relevant to the business of other firms.

Financial Promotion

We have continued to co-ordinate the City Liaison Group's work on financial promotion issues, including:

- the new Financial Promotion Order which governs the FSMA prohibition on financial promotion by unauthorised persons;
- the FSA's proposed guidance on the application of the Financial Promotion Order;
- the separate Order which governs the promotion of unregulated collective investment schemes by authorised persons; and
- the new FSA financial promotion rules for authorised persons.

On all of these regimes we have worked closely with the authorities. We secured more generous transitional arrangements for the financial promotion rules; and important improvements, particularly where the proposals would have restricted or placed unnecessary burdens on communication and information provision in professional and international businesses. However, some important areas remain where the new regime is more restrictive than the old for no good reason. We will continue to press appropriate amendments on the Government and the FSA. Although the new financial promotion framework is intended largely to replicate the previous advertising and cold-calling regimes, the comprehensiveness of the statutory prohibition has necessitated extensive and complex redefinition of underlying concepts and exemptions, some of whose implications are still continuing to emerge because of this complexity.

The need for amendments

Training and Competence

The FSA's rules helpfully give wide latitude to firms to design appropriate arrangements for monitoring and controlling employees' training and competence. In our response to the FSA's Discussion Paper 9 on the proposed review of the examination structure, we urged FSA to ensure that examination and training and competence requirements together continue to reflect the discipline the market imposes on competence where professional customers are concerned. We will continue to comment on the FSA's developing examination review. We will also seek to ensure that the arrangements for the inter-professional market – due to be put in place by December 2003 – are appropriate and limited to what the specialised nature of the markets calls for. (Other aspects of our work on Human Resources issues are summarised in the Personnel section below: page 30.)

Financial Crime

The "prevention of financial crime" is one of the four objectives set for the FSA in the FSMA. This and the associated anti-money laundering procedures have been under the spotlight over the last year for a number of reasons. In June 2001, the FSA obtained its authority for the purpose of FSMA to appoint a competent person to investigate offences and to institute proceedings for any offence under the Money Laundering Regulations 1993. In July, it published its paper "The Money Laundering Theme". The Money Laundering Sourcebook for which Members had been preparing for some time came into effect at N2. In addition, following the terrorist attacks of 11th September in New York and Washington, there was a call for a "crack down" on the funding of terrorism which involved our Members in reviewing their account surveillance and account opening procedures. It is clear that the FSA is concerned that senior management of some firms may not take the drive against money laundering seriously enough. All firms' management must ensure that there are proper systems and procedures in place under the FSA's "Senior Management Arrangements, Systems and Controls" rules, and adequate staff resource to deal with the work.

New Money Laundering publications

Senior management responsibilities

*JMLSG guidance
acknowledged*

The final version of the FSA's Money Laundering rules and guidance generally reflected LIBA's comments. In particular, we persuaded the FSA to include a provision confirming that, in assessing a firm's compliance with its rules, the regulator would have regard to whether the Joint Money Laundering Steering Group's (JMLSG) Guidance Notes had been adhered to, thus preserving their "safe harbour" status.

The JMLSG issued the updated version of the Guidance Notes in February 2001, promising a further revision later in the year, to embody:

- conclusions and recommendations from the FSA's Money Laundering Theme Project;
- the UK Government's further development of anti-money laundering strategy and new legislation;
- the application of the FSA's Money Laundering Sourcebook;
- the enactment of the FSMA subordinate legislation; and
- the experience of firms in applying the Guidance Notes and preparing for N2.

*Revised Guidance
published in 2002*

These revised Guidance Notes – the December 2001 edition – were published in January 2002 and LIBA was closely involved in their preparation. Far more revision was necessary than had been initially envisaged as the Government had just introduced tough new measures in the Anti-Terrorism, Crime and Security Act 2001 – amending the Terrorism Act 2000 – to thwart terrorist financing following the terrorist attacks in the United States in September. These extra measures delayed the production of the Guidance Notes.

Although firms have had to cope with a series of challenges to their anti-money laundering procedures in 2001, the Guidance Notes have continued to be a valuable, practical and effective guide and reflect industry good practice.

In December, LIBA Members met the FSA to discuss matters arising from the earlier Money Laundering Theme report, the regulator's monitoring procedures, its policy towards the JMLSG's Guidance Notes and implementation issues arising from the FSA's risk-based approach to compliance. In addition, Members were able to discuss matters relating to the application of the Guidance Notes within specialist business, for example ownership of hedge funds and introductions from name passing brokers.

Asset Recovery

The Proceeds of Crime Bill, on which we commented, was introduced in Parliament in October. It will create the Asset Recovery Agency for recovery of criminal assets and will consolidate existing law on confiscation and money laundering. The Bill is due to become law in July 2002, and firms are preparing for the changes it will introduce. The JMLSG Guidance Notes are being further updated in 2002 to reflect these requirements.

*Treasury's new
Money Laundering
Advisory
Committee*

In parallel, the Treasury have consulted upon the proposal to set up a public/private Money Laundering Advisory Committee (MLAC). This Committee is to provide the Treasury with a forum of experts to advise on anti-money laundering issues. LIBA made representations about its membership and aims, which have been reflected in revised terms of reference. Initially, the MLAC will have thirteen members, six to be appointed by the JMLSG. The MLAC is due to hold its first meeting in May 2002.

*Data protection
and "tipping off"*

We have also followed up the disquieting reports in February 2002 which suggested that the Information Commissioner's Office had argued that the Data Protection Act (DPA) might force firms to "tip off" individuals. It appeared to

have been suggested that the Act would prevent a firm from declining to provide information which was germane to a decision to report suspicious transactions when the firm had received a “subject access request” from the individual involved. The Treasury are now preparing guidance on this issue. We have stressed that the “prevention or detection of crime” exemption in Section 29 of the DPA can be interpreted widely to justify maintaining confidentiality, as any effective system must do.

Our work on the Anti-Terrorism Crime and Security Act 2001 and on the Second Money Laundering Directive is covered on pages 21 and 26.

