

## Treasury Committee

Oral evidence: [Appointment of Andrew Bailey as Chief Executive Officer of the Financial Conduct Authority](#), HC 568

Wednesday 20 July 2016

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Members present: Mr Andrew Tyrie (Chair); Mr Steve Baker; Helen Goodman; George Kerevan; John Mann; Chris Philp; Mr Jacob Rees-Mogg; Rachel Reeves

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### Witnesses

I: Andrew Bailey, Chief Executive Officer, Financial Conduct Authority

Written evidence from witnesses:

- [Andrew Bailey's appointment hearing questionnaire](#)

## Examination of witnesses

Andrew Bailey, Chief Executive Officer, Financial Conduct Authority

**Q1 Chair:** Thank you very much for coming to see us for this appointment hearing, which is timely, because there is a great deal to discuss, not least as a consequence of the Brexit referendum decision. You are very well known to the Committee, not well known for speaking, for the most part, on conduct issues, but mainly for speaking on prudential issues in your former role as the head of the PRA. Can I begin by asking you about the Brexit decision? What is at stake? What do we stand to lose if we just walk away and try to become a vast Singapore, a large offshore island relying on WTO rules?

**Andrew Bailey:** It is important when talking about trade to distinguish between trade in goods and trade in services. There are obviously some similarities, but there are also quite important differences. What is at stake, when we are talking about trade in services, is that the success of the UK is that it has had access to almost all the markets globally. Of course, of those the European single market is the largest. If this is a scenario in which access to the single market is at risk, that might be a bad outcome. We should seek to have access to that market. Therefore, the important question is: how is that going to be constructed in the future? We will arguably continue to have access to other markets around the world, but the single market is the largest.

**Q2 Chair:** In your field, the field of financial services, what is at risk? What is at stake if we do not maintain access to the single market? Then I will come on to how we might maintain it.

**Andrew Bailey:** A substantial amount of trade in services is at stake. With that would go decisions on location. It is a little early to really know exactly what form those decisions will take. It depends on a whole variety of outcomes.

**Q3 Chair:** I have given you a model outcome at one end of the spectrum. What is the consequence for asset management, wholesale banking, parts of insurance, payment services, whatever? These are the ones are often mentioned. I just want to get a feel for what is at stake and how much we would lose.

**Andrew Bailey:** Currently, there are 11 different passports in European legislation. Those run through a whole range of activities and they are all different, which is also a factor. People tend to talk generically about the passport, but in fact all 11 are different. If you like, we could provide you something in writing to set out the differences, if that would help, and also to set out how much they are used.

**Q4 Chair:** That is the key point: what in practice is at stake, rather than what in principle it might provide for in theory.



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**Andrew Bailey:** Just to give you a flavour of it, the passport in asset management—the so-called UCITS structure—has a greater degree of demand for domicile in the other country than some others, so the ability to passport without domicile is not as easy in the so-called asset management world. You would see—I have talked to quite a lot of asset managers who have made this point—that there are bigger legal entity locational decisions in that world than there are in some of the other passports. In banking, it is predominantly much more wholesale than retail. The retail banking world is still based more dominantly on location and legal entity presences, and is much more in a subsidiary model than a branch model. There is a bit of branching, but it is more of a subsidiary model. Wholesale banking is far more in the branching or services model, so it is not as much about location.

A good example of the newer passports, as you mentioned a minute or two ago, is something like the payment services passport. A lot of the FinTech start-up firms are developing models to be payment services providers. That passport is taking off quite rapidly now and is more of a service provision passport. A big part of payments is inherently cross-border.

Q5 **Chair:** You said, in asset management, domicile is somewhat separated out from the pure passport model.

