



House of Commons
Treasury Committee

**The work of the
Financial Conduct
Authority: the
perimeter of regulation:
Government Response
to the Committee's
Thirty-Fifth Report**

**Fifteenth Special Report of Session
2017–19**

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The Treasury Committee

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Fifteenth Special Report

On 2 August 2019, the Treasury Committee published its Thirty-Fifth Report of Session 2017–19, *The work of the Financial Conduct Authority: the perimeter of regulation* (HC 2594). On 1 October 2019 we received the Government Response to the Report, which is appended below.

Appendix: Government Response

Introduction

1.1 The Treasury Committee has an open inquiry into The work of the Financial Conduct Authority. As part of this inquiry, the Committee published its report *The work of the Financial Conduct Authority: the perimeter of regulation* on 2 August 2019. The Government welcomes the Committee’s report and has considered carefully the Committee’s recommendations, which highlight important issues related to the process for updating the perimeter and the powers of the Financial Conduct Authority (FCA), particularly in relation to unregulated activity. This paper sets out the Government’s response to the Committee’s recommendations.

Government response to the Committee’s recommendations

2.1 The Government has considered the recommendations in the Committee’s report as a whole, and has grouped its responses to these recommendations where relevant. The Committee’s recommendations are in bold and the Government’s response is in plain text. Paragraph numbers refer to those in the report.

2.2 **The Committee recommends that where regulated financial institutions undertake unregulated activity, the regulatory system should ensure that clear and explicit warnings are provided at that point, with the potential consequences of the lack of regulatory cover clearly explained, with sanctions for firms that fail to do so.** (Paragraph 18)

2.3 **The FCA must not in future be constrained, or feel constrained, from providing warnings on financial products that may cause consumer detriment. The FCA should be given the remit to highlight the risks faced by financial services consumers including where an activity is beyond the perimeter of regulation. This should be written into the relevant primary legislation, and include any necessary powers needed to fulfil that remit. This would allow the FCA to identify and provide clear warnings about products and activities that might pose risks to consumers, without fear of breaching its remit. In providing such a remit, the Government should ensure that the FCA has the power to act swiftly and without undue restraint as it sees risks arise.** (Paragraph 34)

2.4 Both of these recommendations seek to ensure that consumers are properly informed when they are engaging with an unregulated financial activity and the risks of doing so. The Government recognises the importance of this. The Financial Promotions Regime has been designed to ensure that consumers are provided with the right information to assess whether a financial product is right for them. The Government notes that, under

the current regime, financial promotions (including those of unauthorised firms) must be communicated or approved by an authorised firm and must comply with specific requirements in the FCA Handbook. This includes a requirement that all financial promotions are fair, clear and not misleading, which is supported by guidance noting that authorised firms' financial promotions for unregulated products which mention that the firm is regulated by the FCA or PRA should make clear that these products are not regulated. If the FCA finds that a firm has failed to adhere to the requirements of the Financial Promotions Regime, it can take enforcement action, including fining the firm.

2.5 The Government is working with the FCA to consider whether further steps may be taken to ensure consumers understand what regulatory protections they may or may not be entitled to when engaging with unregulated products as part of its response to the failure of London Capital & Finance, including the role of the Financial Promotions Regime. The Government will announce the outcome of this work as soon as possible.

2.6 The Government agrees that the FCA must not be constrained from providing warnings on financial products that may cause consumer detriment. Under section 139A of the Financial Services & Markets Act 2000, the FCA has the power to give guidance on "any matter which it appears to the FCA to be desirable to give information or advice". The FCA regularly highlights the risks faced by consumers who engage with activities outside of the perimeter, such as through issuing consumer warnings and guidance (recent examples include mini-bonds and cryptoassets).

2.7 The FCA uses these powers regularly: last year, the FCA issued 521 consumer alerts. Further initiatives taken by the FCA in this area include: ScamSmart, a campaign to educate consumers on the risks of investment and pension fraud, and the FCA's Warning List, a publicly available list of firms and individuals that the FCA knows are operating without its authorisation.