Internal Audit Committee

During the year the Committee considered and commented, amongst other issues, on the Basel Committee’s consultative paper “Internal audit in banking organisations and the relationship of the supervisory authorities with internal and external auditors”. Although the Basel Committee’s subsequent policy statement in October dealt with some of the issues raised by LIBA it still offered a rather out of date picture of the role of internal audit. Moreover, the proposed relationship which supervisors should develop with internal auditors seemed likely to undermine internal audit’s position within a firm. We have consulted the FSA on these issues. They have confirmed that there are no short-term plans to make changes to the provisions for external auditors, nor to change either the Handbook or the risk assessment framework as a result of the publication of the Basel Committee’s policy statement. In addition, in commenting upon our Committee’s request for clarification on the policy about supervisors’ access to internal audit reports, the FSA stated that it was sensitive to the issues surrounding routine access and had no intention of changing its approach. The FSA will continue to ask to see reports from time to time, case by case.

*Basel
consultation*

The Committee commented on the proposals in the FSA’s Reports by Skilled Persons consultation (CP 91), which in general it supported. The Committee was concerned that the FSA should not use this powerful regulatory tool as a way of solving staffing problems; and should discuss the costs of such reporting with a firm’s management. In addition, the Committee pressed the FSA to recognise that consideration should be given to using the skills of firms’ internal audit departments. In March 2002, FSA confirmed that they would be prepared to consider firm’s internal audit reviews in some instances.

*FSA’s Skilled
Person proposals*

During 2002 the FSA will be reviewing its rules and guidance in relation to auditing and regulatory reporting. The Committee will be following this exercise closely.

The Committee has also considered some of the issues relating to the Basel Committee’s proposals on capital adequacy and has worked with the other LIBA committees involved.

UK ELECTRONIC COMMERCE DEVELOPMENTS AND DATA PROTECTION

Electronic Commerce Directive implementation

The DTI consulted in August, and HM Treasury in December 2001, on the UK’s implementation of the Electronic Commerce Directive which, with a few limited exceptions, is intended to introduce mutual recognition of “country of origin” regulation for on-line business. We have urged the Government to implement thoroughly but promptly. But the approach has often appeared slow, hesitant, and uncoordinated. At the time of writing, draft UK legislation and rules to implement the Directive have only just been published with an early-May

Country of origin approach

deadline for responses, even though the deadline for implementation was mid-January 2002. Whilst welcoming the Government's stress on the importance of maintaining the integrity of the country of origin approach, we have expressed concern about the extent to which the proposals retain UK control over incoming retail cross-border financial services. Robust implementation of the country of origin approach is particularly important because of the UK's strong support for the principle in Europe in other contexts, and because some Member States have sought to retreat to greater 'country of destination' control.

FSA's approach to regulation of E-commerce

In a similar vein, our comments on FSA's June 2001 Discussion Paper on its approach to the regulation of E-commerce focused on the need for strong support for the country of origin approach, and for a proportionate approach to the regulation of firms' IT management within the broad context of the FSMA.

Regulation of Investigatory Powers Act and Anti-terrorism, Crime and Security Act

Regulation of Investigatory Powers Act

We have continued to comment on the Home Office's consultations on codes of practice for the authorities under the Regulation of Investigatory Powers Act 2000. The most important and controversial code, and the one whose subject gave rise to our most serious concern while the legislation was passing through Parliament, is on law enforcers' access to encryption keys. However, this has still not been published at the time of writing.

Anti-Terrorism, Crime and Security Bill

In November 2001, alongside the CBI and others, we successfully pressed for amendments to the Anti-Terrorism, Crime and Security Bill to limit the range of circumstances in which firms could be required to retain communications data to preserve them for possible use by criminal investigation authorities.

Information Commissioner's guidance on employer/employee relationships

Improving the Commissioners' guidance

We commented in January 2001 on the Information Commissioner's draft code of practice on employer/employee relationships. The draft code adopted an inflexible attitude to data protection. This could have severely limited firms' ability to manage their business and to maintain and review records of employees' communications with customers, which in many circumstances FSA expects firms to do. We worked closely alongside the CBI, which has secured some important improvements to the draft code during the second round of consultation which began in late 2001. Important issues remain outstanding, however. We are concerned that the Information Commissioner has not yet understood the need to overhaul the earlier proposals, particularly their application to financial services business.

Cross-border data transfer issues

Firms' privacy policies

We have also continued to work closely with the CBI on cross-border data transfer issues, in particular on proposals for draft standard contractual clauses to cover transfers of data to "third countries" which do not provide an adequate level of protection for the processing of personal data. The CBI has also supported our argument that group privacy policies should be recognised as a means of establishing adequate protection when personal data are exported between parts of the same group. We have now discussed these proposals with the European Commission and with the Information Commissioner's Office.

INTERNATIONAL AND EU DEVELOPMENTS AND IMPLEMENTATION OF DIRECTIVES

European legislative arrangements

We have continued to co-ordinate the work of an expanding group of European and international associations on the procedural reforms to European financial services legislation and regulation initiated by the February 2001 Report of the Lamfalussy Committee of 'Wise Men'. Throughout the year we sought a properly balanced resolution of differences of opinion between the European institutions on their relative powers and on the role of the proposed European Securities Committee (ESC) and Committee of European Securities Regulators (CESR). The Wise Men had stressed the importance of ensuring that legislation was amended promptly to keep up with changes in the markets and these two committees were proposed for this purpose. Agreement between the institutions was finally realised in February 2002, and the procedural reforms are now expected to go ahead.

*Lamfalussy
Group reforms*

Implementation of the Lamfalussy proposals is expected to change the pace and impact of European legislative and regulatory developments significantly. To that end, Lamfalussy stressed the importance of openness and consultation at all levels of the process. The group of associations just referred to has initiated a regular dialogue with both the Commission and CESR on consultation policy and practices. This has yielded a significant and positive shift in European perception of the importance of the contribution to policy which industry experts provide. In particular, we secured important improvements to CESR's published statement of consultation practices, consultation on which was in itself a welcome demonstration of the new approach.

