PARLIAMENTARY DEBATES

HOUSE OF COMMONS
OFFICIAL REPORT
GENERAL COMMITTEES

Public Bill Committee

FINANCIAL SERVICES (BANKING REFORM) BILL

Second Sitting

Tuesday 19 March 2013

(Afternoon)

CONTENTS

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not later than

Saturday 23 March 2013

STRICT ADHERENCE TO THIS ARRANGEMENT WILL GREATLY FACILITATE THE PROMPT PUBLICATION OF THE BOUND VOLUMES OF PROCEEDINGS IN GENERAL COMMITTEES

The Committee consisted of the following Members:

Chairs: Mr Peter Bone, †Dr William McCrea

† Ashworth, Jonathan *(Leicester South)* (Lab)
† Clark, Greg *(Financial Secretary to the Treasury)*
† Doughty, Stephen *(Cardiff South and Penarth)* (Lab/Co-op)
† Durkan, Mark *(Foyle)* (SDLP)
† Evans, Graham *(Weaver Vale)* (Con)
† Hands, Greg *(Chelsea and Fulham)* (Con)
† Jamieson, Cathy *(Kilmarnock and Loudoun)* (Lab/Co-op)
† Leslie, Chris *(Nottingham East)* (Lab/Co-op)
† Mills, Nigel *(Amber Valley)* (Con)
† Morris, James *(Halesowen and Rowley Regis)* (Con)
† Mowat, David *(Warrington South)* (Con)
Qureshi, Yasmin *(Bolton South East)* (Lab)
† Rees-Mogg, Jacob *(North East Somerset)* (Con)
† Sharma, Alok *(Reading West)* (Con)
† Smith, Nick *(Blaenau Gwent)* (Lab)
Stevenson, John *(Carlisle)* (Con)
† Thornton, Mike *(Eastleigh)* (LD)
† Williams, Stephen *(Bristol West)* (LD)
† Wright, David *(Telford)* (Lab)

Neil Caulfield, *Committee Clerk*

† attended the Committee

Public Bill Committee

Tuesday 19 March 2013

(Afternoon)

[Dr William McCrea *in the Chair*]

Financial Services (Banking Reform) Bill

2 pm

The Chair: May I draw Members' attention to the fact that copies of the Financial Services and Markets Act 2000, as amended by the Financial Services Act 2012, together with other amended statutes, are now available in the room?

Clause 4

Ring-Fencing of certain activities

Amendment proposed (this day): 26, in clause 4, page 3, line 35, at end insert—

'(3A) In making an order under subsection (2)(b) which—

(a) provides an exemption for UK institutions holding deposits below a specified amount, or

(b) varies the amount previously specified for the purposes of such an exemption,

the Treasury must aim to enhance competition among UK institutions which have a Part 4A permission relating to one or more core activities (in particular by having regard to the likely effect on the number of UK institutions applying for or obtaining such a permission for the first time).'.—*(Cathy Jamieson.)*

Question again proposed, That the amendment be made.

The Financial Secretary to the Treasury (Greg Clark): We were having an interesting debate about the importance of competition in banking. Before lunch, at least, I was feeling accommodating to some of the views that have been expressed. I am pleased to say that my lunch has not changed my mood in this respect. In fact, it might even have fortified the direction in which I was inclined. We will come on to talk at various points about various measures to strengthen competition, including in the important area of payment systems.

Amendment 26 suggests that the Treasury, in determining exemptions from the ring-fencing de minimis procedure,

"must aim to enhance competition".

I find myself wondering whether the hon. Member for Kilmarnock and Loudoun is not going far enough; I would encourage her to be more demanding when it comes to the requirements to promote competition. The amendment gives rather too much leeway to the intentions of Treasury Ministers and officials in years to come, and I would have thought that it could be more robustly expressed. The hon. Lady will know that it is sometimes hard to measure intentions and it is harder still to determine whether those immeasurable intentions have been met in practice. That rather lets us off the hook here.

Amendment 26 also refers to

"UK institutions holding deposits below a specified amount"

and seeking this as an area where competition should be encouraged. As we have debated already, that is certainly a desirable area in which competition should take place. But there might be an opportunity here, not least because the Bill allows for activities other than deposit-taking to be included in future through a particular statutory instrument. However, to constrain the Bill to refer only to competition among UK institutions holding deposits is probably too narrow. It might be better for it to apply to the banking system more generally.

I have reflected on the amendment and the contributions so far and it is my firm determination to use the Bill to drive competition through the system. I will therefore reflect further on the amendments with a view, more than simply accepting their spirit, to ensuring that they go further and are more robust in their requirements on the Treasury in addressing these matters. I hope that satisfies the Committee.

Cathy Jamieson (Kilmarnock and Loudoun) (Lab/Co-op): I am not quite sure what the Minister has had for his lunch. Whatever it was, it seems to have given him strength of purpose in coming back ready not only to take on the points made in the debate but to suggest that he will go even further.

I do not want to be churlish or to cast any aspersions on the Minister, but it might have been nice to have seen some of that resolve in the form of Government amendments tabled at this stage, so that we could have considered them in the context of the amendments we tabled as a result of the recommendations from the Banking Commission.

Given that the Minister seems to be in positive mode, I will resist the temptation to press that particular point any further. I welcome the fact that he has listened to what the Banking Commission has said. It very clearly recommended a specific requirement for a decision imposing or revising a de minimis requirement to have regard to its effect on competition in retail banking—new entrants in the market, in particular. That is why the amendment has been framed as it has.

It would certainly not be the intention in any circumstances to give the Minister too much leeway. We obviously want there to be checks and balances to take account of how Ministers come and Ministers go, as we often say. Future Ministers might not set such a positive tone as the Minister is setting or has set until now—although he may, of course, be reined in before the end of the sitting.

I hear what the Minister says about what would be on the face of the Bill, which would potentially constrain opportunities for the future. The Minister appears to be not only in listening mode, but also prepared to act in terms of the principles of what is outlined in the amendments. Indeed, if I understood him correctly, he will bring forward amendments in the future.

Greg Clark *indicated assent.*

Cathy Jamieson: He is nodding. On that basis, I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Chris Leslie (Nottingham East) (Lab/Co-op): I beg to move amendment 6, in clause 4, page 5, line 35, at end add—

'(8) Within six months of this Act receiving Royal Assent the Treasury shall carry out a review of the regulated activities of dealing in investments as principal, the purposes of which review shall include consideration of—

(a) safeguards that may be required to prevent the mis-selling of investments as principal as part of the core services of each ring-fenced body;

(b) a definition of "simple derivatives", will reference to their size, maturity and basis, the dealing of which will be permitted under section 142C;

(c) the establishment of a maximum ratio, relevant to the size of the balance sheet of a ring-fenced body which provides core services, for the value of investments as principal held as financial assets or liabilities on its balance sheet;

(d) the establishment of a maximum gross volume on the balance sheet of a ring-fenced body which provides core services, for the value of investments as principal held as financial assets or liabilities on its balance sheet; and

(e) the information that may be required for an independent valuation of a financial institutions's assets or liabilities in respect of relevant investments as principal.

(9) The Chancellor of the Exchequer will—

(a) lay before Parliament a report of the review in subsection (8); and

(b) provide, by Order subject to an affirmative resolution of both Houses of Parliament, such safeguards as may be set out in the review in subsection (8).'.

We now come to the amendment to new section 142(d) of the changes to the Financial Services and Markets Act suggested by clause 4. Members will be delighted to know that this is the first of the Labour party's very own home-grown and drafted amendments; it is not at all cut and pasted from the back of the Parliamentary Commission on Banking Standards report, but is very much inspired by the work that the Commission has undertaken so far.

We felt it was important to press the point a little further. We are talking about the sale of derivatives, as well as the activity of providing or selling what are sometimes called investments as principal, or financial instruments such as futures, options or other forms of derivative. The scenario of when that takes place within the context of a ring-fenced retail bank has received considerable attention and discussion.

I am sure hon. Members will be familiar with the original stance taken by the Vickers Commission in its independent report in September 2011, which basically said that derivatives trading should not be allowed—full stop. It was very firm on that. The Commission thought that such trading was a problem for a number of different reasons, and that it should be countenanced by a ring-fenced retail bank only if it was acting as an agent for products sold by others, certainly not if it was acting in its own right as principal provider.

The Parliamentary Commission, however, has subsequently looked into the issue in further detail. Vickers spent a lot of time looking at the capital adequacy of the structural issues, and perhaps did not drill into the derivatives questions as much as the Parliamentary Commission has. It recognises that there are certain services on the margins where some very simple derivative products might be permissible, but they underline the caveat. They caution that

"Allowing ring-fenced banks to sell derivatives other than as an agent creates additional prudential and conduct risks."

The prudential risks are self-evident because of the historic growth of derivatives activities, particularly in the last decade. The mention of conduct risks is an allusion, no doubt, to the mis-selling of derivative products, such as interest rate swaps and hedging instruments, in which many small businesses found themselves entangled. We all know the story—compensation worth billions of pounds has been agreed for such customers. The Commission has been pretty sensible on the matter, and the Opposition agree with its stance.

Clearer protections are needed to prevent abuses from occurring in the ring-fenced retail banks, where derivatives will be allowed in limited circumstances. The mis-selling of interest rate swap products to small and medium-sized enterprises illustrates the danger of information asymmetry, where one party to a transaction is very savvy and knows what the returns will be but the other party—perhaps the purchaser—is not as informed or as aware of the risks.

Financial services practitioners have exploited such asymmetry between customer and vendor for far too long. More broadly, a key lesson we have learned is that to place the financial services sector on a more sustainable footing, we have to leave behind the era in which firms thought they could extract profit on the basis of customer ignorance or lack of information. The practices of that era have to go, and the financial services sector must make its returns on the basis of genuinely added value and the professional acumen that financial intermediaries add to products.

We are in a period of transition from the previous era to a new one, and derivatives are an important aspect of that. They are a lucrative business for many banks, which will, no doubt, attempt to test the boundaries and see what can be done on the margins.

The Parliamentary Commission made it clear that three tests should be met if derivatives are to be permitted in the ring fence. First, the Commission wanted there to be adequate safeguards against mis-selling, and in drafting amendment 6 we were guided by the Commission's recommendations:

"Within six months of this Act receiving Royal Assent the Treasury shall carry out a review of the regulated activities"

of derivative trading within the ring fence. It is essential that we consider what safeguards might be required to prevent the mis-selling of derivatives.

2.15 pm

The Government have attempted to reflect the Commission's views, particularly those expressed in the first report, and the Minister has published some draft secondary legislation on the matter. From what I have seen of it, however, it does not really get into the detail of the mis-selling safeguards that might be needed. It covers other aspects, but it does not give the FCA or the PRA any new powers of enforcement in relation to mis-selling. We are still disentangling the issue of interest rate swap selling. The FSA has done a lot of work on that and on ensuring that the big five banks make arrangements for compensating their customers, which

is the immediate mis-selling problem. There are, however, risks of mis-selling in future, and the secondary legislation does not really deal with those risks.

The second test that the Banking Commission set out was that there needed to be a clear definition of a simple derivative. If we are going to allow simple derivatives, versus complex derivatives which, by extension, are going to be disallowed, then we have got to make sure that we have a line drawn on that.

Again, the Treasury and the Minister have published draft orders on what those particular changes are going to look like, in which they define what they regard as a derivative. First, they say that derivatives should include

"instruments designed to tackle interest rate risk".

We can all imagine those fixed-term mortgage products which I suppose you could say were a simple form of derivative because they are normally sold through the banking environment, but a lot of people might not realise that there is a hedging flavour to those.

The Treasury then adds on other types of derivatives that it thinks come under this definition—exchange rate risk, default risk, liquidity risk or dealing in assets included in the liquidity asset buffers that those banks themselves may need to manage. As I said on Second Reading, that is quite a broad definition of derivatives. In fact, at the time I suggested that it would probably be more useful if the Minister could say what would not be included in that definition. It would be helpful and would give a bit of colour and flavour to the Committee, if we could bring this to life. Give us an example of particular products that would be on the wrong side of the line; what sort of products are permissible derivative activities? That definition is still untested.

We have put in our amendment that we need, within six months, a proper final report on what that definition should be, particularly with reference to the size and maturity of those derivatives and the basis on which they have been agreed. The third test that the Parliamentary Commission set in respect of derivatives was this question about limits on the proportion of a bank's balance sheet that it can expose to derivative activities. The Parliamentary Commission talks about different ways to achieve that. First, it says that there should be a maximum ratio of derivatives to core services relative to the size of the balance sheet. That is a way of devising a metric to test what that maximum limit ought to be. They also say that derivatives should represent a maximum gross volume on the balance sheet of a ring-fenced body that is providing core services. So it has two tests for that and I would be grateful if the Minister would elaborate on that point.

As I was flicking through the draft statutory instrument—you can imagine me with my candlelight late at night, 1 am— I lighted upon the small print that says this is the level, this is the cap, this is the maximum volume. As I recall, the draft order has a percentage figure, but the actual number is missing. It is just one of those frustrating moments when preparing for these things. The Minister has produced the draft order, but they have not quite got to what they feel the figure ought to be. I hope, now that we are in Committee, that the Minister will be able to say, "What should that maximum ratio and volume be? Can we put a figure it?" That would be helpful to get a sense of the Government's thinking.

The other aspect that we have put in our amendment is that we feel that, as a way of assisting the regulator, the Treasury needs to set out more clearly the information that might be required for an independent valuation of a financial institution's assets or liabilities in respect of derivatives. Trying to understand, measure and get a sense of quite how vast derivative exposures are, whether they are mark-to-market or on whatever basis, is a big task. It is important that we get a sense of what the definitions are, how we are going to get the information necessary and what the basis of the evaluation process will be, and we also put that in our amendment.

