

LIBA

LONDON INVESTMENT BANKING ASSOCIATION

ANNUAL REPORT

1999

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.

Chairman's Committee

Mr M.J.P. Marks CBE Chairman
Mr H. Angest
Mr D.J. Challen
Mr P.A. Letley
Ms P. Pope
Mr H. Sants
Mr M.D. Seligman
Sir Adam Ridley Director-General

LIBA Executive Staff

Sir Adam Ridley <i>Director-General</i> E-mail: adam.ridley@liba.org.uk	
Peter Beales <i>Director and Secretary</i> E-mail: peter.beales@liba.org.uk	Chairman's Committee, Regulatory Reform, Finance, Compliance, Data Protection, Taxation and Legal
Timothy Baker <i>Director</i> E-mail: timothy.baker@liba.org.uk	Personnel, Marketing and Communications, E-commerce and EU Action Plan
Deborah Chesworth <i>Director</i> E-mail: deborah.chesworth@liba.org.uk	Financial Regulation and other Prudential Supervision, Risk Management, Equity Financing, Internal Audit and Administration
Ian Harrison <i>Director</i> E-mail: ian.harrison@liba.org.uk	Taxation, Accounting and VAT
Alison Scott-Bishop <i>Director</i> E-mail: alison.scott-bishop@liba.org.uk	Corporate Finance, Securities Trading, Settlement and Treasury Operations

Members of the Executive deal with European Union legislation relevant to their areas of responsibility.

6 Frederick's Place, London EC2R 8BT
Tel: 020-7796 3606 Fax: 020-7796 4345
Website: www.liba.org.uk E-mail: liba@liba.org.uk

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STATEMENT BY THE CHAIRMAN

The far-reaching changes in markets upon which I commented in my first report as LIBA's Chairman last year have continued unabated. The Report of our Chairman's Committee which follows gives a good picture of LIBA's principal activities. For both reasons I will be selective and focused in my comments, which are no substitute for that Report.

The changes in the worldwide financial marketplace open up new opportunities in wholesale banking and securities business for LIBA Members, provided certain conditions are fulfilled. That is in part why I concentrated last year on the need for LIBA to extend its reach into Europe, and devoted relatively few words to domestic issues and the looming Financial Services and Markets Bill. Since then, while LIBA's international priorities have not diminished, domestic regulation has demanded an exceptional, sustained effort both from our staff and from our specialist committees and working groups.

Domestic Regulation

The business of LIBA Members spans a wide range of financial services, so they stand to gain from the unification of the sectoral supervisors into one well-constructed regulator. Building the new system has to be a co-operative process. A sustained, open and constructive dialogue is needed between the Treasury which is writing the law; the Financial Services Authority (FSA) which is creating the new organisation; and the many kinds of businesses in the financial sector which are to be regulated. The FSA's consultative process, with some 45 numbered Consultative Papers to date together with many other Policy Statements and unnumbered papers, is an unprecedented initiative. FSA is to be congratulated on its efforts to obtain industry views on establishing such a complex organisation, although the exercise has not been without difficulty. Latterly, the extent of the consultative process has given rise to understandable concerns that "consultation fatigue" may set in, with neither practitioners nor FSA officials being able to give as much attention to proposed rules as they would wish. We have shared this concern with FSA. One implication is that unanticipated difficulties with the provisions may emerge which will necessitate amendments to the new rule book early on in the new regime.

The Parliamentary Joint Committee under Lord Burns which last year examined the Government's proposals and a consultation draft of the Bill was also an imaginative and productive innovation to which the Government made a significant response. Subsequently, however, there have been relatively few changes of importance to the Bill in response to industry representations on a wide range of major issues and the tabling of a number of important amendments in Parliament. The chief reason for this appears to be that Ministers have felt unable to relax a timetable which has proved to be unrealistically tight. So there is a risk that the Act and associated Orders which emerge later this summer will contain a number of avoidable flaws.

On the other hand and on the credit side, we have been able to develop a very effective ad hoc Group to review and make representations to the authorities on all aspects of the Bill. This "City Bill Liaison Group" includes those City trade associations whose members undertake wholesale business, together with some of the leading City law firms. The model of collaboration which we have evolved is economical, flexible and has proved to be an excellent way of bringing together a good mix of expertise and interested parties. We are using such ad hoc alliances in other areas, and I suspect they can be deployed more widely still.

Much of the pressure behind the reform is the wish to prevent certain quite specific kinds of abuse, and to improve the protection of retail customers. Pursuing these two goals in particular tends to draw regulators into a very prescriptive approach which could seriously inhibit dynamism, and which will almost always be inappropriate to wholesale businesses dealing with professional counterparties. An important feature of FSA's philosophy is the desire to build regulation on the foundations of a small number of general principles. This has understandable attractions. But it also exposes firms and their employees to practical risks once statutory regulation and the enforcement and discipline regimes are in force. Businesses feel they need to be confident that they are not breaching the regulator's requirements. If regulatory

intervention is based largely or wholly on general principles, they will not always be able to establish unequivocally whether or how a principle will apply. Hence they will be exposed to some risk of unforeseen sanctions. This threat will lead some firms to press for more detailed rules in order to secure the certainty they feel they need. But the price of this will, of course, be over-prescription. This awkward tension has been raised with FSA, which we recognise must strike a difficult balance between operating on general principles of market conduct and not taking unreasonable and unforeseen enforcement actions against businesses. All that said and by the same token, in return for "light touch" regulation by principles, businesses must necessarily accept a certain level of uncertainty. We believe that FSA recognises the kind of balance which has to be struck; and we trust that it will be able to respond appropriately to industry concerns.

It is self-evident that London's competitiveness will be undermined if "light touch" regulation for wholesale business is not maintained; that consumers need a measure of protection but must also take some responsibility for their actions; and that some large businesses may be of such systemic importance that it is in the public interest that they should be closely supervised. Today's regulatory efforts are sometimes disproportionately focused on non-systemic entities with at most modest retail consumer involvement, where failure should not be an issue of major concern to the regulators. We have therefore argued that FSA should not pursue a perfectionist policy of "zero failure", but gear the intensity of its supervision of each business to the level of systemic risk and consumer vulnerability associated with that business. The FSA's January 2000 paper "A new regulator for the new millennium" embraces these principles. We wholeheartedly welcome the vision it promises and look forward to what will be done in practice by the regulators under the new regime. In addition current work on the Inter-professional Code reflecting a "light touch" is most heartening.

A further threat to the competitiveness of non-systemic banks and securities houses arises from possible developments in international regulation. Such businesses face the threat that, under a revised Basel Accord, the new capital adequacy standards set for large international banks will be applied dogmatically both to their very different smaller brethren and to securities trading. I comment further on the current discussions about new capital rules below.

It is obviously essential that FSA's operations should increase rather than hinder the market's efficiency. Unfortunately there are still some important features of the Bill - such as the doubts raised about whether the new Market Abuse regime will undermine the authority of the Takeover Panel - which could damage our marketplace.

The creation of a regulator as comprehensive and as powerful as the FSA also raises in the most acute way the issue of accountability: to Parliament; to the sectors which are the object of regulation; and to society at large. Although helpful amendments have been made to the legislation, it will be important that there is regular and systematic reporting by FSA to an established Parliamentary body like Lord Burns' Joint Committee; and also it would be unsettling if the practitioner and consumer panels which are set up as part of the consultative arrangements under the legislation cannot rely on extracting a reasoned response by FSA to their recommendations or comments.

Looking ahead, much remains to be done. By the summer we will be responding to drafts of seven important sections of FSA's new Handbook, namely the Conduct of Business and Interim Prudential sourcebooks, and the Authorisation, Enforcement and Supervision manuals, together with the proposals for the Inter-professional and Market Abuse codes. There will also be a large number of important Parliamentary Orders, which will lay down in detail how the general powers under the Bill are to be used. LIBA staff and Members' staff on our committees will continue to have a great deal to do.

EU and International Developments

Last year I commented on the major decisions to be taken about the future structure of securities trading in Europe. This year has, after some delay, seen action on some of the most important. We must applaud the proposed merger between the Frankfurt and London exchanges, which should create a deep, liquid and transparent market Europe-wide. While there has been significant progress on clearing and settlement where the need for change is perhaps even greater, it has not gone far enough. According to estimates made by a number of our Members, clearing and settling a European trade can cost approaching ten times more than a comparable deal in the USA. The investors who have to bear these large and avoidable excess costs cannot be expected to tolerate them for very much longer.