*Establishing
proper
consultations with
CESR*

We have sought a similar commitment to minimum standards of openness and consultation in the policy development work of the Commission and the ESC. This is particularly important given the Commission's publication in May 2001, without consultation, of badly flawed proposals for Directives on Prospectuses and Market Abuse (referred to on page 10). However, the Commission's approach to the Investment Services Directive review, discussed on page 24 has, by contrast, been very much closer to what we have sought and what Lamfalussy envisaged. In addition, the Commission's July 2001 consultation on European Governance – to which we responded – contains much that is welcome on the need for access to expert advice through consultation and for a proportionate, considered, and well-researched legislative approach.

*... and the
Commission
and ESC*

Other indispensable elements of the Lamfalussy proposals are: the six-man 'Monitoring Group' to be appointed by the European institutions to oversee the proper application of the Lamfalussy structure and to ensure that the institutional balance is maintained; and the Commission's role in monitoring and enforcing Member States' proper implementation of Community law ("Level 4" of the Lamfalussy structure).

*Other elements
of the Lamfalussy
proposals*

Financial Services Action Plan (FSAP)

LIBA's work on the proposed Takeover Directive, Market Abuse Directive, and Prospectus Directive is described in the Corporate Finance section above (referred to on pages 9 and 10).

The need for the Commission to allocate sufficient resources to the enforcement of Member States' implementation of Community law, and to the research and analysis which is essential to effective policy-making, was a major theme of our submissions in the run-up to the Commission's February 2002 mid-term review of the Financial Services Action Plan (FSAP). The industry has an important role to play in supplementing legislators' and regulators' resources with its expert knowledge of markets and products. The Commission has tended to give higher

priority to the throughput of legislative proposals rather than their quality. In so doing it makes it hard or impossible to bring into play the industry's expertise or market needs. In complex sectors such as financial services, it is often impossible to develop good policy without consulting firms and their representative bodies in a measured way.

Capital Adequacy: Basel and EU Consultations

We submitted a joint response with the BBA to the second-round Basel Committee and European Commission consultation papers on reform of the Capital Accord at the end of May 2001. In certain areas, we also co-operated with ISDA and other bodies. It was clear that the consultative proposals were still significantly incomplete in places and that much more work was needed.

Basel developments

During the remainder of the year, Basel released further interim working papers on a number of aspects, including Operational Risk, Transparency, and Asset Securitisation. Basel also conducted a dialogue with the industry on credit risk mitigation and repo/securities lending transactions. In these areas we continued to work with other bodies, in particular the BBA and ISDA. We plan to maintain a collaborative approach for the work on the third full consultative packages from Basel and the EU, which are not now likely to be issued before Spring of 2003.

Our submission to the second Basel consultation built on the key themes which were identified in last year's Annual Report and which remain our preoccupation in our continuing dialogue with Basel and EU representatives, namely:

- the lack of attention given to the consequences of changes for the trading book, and in particular the likely damaging implications for the repo and securities lending market;
- the lack of risk sensitivity and too high a calibration of operational risk charges; and
- the excessively burdensome nature of the disclosure requirements.

A key change in the Basel proposals announced during the year and which reflected the industry's submissions was the acknowledgement that the proposals had been calibrated to require too much capital. Basel therefore proposed lowering the capital charge applied to operational risk, from 20% to 12%. Other welcome refinements included the removal of the proposed floor for credit risk mitigation transactions and the slimming down of disclosure requirements.

EU consultation

The EU consultation on Capital Adequacy was very close to that of the Basel proposals and our joint submission therefore covered similar ground. The Commission maintain the stance that the revised capital adequacy regime will apply to banks *and* to investment firms. The Commission also recognise the need to make adjustments to the capital framework within the EU to take account of specific factors that do not apply in the Basel context. We are developing a dialogue with the Commission through personal contact and supporting papers in order to emphasise such EU specificities. A particular concern is the importance of assessing the overall impact on capital for EU firms with trading book activities, given the consequential effects in the market risk regime as a result of the credit risk and operational risk proposals. The combined effect of these changes has not yet been fully examined. They include: treatment of large exposures; and eligibility of collateral under the Capital Adequacy Directive.

Efficient legislation

Another major question for the EU is how far the new capital adequacy legislation can permit efficient updating, so that the framework in Europe can be "evolutionary" and take account of developments in market and supervisory

practice in the way that the Basel Accord will be able to do. It will be important for the Commission and other interested parties to engage with the Parliament about the appropriate degree of technical adaptability that can be built into what will be a very lengthy legislative text.

Proposal for a directive on the supervision of Financial Conglomerates

This proposal was adopted by the Commission early in 2001. It is a priority under the FSAP, and progress in the Parliament and Council of Ministers has so far been swift. The current Presidency (Spain) is aiming for political agreement by mid-2002 with final adoption by the end of the year. We have prepared a position paper on the issues jointly with ISDA and have explained our concerns with great care to members of the Parliament's Economic and Monetary Affairs Committee as well as to the Commission, the UK authorities and the Spanish Presidency. Our principal concerns are that the treatment of groups with third country parents should be as risk-based and as proportionate as possible. Adjustments to the present sectoral deductions from capital should also be reconsidered to take proper account of the complexity of the issues as well as likely developments in the Basel process. In addition, we believe that the proposal requires fine-tuning in a few other areas such as those relating to the scope of the Directive and the definition of conglomerate.