The amendment is pretty straightforward. It simply calls for the Treasury to do more work, but with a deadline attached; we hope that that is not controversial. We need some assurances from the Minister because some very strong views have been expressed on the matter. In the evidence about derivatives within the ring fence that he gave to the Parliamentary Commission, Martin Taylor said:

"I can't see the point of having a fence round the chicken coop, electrifying it to keep the foxes out and then inviting a family of tame foxes to live inside it."

That is a good way of saying that we have to be very careful about this issue. Vickers clearly had a suspicion about derivatives within the ring fence, which is why he said that that was absolutely forbidden and we had to keep them out.

We can see that there are some questions, on the margins, about ordinary products; that is why the situation needs to be tested. We want to tease the issues out a little more. Setting the deadline of a six-month period after Royal Assent would be the best way of approaching a review. It is reasonable to ask for clarification on the questions covered in the amendment. The Minister will no doubt say that the Prudential Regulatory Authority will review the whole process annually, and that there is a separate Commission recommendation that the PRA's annual review should also look at some derivatives issues and test how derivatives are working within the context of the ring fence. However, that is a separate issue from establishing a baseline from which to measure how far derivatives activities should be allowed. We need the Treasury to lead on that and to come to a conclusion. Of course, we then need the PRA to keep an eye on it, monitor it and audit how things are going, but that is not a substitute for a review.

The public and the business community will want to know—especially as we have had such a scandal about mis-selling of interest rate swap products—what steps the Government are taking to prevent mis-selling. It is not simply a question of mopping up the problem that has occurred; we must prevent difficulties arising again. That is why we have tabled our amendment, and I hope that hon. Members will support it.

Greg Clark: Here is another novel twist for the Committee. We spent the morning debating amendments suggested by the PCBS and tabled by the Opposition, and now we have the Opposition anticipating amendments that the PCBS might have suggested had it got to that point in its deliberations.

It is useful to be able to debate these matters, which, I think, have been one of the more difficult things both for the Independent Commission and the Parliamentary Commission to reach a settled view on. There have been

discussions backwards and forward around this issue. The Government referred the matter to the PCBS and asked it to advise us in its most recent report, and it has thrown it back to us to make the detailed rule. The issue is clearly exercising all sides.

As the hon. Gentleman said, the PCBS has said that there should be three safeguards: adequate protection against mis-selling; a durable definition of what is and is not a simple derivative; and a limit on the proportion of such products on a bank's balance sheets.

There are a couple of outstanding issues that the Committee needs to reflect on. The first is that, as the hon. Gentleman acknowledged, the Parliamentary Commission itself is continuing to reflect on some further aspects, including conduct. He rightly said that that was very important, not least for our constituents, many of whom have been mis-sold interest rate swaps and so have a keen interest in this matter. The Parliamentary Commission has said that it will opine on what the provisions should be on the conduct of the sale of derivatives, and it is appropriate that it should do that.

The other factor that the hon. Gentleman mentioned was that we have published a draft statutory instrument. Given that those recommendations from the PCBS followed some time after some of its other recommendations, the consultation in line with its report will take place in the summer.

Nick Smith (Blaenau Gwent) (Lab): I listened carefully to what the Minister said about the difficulty of reaching a settled view on some of these issues. Indeed, in the Treasury's note on this, there is talk in paragraph 2 on page 18 of further consideration at a later date. However, as we are here in the Bill Committee, will he give us some examples of the types of safeguards that will be needed to protect the consumer? We need more detail, please.

Greg Clark: Indeed I will; I hope that the Committee will be satisfied. The amendment proposed by the hon. Member for Nottingham East calls for a review six months after Royal Assent is attained. In effect, we propose to consult in detail over the summer, including on the points raised in the Parliamentary Commission's recent report that are reflected in the amendment before us. All of those points will be subject to a formal consultation to allow us to establish those positions not six months after Royal Assent but six months before. That is the right way to do it.

One of the matters to be consulted on will be the types of contract that would apply. The hon. Gentleman asked about what should be included in that, and what should not. Again, that will be put out for consultation, but we have limited the types of derivative products to those set out in the current FSA handbook; that is to say that it is principally swaps at the exclusion of option-based derivatives. In other words, there should be a role for hedging against the most common risks that apply and a clear relationship between the price of the underlying asset and the swaps. We would expect anything more complex than that to be outside. However, these matters are reflected in the draft.

In terms of restrictions on the complexity of the instruments, article 4(2)(b) places restrictions on the pricing of derivatives: there should be a clear relationship that means that it is possible to value the portfolio by an objective standard. There are various other aspects: the availability of a market price for the contract is one of the tests that should be there, as is the question of whether a ring-fenced bank can have a limit on exposure. That overall limit of exposure is something that the PCBS said we should consult on over the summer. Valuations are important, but the main purpose is to make sure that the regulator is powerful and competent enough to do its own valuations; it will, in effect, make that decision.

Stephen Doughty (Cardiff South and Penarth) (Lab/Co-op): Will the Minister share with us what the Government have learned from the Markets in Financial Instruments Directive process and the MiFID II talks that have been ongoing? Those are a wider set of regulations that will cover a wider set of issues, but much of that has looked at the status of derivatives and issues that have come out of the financial crisis. To what extent have the Government taken what they learnt in that process to address this? It would be helpful to have a comment on that.

Greg Clark: The hon. Gentleman makes a good point. We have been learning from—and, of course, influencing—that process. The progress that we have made on MiFID in terms of transparency of some of these products is important. They are a very narrow subset of products to the customers of ring-fenced banks and the degree of complexity anticipated in MiFID and the debate on transparency, dark pools and the various technical and sophisticated investment opportunities are absolutely excluded from this purpose.

2.30 pm

The intention is to consult over the summer on both the draft statutory instrument and the recommendations made by the PCBS. I confirm that all the points raised by the Opposition amendment will be included in the consultation, so we will have views from stakeholders across the board. For reasons that hon. Members have expressed, it is right that we have that consultation during the Bill's passage, rather than beyond the end of Parliament's consideration of the Bill. In effect, the consultation will be six months before Royal Assent, rather than six months afterwards. The results of the consultation will be reflected in the final statutory instrument, which I confirm will be under the affirmative procedure, so there will be every opportunity for debate.

Nick Smith: The Minister says that the consultation is important, but I do not think we should, to use a fashionable phrase, kick the can down the road for too long. We need to firm up some of the important issues. Do the Government have a view yet on the proportion of a bank's balance sheet that should be taken up by such products? Do the Government have a working position?

Greg Clark: The PCBS is inquiring into that, and we asked it to advise us. When we referred the matter to the PCBS, it reflected the range of responses to the Government's consultation on the original Vickers review, which was fairly balanced. We thought that the opportunity of having an expert commission consider the matter, of

[Greg Clark]

having another pair of eyes, was sensible. The Commission is considering that, and its advice will be included in the consultation.

I totally agree that we should get those matters tied down. It is right to get agreement in advance, and I understand the reasons for that. The amendment gives us an opportunity to debate the intention of the arrangements for derivatives, but I think everyone would agree that it is better not to wait to finalise such things until six months after Royal Assent but to finalise them in advance.

We have a consultation, and it will include the points that have been raised, as well as further reflections, hence the timing of this summer, which will give the Parliamentary Commission further time to complete its inquiry.

Chris Leslie: I am slightly worried that a pattern is emerging in the attitude towards the legislative process, and towards this Committee, in pinning down some of those things. The Minister says there will be consultation over the summer, but can he tell us by what date the Treasury will conclude those issues? For the sake of trying to hold the Treasury's feet to the fire, we have suggested a date six months after Royal Assent, but can he give us a firm date by which the Treasury will publish such a review, as we have requested?

Greg Clark: Yes. Our intention is to debate those things before the Bill passes to the House of Lords, so there will be plenty of opportunity to consider that and to be informed by the consultation. As hon. Members know, that will give plenty of time for the Parliamentary Commission to complete its recommendations. There is no hidden Government agenda. We have been explicit in asking the Parliamentary Commission for its advice, and it has given some of that advice, but not all of it. This is an area on which we want to proceed with consensus, if possible, but we certainly want to proceed with the expert advice of the Commission and the consultation on which we are about to embark.

Chris Leslie: I appreciate that the process is difficult, and I appreciate that the Parliamentary Commission has a lot of work, but, nevertheless, I am left feeling as though we have been given a holding reply. As hon. Members may know from tabling named day questions, a Minister will reply, "I will answer the hon. Member shortly," and then the hon. Member has to wait and wait. It feels like the Minister is treading water.

We specifically want to know certain things that will be further considered by the Commission, and I accept that pinning down some of those issues is difficult, but it would help if the Treasury gave its view. That does not necessarily have to be a final, conclusive view, but it could be a range: "The maximum ratio will be something between 10% or 30%"—or whatever it happens to be. That would give us some guidance, if the Minister has a sense of what the range will be. That would give a starting point for the Parliamentary Commission to reflect on. Given that the Treasury has even more resources than the wonderful resources that the Parliamentary Commission has—although it has quite a few resources; we will find out about the bill for that at some point in the future—it would help if the Treasury stuck its neck out a bit and said, "If you agree with these particular parameters, then in what ballpark are we talking?" Moreover, some of these suggestions relate to issues where there is a lot of public pressure, particularly on the conduct side. It is not necessary simply to wait for the Parliamentary Commission to talk about action to prevent mis-selling from occurring in the future. This is a more urgent question.

I am left in two minds about whether to test this issue and to press the need for a review six months after Royal Assent, though clearly, the Minister said that his intention was to have it before that process, so I feel as though it would be slightly inadequate to do that. The Minister did not give examples of derivatives that he thought should be in the ring fence versus those that should not be. He did not give us a range of where he felt, in broad terms, those ratios or gross volumes ought to be, so I am in a quandary as to what to do with this particular amendment. On this occasion, it might be sensible to give the Minister the benefit of the doubt, because he is such a genial fellow and I know—I think—that he means well. I might come to regret that statement, but my hon. Friends should not hold that against me.

I will be happy to withdraw the amendment on this occasion, but it would help if the Minister would consider writing to the Committee or to the Chairman of the Parliamentary Commission as a result of this debate to say, "We are consulting and do not want to impede that consultation process", but, to coin a phrase, he is not starting with a blank sheet of paper on this issue; he has a view, broadly speaking, that this is the sort of scale we think derivative activities ought of be and these are the sorts of instruments that we think could or could not be in there. That would be helpful and if the Minister were able to give a little inflection or a nod in that direction then I would feel more satisfied—none has come. I shall not withdraw the amendment just yet; I will keep it on the table if that is alright.

Greg Clark: I am entertained by the hon. Gentleman's speech, because it is customary to speak in favour of one's amendment. He makes some valid points about wanting to have these things clear and upfront—we all have an appetite to do that—but the Committee will want to study the terms of his amendment. He did not address that at all: quite the opposite. All that the Opposition amendment would do is, within six months of the Act receiving Royal Assent, require the Treasury to carry out a

"review of the regulated activities" .

It then deals with the various headings of that review. There is nothing in what the hon. Gentleman is putting before the Committee that would, in any way, speed up the answering of those questions. It is rather the reverse—it is remitting it until after the legislation has left the House.

The Government's intention is in line with what the hon. Gentleman is arguing for—rather than what he is proposing in his amendment—and that is to move as quickly as possible to clarify what the precise arrangements will be while the Bill is still before the House. We have already given him some examples of the products that will be in and out: interest rates, hedging and foreign exchange risks—obviously for small businesses engaged in overseas transactions. That is one of the arguments

that has been made in favour of these products being available within their ring-fence, so that exchange rate risks can be hedged and covered off. We do not expect to see here credit default swaps, options and the various derivatives that do not have sight of the underlying assets. These will be set out in the consultation. I am happy to reassure hon. Members that when the consultation is published, which will be in the summer before the Bill goes to the Lords, we will put forward the number we feel should be consulted on about what the exposure of a bank would be. In short, we are certainly going a long way further than the amendment requires. It will be an exhaustive consultation and will reflect the points made but it would be an eccentric decision to approve an amendment that would require these questions to be answered six months after Royal Assent rather than during the passage of the Bill.

Chris Leslie: I am grateful for those clarificatory remarks. I appreciate the Minister's helpful interjection. He will forgive me for drafting an amendment that sought to put a long-stop date on the process. In drafting these things we tend to consider what would be reasonable. One month after Royal Assent sounds pretty quick, so we chose six months. We were trying to find a device to tease out from the Treasury its view on the dimensions of the saga. I still wish we were having a Committee stage of a fully formed Bill so we could test and scrutinise those dimensions. We are legislating in the dark a little bit here. So we are saying, "Yes, all these powers should be allowed but we are not really sure quite what those powers are. Just trust us. It will come in due course in secondary legislation."

I know there is an affirmative procedure but the Minister and I both know that that is not necessarily the most satisfactory form of scrutiny of these very complex issues. We have therefore tabled another amendment about a different form of scrutiny process for those complex statutory instruments. I will seek to withdraw the amendment because I think the Minister has said that it is his intention to do exactly what it proposes before Report. We want more specificity from the Treasury before Report, even if it is in terms of the ranges of what we are talking about. Otherwise the House of Commons will be legislating without any sense of the broad parameters we are talking about. I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Chris Leslie: I beg to move amendment 3, in clause 4, page 6, line 24, at end insert—

'(1B) If the order confers powers on a regulator or authorises or requires the making of rules or other instruments by a regulator, then those powers, rules or instruments are to be subject to annulment in pursuance of a resolution of either House of Parliament.'.