On the regulatory front, it is clear that the recently completed Basel and European Commission consultations on capital adequacy represent only the first stage in the process. Important elements which will have a significant effect on the industry - for good or ill - will be flushed out over the coming months. We will continue to pursue the objective of a risk-sensitive framework which is flexible enough to allow the financial sector to maintain its rapid pace of development.

We have also been heavily engaged in work flowing from the European Commission's Action Plan for Financial Services which was published last summer. Our Chairman's Committee Report covers aspects of this in detail. LIBA's key objective is to establish a regime across Europe which, for wholesale business at least, recognises that only minimum rules are necessary and that firms can conduct cross-border business subject only to the rules of their "home State".

Electronic Commerce

E-commerce has now become a major "subject" for us. For LIBA Members, with their international interests, it promises many new opportunities, but at the same time reveals new obstacles and pressure for new regulation. Both at home and in the European Union (EU) important legislation is being prepared to clear obstacles and deliver appropriate regulation. The British Government has set an ambitious goal of making the UK the best environment for e-commerce by 2002. We suspect that this necessitates a more ambitious and comprehensive attack on the obstacles than is at present envisaged and are pressing Ministers and officials to raise their sights.

Internationally the regulatory debate hinges round a simple but vital issue. Should e-commerce services be regulated by the country from which a service is provided (home State) or by the country where the consumer resides? It should be evident that a world in which each country regulated all imported e-commerce services to its own distinct standards would be extremely complex and bureaucratic, arguably impossibly so. In contrast, regulation by home States is likely to be dramatically simpler; and can be made acceptable to retail consumers by setting up effective international arrangements for providing redress when disputes arise.

Taxation

Tax arrangements can be as important as regulatory requirements in influencing the location of business and, as the Report of the Chairman's Committee sets out, LIBA has been heavily involved in work on the European Commission's proposals for a "Savings Tax" directive and on transaction taxes imposed within the UK.

Again, much of this work has been taken forward in close co-operation with other bodies. The "City Group" which we formed has been the primary interlocutor with the Treasury and Inland Revenue, which have acted vigorously and effectively as the negotiations on the European proposals have proceeded. We believe that the City's concerns about this misconceived measure are now well understood and that serious efforts will be made to amend the proposals to avoid damage to financial services business in Europe.

On stamp duty, the position is much less satisfactory. We will continue to press the Government to take action before business is lost to the UK. There is very little time to lose.

Relations with Members and other Associations

A trade association is a joint enterprise between its staff and Members. The detailed report which follows makes clear that this combined effort has been to good effect over the past year.

A key strength of LIBA is the willingness of so many Members to contribute their time and expertise. My thanks are due to all those who served on LIBA committees and working groups during the year, and not least to my colleagues on the Chairman's Committee whose advice has been invaluable. We also rely on our staff and I would like to thank them too.

The worldwide nature of the industry makes links between associations such as ours of increasing importance. We continue to benefit from and to participate actively in the International Councils of Securities Associations. In addition we are exploring more active collaboration with appropriate counterparts within Europe on a number of topics of strategic significance such as e-commerce.

Mergers continue in the industry at an increasing rate, and in the light of this we will need to consider the membership fee structure which has been in place since LIBA was formed over ten years ago. I believe, however, that for the foreseeable future it will continue to be necessary to have an association which focuses on the needs of participants in the wholesale markets. The work with other associations which we have led over the past year has demonstrated that it is possible to deliver powerful messages to the authorities by acting together and that, by so doing, wasteful overlap can be avoided successfully.

Finally, in my last report, I recorded that Kit Farrow would be retiring as LIBA's Director General during the year. I must thank him again for all his efforts on Members' behalf since he joined the Association in 1992. His successor, Sir Adam Ridley, is ideally suited to take LIBA's work forward as we address the many difficult issues which face the industry in the years ahead.

M.J.P. Marks CBE
Chairman

REPORT OF THE CHAIRMAN'S COMMITTEE

CORPORATE FINANCE

Share issuing good practice

Bank of England guidance on "Share Issuing Good Practice" The Monopolies and Mergers Commission's (MMC's) report into underwriting in October 1999 led the Bank of England to publish guidance designed to assist companies to make informed choices between the various share issuing methods available to them and, in line with MMC recommendations, to encourage more widespread use of deep discounted issues and of tendering for sub-underwriting.

LIBA had expressed serious reservations about an early draft of the proposed guidance, particularly as regards the inefficient use of resources involved in corporate finance advisers providing issuers with information on the whole range of possible issuing methods, even though some of these would clearly be inappropriate for the issuers' needs or circumstances. The Bank of England made every effort to take LIBA's comments on board. The published guidance was far less prescriptive and far more even-handed in its presentation of the relative advantages and disadvantages of the various issuing methods.

Takeover Panel issues

Proposed Takeover Directive

Throughout discussions on the proposal for an EU Takeover Directive, LIBA has consistently supported the Takeover Panel in its contention that the Directive would increase the risk of litigation during bids as well as threatening the timely and pragmatic approach to takeover regulation which has been one of the most advantageous features of the UK's non-statutory system. The Government's objective has been to make the Directive as palatable as possible from a UK perspective. This has led to the reinstatement of Article 4.5 which is designed to limit the risk of damage to the existing UK system by increased litigation.

The Directive secured political agreement at the June 1999 Internal Market Council meeting. Spain, however, was not willing to approve it because of concerns that it would give the UK the ability to institute a separate takeover authority in Gibraltar. Recent reports suggest that an accommodation has been reached.

The Takeover Code and MBOs

LIBA responded to two consultative papers from the Takeover Panel. The first reviewed the general operation of the Code in relation to MBOs. We contended that the present provisions of the Code – both in their general application to all offers and in so far as they impose specific requirements in relation to MBOs – operate satisfactorily and that there would, therefore, be no benefit attached to the introduction of MBO-specific rules.

Rule 3 advisers' opinions

The second focused on Note 4 of Rule 16 dealing with the giving of a "fair and reasonable" opinion by a Rule 3 adviser upon the remuneration arrangements proposed for offeree managers who are to have a continuing role in the new company. LIBA's view was that, while a Rule 3 adviser could give an opinion as to whether the treatment accorded to such managers in their capacity as shareholders was equal to that accorded to other shareholders, it was not possible to identify positively whether individual elements of their overall remuneration package were given to them in their capacity as managers or shareholders and whether, as a consequence, any inequality arose between them and other shareholders. We expect to discuss the issue further with the Panel before any revised proposals are brought forward.

The new market abuse regime

Finally, LIBA has maintained close contact with the Panel about its concerns over the overlap between the Panel's regulation of takeovers and the FSA's responsibility for administering the market abuse regime, as set out in the Financial Services and Markets Bill. We have vigorously supported the Panel in seeking a solution to this problem.

Amendments to the Listing Rules

Listing Rules for young companies

Towards the end of 1999, LIBA responded to the UK Listing Authority (UKLA) consultative paper proposing a wide variety of amendments and additions to the Listing Rules. LIBA generally welcomed the document's most significant proposal – the introduction of a new chapter dealing specifically with the listing of companies without three year track records. However, we expressed concern about the unduly prescriptive nature of some of the detailed requirements proposed by the UKLA and argued that greater flexibility was required on the UKLA's part if its listing requirements were to accommodate the dynamic nature of such companies.

Sponsors' independence

In earlier correspondence with the UKLA on the subject of sponsors' independence, LIBA had suggested that the conflicts of interest which may arise as a result of employees of a sponsor holding shares in a client company could best be addressed by a disclosure-based regime rather than by way of an outright ban upon such shareholdings, as the UKLA had previously suggested. We were therefore pleased with the UKLA's proposal to introduce such a regime.