*Cross-sectoral
legislation*

Investment Services Directive (ISD)

The Commission published in November 2000 two parallel Communications: the first on how the 1993 ISD should be amended; and the second on the application of Article 11 of the ISD, which deals with the important questions of which authority should regulate cross-border business, and how regulators should take account of the professional nature of investors. In early 2001 we responded to the Commission's consultation and also, with ISDA, briefed MEPs. We believe that our comments made a considerable impression. We stressed the importance of a limited, targeted review of the ISD, focusing on remedying the respects in which the 1993 Directive did not provide for an effective internal market, either because of specific provisions or ambiguities. It is particularly important to extend the 'country of origin' principle beyond the field of the E-Commerce Directive – which was discussed on page 21 of this report – to cover all financial services, whether on-line or off-line, wholesale or retail; and to provide for an appropriate regime for business with professional customers. We emphasised that the basic regulatory structure of the Directive, with its distinction between regulated markets and investment firms, was sound, and could accommodate the development of alternative trading systems (ATSs) in certain markets.

*Consultation
in 2000*

*LIBA priorities
for strengthening
the ISD*

These were also the main themes of our response to the Commission's further consultation in July 2001 on specific proposals for amending the ISD. The Commission's proposals on country of origin control over conduct of business rules; definition of professional investors; and lighter conduct of business rules for business with professionals, were generally welcome. We urged the Commission to press forward urgently with these indispensable elements of an effective single market. The Commission's ideas for restructuring regulatory classifications of investment firms and regulatory markets were, by contrast, controversial and potentially damaging to European markets. We urged a measured examination of the differing regulatory issues in different markets, not amendments to the Directive itself. At the time of writing, further consultation by the Commission is expected before it makes a formal proposal for a new Directive. This would be good consultative practice, not least given the concerns which have been expressed about the regulatory classification proposals.

*ISD Consultation
2001*

CESR standards of regulation under the ISD

At the same time as the Commission's work on the proposed new ISD, CESR and its predecessor, the Forum of European Securities Commissions (FESCO), consulted on proposed pan-European regulatory standards for three areas under the existing ISD: conduct of business rules; classification of investors; and the regulation of ATSS.

CESR and Conduct of Business Standards

CESR consulted twice on conduct of business standards, in February and October 2001. With other associations, we were able to persuade CESR to consider conduct of business standards and customer classification together, since the definition of professional investors cannot be considered in isolation from the rules which apply to business with such clients. The FSA, as a CESR member, would be under an obligation to implement CESR standards in the UK, and it is therefore vitally important that the standards are appropriate. We pressed CESR to ensure that the boundaries both between professional and non-professional investors, and between professional investors and counterparties, are appropriate to their respective needs for protection, and also broadly consistent with the FSA's current boundaries, which are well-judged and reflect fairly the results of intensive consultation. We also urged CESR not to support excessively protective requirements for counterparties, professional customers, or execution-only business. In all these areas some Member States have tended to be over-protective.

Controversy over proposals for ATS regulation

CESR has also consulted twice on regulatory standards for ATSS, in June 2001 and January 2002. CESR is concerned that ATSS with exchange-like characteristics, and investment firms which internalise order flow, may diminish the quality of trading information on regulated markets. We expressed serious concern that CESR's proposals were based on hypothetical concerns rather than identified market failures, that they did not take sufficient account of the benefits that ATSS bring to the market and that they over-emphasised transparency at the expense of other elements of market quality. We also stressed that the proposals did not differentiate sufficiently between the different roles of ATSS in different markets. While CESR has narrowed down its original proposals, we are continuing to press for further improvements; and also for the introduction of the proposed standards to be deferred so that they are not inconsistent with the policy direction of the revisions to the ISD which are in train as outlined above. In 2002 we have helped to co-ordinate a group of European and international associations to brief the Commission and CESR on how transparency interacts with other factors to generate high-quality markets; and on how this points to different kinds of regulation of transparency, varying with the characteristics of different markets.

Electronic Commerce Directive

Country of origin

In February 2001, the Commission published a Communication on the E-Commerce Directive and financial services, which outlined policy orientations on specific sectoral issues arising from the implementation of the Directive. The Communication's broad endorsement of the 'country of origin' basis of regulation was welcome, although we identified a need for a more robust interpretation of the principle in some areas. The Communication committed the Commission to develop guidance on the application of the Directive's consumer protection derogations from the country of origin basis. We briefed MEPs on the Communication, stressing the need to ensure that the guidance should not encourage Member States to undermine the Directive. We have also urged the Commission to monitor closely and enforce proper implementation of the Directive given its importance to the development of a genuine internal market for all financial services, off-line as well as on-line.

At the time of writing, the guidance has still not been published, and many Member States, including the UK, have missed the deadline for implementing the Directive. (Our work on this is summarised on page 20.)

Proposed Electronic Communications Data Protection Directive

Throughout the year we briefed the European Council and Parliament on this proposed directive, which would replace and extend to other forms of electronic communication the 1997 Telecommunications Data Protection Directive. We opposed the Commission's proposal to require that consumers must positively opt to receive unsolicited e-mails and telephone calls, and urged a proportionate approach to the regulation of internet 'cookies' and the recording of communications. On the last point, we are seeking to maintain the position under the 1997 Directive under which recording and monitoring of communications is permitted for lawful business purposes.

Jurisdiction and applicable law

Late 2000 saw the adoption of a new 'Brussels Regulation' on *jurisdiction* over cross-border disputes. Consultation on it was inadequate and did not take sufficient account of the development of electronic commerce or the country of origin basis of the E-commerce Directive. So we pressed the Commission to ensure that the proposed revisions of the international conventions on the *law applicable* to cross-border contracts should be subject to proper consultation. At the time of writing, the Commission had taken no further action in this area, although a thorough consultation has been promised in the near future. We have also continued to track developments in the revision of the Hague Convention, which governs jurisdiction over cross-border disputes beyond the EEA.

*Conflict of laws
developments*

European Commission consultation on European contract law

In July 2001 the Commission also consulted on whether differences in contract law between Member States gave rise to significant obstacles to cross-border business, and if so what action might be appropriate. We stressed the importance of not disturbing laws which formed the basis of investment products; of allowing the market to deal with conflict of law issues without legislative or regulatory interference; and the importance of using the 'country of origin' approach to accommodate diversity of laws. At the time of writing, it is not clear what the Commission's intentions now are.