This is another of our very own homespun amendments. We are starting to look at this rather peculiar new section 142F, which introduces a set of order-making powers for the regulators. This is not simply creating quasi-legislative powers, which we often delegate to Ministers to do on the detail, but in turn, as I read the Bill, Ministers will be able to delegate to the regulators to make rules, to make the law and essentially to say this is how certain activities must be done. This is apparently known as tertiary legislation.

Members will be familiar with secondary legislation and how we have an affirmative procedure where there is an active vote of Members to approve an order that Ministers want to have if it is a serious issue. There is also the negative procedure. Essentially an order is made by a Minister and is taken as being enacted. It lies on the Table for Parliament to take note. If a certain number of Members—although quite how many is not defined—pray against that process, the Minister can be so moved as to agree to a debate on a negative resolution. That is the secondary legislative process.

2.45 pm

We are talking, however, about a tertiary set of legislation here, one that is essentially delegated to the Prudential Regulation Authority and the Financial Conduct Authority—at least, as I read the Bill. Ministers make the orders, and in turn those orders can give order-making powers to the regulators, so there is a sort of trickle-down. That is perhaps something we have grown used to from this Government, but it raises a number of questions about who makes the rules and what those rules are.

It would be useful if the Minister could take this opportunity to elaborate a little and help the Committee by setting out a few examples of the sorts of order-making powers that might be delegated to the regulator, so that we can at least envisage, in an anecdotal way, what might be under consideration here. Until we have a sense of what those powers are, we suggest that it would be safer—and I know that various hon. Members will feel strongly about parliamentary process—to take steps to ensure that the delegated regulation is brought back a step. It should come under the auspices of the parliamentary process, albeit, to be fair, under the negative resolution procedure, whereby the House of Commons and the House of Lords do not necessarily have to debate and vote on each statutory instrument, but if the instruments are prayed against there is a chance that they could be brought forward by the Minister for debate. We feel that would be a better and neater process, and would make sure that Parliament still has a role and some oversight.

We need a sense of what exactly is being talked about here; it is almost as though this small new section is a catch-all, with the Government saying, "Oh well, if we have left anything out the regulators will be able to do whatever they like in terms of rule changes and legislative changes—we will just leave that to them;" I am not sure what the scrutiny process would be for that. We are starting afresh, with new regulators, in about 10 days' time; will the Minister help us by saying what the intention of the regulators will be in terms of telling the wider world about their order-making activities? Will the PRA or the FCA's practice simply be to put such things on a website? Will they take out advertisements in the *Financial Times* saying that they are about to legislate in their own little way? What is the process for regulators making those changes? Or will this measure essentially be supplementing rule-making powers that they already have? Given that we have new regulators coming on stream, it would be useful to have a sense of that.

Our amendment would make a slight change to proposed new section 142F of the Financial Services and Markets Act 2000 as inserted by clause 4. That change would not be massively significant, but would be significant insofar

as there would at least be a process to ensure that there was a little more potential for scrutiny than there is in the Bill. It would safeguard the accountability of rule makers. We are already vesting a phenomenal amount of power in the Bank of England, in particular—let's face it, when we talk about the PRA we are essentially talking about the Bank of England; even if we are talking about the FCA, there are provisions in the Bill and in the Financial Services Act 2012 to the end that the PRA can direct the FCA, so we are talking about the Governor and the Bank being able to direct the regulators—and so we need a few checks and balance to help counteract that. That is the gist of amendment 3, and I hope hon. Members will support it.

Greg Clark: I am grateful to the hon. Gentleman for his speech, because I am struggling to understand the basis of his amendment. From what he said, however, I think he may be labouring under a misapprehension: there is no order-making power for the regulator in the Bill. The regulator will have an ability to make rules under orders that have previously been agreed by Parliament. Those rules are the normal rules that regulators apply, all the time, to turn the purpose they have been given by legislation into action. That explains why the hon. Gentleman has moved the amendment that he has, if he thought that regulators were directly able to make orders—something that is not possible.

What the hon. Gentleman proposes is an extraordinary innovation. In the House we sometimes debate Henry VIII powers, which are given to Governments to do things and repeal things that are unspecified during the consideration of a Bill. Here we have the converse of that. If this measure were adopted, it would give unrestricted powers to Parliament to annul any rule that a regulator might make—it is more of an Oliver Cromwell power than a Henry VIII power in that sense. Not only that, but it would apply in either House, so a vote in the House of Lords or the House of Commons could suddenly strike down any rule made under orders that have been legitimately entered into. I am sure that was not the hon. Gentleman's intention, but I understand from what he said that that may be slightly awry.

I think everyone agrees, and certainly the Parliamentary Commission on Banking Standards agrees, that the precise details of the ring fence should be in statutory instruments—[*Interruption.*] Perhaps I should take an intervention from my hon. Friend the Member for North East Somerset on Cromwell. The precise details should be set out in statutory instruments and of course the regulator has to promulgate particular rules to apply those. They are the bodies that we vest with that; we set them up as the bodies with the technical knowledge and details to be able to undertake their work. The hon. Member for Nottingham East asked for an example of this. Let me take an order that has been published for scrutiny before it has been properly debated in this House, which is the draft ring-fenced bodies and core activities order. It provides for cases where depositors who were eligible to bank with a ring-fenced bank may no longer be eligible to do so. The order allows the regulator to make rules specifying what information a bank may need from a depositor to be able to ascertain whether they qualify to bank in a ring-fenced bank or not. The terms of that order are narrow, technical and operational rather than concerned with conduct or policy.

The process for the regulator ultimately being able to introduce rules should be at the end of a cascade of measures that involves parliamentary scrutiny at every stage, and that is what we doing; we are debating the overall architecture in this Bill, there will then be statutory instruments that then give particular requirements and responsibilities to the regulators, but as is always the case in financial services regulation, these are requirements or invitations on regulators to make rules. There is nothing unusual about that. I am sure it is not the hon. Gentleman's intention, but a veto exercised in this way by either House would be totally unprecedented. None of the wide range of financial services regulations, whether in the Financial Services and Markets Act 2000 or others, is subject to this.

In response to the Delegated Powers Committee, we have accepted its recommendation for the order-making powers that give the power to make rules. It is satisfied with the way we have discharged that. It is an affirmative procedure; it was originally proposed to be a negative procedure. This is a different matter and I hope that the hon. Gentleman will be reassured as to the contents of the Bill.

Chris Leslie: I know that hon. Members will be interested in where the boundary line is being drawn regarding the role of Parliament in scrutinising Executive activities; whether that is the Executive in the form of ministerial Departments or in the form of the regulators. I do not regret tabling the amendment because I think that it is important to test what scrutiny there should be of those order-making powers. I am glad that the House of Lords Delegated Powers Committee did look at this particular issue and I think it is useful to have seen what might have been negative statutory instrument arrangements dragged into an affirmative process, if they were themselves delegating rule-making powers in this particular way. That is one safeguard to be welcomed, but I do not have any regrets about trying to reverse-engineer the Henry VIII powers. The Minister may accuse me of having Oliver Cromwell tendencies, but, if I am a roundhead, there are certainly some cavaliers in the Committee, such as the hon. Member for North East Somerset. At this point in time, however, roundheads and cavaliers would probably agree that we need to keep an eye on what Ministers are doing, in the name of either the Crown or the people, so it is important that we safeguard Parliament's role on these issues.

To my great regret, I do not think that we, as Members—especially when in opposition—actively scrutinise the Order Paper sufficiently to look at the negative statutory instruments that the Government churn out on a daily basis. We need to be schooled in making sure that we keep a beady eye on what exactly is being done in those prerogative powers, though trying to figure out what the instruments are is a big process. I was reassured when the Minister said that those powers will be used only for narrow, technical and operational purposes, which is a good way of constraining what might be done through those rule-making arrangements.

Importantly, we have had the opportunity to say that we want Parliament to scrutinise such matters in this way and we have seen some movement on to the affirmative process, which I will take as a positive development. For those reasons, I will not press the issue to a vote, so I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Chris Leslie: I beg to move amendment 4, in clause 4, page 6, line 38, at end insert—

'(c) has attempted to carry out an excluded activity or to contravene any provision of an order under section 142E.'.

We are still on page 6 of the Bill, but now we are down to the depths of line 38 on that page. We move into proposed new section 142G, which is a provision in respect of the restrictions on ring-fencing bodies and how they may not carry on excluded activities or contravene certain prohibitions. It is the prohibition aspects that we want to look at in particular. The first subsection states:

"A ring-fenced body which…carries on an excluded activity or purports to do so, or…contravenes any provision of"—

any of the other orders provided—

"is to be taken to have contravened a requirement imposed on the body by the appropriate regulator under this Act."

Essentially, we are talking about part of the enforcement process that makes sure that breaches of the rules are punished. We felt that it was important to add a third category into the subsection that was about not just having contravened any particular process, but having attempted to carry out an excluded activity, because attempts to breach the rules also need to trigger enforcement action.

It is important that we look at the test that we place on the behaviour of banks to make sure that, when they look at the ring fence rules, they do not go right up to the letter of the boundaries of impermissible activity but, as was said earlier, adhere to their spirit. If earlier we were legislating about the letter of the rules, perhaps this issue is about the spirit of the rules, with the banks adhering to the system with enthusiasm and not trying to game it or find ways around it.

We all know that the profit incentive probably means that banks will test the ring-fencing rules and attempt to get around them. We therefore tabled this amendment, which is one of several at the heart of tackling banks' attempts to game the system in that way.

3 pm

We do not think that regulators should, in absolutely all cases, need to identify a specific reason to take action, whether that happens to be a warning notice or anything else. It is a bit like tax avoidance regimes; there are schemes that have been dreamt up that are possibly for avoidance purposes. If there is a sense that there are attempts to game the system, a precautionary principle should be taken in respect of how those are pursued.

The amendment seeks to introduce that precautionary principle into the definitions of a contravention of those regulatory requirements. The Parliamentary Commission on Banking Standards said in paragraph 133 of its first report:

"It is essential that the new framework for the ring-fence and the secondary legislation and rules that flow from it are not seen by the banks merely as a basis for negotiation…The regulator's decision-making, in line with its judgement in pursuit of its objective in relation to the ring-fence, should not require it to identify a specific breach of rules in order to take action to maintain the integrity of the ring-fence."

It is very much in the spirit of the Parliamentary Commission's own recommendations that we bring the amendment forward about that particular point of clause 4. In our view, it is part and parcel of the electrification of the ring fence. Indeed, the Chair of the Parliamentary Commission on Banking Standards and the Treasury Committee, the hon. Member for Chichester (Mr Tyrie), said in a recent interview:

"What we've done with the Commission proposals is to put back some of that stiff separation into the ring-fence and then make clear that the key problem—that banks are going to be at the ring-fence all the time, which will be a nightmare for regulators—needs to be dealt with".

That is absolutely what I think the amendment would help to achieve. The former chief executive of Barclays, Martin Taylor, said:

"Now you know you need them [the bankers] in the debate about the future because they understand it better than anybody else does. On the other hand you don't want them to be able to game the new regulatory settlement it seems to me."

That was in the report of the Future of Banking Commission, back in March 2010, which I think was commissioned before we got into this particular process. The rules should imitate aspects of the criminal law in this area, so regulators can punish not only breaches but also attempts to breach or conspiracies to breach the rules. That is why our amendment imposes that standard on the bank, and also sends a message about attempts to game the system.

Greg Clark: The hon. Gentleman rightly refers to the memorable phrase of the Parliamentary Commission on Banking Standards—it wanted to see the "electrification" of the ring fence. That is something on which we agree with the Parliamentary Commission.

The analogy is apt, because the point of a ring fence is that if you touch it you get an electric shock. You do not get a shock if you go near an electric fence, and so this is going rather further than the Parliamentary Commission has advised to date. The points that the hon. Gentleman makes are therefore novel in respect of how banks and other financial services organisations have been regulated to date.

Criminal law has taken a different view of these things in the past, but I will come to some reflections on how we might take the matter forward. There would clearly be a contravention of regulatory requirements, for which the regulator can impose sanctions. A contravention of the requirements can clearly trigger a bank's being forcibly separated. It is very important that the ring fence is strictly enforced.

Proposed new section 142G provides that any breach is a breach of regulatory requirements, with unlimited fines and in some cases withdrawal of permission to operate as well as the separation of powers, which we will come to. It is very important that those powers should be there. Banks' past conduct is also a factor that the regulator should be able to consider in deciding whether to use its power to require separation. As we have made clear, an amendment about separation will be brought forward on Report.

For the purposes of today, how the hon. Gentleman's amendment is constructed would introduce something unprecedented in financial regulation. In no other case is attempting to contravene a regulatory requirement a contravention in itself. Establishing whether a firm has attempted to do so might be problematic.

However, the Commission, and indeed the whole House, is concerned with the spirit of adherence to the rules as well as adherence itself. These are matters

[Greg Clark]

relating particularly to the conduct and the culture of the banks, on which the Commission is continuing to deliberate. It will produce a report about the issues. As I said earlier, if it has recommendations that pertain to the conduct of banks in this regard, of course we will consider them seriously. We have made commitments that we will ensure that Parliament has the chance to consider them. The amendment is not right in terms of the Bill as it stands.