**Andrew Bailey:** It is a passport but it has some more features to it, yes.

Q6 **Chair:** Therefore, it would be wrong to suppose that all the asset management business currently being done in Europe would necessarily be vulnerable. It would be very helpful for the Committee to have—and it will have to be arranged—an estimate of what that would look like on WTO rules, bearing in mind the progress or otherwise of IOSCO on getting to agreed standards on services regulation. I need to have a column with some numbers in it that then can be added up at the bottom so we can get a feel for what is at stake.

**Andrew Bailey:** We will take our best shot at that. The IOSCO point is also the entrée to the second big issue here, which is that, again in the services world, it is standards of equivalence that are important. This is the essentially regulatory equivalence.

Q7 **Chair:** I was going to get into this, because the alternative approach would be some sort of arrangement. At one end of that spectrum is full EEA status, which means that there would be equivalence, but it also means that we would not have a say, as things stand in the current EEA arrangements, about the rules that would then be equivalent in each country.

**Andrew Bailey:** That is correct. I may be anticipating a future question, but, if you ask me what I have observed so far in the period since the outcome of the referendum in terms of developments in Europe, obviously I have changed jobs in the last three weeks. I ended my time in the European Banking Authority and joined ESMA, the securities



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authority, to be on the board. I went to my first meeting last week in Paris with ESMA and this was the first item on the agenda. In things the FCA has said, we have made the point that, as long as the UK remains a member of the European Union, we have a duty to apply the rules and we will do that; we are co-operative; we have no wish to disrupt these organisations and we will be good citizens, for which they are grateful. But we have to recognise that our ability to advance UK agendas has diminished materially. That is true.

The question then becomes: if not that, what will the future arrangement be? For my part, two things come into play there. As the world is organised at the moment—this is more to do with my former role than my current role—in some areas of financial services, there are global standards, which provide an equivalence backdrop. The most obvious one of those would be the Basel standards in banking, but there are others. That, as things are configured at the moment, does not in any way provide a full patchwork, and certainly not in the FCA area.

Then you get to the very big question, which is: if you want access to the single market and you recognise that, in the world of services, equivalence is the other part of that whole structure, how are we going to organise ourselves in future in terms of equivalent standards? What role are we going to have in that world, in terms of having influence over them?

**Q8 Chair:** It is very clear that the Government do not have a negotiating position at the moment. Indeed, that seems to have been clear from what the Prime Minister said today, prior to her visit with Angela Merkel later on this afternoon. It might be helpful also if you set out for us on a piece of paper the main elements of what you think an optimal deal would look like if we had a great deal of negotiating leverage, which we might—who can say?—so we can take a look at what it is one should be trying to work towards, with the main constituent components set out in as much detail as you can.

The other big issue, which we have not yet discussed, is the free movement of labour. What proportion of your staff are from EU countries? What proportion of your staff are from abroad and carry non-British passports?

**Andrew Bailey:** Our best estimate is that 14% of the FCA staff are non-UK citizens; that breaks down to 8% being EU citizens and 6% non-EU citizens. The FCA is not untypical. I do not have the Bank of England's numbers in my head, but it is not that dissimilar, from having worked there for a long time. I do not think we are very dissimilar to other employers. First, I would say—I know this was covered somewhat in the press, because it hit me on my first day there—that we have had to work hard and will have to go on working hard to give reassurance to these staff, because they are very valuable people and they are unsettled, frankly.



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You might say, "That is today; what about the future?" If I come back to the ability to function as an industry that provides internationally traded services, it follows that you have to have quite a substantial international labour force. You cannot sell services and be an international financial centre without having the ability to have a broad base of staff. That industry would not exist if it were staffed only by UK nationals. That is not plausible.

Q9 **Chair:** Have you sounded out major employers that you regulate to see what they say about the current visa arrangements for global immigration, never mind EU immigration, and also specifically the Brexit aspects of that?

**Andrew Bailey:** It is a little unscientific, but those I have seen in the last couple of weeks have shared the view that they are having to do quite a lot of reassurance of their staff and that they are happy with the staffing model they have at the moment and they think it is the right one, which stands to reason, in a way.