The Second Money Laundering Directive

The Second Money Laundering Directive was adopted in November. It extends the existing Directive of 1991 to all serious crime and to lawyers and professional advisers. UK controls have already progressed in these areas but implementation of this Directive will require changes to the 1993 Money Laundering Regulations, on which the Treasury will consult in 2002.

ACCOUNTING

Global Harmonisation of Standards

The last year has seen further progress towards the global harmonisation of accounting standards. As might be expected, given the record of its new Chairman, Sir David Tweedie, the International Accounting Standards Board (IASB) has been taking a noticeably more active approach than in its previous incarnation as the International Accounting Standards Committee. Amongst other significant moves, it has published an important Exposure Draft of a proposed Preface to International Financial Reporting Standards (IFRS) – the term which

*International
accounting
harmonisation*

is to replace International Accounting Standards (IAS) – which “articulates its objective to work actively with national standard setters to bring about convergence of national accounting standards and IFRS”, and has proposed constitutional changes to give its Standing Interpretations Committee a wider brief.

IASB improvement project

At a more practical level the IASB has initiated an “improvements project” with two aims: addressing topics that can be dealt with relatively quickly, particularly those which will reduce the number of options or otherwise improve the structure and drafting of existing international standards; and – crucially – implementing changes that will lead to greater convergence between international standards and the standards in the key “liaison” countries including, of course, the UK.

Proposed EU regulation on IFRS/IAS

In parallel the EU continues to make progress with its proposed Regulation to require all EU listed companies to report under IFRS/IAS by 2005, and in developing the structures needed for its effective operation, particularly the European Financial Reporting Advisory Group (EFRAG). EFRAG will have the job of reviewing new IFRS and recommending whether each new standard should be adopted for use in the EU. Member States will also have the option to make IAS mandatory for all companies under their jurisdiction, and we expect the UK to exercise this option. The timetable imposes considerable pressure on the UK Accounting Standards Board (ASB) and the IASB to harmonise their respective sets of standards before 2005, to make the changeover as straightforward as possible. LIBA is in regular contact with the ASB, the Department of Trade and Industry and other relevant bodies on this issue, and will continue to follow developments closely.

Other Accounting Developments

Accounting for financial instruments

An area of particular interest to LIBA Members is the IASB’s work on accounting for financial instruments. We reported last year that, towards the end of 2000, the then IASC, ASB and several other standard setters published jointly a major Discussion Paper developed by the Joint Working Group of Standard Setters (JWGSS). The Paper’s key proposal was to require the use of fair value for all assets (banking book as well as trading book), with changes in value taken directly to the income statement. LIBA commented in some detail on this Paper, in essence supporting the key proposal – which would entail marking to market all financial instruments – for investment banks, while recognising that other sectors might have serious reservations, and highlighting a number of areas where we believed further work to be necessary. The IASB has now accepted that a move to full fair value for financial instruments is impractical ahead of the 2005 implementation of IAS in the EU, and are concentrating on a shorter-term programme of improvements to their existing standard, IAS 39.

Other initiatives

LIBA took forward work on a number of other initiatives from the ASB and the IASB during the year. This included submissions on ASB papers on a Revision of FRS 3 “Reporting Financial Performance” and Revenue Recognition and the IASB review of Accounting for Share-Based Payments.

Distributable profits

We also raised with the DTI and the ICAEW concerns over the implications for the distributability of unrealised profits of a proposed ICAEW Technical Release – The Determination of Realised Profits and Distributable Profits in the Context of the Companies Act 1985.

FRS 17

We have referred in previous Reports to the risk that new accounting standards may have important implications for key ratios used by LIBA Members’ regulators. The partial implementation of FRS 17 (on pension accounting) from January 2002 has provided a concrete example of this issue, with Members expressing concern that the required publication of any FRS 17 deficits on funded

schemes could damage their capital bases. We raised these concerns with the FSA, who have agreed – at least for the time being – that they will not require an automatic adjustment of the capital base solely because the FRS 17 disclosures show such a deficit.

TAXATION

European Commission proposal for a Directive on the taxation of savings interest

As reported last year, the revised proposals for a European “Savings Tax” Directive which were agreed at the Feira summit in June 2000 and further developed at the November 2000 Council of Finance Ministers (ECOFIN), represented a very significant improvement over the original “co-existence” model. The original proposals would have required Member States either to impose a withholding tax on interest payments made to individuals resident in other EU countries, or to disclose information about such payments. The revised proposals follow concepts developed by HM Treasury, under which information on the savings income of non-residents will, subject to certain conditions, be reported to the individual’s home state fiscal authority. However, three countries – Austria, Belgium and Luxembourg – will initially operate a withholding tax system, moving to exchange of information only after a seven year transitional period.

*Proposed Savings
Tax Directive*

LIBA has continued to provide the Secretariat for the “City Group” – an informal grouping of the principal trade associations and major market operators formed to consider the implications of the savings tax proposals and to co-ordinate industry views on them. Group members include the BBA, IPMA, IMA, the Association of Private Client Investment Managers and Stockbrokers (APCIMS), the Association of Corporate Treasurers (ACT), ABI, the CBI, and the Corporation of London, as well as some fifteen major banks. We have continued to play a very active part in representing the views of Members – and of the City Group – to the Inland Revenue, Treasury and Bank of England, as well as directly to the European Commission and to MEPs.

Following discussion earlier on the detail of the revised proposals, the December 2001 ECOFIN agreed the “final” text of the proposed Directive. Although materially better than earlier versions, the text failed, disappointingly, to include a number of practical improvements proposed by the City Group and other EU market representatives.

This agreed text will form the basis of discussions between the Commission and the designated third countries (notably Switzerland and the US) on their introduction of “equivalent measures”. A report on the outcome of these discussions, and on the corresponding discussions with designated dependent territories over the introduction of “the same measures”, will go to the Council of Ministers in December 2002, who will then decide – by unanimity – whether the Directive is to be adopted.