Chris Leslie: I am sorry that the Minister is taking what sounds a little like a gentlemen's club attitude here—"If you chaps test the boundaries a little, well, good luck to you; as long as you don't cross that particular line you are fine. Just do what you can to get under it or round it." Surely he would accept that in lots of areas of the law there are other instances of criminal or other offences and lesser offences of attempts to do something. The ability to prove attempted contraventions is well established in our legal processes.

Greg Clark: I invite the hon. Gentleman to reflect on the purposes of ring-fencing. We have debated them this morning. The purposes of ring-fencing are to provide that there is continuity of services to core depositors, for example, and that there is the ability to resolve the bank successfully. Those are tangible requirements and either a ring-fenced bank has breached a prohibition or it has not. If it has not, it has not exposed the financial system to risk in quite this way. It is important that we and the legislation should be clear that there are consequences, with the full force of regulatory action behind them, if a bank breaches a prohibition.

Such questions of intent are tied up with cultural aspects. There would be a risk of a lack of clarity in the legislation. The analogy of the electrification of the ring fence was, I am sure, deliberately chosen. I dare say it was in the Commission's mind that the consequences come from touching or breaching the ring fence. The Commission deliberately reserved a right here—indeed, it is coming on to talk about the general aspects of the culture and standards in banking in particular. There will be the opportunity to consider what it says there. These are different circumstances.

Stephen Doughty: My hon. Friend the Member for Nottingham East made a very strong point about the attempt function in other parts of the law. Does the Minister not agree that what our constituents find so frustrating about the banking and financial sectors, or in taxation, is these constant attempts to duck and dive and wheedle around? They want to see tough action and they want those who attempt to circumvent the system to be punished and also to face some sort of sanction or prohibition.

Greg Clark: The hon. Gentleman is absolutely right, and the Commission is producing its next report on precisely those subjects. There are the hard rules and it is important that they should be clear and enforced; then there are the important aspects of the cultural deficiencies—or, as the Commission Chairman put it, the standards in banking.

Those are important matters, and they give rise to precisely the questions that the hon. Gentleman raised about a connection that is fairly common in the criminal law—namely, that conspiracy and intent carry consequences and are subject to sanction in themselves. That is not part of the financial regulations we have—it is alien to them—but the Commission may make recommendations to the effect that more of that approach is fed into the Bill.

Nick Smith: I hear what the Minister said about clear rules on conduct. He went on to the more difficult issue of trying to change culture and how we do things round here, which is often a big problem for large organisations. What suggestions does he have for a more straightforward, more consumer-oriented culture in the institutions he is talking about?

Greg Clark: The hon. Gentleman raises a big and important matter. A number of things contribute. One is the leadership from the top and the consequences that have been visited on the banks for the failure of their culture. The taxpayer has footed the bill for a lot of the failures, but so have the banks' shareholders. Quite rightly, some of the managers have formed a view that operating against the interests of its customers and shareholders is not the best way for a bank to prosper. That is, I think, the beginning of a change in attitudes.

The regulator also has an important role to play. Another contribution will come from the fact that we have made changes to the regulatory system—that includes the Treasury Committee, on which many hon. Members have served—to allow the regulator to look in a more nimble and forward-looking way for prospective breaches of the spirit of the rules. Greater shareholder activism is another aspect that can contribute.

There is an acceptance, which we should reinforce—I am sure the Parliamentary Commission will want to reinforce it—that we should get away from what I am told Bob Diamond said about culture, which is that culture is what people do when nobody is looking. There is a requirement for cultural change, and it is important that the Commission is now devoting itself to addressing that. However, in looking at clause 4, we need to set out the hard and fast rules.

Chris Leslie: The Minister has been generous in giving way. He said, and he has said this on other occasions, that he wanted to support the letter and the spirit of the ring-fencing concept. He is now putting the spirit element purely into the standards, culture and governance box, but it is important that we enforce not only the letter but the spirit of the ring-fencing rules. We know what the letter of those rules is, and the Minister has talked about touching the ring fence and getting a shock from it, but how will he enforce the spirit of the ring fence?

Greg Clark: As the hon. Gentleman knows from the Bill, there is an explicit responsibility on directors of ring-fenced banks to maintain the integrity of the ring fence, so it is reinforced in other ways.

However, the hon. Gentleman is wrong to imply that standards and culture—the spirit of the rules, as it were—are somehow a secondary aspect of the

considerations we will come to. The Commission has started with specific aspects of the hard rules, and we need to get those in place, but I will attend closely to its recommendations on other ways to embed and enforce the change in culture required. Members of the Committee should not be under any illusion that the Commission's recommendations will not become an important component of the Bill when we come to consider them.

3.15 pm

Chris Leslie: I am afraid we have hit upon a big difference of opinion between the Government and the Opposition. Having gone to the trouble of building a firm and sturdy ring fence, it is surprising that there is resistance to ensuring that we do more than simply deal with actual breaches. Once somebody has attempted to vault over the fence or throw a blanket over the barbed wire, it seems that those attempts to break out are going to be disregarded. There are too many "Great Escape" analogies in my mind right now, but my point is pretty simple: conspiracy or intent to breach the rules should carry some sort of sanction. I am not saying it should be the same sanction as for an actual breach—it might be of a different order—but similar measures are discernible in other areas of the law and so I do not see why we should not have a precautionary principle here.

Jacob Rees-Mogg (North East Somerset) (Con): I wonder whether the hon. Gentleman is being a little negative in his approach to the spirit of the Bill. It seems to me that a respectable retail banker who has a request from a customer for, perhaps, a currency derivative to help that customer's business, could find that that was not allowed under the ring fence. However, it would be perfectly reasonable to investigate whether or not it was allowed. If the regulation was so tight that any attempt to help a customer in that situation was automatically an offence, it would mean that somebody who wanted to abide by the spirit of the ring-fencing measures—a Captain Mainwaring-style bank manager—would be caught out by the enforcement of unduly harsh regulation. I therefore wonder whether the spirit of the ring-fencing proposals is not perhaps best supported by the Government's clause rather than by the amendment.

Chris Leslie: I would say, "Don't panic, Captain Mainwaring," because there are defences for people whose behaviours are misinterpreted in the way the hon. Gentleman describes. We should really also be talking about appeals processes for that innocent banker who is accused either of breaching or of attempting to breach the ring fence. There needs to be a proper process so that if someone is acting in an innocent and well-meaning way a defence can be mounted.

I do not think, however, that the hon. Gentleman's example negates the point that we are considering, as we can also think of the malign bank manager, trader or executive. In 10, 15 or 20 years' time banking will have changed; financial instruments will have morphed and could have a character that is totally different from the one they have today—and heaven knows, they are evolving at a very quick pace—so we should ensure that the rules are set out and that the regulators have enough power to deal with the devices being used to plot to get around the ring fence.

This is an important principle. We should have some sanction for attempts to carry on excluded activities, as well as for actual breaches. I would therefore like to test the view of the Committee on the amendment.

Question put, That the amendment be made.

The Committee divided: Ayes 6, Noes 9.

Division No. 1]

AYES

Ashworth, Jonathan	Leslie, Chris
Doughty, Stephen	Smith, Nick
Jamieson, Cathy	Wright, David

NOES

Clark, rh Greg	Mowat, David
Evans, Graham	Rees-Mogg, Jacob
Hands, Greg	Thornton, Mike
Mills, Nigel	Williams, Stephen
Morris, James	

Question accordingly negatived.

Chris Leslie: I beg to move amendment 28, in clause 4, page 7, line 45, at end insert—

'() provision requiring that shares or voting power in a ring-fenced body are held only by another member of the ring-fenced body's group which is not carrying on an excluded activity or by other members of that group none of which is carrying on such an activity;'.

We now turn the page and find ourselves right at the bottom of page 7 of the Bill, albeit still on clause 4, which is the meat of the legislation. We are now into the detail of the ring-fencing rules. What would our amendment mean? It was suggested by the Parliamentary Commission, so I cannot claim credit for it; our inspiration was very much taken from its most recent report but one. It focuses on the ways in which we can ensure that a strong level of independence is given to the new ring-fenced bank bodies.

The Commission suggested that an amendment was needed to ensure that the ring fence operates effectively and cannot be easily undermined. Proposed new section 142H sets out the rules that must be made by the regulator in relation to the ring fence. Proposed subsection (4) creates a series of ring-fencing purposes and proposed subsection (5) sets out the ring-fencing rules that must be made for those ring-fencing purposes.

Those provisions include restrictions and requirements on ring-fenced bodies and are all intended to ensure the effectiveness of the ring fence through the independence of ring-fenced bodies and their ability to continue to provide core services that are minimally influenced by other members of their groups. The amendment would add to the list of required rules by restricting the bodies that could hold shares or voting powers in a ring-fenced body to members of the ring-fenced body group who were not carrying on an excluded activity. The intention is to require ring-fenced bodies to be held by a holding company rather than by an investment bank.

In the Government's response to the Vickers Commission report, they said:

"The ring-fenced bank should be legally and operationally independent from the rest of its corporate group".

[Chris Leslie]

The amendment is, therefore, absolutely necessary to achieve that aim and to ensure that ring-fenced bodies are capable of acting independently of other group members.

It is here that we get into the joys of corporate law, control and other governance issues, and we will look specifically at how that applies to banking structures. It is always good to have a homespun family analogy, so a sibling structure, as opposed to a parent-child structure, between retail and investment banks—in other words, for retail and investment banks to be siblings, rather than having the investment bank as the parent, directing the retail bank—would be a preferable corporate construct, and that was the strong recommendation of the Parliamentary Commission.

That structure would also ensure that retail banking businesses were better insulated and would allow for different resolution tools to be used for each branch. If an investment bank owns a retail banking arrangement and gets into difficulties, it does not take a genius to figure out that there will be swift downstream consequences for the resolution and recovery of that investment bank, which could impinge on the viability and the sustainability of the retail bank.

If, however, the investment bank and the retail bank are in a more independent relationship, there is a better prospect that we can have safety and continuity of business for that r retail bank. That is, after all, what the changes that we are making to the law are designed to achieve. The Parliamentary Commission says that it is disappointing that the Government have not adopted that approach more vigorously.

The Vickers Commission commented on some of the arrangements in question, but I am told that Sir John Vickers is now in favour of such a provision. When he gave evidence to the Parliamentary Commission on Banking Standards on 16 January he said that he now doubted his earlier, more permissive views on investment banks owning retail banks, and that preventing that was sensible. Therefore, having looked at the Commission's suggested arrangements, Vickers has modified his view. If Vickers and the Commission are of that view, we surely have to consider it with great seriousness.

Nigel Mills (Amber Valley) (Con): I can see the attraction in what the hon. Gentleman is arguing—that a sibling structure with a neutral holding company is better than an investment bank having all the power over the ring-fenced one. However, I am not clear that the wording in the amendment would actually work. There is no mention of shares or voting power being held directly or indirectly, so I think it would allow a shell holding company to be sat between the investment bank and the ring-fenced bank. That would meet the terms of the amendment but not actually achieve anything.

Chris Leslie: I will be happy to hear what the Government have to say about the arrangement. The Commission's view was that a holding company would be a better parent than an investment bank. That would make a resolution arrangement simpler to achieve, because the ultimate liability would fall on the holding company and would be one step away from those in the retail bank. The wiring is still there, and I am more than open to hearing alternative views, but given the nature of limited liability and corporate law, having that one step of protection would provide a greater degree of integration than if we had a parent-child relationship in the corporate structure. In addition to weakening the ring fence, allowing investment banks to own their retail divisions would risk throwing some doubt on the credibility of the separation arrangements that have been designed in the ring-fencing rules.

We think that the Commission's proposals are sensible and would help reinforce the ring-fencing process. If Ministers do not feel that they can accept the amendment, it is important that they do not just take issue with its drafting but really get into the detail. Can we not use corporate governance structures to ensure that we add to the separation and insulation of the ring-fenced banks? That is important, and we want to achieve it.

Greg Clark: In responding to the hon. Gentleman I would say that it is not the drafting of the amendment that causes any problem for the Government in this instance. It is really of whether the benefits of such a change are worth the candle. The Government have moved some considerable way, quite rightly, in respecting the views of the Commission regarding the institutional separation of ring-fenced banks from investment banks and the embedding of the Haldane principles. Those principles are the important requirements that Andy Haldane suggested in evidence to the Commission, which constitute a pretty rigorous set of required aspects of separation.

3.30 pm

I am aware that the sibling structure has been proposed. It was not in the Independent Commission's report. The ICB did not consider the proposal to be one of its core recommendations; in fact, it did not make any recommendations about it. Clearly, however, the objectives of separation need to be clear and understood. The ICB recommended that ring-fenced banks should be legally, operationally and economically independent of their corporate groups. The Bill already provides for that by requiring the regulator to make rules to ensure that ring-fenced banks are not adversely affected by the acts or omissions of other group members; that they are able to take decisions independently of other group members; and that they do not depend on another group member for financial or other resources that would cease to be available if that other group member became insolvent.

To achieve those outcomes, the Bill will require the regulator to make rules to ensure that ring-fenced banks have independent governance, including their own boards, independent directors, separate human resources and remuneration policies and separate risk management policies, in addition to the separate balance sheet management that is inherent in ring-fencing. The Haldane principles are an explicit response to the PCBS's recommendation. The Bill will also require the regulator to make rules to ensure that ring-fenced banks deal with other group members only on an arm's length basis.

Given that the Bill already includes such requirements, it is not clear—I would be interested to hear contributions from members of the Committee on this—what additional value there would be in requiring groups to adopt a particular corporate structure, either for ensuring the

independence of ring-fenced banks or for separate resolvability. There would seem to be no consequences relating to resolvability.