Q10 **Chair:** It seems that this issue is one that we will have to return to in more detail. In the meantime, it might be helpful if the two main regulators tried to think of a way of collecting some information on this more systematically, including with respect to non-EU immigration; that is, the immigration that might have been affected by the new visa requirements. Anecdotally, I have had a good deal of complaints coming to me personally from firms saying that they find it difficult to get hold of staff from around the world.

**Andrew Bailey:** I have heard similar comments.

Q11 **Chair:** Exactly. There is also the new angle to this coming down the line, which is the Brexit angle. Both need to be looked at, and so does the two-year window after Article 50 is pressed, because there is overwhelming support in the House of Commons for making sure that existing citizens should be looked after, although we still have not had quite the assurances that people would like to have from the Government on that. There is the issue of whether EU citizens will come here in the interim period, until they find out what the ensuring arrangements will be.

**Andrew Bailey:** Yes, you are right.

Q12 **Chair:** Therefore, how to handle that period also needs to be addressed. I would also be grateful if you would set out in anything you send us what advantages may come with the removal of some of these passporting requirements, were we to go down the road of the Singapore option; I am calling it that for shorthand. For example, I am thinking about the relatively lax standards of consumer protection that enable some financial products to be sold out of Cyprus and Malta, which it might be held that we should be blocking, but we find it difficult to block as things stand. It is not all one-way traffic, and we need to think about that issue carefully.



There may also be opportunities that come from being wholly outside the zone of regulation with respect to, as you were describing a moment ago, the need to develop IOSCO and the need to get global standards to a higher level. An assessment of the practicality of that in a meaningful time frame—within a few years—also needs to be set out.

I would just like to raise one or two points with respect to the questionnaire you have helpfully filled in for us. It is clear when approaching your work at the FCA, Mr Bailey, that you are intending to take a pretty robust line on a number of issues. It is also clear that you think the current FCA has been making a number of quite serious mistakes and it has quite serious shortcomings. You say you need “to make the FCA a highly effective regulator”, which suggests you do not think it is now. You say the first priority is to “establish a well understood mission at the FCA”, which suggests that it does not have one now. I can go on like this for some time with these; I have about half a dozen, so why don’t I just stop there? This is almost a mea culpa list for the institution that you have just started to head up. You are clearing the decks, aren’t you?

**Andrew Bailey:** I have had a while to think about this since I was appointed. There are two headings that I would put it under. One is this question of the mission. Let me explain briefly what my thinking is there. The simplest way to put it is that, like all public bodies, the FCA has objectives given to it by Parliament, which is absolutely right and sensible. However, like all such objectives, including those of the PRA, they are very high-level. That is a good framework for doing it, but you have to recognise they are as such. If you look at the FCA, you have the very high-level statutory objectives and then you have an annual business plan, which is essentially a document that says, “This year, we are going to do the following things.” There is not a lot in between.

What is the issue there? The issue there is how you interpret the statutory objectives. That is important, particularly for the FCA, because it is operating on a very big landscape. To put a scale on that, one of the simplest ways of looking at it is that the FCA authorises 56,000 firms. Sam Woods gave you a number for the PRA yesterday; it is obviously a small number by comparison. This is a big landscape. You have to, therefore, make choices as to what you do. Those choices, in a way, are embodied in the business plan. You, therefore, have to have a guiding set of principles and a mission as to how you make those choices, because behind those choices lie important questions.

To highlight two of them, the FCA has a very big range of tools it can use, bigger than most other regulators around the world. It has, in no order whatsoever, supervision tools, enforcement tools and more competition powers than any other financial regulator I can think of. It can do what it tends to call thematic work, which is looking across sectors to supplement firm-level supervision. To start with, you have to have an understanding of how you choose between those tools.