*Discussions with
non-EU countries*

In the meantime, a Technical Working Party established under the auspices of the City Group has begun detailed discussions with the Inland Revenue on their proposed approach to the changes to the UK legislation which will be necessary to implement the Directive. While there will inevitably be issues over the precise drafting, we remain cautiously optimistic that the final outcome will be acceptable, both to LIBA Members and to the wider City Group, and that it will in any case represent a radical improvement over the misconceived measures in the original 1998 proposal.

Changes in UK tax legislation

Review of tax legislation

The 2001 Budget speech announced substantive reviews of several areas of existing tax legislation, including two consultative documents of particular interest to the financial sector on “Large Business Taxation: the Government’s strategy and corporate tax reforms”; and on “Corporate Debt, Financial Instruments and Foreign Exchange Gains and Losses”. Both have been the subject of major – and effective – consultation exercises, to which LIBA has contributed significantly, particularly in the area of financial instruments where our Members have unparalleled knowledge and experience. Although these consultations are continuing at the time of writing, both are now focused on the details of draft legislation. We believe the result should be noticeable improvements.

Progress on tax policy

At a more detailed level, we have also seen progress in three areas of specific interest to LIBA Members:

- the treatment of certain types of debt instruments issued by banks and securities houses (under s.209 TA 1988);
- the differential treatment of annual interest (under s.349 TA 1988) between banks and securities houses; and
- possible further simplifications to the treatment of manufactured overseas dividends (MODs).

Following detailed discussions with the Inland Revenue, we hope to see satisfactory solutions to the first two issues in the 2002 Finance Bill, although improvements to the MOD regime – despite indications of Inland Revenue sympathy for our views – are likely to take a little longer to achieve.

Stamp duty

On a less positive note, we were disappointed that a further year passed with no sign of progress towards the reduction or abolition of Stamp Duty and SDRT on securities transactions. As LIBA and many others have stressed, these taxes are levied at a significantly higher level than corresponding taxes in other jurisdictions. They thus create, amongst other problems, a major disincentive for the largest multinational corporations to remain registered in the UK. We believe that the revenue from these taxes will be increasingly eroded as professional investors find ways to circumvent them, not least by avoiding altogether the purchase of UK registered shares. So attempting to preserve them risks irreversible damage to the UK securities industry. We will continue to use every opportunity to press for the eventual abolition of these taxes.

Other tax issues

Representatives of the Taxation Committee had a useful meeting with the Inland Revenue as a part of the Department’s “Review of Links with Business” – also known as the “Hartnett Review” – which accompanied the review of large business taxation referred to above. We also hosted a meeting with a senior representative of the US Internal Revenue Service at which we raised a number of issues over the Qualified Intermediary (QI) regime.

OECD on taxation of branches

The OECD is undertaking a major review of the attribution of profits to permanent establishments – a key element in the tax treatment of offshore branches. LIBA has had significant involvement in these discussions, which offer at least the possibility of reaching international agreement on a common approach to the taxation of branches. This is both of considerable interest to many LIBA Members and of importance to London’s competitive position. We, with the BBA and the Foreign Banks & Securities Houses Association, had stressed to the OECD the importance of individual governments not acting early or on their own on this issue – which was, nonetheless, what the British Government proposed in its April 2002 Budget.

On more general matters, our annual tax submission again underlined the importance of the fiscal legislative process working – and being seen to work – in an equitable and sensible manner. We restated the principles which we believe should be followed if this is to be achieved: cost-benefit analysis of the effects of prospective changes, full consultation wherever possible, confining new anti-avoidance measures to specific targets, avoiding sudden legal changes, ensuring that legislation keeps up to date with changes in the traditional divisions between different types of firm, and ensuring that adequate notice is given of the date when new measures are to take effect.

VAT

Our regular bilateral meetings with senior officials of HM Customs & Excise continued during the year. These appear – as we had hoped – to have significantly improved communication between LIBA Members and Customs, and thus to have created the basis for a lasting improvement in relations.

*Relations with
Customs*

Specific issues covered during the year included the drafting of a new Finance and Securities Notice setting out the basic principles of the application of VAT to the financial sector, proposed marginal changes to the borderline between exempt and taxable supplies following a series of European Court of Justice and UK cases in this area, and the likely impact of e-commerce on the development of the wholesale banking and securities sectors. A particular success was the EU VAT Committee's publication of very helpful guidelines, which will significantly limit the tendency of certain Member States to apply the "force of attraction" concept so as to require local VAT to be charged by branches on services supplied wholly from another Member State. This followed representations made by Customs on our behalf.

Members of our Committee also participated in an useful presentation on the likely VAT treatment of transactions in the emissions trading market, which is due to start in the near future. The presentation identified a number of issues which we will be taking up with Customs.

PERSONNEL

Our Personnel Committee is concerned with a wide range of subjects covering employment law and practice, and provides a forum for Members to exchange views and experiences. During the year the Committee considered in conjunction with the CBI a number of issues including the Employment Bill and the Government's proposals on Directors' Remuneration. LIBA supported the CBI submissions. The Committee also considered and commented on several other employment law and practice matters. This included drafts of the Information Commissioner's Code of Practice on employer/employee relationships, particularly in relation to the provisions for monitoring employees' use of communication systems (see page 21). Other issues covered included changes to the exceptions for financial services in the Rehabilitation of Offenders Act to meet the FSMA's requirements; the protection of fixed term employees against pay and pension discrimination and the Fixed Term Work Directive proposals; the new systems for handling disputes including grievance conciliations and arbitration procedures; and the European Charter of Fundamental Rights.

Employment Bill

*Rehabilitation of
Offenders Act*

The Committee met the FSA in March to discuss the Training and Competence Sourcebook and, in particular, how the FSA would monitor compliance. This meeting provided Members with an opportunity to discuss training for wholesale business, where there is a need to take account of the diversity and specialisms of many individual participants and the competitive pressure to maintain and enhance the competence of staff.