Stephen Doughty: It is a point of principle that we ought to make the safeguards as strong a bolster as possible. We do not want to be in a situation a few years down the line where we find that banks or others have circumvented the procedures and that we have to try to amend the law again. If we can spot holes now, why not bolster the safeguards as strongly as we can, so that we can have as safe and secure a system as possible, rather than wait and have to do that retroactively? We know that people try to exploit holes; we see it in other forms of corporate governance. My hon. Friend the Member for Nottingham East has made a clear case of where he thinks that is likely to happen, so why not act?

Greg Clark: It is not clear what the hole is to which the amendment would be the solution. That is the difficulty. If there were a hole that the amendment would fill, I would be the first to say that we ought to contemplate it. However, it is not clear, given the commitment in the Bill to the five required principles of separation, which the regulator will have powers to enforce, whether the amendment would add anything.

It will always be open to the Committee to consider further requirements, tests and provisions. However, we have to ask ourselves questions, lest we reach the end of the debate in Committee, let alone the complete consideration of the Bill, with provisions for which we have not identified a particular case but that we have chucked in anyway, and end up with measures that go beyond what is necessary to achieve the Bill's objectives.

I am happy to consider suggestions from the hon. Gentleman or any other hon. Member on whether there is something specific that the structural solution in the amendment would give us, over and above what is already in the Bill.

Stephen Doughty: People want to see steel cladding around this, not some sort of rough netting. They want us to cover every possibility, even the most hypothetical. I appreciate the Minister saying that he does not see the hole, but we do see a hole and we want to see it covered up. We ought to present the strongest possible structure, particularly given what we have seen over the past few years.

Greg Clark: I am still not clear from the hon. Gentleman's answer what the hole is. If he can identify it, we might be able to talk about whether the amendment is a solution to it. It is necessary to be rigorous, and we have many weeks and months to consider the Bill. If we can identify the hole I will happily consider it, but I do not think we have reached that point yet.

Nigel Mills: Can I give the Minister one scenario? Say the ring-fenced entity urgently needs to raise some equity capital to bring its balance sheet back into line. That cash would presumably have to be raised by its parent company and then flow down through the structure. I think it would be preferable if it came only through clean, non-trading entities, rather than having to be routed through some investment bank with its own liabilities and issues, which might impinge on the ring-fenced bank. It would seem to be much cleaner for there to be a clear structure right up to the end of the group, rather than cash having to be routed through risky casino activities.

Greg Clark: The requirements is that the arrangements should be at arm's length and transparent. One of the arguments made by the original Vickers Commission, the Independent Commission on Banking, for not having a Glass-Steagall type solution of the total separation of groups is that it should be possible for funds to flow from the investment bank to the retail bank, especially in times of stress, but obviously not the other way round. To insist on the structure suggested in the amendment could only put obstacles in the way of the choice of debt issuance, to no particular advantage. If the requirements are as expressed in the Bill—to have separation of the principal functions, including balance sheets, of the ring-fenced bank and the non-ring-fenced bank—I do not think the amendment is necessary.

Chris Leslie *rose—*

Greg Clark: I am happy to take representations as to whether it is, including from the hon. Gentleman.

Chris Leslie: The intervention of the hon. Member for Amber Valley was helpful in one respect. We can imagine the converse scenario—an investment bank that owns a retail bank going into administration. Of course, its assets would then come into play to a degree. I want the Minister to say with a straight face that he does not think that would in any way be a threat or a problem to the ring-fenced retail bank that was owned by that investment bank.

Greg Clark: Of course. It will be part of the obligation of the regulator to ensure that the conduct of the bank, including every director there, is not vulnerable to those circumstances. That is the entire point of ring-fencing. If the hon. Gentleman is sceptical that that is meaningful, that goes to the heart of whether we should have a ring-fencing approach whereby it is possible for funds to flow from an investment bank into a retail bank but not the other way round. The Independent Banking Commission, and indeed the Parliamentary Commission following the scrutiny that it has given the idea, accept the basic premise that it can be useful and economical for that arrangement to be possible.

This is not an abstract question. The ability of banks to fund themselves efficiently is ultimately transmitted to people with mortgages, people with business loans and people who operate bank accounts. It is important that we do not put in place unnecessary obstacles that would add cost without any benefits. The point of the Bill is to ensure that we put in place exacting requirements where they are of benefit and where they are required to aid either resolvability or the protection of public funds. However, we have to be clear that we should not proliferate them unless we can see that there will be a benefit. I am not persuaded that that is the case at this point, but we will have other opportunities to debate the matter during the passage of the Bill.. There is no objection to the idea as a matter of principle, but the job is done by the

[Greg Clark]

measures we have taken since publishing the draft Bill, by including the Haldane principles of separation that were recommended to us.

Chris Leslie: I am sorry, but I find it surprising that before we have even filled the Bill with specific protections and seen some of the secondary legislation, the Minister is already starting to say things such as, "Well, maybe we are in danger of throwing too many things into these safeguards. We do not want a proliferation of such safeguards." That is a very weak attitude to take towards what we now know to be potentially some of the most dangerous institutions for consumers, for taxpayers and for the economy at large. It is right to take time to think through how we can protect our economy and our public finances from the banking system.

Greg Clark: I agree with the hon. Gentleman's analysis. Of course it behoves us to take time to consider what protections we need to put in place to prevent the consequences he describes. I issue an invitation to him to say what the problem is, to which this is the solution, that is not covered by other features of the Bill. I am genuinely eager to hear from him on that.

Chris Leslie: This is not just the Labour party speaking. I do not wish to stain this notion by attributing it to one political party that the Minister may not warm to. This was the view of the Parliamentary Commission across all parties. It is something that will undoubtedly come up in the House of Lords when the Bill is considered there. The Minister needs to bear in mind that there will be a lot of force behind the arguments of members of the Commission in the other place when they look at this issue. Sir John Vickers himself reflected on the notion of this corporate structure and the added protections that that one step removed might give. These are all serious considerations.

Essentially, the potential benefit is having that relationship between the riskier investment bank at one step removed from the retail bank rather than having it in an ownership capacity. Ownership and the influence of ownership are imperative. They are phenomenally powerful forces. If one company owns another, then no matter what rules are written down, the sunflower will turn to face the sun in the normal course of its ecology. Similarly in a corporate structure we all know that these are potential risks.

I throw the Minister's question back at him but in reverse: what harm would come from not having this sibling relationship in this way? He has not really given a reason for saying that there are some onerous costs involved here, and that there is a problem with having that holding company arrangement and making sure that there is that sibling relationship. I have given him examples of the ownership issues about which I am concerned, particularly when an investment bank goes into administration. Those are indirect anxieties that were felt by the Commission and by Sir John Vickers in his evidence.

I have forgotten, Dr McCrea, whether I am intervening or making a speech. I think I am summing up. In which case, I will continue. The Minister has not really given enough reasons why not to have this safeguard put in place. It is not good enough to say, "Don't throw everything in. Too many protections got in. We are overdoing it with protections." I still think we should err on the side of caution. The Minister should bear in mind that the jury is still out on ring-fencing. This is an untried arrangement. It is better to take a precautionary approach in these circumstances rather than saying it all sounds very onerous. Anti-regulatory tendencies exist, I know, in some hon. Members who are starting to bristle a little now, but they should learn the lesson of history: regulation is necessary and it needs to be tougher. All Conservatives now have to swallow that particular pill.

3.45 pm

Jacob Rees-Mogg: Will the hon. Gentleman give way?

Chris Leslie: Of course. I knew that would provoke the hon. Gentleman.

Jacob Rees-Mogg: It is not a question of more and tougher regulation but of right and effective regulation. In 2008, masses of regulation had been introduced by the previous, socialist Government, which turned out to be useless.

Chris Leslie: I wait to hear about the speech that the hon. Gentleman made when he was campaigning in that Mercedes around his putative constituency, in which he said that we needed more effective regulation of the banking sector.

It is clear that we need tougher regulation. I have no compunction in saying that, as the argument has been won in that regard. However, I do not want to digress too far from the amendment. It is not a measure that we devised, as it was drafted by the Commission, but I am minded to test the Committee on the amendment.

Greg Clark: The hon. Gentleman, like all members of the Committee, has to consider the provisions in the Bill, rather than considering an imaginary Bill with problems to which the amendment would be a solution. The different parts of the bank—the ring-fenced bank and the investment bank—are not simply one step removed; there is an electrified ring fence between them. That is the import of the Bill. The electrification of the ring fence is rigorous and maintains that separation, as well as maintaining a requirement on directors to enforce that separation. We should not be lulled into thinking that the amendment is in some way necessary to enforce the separation that we want. We want to see lots of safeguards to make sure that people, whether they be depositors or taxpayers, are not exposed to the consequences of the failure of banks, in particular, the failures of investment banks. However, those safeguards should be ones that work. We should not be adding purely symbolic measures to the Bill simply to make a rhetorical point. The Bill's purpose is to have rigorous safeguards that are effectively implemented.

When it comes to imposing corporate requirements, we know that maintaining separate corporate structures has a cost for banks. To have to migrate debt up to the holding company is a potentially costly measure. Having

the powers in the Bill to enforce an electrified ring fence is surely the way to maintain the confidence needed in the system.

Chris Leslie: The wonder of moving an amendment is that the mover gets the last word; there is sometimes competition over who gets the last word, but on this occasion, I do, which is very rare. I do not agree with the Minister, and I do not think that we will reach a consensus on this issue. I do not think that the amendment would be purely symbolic. I accept that there are other rules in place to govern the ring fence, but the amendment is a necessary supplement to those rules and safeguards. I urge the Committee to support the amendment.

Question put, That the amendment be made.

The Committee divided: Ayes 6, Noes 9.

Division No. 2]

AYES

Ashworth, Jonathan	Leslie, Chris
Doughty, Stephen	Smith, Nick
Jamieson, Cathy	Wright, David

NOES

Clark, rh Greg	Mowat, David
Evans, Graham	Rees-Mogg, Jacob
Hands, Greg	Thornton, Mike
Mills, Nigel	Williams, Stephen
Morris, James	

Question accordingly negatived.

Chris Leslie: I beg to move amendment 17, in clause 4, page 8, line 34, at end insert—

'(7A) The Treasury must make regulations prescribing requirements with which ring-fencing rules made for the group ring-fencing purposes must comply.'

The Chair: With this it will be convenient to discuss amendment 18, in clause 4, page 12, line 31, at end insert—

'() section 142H(7A);'.

Chris Leslie: Amendment 17 looks again at the question of the ring-fencing rules, which follows on neatly from the debate that we have just had because it is very much to do with how we make and enforce rules regarding the height and strength of the ring fence, and the quasi-separation between retail and investment banking purposes. That amendment is accompanied by amendment 18, which relates to how we define the independent character of ring-fenced banks and how we scrutinise those arrangements.

The Parliamentary Commission on Banking Standards can claim credit for the amendment—thank goodness my hon. Friend and I decided to table this amendment; otherwise, what else would we have to discuss and while away the hours this afternoon? We cannot claim credit for the idea, but we were convinced by the weight of the Commission's argument. After all, its members include not only a former permanent secretary, a former Conservative Chancellor of the Exchequer and a former Treasury Committee chair, but the Archbishop of Canterbury, no less—*[Interruption.]* I know that that provoked a reaction from the hon. Member for North East Somerset, but let us not dwell on exactly what that reaction was.

Jacob Rees-Mogg: For the sake of the record, I am all in favour of that; I think that it is rather wonderful that we are seeing clerics come back into the centre of British life, just as we see one chairing our debate.

Chris Leslie: I feel the spirit of the rules coursing on through me, not just their letter. In our view, it is important to add the weight of parliamentary backing to rules made by the regulator on the height of the ring fence that is to be created, to ensure the independence of the ring-fenced bank from the rest of the group. The rules on the height of the ring fence, as it has been characterised in shorthand, are designed to protect the core activities of a ring-fenced bank, such as deposit taking, from future problems in the riskier operations outside of the ring fence.

Originally, the draft Bill left the question of the extent of separation between the ring-fenced retail bank and the rest of the group in the hands of the regulators, together with issues on how independent the ring-fenced entity would be. Even the regulators themselves, however, expressed doubts about delegating that much power in the evidence that they gave to the Commission.

The Commission's first report said that the height of the ring fence should be determined not just by the regulator alone; it would have greater authority if backed by Parliament. In paragraph 139, the report states:

"A regulator enforcing rules of its own creation will have less authority in doing so than a regulator giving effect to a clear mandate in legislation with parliamentary authorisation. There is a compelling case for strengthening the regulator's hand when it makes ring-fencing rules through such a mandate."

The Government then moved to ensure that there was more explicit guidance for the regulators on these issues in the Bill. So far, the height of the ring fence has been dealt with only in the proposed new section 142H. It makes much sounder common sense, however, for all issues relating to the height of the ring fence to be determined in a statutory instrument at the very least.

The Commission wanted to add this amendment to test the Government's approach to the whole issue of the independence of ring-fenced retail banks from their group and investment bank owners. Andrew Bailey, the chief executive of the new Prudential Regulation Authority said in his evidence to the Parliamentary Commission:

"What we have to get right is the balance between giving us the job of implementing a rule book essentially—the short version of it—and Parliament having sufficient hands on in terms of the objectives so that the legitimacy and authority of Parliament is very clearly behind it. That is a balance. At the moment, this is a very short piece of legislation in a sense. It says, ″We'll define some objectives and then send you off to police them″".

That is an important point from the regulator himself, so we have to listen to what the regulator says would help him in that particular process.