Advisers' responsibilities

LIBA circular on advisers' responsibilities

In December 1994, LIBA wrote to Members about the standard wording, previously agreed with the London Stock Exchange (LSE), for use in shareholder documents to describe the role and responsibilities of an investment bank in advising on a transaction. During 1999, LIBA's attention was drawn to the fact that Members are sometimes asked to agree to different wording in relation to such transactions, which increases both their responsibilities and potential liabilities. Consequently, the original 1994 circular was re-issued to Members in November with a covering memorandum which drew attention to recent changes in standard practice and to the disadvantageous implications which such changes may have for advisers.

Year 2000 disclosures

Guidance on Year 2000 disclosures

LIBA held extensive discussions with the UKLA on the difficulties faced by sponsors in providing disclosures and confirmations required under the Listing Rules (most particularly in relation to working capital) as a result of the uncertainties caused by the year 2000 date change. These discussions resulted in the UKLA issuing guidance to listed companies and their advisers at the end of March 1999. The guidance took our comments and proposals on board and provided an acceptable compromise solution.

Transfer of UK Listing Authority to FSA

Transfer of UK Listing Authority

In February 2000, LIBA responded to consultation papers from the FSA (CP 37) and from the LSE about the transfer of the UKLA function from the LSE to FSA. We pointed out the scope for difficulty caused by the proposal to delineate a separation between the concepts of “admission to listing” by FSA and “admission to trading” by the LSE. The concept that officially listed securities are “listed on the LSE” is deeply embedded in many areas of law and practice and FSA’s proposals may run counter to this. In addition, LIBA expressed concern at the LSE’s proposal to apply an additional layer of regulation on top of that to be applied by FSA. We understand that the UKLA has taken these concerns on board.

Interim Moratorium

Interim Moratorium

During the year, discussions continued on the operation of the Interim Moratorium which sets out general principles on the circumstances in which reporting accountants may seek to limit their liability when advising on corporate finance transactions. Since LIBA and the then “Big Six” accountancy firms entered into the Moratorium in December 1995, the accountants have informally indicated that, because of subsequent changes to the market, they wish to terminate it, although no formal notification of termination has been received so far. Given this, in August 1999, LIBA sent a circular to Members informing them of the likelihood of the Moratorium ending and of the legal advice which we had received as to the measures which investment banks could take to protect their interests in such an event.

SECURITIES TRADING

LSE implementation of the market model

Following the LSE’s announcement of its intention to move away from a project-based approach to systems development to a six monthly release-based approach, a number of LIBA groups met LSE representatives to consider how different attributes of the agreed market model could be put into effect in the UK markets.

LSE Release 3.1

The LSE has provided detailed briefings on the technical aspects of the implementation of LSE Release 3.1 as part of its regular sequence of meetings with LIBA’s Trading Systems Implementation Working Party. This release will introduce enhanced auction and price monitoring functionality to SETS in May 2000. The Working Party expressed concern over the proposed arrangements for firms to test their upgraded software against the existing and new systems. Subsequently, the LSE increased the number of testing options available to firms.

Central counterparty

LIBA’s Settlement Working Party also met representatives from the LSE, London Clearing House and CRESTCo to hear how the project to support anonymous trading by means of a central counterparty was being taken forward and to discuss detailed aspects of the proposed functionality and implementation timetable for this project including, in the medium term, the introduction of netting facilities.

Regulation of exchanges

FSA and FESCO work on regulation of exchanges

During 1999, we discussed with both FSA and the Treasury the regulation of Recognised Investment Exchanges (RIEs) and alternative trading systems (ATs). We expressed concern about regulating the former as if they continued to be near-monopoly suppliers of market services when in fact they are operating in an increasingly competitive world where securities houses have access to a variety of different trading mechanisms, many of which are not subject to the same type or level of regulatory obligations.

Since then, both the Forum of European Securities Commissions (FESCO) and FSA have sought views on the need to regulate the operation of ATs. LIBA submitted responses to both documents. We recommended that, in view of the current uncertainty surrounding the impact of ATs on European securities markets, regulators should be cautious about imposing regulations in order to avoid prejudicing future consideration of complex issues such as transparency obligations and access requirements. Regulators should aim to ensure that a level playing field is maintained and anti-competitive practices are not allowed to develop, while allowing market forces rather than regulation to determine the eventual structure of the market. (Our work on European initiatives is discussed in the Financial Services Action Plan section on page 17.)

Competitiveness of the UK securities industry

UK competitiveness

During the year, our Securities Trading Committee considered a number of issues which could threaten the position of the UK securities industry, given an increasingly competitive and internationally mobile market place for financial services and the clear determination of the authorities in other European countries to do all they can to attract business to their financial centres. Issues identified by the Committee and raised with the Treasury at a high level included the continuing imposition of stamp duty, the stringency of UK transparency requirements, the weakness of the UK's capital raising facilities for smaller companies as well as the exchange development issues mentioned above.

Market infrastructure

Market infrastructure issues

The Securities Trading Committee has continued to meet the LSE to discuss current issues. In particular, in a meeting in December 1999, senior LSE executives updated the Committee on progress with a number of initiatives including the status of the European exchanges alliance and potential next steps, the LSE's ability to compete with alternative trading mechanisms, the impact on the LSE of the euro and the UK's position in relation to EMU, the transfer of the UKLA to FSA, the LSE's plans for demutualisation, and work to persuade the Treasury of the merits of the abolition of stamp duty on share transactions.

Members of the Chairman's Committee and the Securities Trading Committee also met senior FSA personnel to discuss a number of initiatives including FSA's plans to publish a regulatory sourcebook setting out the approach to the regulation of RIEs and Recognised Clearing Houses, their plans to publish a Discussion Paper on ATs, the latest FSA thinking on best execution, the transfer of the UKLA from the LSE to FSA, and FSA's work on finalising the way in which the Market Abuse Code will interact with the rules of the RIEs and the Takeover Code.

Migration of settlement of gilt-edged securities from CGO to CREST

Transfer of gilts to CREST

We have been closely involved in the plans for the migration of gilts to CREST in the second quarter of 2000. We considered the test scripts issued by CRESTCo for the trialling of gilts in CREST and outlined a number of concerns to CRESTCo to which they have responded.

Delivery versus Payment models

DvP

Pursuant to the list of settlement development priorities established as a result of the Bank of England's Securities Settlement Priorities Review, the Bank established a DvP Steering Group whose main task was to agree the high level design for a DvP model to be adopted in the UK. This will provide settlement in central bank money in accordance with European Central Bank guidelines. A wide variety of organisations with interests in securities settlement and payment systems were involved in the Steering Group and the Chairman of our Settlement Working Party was LIBA's representative. The Steering Group agreed a high level model which was then passed to a second "owners" group which is overseeing the development of the project.

Future settlement arrangements

European settlement issues

LIBA's plans to replace the Settlement Working Party with a more strategic Securities Operations Committee were put on hold during 1999. While the Directors of Operations of a number of major firms agreed that it would be useful for them to have a forum through which they could seek to influence the way in which developments in settlement and clearing are taken forward, some considered that the forum would need to be more European-based. In the meantime, a number of major players in the European securities industry formed the European Securities Industry Users' Group (subsequently rebranded as the European Securities Forum) which aims to fulfil a similar role to the proposed Securities Operations Committee.

Equity financing

Global Master Securities Lending Agreement

Work in the equity stock lending and repo area has been dominated by documentation issues. Throughout the year, we undertook lengthy and detailed discussions with the International Securities Lenders Association (ISLA) about their proposed new Global Master Securities Lending Agreement, which is much improved as a result. The differences between LIBA and ISLA are now very few and these points will no doubt be dealt with by bilateral negotiation between participants. These discussions also led to a proposal that the 1995 Stock Borrowing and Lending Code of Guidance should be updated and we are participating in the work of a sub-group of the Stock Lending and Repo Committee (SLRC) which is taking this project forward.

Cross Product Master Agreement

LIBA was one of the Publishing Associations which, led by The Bond Market Association, launched a new Cross Product Master Agreement in February 2000. This "umbrella" agreement aims to facilitate bilateral set-off of close-out amounts outstanding under various industry master agreements following an event of default. This agreement is an important step in the industry's continuing efforts to improve the management of counterparty risk.

UK vote execution

In the summer of 1999, the Committee of Enquiry into UK Vote Execution, a group sponsored by the National Association of Pension Funds, issued its report. This included recommendations about the voting of stock on loan, in response to which we prepared a discussion paper analysing the complex practical and legal issues surrounding this subject. The issue is now being pursued in the wider forum of the SLRC.