Training

Common international standards

The Committee also discussed with the FSA the need for international examination standards to be set and administered by international bodies in order to facilitate the free transfer of staff within global businesses. The Committee encouraged the FSA to consider a modular approach to examination qualifications, which should include the inter-professional markets, emphasising the need for such examinations to be relevant to the particular markets. As noted on page 18 the FSA published a Discussion Paper in November that reflected a number of these recommendations. This afforded the Committee the opportunity to restate its views on training needs in specialised professional markets where it was pointed out that examinations are likely to be too crude a means of measuring staff competence and skills. Other points were the need to develop common international standards or recognition by the FSA of overseas qualifications and experience to permit international mobility; maintaining control over the examination setting process to ensure that there is a balance between the interests of professional bodies which provide and derive income from examinations and the firms which are affected by them; and the need to ensure that the FSA's Approved Persons register provides up to date information about an individual's qualifications.

Approved Persons

The Approved Persons regime created significant work for Members in reviewing job descriptions, allocating individuals to Controlled Functions, checking the FSA's listings, as well as extensive training on individual obligations in relation to the Code introduced by the regime. Two LIBA workshops were held in August, where Members exchanged experiences and discussed solutions to issues, particularly about the "Significant Influence" functions in non-EEA firms and EEA branches. In addition, the "Customer Functions" and "Grandfathering" provisions were examined. These exchanges enabled us to explain the difficulties being encountered by firms to the FSA, which led the FSA to review some of its procedures.

Whistleblowing Consultation

In addition, the Committee commented on the proposals in the FSA's Consultation Paper on "Whistleblowing" (CP 101), which it generally supported. We pointed out, though, that the FSA should maintain a log and record all calls to its helpline and should make it clear that anonymity for the employees using this facility could not be guaranteed in all cases as the law may require disclosure on occasion. The Committee also believed that the FSA should review allegations made and check to establish the extent that they are proven, and that the results should be published. We expect these points to be reflected in a Policy Statement to be issued shortly.

ADMINISTRATION, CONTINGENCY PLANNING AND BUSINESS CONTINUITY

The Administration Committee continued to provide a forum for Members to discuss a range of administration issues during the year. Following the terrorist attacks in the United States of 11th September, the main area of discussion was contingency planning and disaster recovery.

After the attacks Members have reviewed, improved and tested their contingency plans, taking into account the lessons learned from New York. The authorities have also been assessing the robustness of the various utilities to withstand attacks and their own arrangements for dealing with terrorist acts.

City of London Police and the Corporation of London

LIBA has been heavily involved in these matters. In December, we organised a meeting in conjunction with the City of London Police and the Corporation of London to give Members the opportunity to discuss, in particular, the preparations in the City. Members were informed in detail about how an incident would be handled and useful suggestions were made about matters firms would need to consider when drawing up their own plans and training arrangements.

Being able to maintain or re-establish good communications is of overriding importance in an emergency such as was experienced in New York. Until then contingency planners had envisaged a narrow range of emergencies such as bombs, fire or other physical damage to property. We are now faced with much greater uncertainty, both about the method of attack and about the scale and the secondary, indirect, consequences of the initial event. It is absolutely clear that firms need to be able to contact quickly, by one means or another, their counterparties, employees, clients, public service providers, market infrastructure or regulatory and other authorities. From the start, while more comprehensive long-range plans were prepared, LIBA has been concerned to ensure that the authorities are aware of the importance of having in place very quickly a procedure to enable firms to communicate with the principal public authorities and infrastructure providers. We have stressed that firms need to be informed of the process so that it can be built into their contingency plans.

*Communications
vital*

For its part, the FSA began to gather firms' contact details towards the end of the year. In emergencies the FSA will provide a website of this information about individual firms, which is to be updated monthly by each regulated firm. In addition, the FSA has been conducting a review of the state of readiness of firms and markets and will, as part of the Interim Prudential Sourcebook in Spring 2002, publish some guidance and recommendations on business continuity management.

FSA Initiatives

The Bank of England together with the Treasury and the FSA are co-ordinating the authorities' disaster recovery activities. They have held two meetings to which LIBA and others were invited to discuss the progress made and to obtain views from those attending. We have urged that this group needs to communicate its activities and contact points properly. The group is proposing to provide a web-based method of communication in emergencies which is expected to be available for public access.

*Official
co-ordination*

The investment banking community established the Securities Industry Business Continuity Management Group - Europe (SIBCMG-Europe) to focus specifically on the securities industry, covering topics related to business continuity, disaster recovery and crisis management as well as identifying ways to mitigate the risks. The Group has invited LIBA to attend and participate in its quarterly meetings, for which we are most grateful. Summary minutes have already been circulated to Members of the Compliance and Administration Committees and are available on the Members' Website.

SIBCMG

Terrorism and the insurance industry

Following the terrorist attacks, it was clear before the end of 2001 that insurers and reinsurers would reassess their ability to provide cover for acts of terrorism. We contacted Members to seek information and are still working with the ABI, the CBI and others to discover how serious the issue may become. Although Members had then either just renewed their insurances, or were some time away from doing so, a number were able to provide valuable information about the restrictions, definition changes, increases in excesses, limitations of maximum cover and gaps in cover that were emerging in the market place.

*Problems of
insurance cover*

At a meeting in March 2002 where the ABI and CBI met the Economic Secretary, Ruth Kelly, our Members' experiences were to form a useful aid, alongside other information, in helping to determine that there had been a degree of market failure in the provision of terrorism insurance. As a result the Treasury is to consider what can be done to extend the remit of Pool Re beyond property damage caused by fire and explosion to other causes of property damage linked to terrorism (for example, aircraft impact).

*A better public
safety net?*

Other insurance areas giving rise to concern are Employers and Public Liability cover. Here the industry has seen the introduction of a variety of exclusions and limitations on cover. Some cover does, at present, seem to be available, but with significant restrictions and increased cost leaving uninsured risk because of much increased “deductibles”. In addition, personal accident and travel insurance is becoming more difficult to obtain, with greater restrictions and strict adherence to reporting of travel destinations.