Most commentators—and the Government—have welcomed the proposals by one of the directors of the Bank of England, Andrew Haldane. He set out what he felt were the necessary ingredients to be able to say genuinely that ring-fenced banks were deciding things "independently". The Haldane principles that the Minister mentioned are that the ring-fenced banks should have separate governance; separate risk management; separate

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balance sheets and balance sheet Treasury management; separate remuneration structures; and separate human resources arrangements. Sir John Vickers added to those Haldane tests and said that separate capital and liquidity provisions should also form part of the test of whether an entity was independent in that particular way.

While we welcome the Treasury placing many of these issues on the face of the Bill in proposed section 142H, I would be grateful if the Minister could also say that he expects that last Vickers test for separate capital and liquidity provisions to be part of that definition of independence. That seemed to form part of that discussion as it was developing on those Haldane principles—Haldane plus, if you will. Will the Minister say whether that concept will form part of the secondary legislation? It would also help if the Minister could say if he thinks it would be sensible to place responsibility on directors of a ring-fenced bank firmly in statute, to preserve the integrity of that bank. A lot of changes have been made on that already, so I think we have an indication of movement on that particular issue.

Amendment 18 is consequential in that it adds proposed section 142H(7A) to the list of subsections that would be subject to the affirmative resolution procedure. Again, I would be grateful if the Minister said whether he thinks that would be a sensible arrangement.

The Committee can see where we are coming from on this particular issue. The Commission made a sensible suggestion, and I would welcome the Minister's response to its suggested amendments G and H, as it characterised them, which appear as amendments 17 and 18 today.

Greg Clark: I do not think there is any substantial difference between the Government and the Parliamentary Commission on Banking Standards on this point. The new subsection would require the Treasury to make rules to set out the parameters, within which the regulators own rules would operate. As the hon. Gentleman said, the amendment appears to stem from the recommendation of the Parliamentary Commission in its December Report that

"section 142H of FSMA be amended either to define the parameters of the rules to be set by the regulator more fully or to require that secondary legislation made by the Treasury and subject to the affirmative resolution procedure defines the parameters".

The Government have accepted that recommendation and we have done two things, and the hon. Gentleman has made reference to this. First, we made a commitment to put on the face of the Bill the so-called Haldane principles, so it is clear what constitutes the separation that the regulator is required to enforce. Secondly, we have introduced a new power in new section 142I that would do precisely what the PCBS has asked for. This new section enables the Treasury to require the regulator to include in its rules any further matters not included in section 142H and to set out more detailed requirements in relation to the matters already covered in section 142H(5).

In fact, the PCBS said in its second report—its most recent report—that the Government had gone further than it had recommended. It said:

"We strongly support the Government's decision to place on the face of the Bill some of the key parameters for ensuring the operational and economic independence of ring-fenced banks."

We have made the change that the PCBS requested. We have consulted the regulator on the drafting of the section, with which the regulator is happy. The Treasury has the power to add any additional requirements in relation to the ring-fencing rules, which may prove in time to be necessary.

In answer to the hon. Gentleman's question on the Vickers capital and liquidity provisions, yes, we are following the recommendations, which are provided for by these powers. Given that everyone is happy that we have gone further than the Parliamentary Commission advised, I hope he can accept those assurances and withdraw his amendment.

4 pm

Chris Leslie: I am grateful to the Minister for those comments, all of which describe perfectly sensible concessions made by the Government in response to the Commission. It is important that the Haldane principles are set out in that way—it would be nice to have a set of principles named after me, and we might come to characterise these as the McCrea principles at a later point in our consideration of the Bill.

As we said in earlier debates, we still think there are other ways to supplement those safeguards on the independence of a ring-fenced bank, and we will return with other safeguards beyond those already proposed, particularly in relation to ownership and corporate control, but, for the time being, the Minister has made the point about new section 142I, which is very welcome. I beg to ask leave to withdraw the amendment.

Amendment, by leave, withdrawn.

Chris Leslie: I beg to move amendment 24, in clause 4, page 9, leave out lines 8 to 21 and insert—

'Reviews

142J Reviews of ring-fencing

'(1) The Treasury must make arrangements for the carrying out of reviews of the effects of the operation of the provision made by or under this Part in relation to ring-fenced bodies, including ring-fencing rules made by the PRA and the FCA. Such arrangements shall be set out in a statutory instrument subject to approval by resolution of both Houses of Parliament.

(2) The first review must be completed before the end of the period of two years beginning with the date on which section 4 of the Financial Services (Banking Reform) Act 2013, so far as it inserts this section, comes into force.

(3) Subsequent reviews must be completed before the end of the period of two years beginning with the date on which the previous review was completed.

(4) Not less than nine months, nor more than 12 months, before the date on which a review is due to be completed, the PRA and the FCA must publish a joint assessment of the impact of the operation of their ring-fence rules.

(5) For the purposes of this section a review is completed when the report of it is published.

142JA Persons by whom reviews are to be conducted

'(1) The Treasury shall appoint not fewer than five persons to conduct a review of whom one is to chair it.

(2) A person may not be appointed to chair a review unless the chairman of the Treasury Committee of the House of Commons has notified the Treasury that, in the chairman's opinion, the person is likely to act independently of the Treasury, the PRA and the FCA in carrying out the review.

(3) The persons appointed to conduct a review must include at least one person with substantial experience in central banking or financial regulation at a senior level.

(4) The reference in subsection (2) to the Treasury Committee of the House of Commons—

(a) if the name of that Committee is changed, is to be treated as a reference to that Committee by its new name, and

(b) if the functions of that Committee (or substantially corresponding functions) become functions of a different Committee of the House of Commons, is to be treated as a reference to the Committee by which the functions are exercisable;

and any question arising under paragraph (a) or (b) is to be determined by the Speaker of the House of Commons.

142JB Reports of review

'(1) The persons appointed to conduct a review must give the Treasury a report of the review.

(2) The report must include an assessment of the extent to which the provision made by or under this Part in relation to ring-fenced bodies, including ring-fencing rules made by the PRA and by the FCA, are facilitating the advancement by the PRA of the objective in section 2B(3)(c) and by the FCA of the continuity objective.

(3) If the report is made before section 4 of the Financial Services (Banking Reform) Act 2013, so far as it inserts section 142JD, has come into force it must also include a recommendation as to whether or not section 4 of that Act should be brought into force to that extent.

(4) The report must include—

(a) recommendations to the Treasury as to the provision that should be included in orders and regulations under this Part, and

(b) recommendations to the PRA and the FCA about the provision that should be included in ring-fencing rules.

(5) The Treasury must lay a copy of the report before Parliament and publish it in such manner as it thinks fit.'.

Amendment 24 is important because, again, it was suggested by the Parliamentary Commission. I feel as though I am channelling the Commission's important work, although I have not spent as long as it has poring over the particulars of these issues. The amendment would replace new section 142J with alternative procedures for the review of ring-fencing rules. The review process is incredibly important because, as the Commission rightly says, the jury is out on whether the ring-fencing rules are effective. We need to keep the rules under scrutiny, which is why the Opposition have argued that we need a set of strong back-stop powers in case the ring-fencing rules collapse or do not work. That is not just the firm-by-firm ability to separate fully retail banking from investment banking if there is a contravention by a specific firm, but the ability of the sector as a whole to do so if need be. That is why we need such review arrangements.

We suggest that the Treasury should ensure that there are reviews of the operation of the ring-fencing arrangements, including the way in which the regulators oversee those arrangements. In particular, the review needs to be held in a parliamentary context. We have not exactly followed the Commission's suggested review arrangements; we have sought to build upon those because we believe that the review arrangements should be set out in a statutory instrument, subject to approval by resolution of both Houses. We have called for a regular parliamentary review to ensure that routine oversight of the ring-fencing arrangements is subject to serious monitoring. For those purposes, we want the concept of parliamentary involvement to be achieved via the affirmative statutory instrument process.

Nick Smith: We want the reviews because our constituents are still very cross about the effects of the banking crisis. If there is going to be an electrified ring fence, our constituents want to ensure that its related enforcement measures, for example, on anybody who behaves badly, are as strong as possible and that anybody who misbehaves ends up black and charred from trying to get around the ring fence. It is important to our constituents that the reviews are regular and attended to carefully.

Chris Leslie: That is why we wanted to alter the Banking Commission's proposals so that, instead of a review on a four-yearly cycle, a two-year period should elapse between the reviews and when they must be completed. That is why we made the second set of adjustments to the review arrangements suggested in Commission amendment M. First, we propose that the review should be set out and approved by Parliament and done in a parliamentary context. Secondly, it should be conducted every two years, not every four years. If a week is a long time in Parliament, four years is a lifetime in banking.

Stephen Doughty: On that point, such measures are crucial due to the rapidity of change in the financial services sector over the past 10 to 15 years and how quickly the products were developed and grew into use. The regulatory system simply was not able to keep up with that level of complexity and change. I was surprised when I read in the Bill that there was a five-year period, because so much can change in that time. We need much more regular reviews to reassure our constituents and players in the economy more widely, as my hon. Friend the Member for Blaenau Gwent said.

Chris Leslie: Absolutely, and our constituents would expect nothing less than that we put the issue higher up the agenda to which Parliament and Government attend. It needs to be there. As we know, with many political issues, events happen and agendas change, so things quickly fall off the edge of media concerns. Ensuring that these matters remain at the heart of the Treasury's concerns and that Parliament has a regularised ability to debate and discuss the adequacy of the ring fence is essential. After all, if we are going to have the threat of partial or full separation if ring-fencing fails, in order for it to be an effective backstop to the arrangements, it must be supported by regular reviews of the conduct of the banks in relation to the ring fence.

The more robust review process that we suggest would replace Government proposals for a review carried out by the Prudential Regulation Authority. Those proposals are not sufficiently substantial, and our suggestion would ensure that we have a periodic, independent review process. It is independent to ensure that, while the regulators are policing the arrangements day to day, there is the prospect of an independent group, sanctioned by Parliament, coming together every couple of years to oversee the stocktake of how everything is working.

The Commission itself said that the jury was still out on the issue. We do not want it to fall out of the spotlight. The Government's current provisions for the reviews are unsatisfactory on several counts. Making the regulator who broadly creates the ring fence and the ring-fencing rules responsible for reviewing their effectiveness

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strategically is obviously not an ideal form of scrutiny. As the hon. Member for Chichester (Mr Tyrie), the Chairman of the Treasury Committee and the Chairman of the Banking Commission, said, it is "wholly inadequate" and amounts to nothing more than

"the regulator marking its own examination paper."

In another context, we have discussed who marks the homework. There also needs to be a stocktake of how well the regulators are able to police this ring-fence arrangement, which is why an independent process is important. The Commission is quite clear in this regard.

Secondly, the new review still enables input by the PRA, by requiring it to publish a joint assessment with the Financial Conduct Authority on the operation of the ring-fencing rules. An independent review process would supplement the findings and the suggestions of the PRA and the FCA. The independent review would not be conducted instead of their work; it would be conducted as well as it.

Thirdly, the scope of the current review suggested by the Government under the PRA is confined to the ring-fencing rules, but we believe that is an inadequate means of properly monitoring the operation of the ring fence. The amendment creates a review of all the provisions in relation to ring-fenced bodies, including assessments about the continuity objective and the desirability of implementing full separation. In other words, the technical deficiencies of ring-fencing should not be looked at as the be-all and end-all of everything. The independent review needs to weigh up the balance of that particular structure and protection, versus what could be gained if full separation was also on the table.

Our amendment provides for reviews every two years. That is preferable to the current provision for review every four or five years. Given the constant innovation of financial services products, a report every four or five years is inadequate to ensure effective supervision. In the Government's document on "Banking Reform: Delivering Stability and Supporting a Sustainable Economy", they themselves commented that monitoring is increasingly important in these particular areas, but they have chosen to do it by what I think is an inadequate form of regulatory review. An independent process is needed for proper scrutiny, and also of course to boost public confidence. The Government's response to the Commission's first report said that:

"The Government agrees with the PCBS that it is essential to preserve the robustness of the ring-fence".

The Government have of course conceded that. In order to do that, we need the electrification process, and we need this review to form part of that arrangement. Ministers should support the amendment, which I hope would give credibility and strength to the policing of the ring fence, and take systemic reviews out of the hands of purely the regulators and into those of independent, experienced figures. Those people would not merely be parliamentarians, because the amendment offers the means to appoint senior people with substantial experience in central banking or financial regulation to form part of the group of

"five persons to conduct a review".

We also suggest that

"A person may not be appointed to chair a review unless the chairman of the Treasury Committee of the House of Commons has notified the Treasury that, in the chairman's opinion, the person is likely to act independently of the Treasury, the PRA and the FCA in carrying out the review."

A lot of thought has gone into the Commission's amendment. We have added our own changes to that, which I hope build upon it. I commend the amendment to the Committee.

Greg Clark: Success breeds success. The Vickers Commission and the independent Commission have established a reputation for a good job done well and effectively, and this has created a respect—and indeed, an appetite—for independent reviews of the important matters before us. Certainly, that is a reflection on the contribution made by the Vickers Commission and it is a tribute to its impact. However, we need to bear it in mind that we should be careful not to review reviews constantly, or have different bodies conducting different reviews when other bodies have just concluded their reviews.

Let us think back to the reasons for establishing the Vickers Commission in the first place. The Chancellor said in evidence to the Parliamentary Commission in November last year:

"I well remember, in my previous job as the Opposition spokesman, going to a Mansion House dinner and hearing the Chancellor of the Exchequer say one thing and the Governor of the Bank say something else, at the same time that the then Prime Minister was saying a third thing and the chairman of the regulator was saying a fourth thing. So creating the Vickers Commission, and trying to bring together all the disparate voices into one place where we could try to form a consensus and get to the best possible solution, was the approach I undertook."