2.8 We therefore recommend that the FCA be given the formal power, and necessary remit to be able to formally recommend to the Treasury changes to the perimeter of regulation, where that would enhance its ability to meet its objectives, in particular to prevent consumer harm. It should set out any costs, both to firms and consumers, from such a move at the same time. It would then be for the Treasury to consider such a recommendation promptly. All such recommendations and Treasury replies should be publicly disclosed. This would formalise the relationship described by the Minister, and in so doing provide greater transparency and focus to the process. (Paragraph 31)

2.9 This Report contains a number of recommendations about the remit and powers of the FCA. The Treasury is currently considering the wider scope of financial regulation, including potential action to improve coordination between the regulatory authorities. If the Treasury is not content to provide the changes in remit and further powers to the FCA as recommended by this Committee in this Report, the Treasury must acknowledge that it has itself fully retained these responsibilities. If that is the decision of the Treasury, this Committee recommends that the Treasury reports annually on the work it will do to monitor the perimeter of regulation, the risks that may have arisen beyond the perimeter, and how it has acted to detect and prevent consumer detriment. This could usefully be done in response to the FCA's annual Perimeter Report. (Paragraph 42)

2.10 Decisions on which activities should be within the perimeter of regulation should ultimately be for Ministers, with approval by Parliament. The Government therefore takes full responsibility for consulting on and proposing any changes to the perimeter to Parliament. The Government monitors the perimeter on an ongoing basis and acts when it sees consumer detriment. In order to ensure that this is done effectively, HMT already engages regularly with the financial regulators (including the FCA) at both official and Ministerial level on whether the perimeter needs to be changed. These discussions have contributed to the Government deciding to bring several financial services activities into FCA regulation, including consumer credit and peer-to-peer lending. The Government does not therefore see the case for providing a formal power for the FCA to request changes to the perimeter.

2.11 The Government welcomes the FCA's publication of its Annual Perimeter Report in June 2019. The report is a helpful annual summary of the issues the FCA has faced at and beyond the perimeter, and the Government will continue to use the report to inform its thinking.

2.12 The FPC has the power to recommend that the Treasury order additional information from unregulated entities to help meet its objectives. At the very least, this should be replicated for the FCA in relation to its own present objectives. Indeed, there may be a good case to exceed the FPC's power, given the fast-paced nature of risks consumers may face at the perimeter, and the FCA itself should be able to determine whether it should gather data from non-regulated entities, as needed to meet an expanded remit beyond the perimeter. The Committee recommends the Treasury undertake research on this point, and in doing so canvass the views of FCA. The Committee would then welcome the Treasury's views in its response to this Report. (Paragraph 39)

2.13 The FPC has the power to recommend that the Treasury orders the PRA to require entities, including unregulated entities, to provide information. The FPC has been given this power because it has the macro-level responsibility of identifying and removing systemic risks in financial markets – which is a very different remit to that of the FCA. The FPC's power is restricted, since it must consider that the information required is relevant to ensuring the stability of the UK's financial system. Furthermore, the FPC is required to consult the Treasury before it exercises this power, and the Treasury must seek approval from Parliament to make the order to the PRA.

2.14 The recommendation proposes that this power is replicated – and even exceeded – for the FCA. This would be a significant change to the FCA's remit, and important considerations need to be taken into account. Parliament has decided that the FCA should focus on regulating authorised firms – i.e. those firms which undertake at least one regulated activity. Asking the FCA to gather and process data from unauthorised firms would add significantly to the FCA's supervisory responsibilities and have considerable resource implications, carrying the risk that the FCA's ability to supervise authorised firms is reduced. The Government will have further discussions with the FCA on the merits of this power, taking into account these considerations.

2.15 The Committee notes Andrew Bailey's comments around the potential to change the perimeter following Brexit. The previous recommendations in this Report, in our view, do not need to await that event, and should be considered and brought forward by the Treasury as soon as possible. (Paragraph 44)

2.16 As noted in this response, the Government monitors the perimeter on an ongoing basis and is already working with the FCA to consider issues related to it. The conclusions of the Government's work in response to the failure of London Capital & Finance, including on the Financial Promotions Regime, will be brought forward as soon as possible.