There is no doubt that the insurance market has become a much harder place. We shall maintain a close watch on developments through contact with our Members and will not hesitate to act where we can defend or promote their continuing ability to do business in London at reasonable cost.

LIBA'S WEBSITE

A “Members only” area went live in January 2002. This provides LIBA Members with easy access to documents and papers that we produce. As part of the development of this area we have also started to publish summary agendas and summary minutes for the Compliance and Administration Committees. Others will follow. This will enable Members to keep up to date with the subjects and issues that are being considered and, as a result, comment more easily on issues with which we are dealing.

In the coming months we also intend to introduce subject pages, the first of which will cover Disaster Recovery Planning and Business Continuity Management. In addition, we shall be considering the future use and development of the LIBA website, particularly whether links to other relevant sites should be provided. Members' views on how best to develop the website will be welcome.

COMMITTEES OF THE ASSOCIATION

The Association has five committees representing Members' interests in, Corporate Finance, Securities Trading, Compliance, Banking and Finance. In addition, there are specialist committees (listed below) and working parties are appointed to deal with particular issues when the need arises. The Accounting, Financial Regulation, Tax and VAT Committees report as necessary to the Finance Committee.

The work of all the committees is co-ordinated by the Chairman's Committee.

COMMITTEES

The members of the Functional Committees as at 31st March 2002 were as follows:

Corporate Finance

Sir Mark Wrightson (<i>Chairman</i>)	- Close Brothers Corporate Finance Ltd
M. Breuer	- J. P. Morgan plc
J. Crookenden	- Credit Suisse First Boston (Europe) Limited
S. Dingemans	- Goldman Sachs International
P. Drayton	- Schroder Salomon Smith Barney
J. Grace	- Investec Investment Banking
Miss R. Hedley-Miller	- Dresdner Kleinwort Wasserstein
H. Kahnamousyipour	- UBS Warburg
A. Phillips	- Morgan Stanley International Ltd
Miss P. Scott	- Rothschild
K.J. Smith	- Merrill Lynch Europe International
J. Wilford	- Lazard

Securities Trading

A.C.D. Yarrow (<i>Chairman</i>)	- Dresdner Kleinwort Wasserstein
M. Ackers	- ABN AMRO Bank N.V.
J. Brown	- Goldman Sachs International
M. Davids	- Merrill Lynch Europe
J.R. Davie	- Credit Suisse First Boston (Europe) Limited
S.J. Dobbie	- Deutsche Bank AG London
C. Hipkins	- BNP Paribas
R. Kyle	- Schroder Salomon Smith Barney
P.A. Letley	- CIBC World Markets PLC
D.L. Mayhew	- Cazenove & Co. Ltd
A. Phillips	- UBS Warburg
D. Russell	- Morgan Stanley International
R. Sinclair	- Instinet Europe Limited

Compliance

R.J. Levy (Chairman)	- Goldman Sachs International
M. Blane	- WestLB
D. Cooper	- HSBC Investment Bank plc
Ms. P. Curtis	- UBS Warburg
N. Gibson	- ABN AMRO Bank N.V.
D. Gordon	- Nomura International plc
P. Gough	- Knight Securities International Ltd
A. Greatbatch	- Deutsche Bank AG London
M. Hart	- BNP Paribas
B. Harte	- Barclays PLC
G. Lewis	- CIBC World Markets PLC
P. Maskrey	- Schroder Salomon Smith Barney
D.J. McMillan	- Lazard
K. Palmer	- Dresdner Kleinwort Wasserstein
A. Sowter	- Bear, Stearns International Limited

Banking

H. Angest (<i>Chairman</i>)	- Secure Trust Banking Group PLC
M.R. Aish	- NM Rothschild & Sons Limited
C.B. Price	- Singer & Friedlander Holdings Limited

Finance

A. Ballantyne	- Morgan Stanley International Ltd
S. Glass	- HSBC Investment Bank plc
M.J. Conway	- Mizuho International plc
P. Deighton	- Goldman Sachs International
D. Gendron	- Merrill Lynch Europe PLC
M.M. Moses	- JPMorgan Chase Bank
J.V. Ozanne	- UBS Warburg
D.G. Penfold	- Deutsche Bank AG London
G. Pennells	- Citigroup
M.R.P. Power	- Cazenove & Co. Ltd

SPECIALIST COMMITTEES

Accounting
Administration
Financial Regulation
Internal Audit
Personnel
Taxation
Treasury Operations
VAT

MEMBERS OF THE ASSOCIATION AT
31st MARCH 2002

Ansbacher & Co. Limited	Hawkpoint Partners Limited
ABN AMRO Bank N.V.	HSBC Investment Bank plc
Arbuthnot Latham & Co., Limited	ING Bank NV
BNP Paribas	Instinet Europe Ltd
Bank Insinger de Beaufort plc	Investec Bank (UK) Limited
Barclays Capital	J.P. Morgan Securities Ltd
Bear, Stearns International Limited	KBC Peel Hunt Ltd
Beeson Gregory Limited	Knight Securities International Ltd
Cazenove & Co. Ltd	Lazard
CIBC World Markets Plc	Lehman Brothers
Citigroup Inc.	Merrill Lynch Europe PLC
Close Brothers Corporate Finance Ltd	Mizuho International plc
Collins Stewart Limited	Morgan Stanley International Ltd
Commerzbank AG	Nomura International plc
Credit Suisse First Boston (Europe) Ltd	N M Rothschild & Sons Limited
Daiwa Securities SMBC Europe Limited	Robert W. Baird Group Limited
Dawnay, Day & Co., Limited	Singer & Friedlander Limited
Deutsche Bank AG London	Société Générale
Dresdner Kleinwort Wasserstein	3i Group plc
Goldman Sachs International	The Toronto-Dominion Bank
Greenhill & Co. International LLP	UBS Warburg
	Westdeutsche Landesbank Girozentrale