4.15 pm

It is worth reflecting on that aspect of the success of the Vickers Commission. Painstakingly, over a long period time, through the publication of an issues paper, the call for evidence, its interim report and the consultation on that report, through to its very well received final report and the consultation the Government undertook on that, there has been a serious and sustained consideration of the issues that we are debating today, in a way that has not been outside the process that has been established but instead has involved parties from right across the different sectors of the economy feeding into it.

We therefore need to pause before prescribing too much in the way of very specific reviews at this stage. We must consider whether we might not be in danger of undermining the very purpose of the Commission, which sought to establish a consensus and to bring all voices together, after careful and expert consideration. We must avoid establishing a cacophony of different voices in the future, all speaking about an issue on which we have so far had an orderly process that has commanded respect. That is the background which we need to bear in mind when approaching these matters.

The hon. Gentleman's amendment is very detailed in terms of specific arrangements, membership and timing. It is not right, at this stage, to put in the Bill such a detailed set of prescriptions for having reviews in the future. It is always open to the Government and to Parliament to initiate a review in the future. That does not require such specificity in the legislation at this stage.

In his evidence to the Parliamentary Commission recently, the Chancellor said that he is not set against independent review, but that we need to consider its scope, remit and composition very carefully. During the passage of the Bill we will of course do that. However, the Committee should remember the reviews that are already envisaged and are in place—reviews, in fact, that the Bill builds into the process. The regulator will report annually on the operation of the ring fence. The PRA will be required to report every five years to the Treasury and, through the Treasury, to Parliament—and no doubt specifically to the Select Committee—on how it is discharging its duties. However, that is different from binding a future Government to ongoing reviews, especially if there is a risk that they would revisit, at too frequent an interval, the very premise of the policy on which Parliament has legislated.

Members ought to reflect that we need to balance the need for reviewing whether things are working against the very reason that the ICB was set up, which was to have arrangements that will endure in the banking sector and to settle uncertainty over the future of that sector. Constant reviews would create constant uncertainty and would require the Government to revisit the very premises of the policy. That would not be the right approach.

David Wright (Telford) (Lab): What is the Minister's thinking on the assurance the amendment would provide to the sector? The amendment lays out fairly comprehensively for those who would be subject to review what would happen and what would be reported. If we look at the Bill, new section 142J is pretty open in terms of what review activity could take place. That does not provide much certainty for the sector about what is going to happen during a review, whereas the amendment would give a concrete platform upon which reviews could be undertaken. Which specific elements of the amendment is the Minister opposed to?

Greg Clark: This is one review among others. A wholesale review of whether this is the right mechanism is different from a review that the PRA should carry out about whether the operation of the rules is properly conducted. When we come to consider this later we need to specify precisely the intention of the reviews, whether it is about policy or whether it is the implementation of the policy. There is a danger that through a review, no doubt consisting of the experts to whom the hon. Member for Nottingham East referred, we would reconvene the Independent Commission on Banking in perpetuity. We had a commission to look into this. To have a committee of wise men and women who have the authority of Parliament to constantly revisit these arrangements would not be conducive to the stability that we have in mind.

Nick Smith: What would the Minister say to our constituents who want us to keep a really beady eye on this? I have listened carefully to what he has said today. He takes a fairly iterative approach to all this with the reference to responding to the response to the response and so on. I accept that this is tricky ground, that it all has to be considered and that we need as much input as possible. But our constituents want us to bear down on this topic very carefully. That is why I think a two-year review would be helpful, particularly in the first few years after the establishment of these new institutions. It would give our constituents some comfort that we are keeping a beady eye on all of this.

Greg Clark: The hon. Gentleman is right. We need to keep a beady eye on it. We need to make sure that the provisions work. But one of the aspects of the amendment that is difficult is that it expressly requires the terms of reference for the review to include the case for full separation, for example. That, in effect, reopens the question that we are debating here, which came from the repeated iterations that the Vickers review obtained during its public consultation. We need to have enough certainty here. While the PRA should account for and report on its effectiveness in operating and maintaining the rules, setting in train already a review that would require full separation would not be the right approach.

We should bear in mind that it is an annual review of the ring fence that the PRA is required to engage in, specifically with regarded to firms' behaviour. When the hon. Gentleman says that our constituents want to be reassured and to know that a beady eye is kept on the behaviour of particular firms, that is expressly provided for. But that is why to conflate that with a commission of experts looking at the underlying premise of the policy would be unhelpful at this stage.

We have already established during the course of the morning and the early part of the afternoon that we want to leave the Bill with a sensible set of provisions. Clearly this needs to involve the right reviews. The Chancellor told the Parliamentary Commission that he was not set against the case for an independent review but that we need to consider how that coheres with the other aspects.

This is at an early stage. We will reflect on recommendations that the Commission have made. We will need to consider carefully during the passage of the Bill how at every juncture we can have the most appropriate review for the purpose so that the PRA reports to Parliament on the discharge of its responsibilities in terms of maintaining the ring fence that is there. We should look at the performance of the system overall. I do not think that it is the right approach to set that out at this stage in such detail, conflating those objectives.

Mark Durkan (Foyle) (SDLP): Does the Minister accept that the five-year review of the ring-fencing rules in new section 142J will probably take place in the latter half of the next Parliament? The chances are that there will be issues of contention and assessment of how some of the aspects are working and whether there needs to be further separation. Is it really feasible that a new Government in 2015 will simply say, "We can do nothing until the five-year review"? Surely, as the Minister has implied, the Treasury Committee might seek to look at the matter before then, in which case it will be accused of undermining, interfering and cutting across the proposed five-year review by the PRA. Would it not be much more stable for the Government to front-load an independent review into the plan to ensure that the matter will be reviewed independently early in the next Parliament, which will allow them to make any adjustments that they need to make in the light of earlier experience?

Greg Clark: There is a provision for a five-year review as well as a one-year review, and the hon. Gentleman is right to say that it is always open to the Treasury Committee—as to any other Committee of Parliament—to take evidence and to make inquiries. Between the one-year review and the five-year review, we have provided for an appropriate time frame in which to consider the matter. That is one of the reasons why it is difficult to envisage being so detailed and prescriptive about the content of the review, in particular the premise of ring-fencing. We do not know whether our successors in a future Parliament will want to look at that, but they will be perfectly able to conduct a review to address the issues that pertain at the time.

We would be front-loading the arrangement unnecessarily if we anticipated—before the Bill has been enacted, let alone implemented—the aspects of the Bill that it will be important to review, especially given the fact that Parliament is unconstrained in its ability to choose what to review. If we did so, we would only undermine the purpose of the independent Parliamentary Commission on Banking Standards, which was to bring together the different voices, to establish a consensus as far as possible and to root it in the evidence that was submitted by expert figures. I do not think it would be right for us to set up a potential vehicle for second-guessing that, but that is not to say that Parliament will not be able to revisit the matter in due course.

David Wright: I have a simple question. The Bill states that the Treasury would

"lay a copy of the report before Parliament."

Will the Minister explain the procedure for doing that? Would there be a debate in Parliament, or would the report simply be placed on the Order Paper? Would it go before the Library? How exactly would that be done and what format would it be in?

Greg Clark: There are multiple ways of having such things debated, and anything that is put before Parliament is susceptible to debate. I will be able to advise the hon. Gentleman shortly about the envisaged route.

The provisions that we are debating, particularly in new section 142J, do not prevent a future Government from conducting a review before five years have passed if, in deference to what the hon. Member for Foyle said, they consider that the time has come to do so. There is nothing to preclude them from doing so. The only question is whether we should decide in advance to timetable a review at a certain point.

On the parliamentary scrutiny of these arrangements, inspiration is rapidly reaching me. The proposal would be that a written ministerial statement would be made, with the review placed in the Library of the House. Of course, an oral statement could be considered if that would be a more effective way to scrutinise the matter.

4.30 pm

David Wright: I thank the Minister for putting on the record exactly how the report would be made to Parliament, because government tends to have different mechanisms. His saying formally that he would envisage a written statement—at least—being presented before Parliament is welcome.

Greg Clark: I am grateful to the hon. Gentleman. I hope that he knows—he will be able to discern this over the weeks ahead—that the process of parliamentary scrutiny is important to us. I do not regard one of the Government's objectives to be simply to get their legislation through. Legislation can be improved by the scrutiny of colleagues, and that is the appropriate way in which to proceed.

Nick Smith: I have a similar question to that asked by my hon. Friend the Member for Telford. It seems to me that if the Treasury Committee has the opportunity to scrutinise this work, that will be important, but will other parliamentary bodies such as the National Audit Office and the Public Accounts Committee, which look for efficiency and value for money, equally have a role?

Greg Clark: It is for the Chairmen of the Committees and the Committees themselves to direct their inquiries. Their terms of reference are sufficiently widely drawn—I say this as a former member of the PAC—to be able to inquire into the proper use of public money. It is not, therefore, simply the Treasury Committee that can scrutinise the matter but also the other Committees established by Parliament. There are other means, too, such as the possibility of arranging debates. I am sure that the Backbench Business Committee will take an interest in these matters in the years to come.

I expect that, whatever we decide about timetabling reviews, the operation of the arrangements that we will debate during the weeks ahead will be much reviewed, much debated and much scrutinised by all of us in the House and by our successors. I do not think that there will be any absence of that. As I say, however, and as the Chancellor has said, during the passage of the Bill we will reflect more on the arrangements for scrutiny, and I will come back to the House with some suggestions.

Chris Leslie: I can see where the Minister is coming from: he wants to get this issue out of his hair and put it to bed. It is a royal pain in the Department for him and, essentially, he wants to move on to other issues, but I have to say to him that we need to keep the banks on their toes. It is absolutely essential to build in a device so that policy makers can evolve their approaches towards clever, affluent banking executives who have a strong motivation to test the rules and push the boundaries of the ring fence so that they can build their businesses in a way that is to their advantage.

The Minister expressed the notion of, "Oh well, I don't think there will any absence of willingness to review these things in the future", but he should learn that issues come and issues go; they can dive down the pecking order as politics flits around from issue to issue. That is why we have to build into the Bill a device to maintain a review that is strong, rigorous and comprehensive.

I am afraid that I disagree with the Minister's assessment that the amendment is far too detailed. My hon. Friend the Member for Telford was spot on when he said that it is clear, specific and sets out for the financial services sector what will be expected by Parliament in an independent review process. We have not set out in the amendment issues that will be subsumed by other events in the future. We are simply saying, that we should look at the adequacy of the ring fence but juxtapose it with what might be on offer if full separation is needed.

The Minister's argument gets into a real tangle. He says that the amendment should not include consideration of separation, but he has conceded that we should have separation on a firm-by-firm basis. That is not as much of a concession as I would want to see, and how on earth will we test it? Is he seriously suggesting that every five years, the regulators will have the strength to go for full separation without the rigour of an independent review that is sanctioned by Parliament and therefore has seniority and seriousness? The Government's provision is a way of downgrading what everybody thought was a concession by the Chancellor when he said that he would allow a backstop reserve power for separation on a firm-by-firm basis. How do we test whether that separation is necessary? It can only be done by some sort of serious review process.

If we pull away the rug from under that review process, we essentially undermine the strength of that backstop, that reserve power that threatens, "If people breach the ring-fencing rules, this could be the consequence." The amendment is part and parcel of that. We have carrots, but we also have need to have sticks hanging over the system just in case there are contraventions. The electrification of the ring fence has to be supported in that way.

The Minister started by saying that we should not constantly revisit the arrangements, because it would not be conducive to the conduct of business. I strongly counsel him against going down that route. He implies that it is all very tiresome and that we should simply deal with it, move on and put a lid on the whole issue.

James Morris (Halesowen and Rowley Regis) (Con): Is there not a danger in the approach that the hon. Gentleman describes of separating the operational review from the policy review? He seems to be mixing up the two in his description of how his review proposals would work. On the one hand there are operational questions about whether the rules are being implemented, and on the other there are policy questions about whether the market has moved on and whether ring-fencing remains a viable idea because of market changes. He seems to be conflating the two in what he proposes.

Chris Leslie: I do not think it should be either/or. Of course, we have to have operational reviews, and that is why the regulators do their day-to-day business. But who does the hon. Gentleman expect to do that policy review? Are we really going to trust that the regulators will have the strength of purpose, the wherewithal and the necessary political strength to do that? It would have to be quite strong to say, "We are going to go for a complete separation", especially bearing in mind that the Minister has said that the Government do not want a review that even looks at the prospect of separation in contrast to what ring-fencing can deliver. It is a completely wrong approach to underpinning the strength of the ring fence. That is why the Commission came out with the recommendation that it did.

Greg Clark: Is the hon. Gentleman suggesting that the use of the separation power under the electrification provisions should not be exercised by the PRA, but should wait for the independent review that he has in mind?

Chris Leslie: No, obviously, if the PRA is confident that it is a clear-cut case, then it should be open for it to act. But in all reality, the Minister will know that particularly when there are so many other things going on and issues can fall off the media agenda, regulators are unlikely to have the political strength necessary to do that. It would be a big thing. Full separation, even if it was just for one bank, would require the capacity for an independent review to help put some weight behind a regulatory judgment of that sort every two years, as we have suggested. I see the amendment as supplementing what the regulators could bring to bear.