REGULATORY REFORM

City Bill Liaison Group

Assessing and responding to the new legislation and to FSA's consultation papers has dominated the work of our Compliance Committee and the various working parties which it has established to consider specific issues. In addition, we established an informal grouping of trade associations and some of the leading City law firms, known as the City Bill Liaison Group, to work together in raising industry concerns with the Treasury and briefing Parliamentarians. The members of this Group have been the Association of British Insurers (ABI), the British Bankers' Association (BBA), the Futures and Options Association (FOA), the Fund Managers' Association (FMA), the International Primary Market Association (IPMA), the International Swaps and Derivatives Association (ISDA), Clifford Chance, Freshfields, Linklaters & Alliance as well as LIBA. This co-ordinated approach has delivered a focused and influential City response.

The Financial Services and Markets Bill

The Burns Committee

The Joint Committee of both Houses of Parliament, chaired by Lord Burns, was formed to consider the draft Bill and representations made on it. Our submissions concentrated on improving FSA's accountability, the operation of its disciplinary policy, the importance of the legislation distinguishing adequately between wholesale and retail business, and serious defects in the new market abuse regime. LIBA was a significant contributor to the Joint Committee's work. Uniquely amongst trade associations, we were asked to give oral evidence on two separate occasions, and our written submissions were published as part of the Committee's two reports.

European Convention on Human Rights

On market abuse, there was a serious concern that the draft Bill's provisions would breach the European Convention on Human Rights. Lord Lester QC, who was briefed by the City Bill Liaison Group, concluded in an influential opinion that, on a number of counts, the provisions as drafted would be at risk of successful challenge under the Convention if the legislation was not amended. Following the Joint Committee's reports, the Government agreed that the risk of challenge was such that a number of changes to the legislation should be made. These included amending the definition of the market abuse "offence", recognising that compelled statements cannot be used in market abuse proceedings, and introducing arrangements for the provision of legal assistance to those who do not have sufficient means to contest market abuse proceedings against them. Serious concerns remain, however, about the new regime. In particular: the Government has not accepted the industry's argument that the legislation should include an intention test; the provisions in the Bill remain very generally drafted; and it is not clear whether FSA's Market Abuse Code will provide sufficient certainty about the kinds of behaviour which will be regarded as being in breach of the requirements. FSA is still re-drafting the Code.

Lord Lester's opinion suggested, in addition, that FSA's disciplinary process – as it will apply to authorised firms and "approved persons" – would also need to provide the various procedural safeguards applicable to proceedings deemed to be "criminal" under the Convention. For LIBA Members, perhaps the

most important aspect of this was the Convention requirement that the breach of a rule should be reasonably foreseeable at the time an action is taken. The Government, however, concluded that FSA's disciplinary process would not be regarded as criminal under the Convention. While FSA has stressed that it is not the intention to impose standards which cannot be clearly understood, they continue to believe that the Principles alone will provide a basis for enforcement action in appropriate cases.

Accountability

On accountability, the Joint Committee made a number of important recommendations, including proposals for strengthening the Bill's provisions for the establishment of an independent investigator – a sort of ombudsman – to deal with complaints against FSA. We particularly welcomed this because, early on in our consideration of the draft legislation, we had thought that the investigator would provide an important element in the checks and balances structure for which the breadth of FSA's powers calls.

The Government also agreed that the legislation should explicitly require the establishment of the Practitioner and Consumer Panels – again a change which LIBA had pressed for – although some of the Joint Committee's recommendations about aspects of the Practitioner Panel's role have not been accepted by the Government so far. In particular, they have rejected the recommendation that where FSA decides not to follow the guidance offered by the Panel it should report that it has done so. We believe, nonetheless, that the Panel will have an important role in ensuring that FSA gives due regard to the industry's views. In January 2000, the Panel – currently entitled the Practitioner Forum – published its first annual report which included the results of an important survey into the industry's views on the regulatory structure and FSA's approach to regulation.

Competition

Another area of significant change concerns the provisions in the Bill on competitiveness, which were amended following the Cruickshank interim report recommendations, and which may be amended further following the final report "Competition in UK Banking". Although the Government has not accepted that promoting competition should be a formal FSA objective, a stance which the industry has generally supported, amendments have been made to the clause which sets out the various principles of good regulation which FSA must follow, and the Competition Commission has been given additional powers to assess FSA rules, guidance and practices.

Overall, the Joint Committee exercise was extremely valuable in scrutinising thoroughly some important areas of the legislation, even though there was widespread disappointment that a number of the Committee's recommendations were not accepted by the Government. In addition, there were a number of provisions in the Bill not considered by the Joint Committee – for example those dealing with the new financial promotion regime, the territorial extent of FSA's reach and the "reduction of financial crime" objective. We have continued to discuss Members' concerns on these matters with the Treasury.

The Bill was formally presented to the House of Commons in June and, at the time of writing, the measure was being considered in the House of Lords. There is general agreement that the Bill as presented to Parliament and subsequently amended is much better than the draft on which the Treasury consulted in 1998. However, there are a number of outstanding concerns which we have continued to pursue. It has also been necessary to consider a large number of Government amendments, including those needed to implement the decision to transfer the UKLA from the LSE to FSA. Whilst recognising the valuable progress that has been made in the earlier stages of consultation, there must be serious concern that it has been necessary for the Government to bring forward so large a number of amendments at extremely short notice, which has allowed little or no time for Parliamentarians, let alone the industry, to respond.

After Royal Assent, a large number of statutory instruments will need Parliamentary approval before the new legislation can be brought into operation. So far the Treasury has consulted on only three of these, dealing with financial promotion; the markets and instruments to be prescribed for the market abuse regime; and the activities which will be prescribed for the purposes of the legislation's authorisation

requirements. We have made submissions raising serious concerns about the proposed drafting of all of these. It is essential that there is a further round of consultation in good time before the Orders are finalised.

Prudential supervision

FSA's approach in supervision

In last year's Annual Report, we explained how Members' perceptions that supervision was becoming more burdensome and less pragmatic, and concerns about its future direction, had led us to instigate a programme of discussions with senior FSA officials in the supervisory area. In our meeting with them in May, we stressed the principles that it would be wrong for FSA to pursue a policy of "zero failure" and that the intensity of supervision applied to an institution should be linked to its systemic significance and the nature of its customer base. These were themes which we continued to pursue with FSA during the succeeding months. Against this background, it was particularly gratifying that FSA's January 2000 paper "A new regulator for the new millennium" established both of these principles at the core of its intended approach. The paper contained a clear rejection of zero failure and a strong commitment to a regime under which the amount of supervisory attention devoted to any particular issue or institution will be determined by reference to the magnitude of the threat which it poses to FSA's achievement of the objectives set for it under the legislation. Whilst this is clearly very welcome, our attention now shifts to what arrangements FSA proposes for delivering the new approach in practice and for monitoring performance "on the ground".

Prudential Sourcebook

A parallel debate which has run through the year relates to the development of FSA's Prudential Sourcebook. At the time of last year's Annual Report, FSA had already announced its intention to pursue a "twin track" approach. There would only be minimal changes when the legislation is implemented, and an "integrated" Prudential Sourcebook would be introduced at a later date. The regulator's thinking has continued to develop on both fronts and we have made several submissions over the course of the year. We welcomed FSA's confirmation that it would keep interim policy changes to a minimum, but we have continued to stress that firms should not find themselves exposed to disciplinary or other action if FSA fails to publicise changes to policy at this stage. Consultation drafts of the interim prudential requirements for banks and securities firms are expected in June.

The most recent consultation paper on the integrated final Prudential Sourcebook took on board most of the points which we had been pursuing. Specifically, FSA confirmed that the integrated prudential rules will not be introduced until 2002, with a minimum implementation lead time of a year, and has recognised that there are good reasons for differentiating between types of firm and between individual firms. On this latter point, we are considering the recent FSA Occasional Paper "Some aspects of regulatory capital" which contains important material, including early insights into how differentiation between types of firm might work in the light of FSA's supervisory objectives. We are strongly represented on FSA's Prudential Sourcebook Advisory Group and we will be consulting Members on draft chapters as they emerge over the coming months.

