

Verena Ross & Helen Roberts
Financial Services Authority
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17 December 2007

Dear Verena and Helen,

Principles-based regulation – Focussing on the outcomes that matter & Policy Statement 07/16 – Feedback on DP 06/5: Confirmation of Industry Guidance

The Depository and Trustee Association (DATA) promotes the role of trustees and depositaries which provide protection to investors in authorised collective investment schemes (unit trusts and OEICs) in the UK.

DATA welcomes the opportunity to jointly respond to both the Principles-based regulation document and Policy Statement 07/16 – Feedback on DP 6/05: Confirmation of Industry Guidance.

Principles-based regulation

We recognise, and in general terms, support the implementation of Principles-based regulation in the UK. We do, however, note the limitations and challenges of applying such a regime.

We note that external influences such as European Directives will require relevant parts of the FSA Handbook to continue to be prescriptive and such rules should be clearly distinguishable from those that are intended to implement a principle.

In our view confusion exists in the industry as to how the Principles-based regulatory process will work. For example, with reference to comments in the Principles-based regulation paper, the first paragraph under “FSA guidance and supporting material” (page 10), could be interpreted to have general application throughout the Handbook rather than purely for those requirements that can be and are principle based. We are concerned, therefore, that regulated firms will be unaware of the intended application of the rules i.e. a prescriptive rule or a rule through which the FSA intends to promote a desired outcome.

The final paragraph on page 10, includes the suggestion of utilising the ‘dynamic approach’ of “Dear CEO letters” and case studies to achieve appropriate outcomes. We are concerned that “Dear CEO letters” may result in regulation without industry consultation. If “Dear CEO letters” are to become more prominent, we feel that their use should be limited to the reiteration, reinforcement or support of existing rules and principles. We are also concerned that these letters, in conjunction with case studies, will result in fragmentation of the regulatory framework caused by regulatory requirements and ‘desired outcomes’ being scattered and not held in one central place. We believe that such an approach will reduce the effectiveness of the UK regulatory framework.

Industry Guidance

We believe that the change of emphasis that will follow as a result of moving away from regulation to market based solutions brings with it certain risks. In particular, we are concerned about a potential scenario where, having investigated an issue, the FSA concludes that use of its rule-making powers cannot be justified but a decision is made nevertheless to proceed with a market solution.

Market solutions can be effective where the FSA and the industry have agreed the issue and more importantly the proposed market solution. However, where the FSA sees a risk of market failure and/or there is disagreement over the appropriate market solution to be applied, we have concerns that the alternative approach may not provide consultation opportunities and cost/benefit considerations equal to the established channels for rule making. However, our concerns will be somewhat alleviated depending on the extent and practical implementation of comments in Policy Statement 07/16, paragraph 1.7 and, in particular, the second bullet referring to what the FSA *will* do and the fourth bullet addressing what the FSA *will not* do.

While we welcome this new approach to issue resolution, further consideration should be given to the practical implications facing both regulated firms and the FSA.

In summary, DATA believes that:

1. it is important for all users of a Principle based rule to know what the FSA expects as the outcome. This may be achieved by including the expected outcome within Guidance attached to the Rule;
2. with the issue of "Dear CEO" letters/equivalent publications, or references in FSA speeches to a particular approach, any expected outcomes, which extend beyond existing rules and principles, should be the subject of formal consultation.
3. DATA is keen to continue to work with the FSA and other trade bodies to help ensure that appropriate outcomes are achieved in a principles-based regulatory environment.

Should you have any comments, please don't hesitate to contact us.

Yours sincerely

John Cargill
Chairman