This is about strengthening the ring fence. That fence must have firm foundations to make it sturdy, one of which has to be a review process that is built into the protections for consumers, taxpayers and the economy at large. That is why it is important to have the arrangements that we have set out. As I have said, their detail has come not just from us but from the Commission. I hope that the Minister will at least think further about what a review could do, especially given that he is conceding on the separation issue. He has to accept that separation would be a big step to take, and leaving it wholly to the regulator would make it unlikely to happen.

We have other criticisms about simply going for separation on a firm-by-firm basis, but we are about to come to them under other amendments. It is important that we have a rigorous and strong review process, so I will press the amendment to a vote.

Question put, That the amendment be made.

The Committee divided: Ayes 7, Noes 10.

Division No. 3]

AYES

Ashworth, Jonathan	Leslie, Chris
Doughty, Stephen	Smith, Nick
Durkan, Mark	
Jamieson, Cathy	Wright, David

NOES

Clark, rh Greg	Mowat, David
Evans, Graham	Rees-Mogg, Jacob
Hands, Greg	Sharma, Alok
Mills, Nigel	Thornton, Mike
Morris, James	Williams, Stephen

Question accordingly negatived.

Chris Leslie: I beg to move amendment 20, in clause 4, page 9, line 21, at end insert—

'*Power to order full separation*

142JC Power to order separation in case of particular groups

'(1) Where—

(a) the members of a group include one or more ring-fenced bodies and one or more other bodies, and

(b) it appears to the appropriate regulator that the conduct of any one or more of the members of the group is such that there is a significant risk that the appropriate regulator will not be able to advance the objective in section 2B(3)(c) (in the case of the PRA) or the continuity objective (in the case of the FCA) otherwise than by acting under this section,

the appropriate regulator may give a notice to each of the members of the group.

[Chris Leslie]

(2) The notice must state that the appropriate regulator proposes to require the taking of relevant steps in relation to the group before the date specified in the notice.

(3) In this section "relevant steps" means steps to secure one of the following results—

(a) that there is no member of the group with a Part 4A permission to carry on a regulated activity of a description specified in the notice;

(b) that no member of the group is a ring-fenced body;

(c) that there is no member of the group with a Part 4A permission to carry on a regulated activity which is not a ring-fenced body.

(4) The notice must—

(a) specify a period, of not less than 3 months, during which any member of the group may make representations to the appropriate regulator in relation to its proposal, and

(b) name an independent reviewer who is to report on the conduct of the members of the group and the appropriateness of the proposal made by the appropriate regulator.

(5) A person may not be named as the independent reviewer without the consent of the chairman of the Treasury Committee of the House of Commons; and the reference in this subsection to the Treasury Committee of the House of Commons—

(a) if the name of that Committee is changed, is to be treated as a reference to that Committee by its new name, and

(b) if the functions of that Committee (or substantially corresponding functions) become functions of a different Committee of the House of Commons, is to be treated as a reference to the Committee by which the functions are exercisable;

and any question arising under this paragraph (a) or (b) is to be determined by the Speaker of the House of Commons.

(6) After receiving any representations made in relation to the proposal by members of the group and the report of the independent reviewer, the appropriate regulator must decide whether it intends to implement the proposal.

(7) If the appropriate regulator decides that it does intend to implement the proposal, it must publish notice of the proposal, and of its decision to implement it, at least 60 days before it is implemented.

(8) A person who is aggrieved by the decision of the appropriate regulator that it intends to implement the proposal may refer the matter to the Tribunal.

(9) The proposal may not be implemented without the consent of the Treasury; and the Treasury must publish their decision on any application made by the appropriate regulator for consent, together with their reasons for the decision, at least 60 days before it is implemented.

(10) Once the Treasury has consented to the implementation of the proposal and either—

(a) any reference to the Tribunal under subsection (8) has been dismissed, or

(b) the period for making such a reference to the Tribunal has expired without a reference having been made,

the appropriate regulator may implement the proposal by giving notice to the members of the group requiring the taking of the relevant steps specified in the proposal before the date so specified.

(11) If the relevant steps have not been taken by the specified date, the appropriate regulator may—

(a) in a case where the relevant steps are aimed at securing the result in paragraph (a) of subsection (3), take the action specified in subsection (12),

(b) in a case where the relevant steps are aimed at securing the result in paragraph (b) of subsection (3), take the action specified in subsection (13), or

(c) in a case where the relevant steps are aimed at securing the result in paragraph (c) of subsection (3), take the action specified in subsection (14).

(12) The action referred to in paragraph (a) of subsection (11) is—

(a) to cancel the Part 4A permission of any member of the group to carry on the regulated activity specified in the notice, and

(b) to refuse to give a Part 4A permission to any member of the group to carry on that activity.

(13) The action referred to in paragraph (b) of subsection (11) is—

(a) to cancel the Part 4A permission of any member of the group that is a ring-fenced body to the extent that it relates to a core activity, and

(b) to refuse to give any member of the group a Part 4A permission to carry on a core activity.

(14) The action referred to in paragraph (c) of subsection (11) is—

(a) to cancel the Part 4A permission of any member of the group that is not a ring-fenced body, and

(b) to refuse to give a Part 4A permission to any member of the group that is not a ring-fenced body.'.

The Chair: With this it will be convenient to discuss amendment 21, in clause 20, page 21, line 23, at end insert—

'( ) No order may be made appointing a day for the coming into force of section 4 so far as it inserts section 142JC of FSMA 2000 unless the day is later than that on which the report of the first review under section 142J of that Act is published.'.

Chris Leslie: We now come to probably some of the most important debates on the Bill—on amendments 20 and 21, followed by amendments 22 and 23. It will be difficult to avoid straying into the latter group, as both groups relate to the concept of having a back-stop reserve power to create full separation between retail and investment banking if ring-fencing fails. Retail customers need a level of protection, which is why we have gone along with the ring-fencing process, but if the notion fails and the system can be gamed—if the system does not function and system failure is judged to have happened—we should move into an environment where we have full separation, which may well be necessary for the protection of customers.

We feel strongly that that needs to be part and parcel of the Bill. My right hon. Friend the Leader of the Opposition made that point in his speech at the Labour party conference in September 2012. The PCBS, which published its report in December 2012, also recommended that. If we are to have a ring fence, we must also have a back-stop power to reinforce it, and the amendments are an element of that.

I am grateful to the PCBS for helping to draft amendment 20. Hon. Members will see that it is quite substantial and may even have exceeded my own, amateur drafting capabilities. I am getting a little bit better at the legislative process, but I do not want to blow my own trumpet in any way, especially given that the people who do the work are sitting not too far from me.

4.45 pm

The amendment would provide what we regard as the minimum power necessary to electrify the ring fence and prevent firms from trying to game the system by giving the regulator the ability fully to separate an independent banking group into totally different entities. In a speech on 4 February, the Chancellor of the Exchequer said:

"My message to the banks is clear: If a bank flouts the rules, the regulator and the Treasury will have the power to break it up altogether—full separation, not just a ring-fence".

The Committee will notice that he referred to "it" rather than the sector as a whole. Since that is the Chancellor's message, it seems strange that the Minister has not tabled an amendment to that end in time for consideration in Committee. Will he explain why he has not? Was he simply relying on the Opposition to come to his rescue again?

The Minister can give us the benefit of his views on the adequacy of the Commission's drafting, but if such a provision is now central to the Government's view, given the welter of advice and support available from departmental officials, why on earth have the Government not either put their name to the Commission's amendment or tabled one of their own to introduce such separation on a firm-by-firm basis? Yet again, the Government seem to be dragging their heels over the implementation of some of the reforms.

David Wright: It is crucial to think about people who work for the banks as well, not just the customers. One thing that shocked people in the financial crisis was that people who were working hard and diligently to serve customers in retail banks on the high street did not realise what some of their colleagues back at base were doing. Not only customers but people who work for banks must have confidence in the system so that we have a viable structure. It is important for employees in large banks to know that if something goes wrong of which they, as front-line service providers, are not aware, somebody will be dealing with the problem.

Chris Leslie: That is an incredibly important point to put on the record. We talk in shorthand about the behaviour of banks, but that should never be taken as a criticism of the front-line cashier or the junior bank manager in the local branch. We often talk in general terms, but even those who work in the banks have been aghast at some of the behaviour of their senior colleagues—the executives and the traders—who took enormous risks with billions and billions of pounds.

David Wright: The point is simple. During the run on Northern Rock, the abuse that people working in branches took was appalling. Some of my constituents work in retail banks on the high street, and it is appalling how much abuse they received as a result of the actions of people whom they had never met and did not know, back at their corporate headquarters. We need to make it very clear that we are standing up for such people.

Chris Leslie: I am sure that Members on both sides of the Committee would all say "hear, hear" to that. I completely agree with my hon. Friend.

Amendment 20 would empower the regulator to require a group to sell off either its retail or its investment bank in certain circumstances. The power to trigger separation of a group needs to lie at the heart of a serious approach to reform. The Commission on Banking Standards has said that such powers are needed to

"provide adequate incentives for the banks to comply not just with the rules of the ring-fence, but also with their spirit"

and that failure to introduce such proposals would increase the risk of the ring fence failing. Separation is one of the ultimate sanctions available and would trigger fundamental change at a financial group with an impact far beyond that of fines, which, even in this era of LIBOR and PPI scandals, account for only a very small percentage of banks' revenue. A number of approaches have been taken to drafting the back-stop, reserve power of separation. It is interesting that the Commission has concluded that the particular amendment should be drafted in this way. Some have said that we should draft a separation provision, so that something in statute is triggered if a number of tests are passed, but the way the provision works, and the reason why it is linked with amendment 21, is that the provision for separation is essentially put into law as though it is happening, but the commencement of the provision would be ultimately in the hands of Ministers, in case the circumstance arises. That provision is somewhere towards the end of the Bill. The statute essentially sits dormant until such time as it is needed. Ministers could activate those sections of the Act in response to the triggering process.

The Commission's first report said that it found

"the evidence that it has received on the benefits for financial stability of some form of separation convincing. The evidence that there has been damage to standards and culture by having these activities side by side, an area not examined by"—

the Vickers commission—

"is comprehensive and a crucial consideration. There is evidence to suggest that, as well as supporting financial stability and reducing the risk to the taxpayer, separation has the potential to change the culture of banks for the better and to make banks simpler and easier to monitor."

That is the direction in which the Commission was heading. The current Governor of the Bank of England, Sir Mervyn King, told the Commission, in paragraph 162 of the first report, that he had

"always felt that total separation was the right way ultimately to go."

and that he was

"glad that many more people are now coming on board the idea that a move to some kind of serious separation is the right thing to do."

As we have discussed however, the amendment does not necessarily lead to the separation of banking groups, but empowers the regulator or the Treasury to take such action, where necessary.

In addition, full separation remains the last resort. Steps can be taken under the Bill only if the regulator is incapable of advancing its objectives by any other means. The crises at various banks fell on both sides of what will become the ring fence. From the liquidity crisis at Northern Rock to RBS's doomed acquisition of ABN AMRO investment bank and HBOS's disastrous lending

[Chris Leslie]

decisions in its corporate division, transactions show how a problem in one part of a bank spreads to another and underlines the importance of a power for separation.

We would of course prefer to implement fully all of the parliamentary Commission's recommendations, including a full reserve power for the total separation of the entire retail and investment banking sectors, because there is so much interconnected behaviour these days between banks. That would be the real warning and caution to all bankers to beware of contravening the ring-fence rules. It is important that the power is available in statute, ready to be triggered by regulators with Ministers.

We know that there is strong support for such a power from the Government, so I would be grateful if the Minister set out the Government's intention for the legislation. We are yet again in Committee with the amendment generated by the Opposition. What Ministers intend would trigger such a separation power or how they would have such power on a firm-by-firm basis always on the table is not yet clear. Nor is it clear how it would be reviewed. Hearing what the Minister has to say will help the Committee to test the Government's commitment to the electrification process and backstop arrangements.

Jacob Rees-Mogg: I oppose amendment 20 on a narrow, but important, constitutional ground. New section 142JC(5), proposed in the amendment, relates to the Treasury Committee of the House of Commons. That provision seems to me to go against the Bill of Rights, because it would bring the proceedings of the House into the ambit of the courts. Should the amendment be introduced by the Government at a later stage, or introduced by any other means, the proceedings of the House ought not to be part of statute law. There are other mechanisms, whereby statutory instruments may be used and those statutory instruments may be introduced according to the proceedings of the House. I strongly oppose the amendment, purely on the grounds of new section 142JC(5).

Greg Clark: As hon. Members will understand, we are amenable to the thrust of the amendment, if not to every particular detail of it. The Parliamentary Commission's report has been extremely influential, and has persuaded us that the institution of a firm, specific electrification power can be important in sending a clear message to banks and to those who work within them that a repeat of the problems that brought down the banks in the past simply cannot be tolerated and will have severe consequences. As hon. Members know, the Government have agreed to table their own amendment to give the regulator the power to split up a bank under certain circumstances. We therefore welcome the amendment moved by the hon. Member for Nottingham East, which has allowed the Committee to consider those issues.

The amendment suggested by the Commission stayed our hand in producing our own amendment for debate in Committee. The Commission's amendment is pretty well crafted and some time clearly went into it. It is worth reflecting that the Commission has the benefit not just of its own expert members but of expert parliamentary draftsmen. Rather than simply setting that aside, we preferred to consider the terms of the amendment in detail. As Members will know, it is important to get the details of the firm, specific electrification right, so we have taken the amendment very seriously. We are working with the regulator, and indeed with the Bank of England, to cast our amendment in precise terms.

Ordered, That the debate be now adjourned.—*(Greg Hands.)*

4.58 pm

Adjourned till Thursday 21 March at half-past Eleven o'clock.