International capital adequacy developments

On the international financial regulation front, recent months have been dominated by consultation papers from the Basel Committee on Banking Supervision and the European Commission on proposals to update, respectively, the Capital Accord and the EU capital adequacy Directives. In our submissions, we argued, amongst other points, that the proposed new internal ratings approach to credit risk capital charges should be sufficiently flexible to allow a wide range of methodologies and degrees of sophistication, that there should not be a mathematically-based charge to cover operational and "other" risks and that capital relief should be available for all robust forms of credit hedging. We also stressed our support for "Pillar 2"

of the proposals – the idea, familiar to UK institutions, that supervisors should undertake a qualitative review of the adequacy of capital in the light of a firm’s overall risk profile and control environment.

On the European proposals, we also commented on the extent to which it is appropriate to extend methods developed by the Basel Committee for internationally active banks to all credit institutions and investment firms, and on proposals from the Commission to introduce more prescriptive rules on consolidated supervision. In addition, we took the opportunity to revisit the issue of deductions from capital for “holdings” in other credit and financial institutions. We had concluded from our debates last year with the UK regulators that the relevant provisions in the Own Funds Directive were flawed and the current review should provide a good opportunity to remedy them.

Other issues

Over the last year, other issues in prudential supervision and related areas have included FSA’s consultations on the arrangements under the new legislation for authorisation and permission and detailed policy debates on collateral, securitisation, credit derivatives and outsourcing.

Other FSA consultations

In parallel, we have responded to those FSA consultation papers which are important to Members. At the time of writing 45 numbered consultation papers had been published, covering areas ranging from the new Ombudsman and Compensation schemes to customer classification, the responsibilities of senior managers and other approved persons, and FSA’s approach to discipline and enforcement. We have kept Members informed of our deliberations through the regular circulation of Committee minutes and drafts of submissions as they have been prepared.

Major themes have included the importance of avoiding over-prescriptive rules, which would undermine innovation, and the need to avoid applying to wholesale business provisions which are designed to protect retail clients. The latter is not only important in the drafting of the rules which will apply to wholesale business, which we await. It also affects the structure and financing of the new Compensation and Ombudsman schemes. In response to the consultation papers on the latter (CP 24 and CP 33), we stressed that wholesale, international businesses should not be expected to contribute to the financing of schemes for protecting UK retail clients except to the extent to which such firms undertake private client business here, and that the structure of the schemes should be modified to reflect this.

Discipline

A continuing concern has been how FSA will use the disciplinary powers which the legislation provides and we have raised Members’ views about this at the highest levels within FSA. These concerns have coloured a number of our responses to consultation papers during the year including, in particular, the proposals on Approved Persons (CP 26) and on Senior Management Arrangements, Systems and Controls (CP 35). We have continued to stress that the kinds of behaviour which would give rise to a breach of the rules should be foreseeable and that the test of whether behaviour has failed to meet the regulator’s expectations should be based on an objective assessment of what could be reasonably expected of the firm – or individual – in the light of the circumstances at the time decisions were taken. FSA is still to bring forward its consultation paper on the Enforcement Manual, but it has stressed that it will not take decisions on whether to impose disciplinary sanctions with the benefit of hindsight. In particular, in the Approved Persons consultation paper, FSA emphasised that it recognised that “the senior manager will have to exercise his own judgement in deciding how issues are dealt with, and that in some cases that judgement will, with the benefit of hindsight, be shown to have been wrong. The senior manager will not be in breach ... if he can show that he exercised due and reasonable consideration before he delegated the resolution of an issue or compliance problem and reached a reasonable conclusion”. We believe that reassurance on these questions is essential and must be included in the new rule book.

Guidance and waivers

An overlapping issue is how FSA will respond to requests for guidance and for rule waivers: this will be particularly important given FSA's ability to apply disciplinary sanctions for breaches of the Principles alone. September's Policy Statement on this subject was generally encouraging. This did not take the form of a consultation paper but we submitted detailed comments on a number of aspects. Although FSA indicated that it would respond quickly and substantively to "reasonable requests" for guidance on regulatory requirements, there was a fear that it might respond less readily to requests from larger firms. In parallel, we have pressed the Treasury to include an additional provision in the new legislation to allow FSA to grant waivers in a wider range of circumstances than the Bill allows.

Other regulatory issues

Financial promotion

We responded to two consultations by the Treasury on the proposed regulatory regime for financial promotions. Representations by us and other bodies on the first consultation yielded considerable improvements in the proposed framework. Significant concerns remain, however, on which we are continuing to press. The main issues are, first, that the legislation is not sufficiently specific, so that it may prohibit communications whose purpose is not promotional; and, second, that the territorial scope which it asserts may result in firms' cross-border promotions being exposed simultaneously to overlapping regulatory regimes in different countries. We have also sought to ensure that existing exemptions which are particularly important to the wholesale markets are maintained in the new regime.

Money laundering

We have continued to participate in the Joint Money Laundering Steering Group (JMLSG), which publishes guidance to firms on compliance with the Money Laundering Regulations. We have also participated in the discussions between FSA and representatives of the financial services industry on FSA's proposals for a separate regime of money laundering rules under the new legislation. Our main priorities in this work have been to ensure that FSA's rules would neither undermine the legal effect of the JMLSG Guidance Notes, nor subject firms to unnecessary, overlapping or conflicting compliance obligations.

Training and competence

FSA has brought forward draft rules imposing on firms obligations to have standards of competence for their employees (CP 34). FSA has consulted us extensively and we have stressed the need for a regime for the wholesale and inter-professional markets which does not impose unnecessary, inappropriate, or intrusive obligations. The regime must recognise both the highly specialised expertise of many employees of investment banks and the great extent to which commercial pressure on firms ensures that they provide customers and counterparties with a highly competent service.

Other submissions

We have also made submissions on proposed changes to the default rules and on best execution. Draft rules on these are still awaited.

Insolvency law

We participated in the BBA's work responding to the Government's consultation on amendments to insolvency legislation. Our submission argued strongly against the inclusion of powers for the introduction of a requirement for a period of notice to be given before the appointment of an administrative receiver. The Government accepted the industry's representations on this point, which were also supported by the CBI. In addition, we have encouraged the Government to use the new insolvency legislation as a vehicle for adopting the widest possible interpretation of Article 9.2 of the Settlement

Finality Directive. This specifies how to determine governing law for the purposes of proving interests in securities in insolvency situations. This suggestion has not been accepted but other options are being explored.

ELECTRONIC COMMERCE

Electronic commerce in all its forms continues to increase in importance for all Members and there are important developments in the UK, in Europe, and at the World Trade Organisation (WTO). We have made extensive representations in all three fora to secure a sound legal framework for electronic communications and electronic commerce.

Proposed E-commerce Directive

In Europe the focus has been on the proposal for a directive on certain legal aspects of electronic commerce, which aims to establish a single market for electronic advertising and trading. Our representations have concentrated on reinforcing the internal market approach of the directive, based on: control by the State from which the service provider operates; minimisation of the scope for protectionist restrictions; and applying these principle as broadly as possible to all aspects of services provided electronically. We have provided advice to the DTI on the negotiations in the Council of Ministers, and have made detailed representations to the European Commission and MEPs.

Applicable law and jurisdiction

We have also made representations to the European institutions on the revision of the international Conventions which govern the applicable law and jurisdiction for contracts concluded between parties in different Member States, again to ensure, wherever possible, that control is by the State from which the service provider operates. A similar approach has governed our recommendations on the Commission's planned Communication on electronic commerce and financial services. Many of the proposed European measures are linked, and we have supported a comprehensive approach to updating the European legislative framework for electronic commerce.

Proposed Distance Marketing Directive

LIBA and other bodies have continued to track the progress of negotiations on the proposed directive on distance marketing of financial services to consumers. There has been little progress recently, but we still hope that the approach we have supported will prevail. In particular, Member States should be obliged to respect internal market principles and thus be prevented from introducing "host State" requirements more restrictive than those of the "home State".

UK legislation

In the UK, our work has concentrated on the Electronic Communications Bill, which will provide for a self-regulation scheme for "trust service providers" and for legal recognition of electronic signatures and electronic writing; and on the provisions on the law enforcement authorities' power to obtain access to encrypted information, which have now been transferred to the Regulation of Investigatory Powers Bill, as we and others advised.

On the Electronic Communications Bill, we have supported self-regulation as opposed to a statutory scheme, and we are continuing to press for a more comprehensive and permissive approach than the piecemeal update of existing statutes which is proposed. We are also seeking, with other interested parties, to initiate a more comprehensive review of law which may interact with electronic commerce.

Our work on the measures which are now in the Regulation of Investigatory Powers Bill has concentrated on preventing the establishment of any system of key escrow. We are also seeking to ensure that law enforcement authorities' powers do not conflict with confidentiality obligations, do not impose unrealistic

obligations on firms to maintain systems to enable them to provide keys or decrypted information to the authorities, and do not involve firms in excessive cost.

The Regulation of Investigatory Powers Bill also includes provisions to implement Article 5 of the 1997 "ISDN" Directive, which allows for lawful interception and surveillance of communications for business purposes. Our objective is to ensure that recording and monitoring practices conducted for good commercial reasons and subject to proper safeguards may be lawfully continued.

EU DEVELOPMENTS AND IMPLEMENTATION OF DIRECTIVES

Financial Services Action Plan

Financial Services Action Plan

The European Commission published its Action Plan for Financial Services during 1999, and initiated work on a number of the priority action points. The Commission's objective is to update the framework of European legislation for the financial services sector in order to reinforce the single market and take account of the changes occasioned by the introduction of the Euro and electronic commerce. The areas of particular interest in which LIBA has been most closely involved are the proposed Green Paper on the Investment Services Directive (ISD), the impact of ATSS, the proposed Commission Communication on the categorisation of investors, the review of market manipulation provisions, and the proposed Commission Communication on Electronic Commerce and Financial Services. On many of these issues we have worked closely alongside other associations representing participants in the wholesale markets.

Investor categorisation

LIBA responded to FESCO's consultation on categorisation of investors, which will inform the Commission's thinking as they develop their Communication. We emphasised to both FESCO and the Commission the importance of adopting a categorisation which reflects the needs of customers and counterparties, and which includes enough categories to provide an appropriate gradation of protection. Agreement between Member States on the categorisation of investors is important partly because it is likely to be easier to press forward on achieving a genuine single market for wholesale business than for retail business. LIBA has stressed the importance of basing the single market on mutual recognition by Member States of home State control over conduct of business rules, for which there is a particularly acute need in the inter-professional markets. This approach builds on interpretations of directives which the Commission has already given, and is consistent with the general thrust of European legislation on electronic commerce. We have stressed that approaches based on either full harmonisation of rules or control by the host State are unlikely to be workable.

ATSS

On the regulation of ATSS, market development should be driven by investor demand unless there are compelling reasons to do otherwise. We have emphasised to the Commission and FESCO that regulators of ATSS should not act on the basis of preconceptions about the effect of electronic trading mechanisms on liquidity or transparency. The main issues which we have stressed in our representations have been that the emergence of ATSS is driven by inefficiencies in regulated exchanges; that the technology and the markets themselves are rapidly evolving; and that technology itself offers new means of providing liquidity and transparency.

Market manipulation

On market manipulation, our representations have focused on the need for a cautious approach to legislating in view of the diversity of interpretations across Europe as to what is and is not market

manipulation. The Commission seems inclined to propose a directive, but it is unlikely that Member States' arrangements can be sufficiently harmonised, so a Commission Recommendation would be preferable.

Other European issues

Data protection

On data protection, the legislation implementing the 1995 Directive came into force in March 2000. We have continued to work closely with the CBI on cross-border data transfer issues. They have supported our argument that groups' own data protection policies should be recognised as a means of establishing adequate protection when personal data are exported. It now seems likely that the US authorities and the European Commission will reach agreement on "safe harbour" provisions which will permit transfers of personal data to the USA. In addition, and in part because of the Data Protection authorities' concerns about enforcement issues when personal data are transferred outside the EU, we made submissions to the Lord Chancellor's Department about the Contracts (Rights of Third Parties) Bill which amended the UK law on privity of contract. We were pleased that the Department agreed to amend the Bill, as we had suggested, to allow parties to apply the new legislation from the date of Royal Assent.

State aids

We have continued to monitor the development of the European Commission's work on the application of the EU Treaty state aid rules to guarantees provided by Governments and other State bodies. The final version of the Commission's Notice, which was adopted in November, addressed a number of the concerns which we and other bodies, including the Financial Law Panel, had raised.

Money laundering

We commented to the Treasury on the European Commission's proposal for a Second Money Laundering Directive. We welcomed the proposed extension to the existing Directive's coverage, although we are concerned that the European measure will not have as broad a coverage as the UK requirements.

ACCOUNTING ISSUES

Global harmonisation of accounting standards

International accounting harmonisation

1999 saw further moves towards the global harmonisation of accounting standards. The reorganisation of the International Accounting Standards Committee (IASC), which was announced towards the end of the year, is intended to transform the IASC into a body with the credibility to take the lead in setting global standards and to gain the backing of key bodies including the Securities and Exchange Commission and the European Commission.

In the UK, the Accounting Standards Board (ASB) has been increasingly reluctant to take a view materially different from the international consensus, even where there may be a good reason for UK companies to prefer a different approach.

LIBA broadly welcomes moves that will lead towards greater transparency across international financial markets and enable international companies to follow a single set of accounting standards for all their operations. There may be disadvantages, however. We will in particular need to be vigilant lest the financial weight of the US markets leads to the imposition of US approaches in cases where these may be unsuitable for application in the UK.

A separate risk is that new international standards may lead to significant changes in key ratios used by the regulators to monitor financial institutions. For example, the use of market values for pension fund assets could lead to significant short-term balance sheet volatility, despite the extremely long-term nature of the corresponding liabilities, and it is far from obvious how a regulator should regard such changes. We have discussed this issue with FSA staff, who have reassured us of their sensitivity to such problems. We will press the ASB to ensure that, where such problems may arise, ample time is allowed for full consultation with FSA before new standards are implemented. More generally, we will continue to consult Members to ensure that their views are given the fullest possible hearing, both on the harmonisation of standards and on any regulatory issues.

Other accounting developments

UK accounting standards

The ASB's exposure draft on current tax (FRED 18) contained an unsatisfactory proposal for the treatment of foreign dividends carrying payable tax credits, which we were disappointed to see was not rectified in the corresponding new standard (FRS 16). This could cause difficulties for securities houses which trade extensively in foreign stocks. So we have been exploring whether the Urgent Issues Task Force might address this issue. The ASB proposals for retirement benefits in FRED 20, and particularly the combined effect of using market values for assets and a corporate bond discount rate for liabilities, are likely to result – as noted in the previous paragraph – in significantly greater volatility in pension figures, which we believe could cause corresponding and damaging volatility in financial institutions' capital adequacy ratios. Our submission to the ASB highlighted this potential problem and asked it to reconsider its arguments for the choice of discount rate or, at least, to ensure that the transitional period is long enough to find practical solutions to any consequential regulatory problems.

Other international developments

LIBA commented during the year on a number of proposals from the IASC and the "G4+1" Group including papers on business combinations and on reporting financial performance. We have also continued to monitor the IASC and ASB work on financial instruments, where the key issue is the extent to which marking to market should become mandatory, and we are considering a substantial new G4+1 paper on leasing. On the European front, we have continued to comment on the Commission's proposals for a Recommendation on financial instruments disclosures by banks. In addition, the Commission's long-running project to amend the 4th and 7th Company Law Directives to allow non-banks to mark certain financial instruments to market has now resulted in a proposal for a Directive. At the time of writing, we are assessing its possible implications.

TAXATION

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

Proposed Savings Tax Directive

The European Commission's proposed "Savings Tax" Directive has again been the focus of considerable activity during the year. Under the proposal's "co-existence" model, Member States would be required either to impose a withholding tax on interest payments made to individuals resident in other EU countries or to disclose to other EU governments information about such payments to non-residents. There was from the outset a wide consensus in the UK – both among Members and among other financial institutions – that this proposal would be highly damaging to EU financial markets, particularly to the largely London-based international bond market and to private banking. Adverse effects would include acute market disruption from the triggering of call provisions in some bond issues, the risk of driving

paying agent and private banking business to countries outside the EU where the requirements would not apply, and higher costs for bond issues in the EU.

LIBA has continued to play the leading role in representing Members' views to the Inland Revenue, Treasury and Bank of England, as well as directly to the European Commission, to Finnish and Portuguese officials (during their countries' respective presidencies of the Council of Ministers), to key officials of other Member States, and to MEPs. We have co-ordinated the activities of the "City Group" – an informal grouping of the principal trade associations and major market operators formed to consider the implications of the proposals and to organise industry lobbying on them. The Group includes the ABI, BBA, IPMA, the International Paying Agents Association (IPAA), the Association of Private Client Investment Managers and Stockbrokers (APCIMS), the Association of Corporate Treasurers (ACT), the CBI, and the Corporation of London, as well as some fifteen major financial services firms.

The City Group has regularly met the Inland Revenue, Treasury and Bank of England. A series of notes was produced under the Group's auspices, setting out in some detail the key problems identified with the Commission proposals, and summarising the type of changes necessary to eliminate, or at least alleviate, them. These notes were welcomed by the Commission as providing "a very clear presentation of [the City's] position on each particular issue [which] will certainly be helpful for ... future work".

Exchange of Information

The UK Government submitted a paper to the Council of Finance Ministers (ECOFIN) in early September setting out its position, which to a large degree reflected the City Group views. The paper reiterated the Government's full support for "the fight against tax abuse and evasion", but stressed its belief that this was best achieved through exchange of information "on as wide an international basis as possible", rather than through the co-existence model. At the same time it offered a compromise approach based on full grandfathering for existing international bonds and exemption for new issues of bonds held in a clearing system. The UK continued to maintain a very firm line in opposing the proposed Directive at the December Helsinki summit, and under the subsequent Portuguese presidency. In February 2000 the Treasury published a further paper setting out in more detail the case for countering tax evasion by exchange of information and explaining how such an approach would operate. This policy was reinforced by the March 2000 Budget announcement that the UK's own paying and collecting agent withholding tax system is to be abolished and that new measures will be introduced to facilitate the exchange of information with other countries (also see "Transaction taxes" below).

LIBA strongly supports the principles adopted by the Government in these recent developments while, of course, stressing that there are many practical problems to be solved.

Transaction taxes

LIBA's annual tax submission was sent to the Inland Revenue and to the Treasury in early November. It focused particularly on the harm caused by transaction taxes (defined as taxes relating to the individual transactions conducted or processed by a business, as opposed to those levied on the results of the business itself) on the competitive position of London as an international financial centre. Apart from the proposed EU savings tax, the submission outlined the harm caused by, and the case for change or abolition, of the UK withholding tax rules for paying and collecting agents; the tax treatment of manufactured dividends; and the artificial distinction between banks and other financial institutions in relation to the treatment of annual interest. We also restated the case for abolishing stamp duty and SDRT on securities transactions, or at least announcing a target for their eventual elimination.

Paying and collecting agent rules

The arguments for abolition of the paying and collecting agent system, the administration of which has been causing serious problems for a number of our Members, were reiterated in meetings with the Inland Revenue in December 1999 and in February 2000. We were accordingly very pleased to see the

announcement in the Budget that these rules are to be repealed from April 2001. The details of the new measures for the routine provision of information to

the Inland Revenue are as yet unclear. It will obviously be necessary to ensure that they are not unduly burdensome on Members and, critically, that they do nothing to make the UK financial markets less competitive internationally. We are liaising closely with the Inland Revenue on the development of these measures.

Stamp duty

On a less positive note, we deeply regret that there was no reference in the Budget to the reduction or abolition of stamp duty and SDRT on securities transactions, despite indications that the Government is aware of the problems caused by these taxes. As LIBA and many others have repeatedly stated, these taxes are levied at a significantly higher level than corresponding taxes in other jurisdictions. So they create, amongst other adverse effects, a major disincentive for the largest multinational corporations to remain incorporated in the UK. It seems clear that the revenue from these taxes will be eroded as the markets circumvent them, and that attempting to preserve them risks irreversible damage to the UK securities trading industry.

Other tax issues

Other issues

Other issues which we have raised with the Inland Revenue during the year include the taxation of debt instruments issued by banks and securities houses and of ratcheting margins (the so-called section 209 issues), the need for a review of the three-year old rules covering loan relationships, the proposed extension of local currency elections to non-trading companies and the possible relaxation of the rules for UK branches of non-resident companies. We are pleased to report that positive progress has been made in each of these areas. It was announced in the Budget statement that the tax treatment of ratchet loans will be brought into line with most other commercial loans (although we are still debating other section 209 issues with the Inland Revenue) and that the loan relationship rules are to be reviewed later in the year. An extension of the system of local currency elections was announced in January 2000. An Inland Revenue paper published in March 2000 confirms that they intend to make the changes we sought in the taxation of UK branches of non-resident companies.

We were closely involved in the revision of the CREST "Blue Book" dealing with stamp duty and SDRT. A particularly important aspect of our efforts was to agree with the Stamp Office practical arrangements for the evidence required to support the use of the various stamp exemption flags in CREST.

Six principles for fiscal legislation

In our annual tax submission we again stressed the importance of the fiscal legislative process working, and being seen to work, in an equitable and sensible manner. We set out six principles which 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

Administration of VAT

During the year a number of Members expressed increasing concern over aspects of the administration of VAT by HM Customs and Excise, with particular reference to the inadequacy of consultation on certain recent legislative changes, including those announced in the 1999 Budget, and Customs' increasing

tendency to classify as avoidance certain measures which our Members (and their advisers) regard as no more than legitimate tax planning. These concerns were discussed at a meeting in October with senior Customs officials. The meeting focused particularly on the need for more effective channels of communication between LIBA Members and Customs, which it was hoped would lead to better consultation on prospective legislative changes, and on the need for Customs to understand that it would make no sense for LIBA Members, who included many of the leading global investment banks, to indulge in short-term schemes for VAT avoidance.

The tone of the meeting was encouraging, with constructive and open discussion on both sides, and agreement was secured to work towards better communication. The first of what is anticipated to be a regular programme of working sessions between LIBA and Customs was held in January 2000, at which we discussed a number of specific issues such as the status of the EU study on the application of VAT to financial services, the differential treatment of pension fund management between insurance and non-insurance companies, and the treatment of input tax in relation to securities research publications. We hope that a basis for a lasting improvement in relations has been established.

LIBA presented evidence to the Treasury Sub-committee inquiry into the work of Customs and Excise, focusing on our concerns about the lack of consultation on new legislation and on the increasing difficulties created by the ill-considered use of anti-avoidance measures. The Sub-committee's report was published in February 2000, and it was clear that similar representations had been made by other bodies. Amongst the Report's conclusions likely to be relevant to LIBA Members were a recommendation that Customs and Excise and the Inland Revenue should be merged, an expression of concern over the slow pace at which the Closer Working programme between the two departments had developed, and recommendations dealing with the need for greater clarity in "what [Customs] considers to be tax avoidance" and with the need for improved effectiveness of anti-avoidance procedures. We also presented evidence in similar terms to the National Audit Office (NAO) in relation to their current study of VAT avoidance.

Other VAT issues

Amongst other issues, LIBA made representations to Customs to express Members' considerable concern over a proposal to introduce a box on the VAT return to capture information on partial exemption. We believed that Customs had seriously underestimated the costs of implementing this proposal and that it would in any case have had no impact on the tax yield. We were therefore pleased that the proposal was abandoned in January.

PERSONNEL, ADMINISTRATION AND OTHER ISSUES

Personnel Committee

We cooperated with the CBI and other bodies on responses to a number of developments in employment law, in particular the welcome amendments to the Working Time Regulations which extended the scope of unmeasured working time and removed the requirement to record hours worked by employees who have opted out of the standard 48 hour week.

Our Personnel Committee has continued to operate as a useful forum for Members to exchange views and experience on a range of issues in employment law and practice, including aspects of the Employment Relations Act, data protection issues, European Works Councils arrangements, "whistleblowing", telephone and e-mail recording and monitoring, and contingency arrangements for the Year 2000 date change. The surveys of staff turnover and human resources productivity were continued, with the results made available to participants.

The Committee also contributed to LIBA's comments to FSA on its proposed Training and Competence rules (see Other regulatory issues above), and contributed to discussions on the proposal for a National Training Organisation for the financial services sector. As in the case of FSA's rules, a major theme here is the need to make special allowance for the specialised nature of much investment banking activity.

Administration Committee

Members of the Administration Committee meet quarterly to discuss and exchange views on issues of relevance to administration and facilities managers. Topics during last year have included preparations for the Year 2000, global supply contracts, outsourcing, relocation issues, document archiving and corporate travel policies.

Internal Audit Committee

The Internal Audit Committee has historically provided an opportunity for heads of internal audit (mainly from LIBA's UK-owned Members) to discuss matters of common interest in a relatively informal setting. Meetings have continued in this vein over the last year and subjects covered have included corporate governance reporting, fraud risk management, operational risk, outsourcing and internal audit involvement over the Millennium weekend. More recently, however, the Committee has been considering whether LIBA's activities in the internal audit sphere should be restructured. The proposal, on which at the time of writing we are consulting Members at large, is that a new committee, smaller but more representative of the range of LIBA's members, should focus on contributing to the development of policy whilst the networking aspects of the current arrangements should be preserved in a separate, wider forum.

Treasury Operations Committee

During the year, the Treasury Operations Committee reviewed the impact of the introduction of the euro and, in this context, monitored discussions by the "Heathrow Group". In addition, the Committee discussed Year 2000 preparedness and maintained a dialogue with organisations including, in particular, the Corporation of London on the practical arrangements for the Millennium weekend. The Committee also maintained close contact with the Bank of England's review of sterling money market instruments and is represented on the Bank's Sterling Money Markets Liaison Group and Money Market Instrument Review Working Group.

In July 1999, the Committee considered a document from the Association for Payment Clearing Services (APACS) on "UK Securities Settlement and Wholesale Payment Systems: Strategic Road Map" and discussed a number of issues arising out of the document with APACS. The Committee welcomed APACS' initiative in tracking the range of projects which were being undertaken in the settlement and payment area and has remained in close touch with developments.

The Committee was also briefed on the development of Continuous Linked Settlement and its plans to simplify the payment process in the foreign exchange market throughout Europe with effect from October 2001.

Year 2000 date change

We kept closely in touch with the preparations of Members and the authorities for the Year 2000 date change. In particular, we facilitated Members' discussions with the Bank of England on the management of liquidity in the interbank market in the run-up to the end of the year.

LIBA'S WEBSITE AND ELECTRONIC COMMUNICATIONS

LIBA has developed a website whose address is www.liba.org.uk. At present the site includes only public information, including a list of issues on which LIBA is working, on-line versions of LIBA publications, and a list of Members. Over the next few months we plan to extend the site to provide a private section accessible to Members only. This will include on-line versions of "LIBA Update" and LIBA responses to consultation documents and other briefing papers.

We have also updated our arrangements for e-mail communication, and all staff now have individual e-mail addresses on the liba.org.uk domain.

COMMITTEES OF THE ASSOCIATION

The Association has five committees representing Members' interests in Banking, Corporate Finance, Compliance, Finance and Securities Trading. 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

Banking

H. Angest (<i>Chairman</i>)	–	Secure Trust Banking Group PLC
M.R. Aish	–	N M Rothschild & Sons Limited
S.J.C. Dick	–	Henry Ansbacher & Co. Limited
C.B. Price	–	Singer & Friedlander Limited
M. Snyder	–	Saudi International Bank

Compliance

Ms P. Pope (<i>Chairman</i>)	–	Morgan Stanley Dean Witter
M. Blane	–	BNP Paribas
Ms P. Curtis	–	Warburg Dillon Read
R. Fiddemont	–	Singer & Friedlander Holdings
D. Gordon	–	Nomura International plc
A. Greatbatch	–	Deutsche Bank AG London
B. Harte	–	The Chase Manhattan Bank
R.J. Levy	–	Goldman Sachs International
D.J. McMillan	–	Lazard Brothers & Co., Limited
K. Palmer	–	Dresdner Kleinwort Benson
J. Westcott	–	N M Rothschild & Sons Limited

Corporate Finance

M.D. Seligman (<i>Chairman</i>)	–	Credit Suisse First Boston
Sir Mark Wrightson (<i>Deputy Chairman</i>)	–	Close Brothers Corporate Finance Ltd
R. Aylard	–	Deutsche Bank AG London
C. Baker	–	Hawkpoint Partners
M. Breuer	–	J P Morgan
J. Grace	–	Investec Henderson Crosthwaite
Miss R. Hedley-Miller	–	Dresdner Kleinwort Benson
H. Kahnamouyipour	–	Warburg Dillon Read
Ms P. Scott	–	N M Rothschild & Sons Limited
R.W.A. Swannell	–	J. Henry Schroder & Co. Limited
M. Tory	–	Morgan Stanley Dean Witter
P.J. Yates	–	Merrill Lynch Europe PLC

Finance

C.B. Tilley (<i>Chairman</i>)	–	Granville Baird
P. Freeman	–	Dresdner Kleinwort Benson
M. Moses	–	J P Morgan & Co Inc
J.V. Ozanne	–	Warburg Dillon Read
D.G. Penfold	–	Deutsche Bank AG London
G. Pennells	–	Salomon Smith Barney
M. R. P. Power	–	Cazenove & Co.

Securities Trading

P.A. Letley (<i>Chairman</i>)	–	CIBC World Markets Plc
H. Sants (<i>Deputy Chairman</i>)	–	Donaldson, Lufkin & Jenrette
M. Ackers	–	ABN AMRO Bank N.V.
J.R. Davie	–	Credit Suisse First Boston
S.J. Dobbie	–	Deutsche Bank AG London
S. Gee	–	S.G. Securities (London) Ltd
D. Hegglin	–	Morgan Stanley
C. Hipkins	–	BNP Paribas Group
R. Kyle	–	Salomon Smith Barney
D.L. Mayhew	–	Cazenove & Co.
A. Phillips	–	Warburg Dillon Read
D. Smith	–	Merrill Lynch International
G. Ward	–	Goldman Sachs International
A. C. D. Yarrow	–	Dresdner Kleinwort Benson

SPECIALIST COMMITTEES

Accounting
Administration
Financial Regulation
Internal Audit
Personnel
Taxation
Treasury Operations
VAT

MEMBERS OF THE ASSOCIATION
AT 31st DECEMBER 1999

Henry Ansbacher & Co. Limited	Robert Fleming Holdings Limited
ABN AMRO Bank N.V.	Goldman Sachs International
Arbuthnot Latham & Co. Limited	Granville Baird Ltd
BNP Paribas	Greig Middleton & Co. Limited
The Bank of New York Europe Limited	Gresham Trust p.l.c.
Barclays Capital	Hawkpoint Partners Limited
Bear, Stearns International Limited	HSBC Investment Bank plc
Beeson Gregory Limited	ING Barings
CIBC World Markets Plc	Investec Bank (UK) Limited
The British Linen Bank Limited	Lazard Brothers & Co., Limited
Cazenove & Co.	Lehman Brothers International Limited
CCF Charterhouse plc	Merrill Lynch Europe PLC
The Chase Manhattan Bank	J.P. Morgan
Close Brothers Corporate Finance Ltd	Morgan Stanley Dean Witter
Commerzbank AG	Nomura International plc
Credit Lyonnais Capital Markets PLC	Peel Hunt plc
Credit Suisse First Boston International	Royal Bank of Canada
Daiwa Securities SB Capital Markets Europe Limited	N.M. Rothschild & Sons Limited
Dawnay, Day & Co., Limited	Salomon Smith Barney
Deutsche Bank AG London	Saudi International Bank
DKB International plc	J. Henry Schroder & Co. Limited
Donaldson, Lufkin & Jenrette International	Singer & Friedlander Holdings Limited
Dresdner Kleinwort Benson	Société Générale
EFG Private Bank Limited	Sumitomo Finance International plc
English Trust Company Limited	3i Group plc
	Tokai Bank Europe plc
	Warburg Dillon Read