To give you a concrete example of this, the FCA has just had one of its outside surveys done of what people think. One observation that comes back is that the competition tool is least well understood in terms of how it is being used and what the FCA is aiming to do with it, notwithstanding the fact that I can assure you, inside the FCA, it gets a lot of attention. To my mind, that gives you an answer that says there is still work to be done to explain how those tools work together and how you make choices. That is one thing.

The second thing of the two I would give is, taking the really important thing about consumer detriment, how you decide, with your limited resources, what you focus on. There are judgments applied on that. One of the crucial issues I would highlight there is: are we protecting all consumers to some equal level? Are we protecting vulnerable consumers more than others? There is a duty to consumers embedded in the broad framework. I will give you my personal starting point: I would tend always to have a concern for the more vulnerable consumers, because they are at a relative disadvantage in the same market, but there is nothing there that tells you the answer to that question and helps to guide you through.

I will say two final things. First, this is important not only for the FCA in terms of how it makes its decisions, but also in terms of accountability. The absence of this has hampered accountability. It is also important for transparency. That is very important, frankly. It is also important internally in terms of explaining to people how we go about our business, what we are there to do and how we do it. Without that, it is harder to do the job.

The second thing, which I will be very short on, is that the place needs to be run effectively and tightly. Let's be honest: you have had hearings on these things. There have been quite big incidents in recent years within the organisation, which had damaged the reputation, standing and internal morale within the institution. That is well acknowledged and one of my very clear objectives. For the benefit of the whole organisation and for the staff, we have to run an organisation that does not get into those situations.

- Q13 **Chair:** There is overwhelming support round this table, although we have not specifically discussed it, for concentrating on the most vulnerable consumers who are most severely affected by asymmetric information, given the fact that they cannot get hold of the information and, even if they could, they probably would not be able to digest it. That problem is made much worse by the fact that there is often very little competition in these markets, or certainly inadequate competition, particularly for the provision of services to more vulnerable people. Parts of retail banking are examples of this—overdraft facilities, for instance. These are the sorts of issues that, round this table, we have felt very strongly about for some years. We want you to focus on them, but also to use those competition powers.



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There is a great deal of asymmetric information about what you buy in Sainsbury's and what is actually in the can. Competition is an extremely powerful regulator. If people think Sainsbury's are giving them a bad deal or there are fewer baked beans in the can, they will go down the road to the other store. In banking, that is very difficult. That is true of a good range of products that sit just above the provision of very basic banking services, but which millions of people want to have access to.

**Andrew Bailey:** The interesting thing there, which has come up in the context of the overdrafts question, is that the FCA is in a more powerful position than the CMA here because, as I understand it, the CMA can only address a competition issue as a competition issue. If you take the overdraft question, which is very important, to be fair to the CMA, its remedies must address it as a competition issue. The FCA can bring more powers to bear, because it can say it is a competition issue but it is also a consumer detriment issue in the broader conduct world. That is where the FCA can do more than the CMA can do, as I understand it.

Q14 **Chair:** Assuming that the CMA is doing a good job. We are becoming a bit nervous about the way it has been approaching its banking work.

**Andrew Bailey:** I agree with that. The point there is that when the CMA—

Q15 **Chair:** Are you agreeing that we are right to be nervous about the way it approaches its work?

**Andrew Bailey:** The reason I make that comment is that, when the CMA hands over the issue to the FCA—to take the overdraft issue, because it is a good one—the FCA can broaden the line of sight on this issue at that point, because it can say, “We take the competition points, but we can also look at this through another lens as well.”

**Chair:** I am going to move the questioning on, because your answer to that final question I asked you about how you intend to approach the job turned out to be longer and more detailed, but very interesting.

**Andrew Bailey:** I apologise; I am very keen on it.

Q16 **Helen Goodman:** Good afternoon, Mr Bailey. It is very hot and, like the Chairman, if you want to take your jacket off, that would be absolutely fine.

**Andrew Bailey:** Mr Rees-Mogg has not.

**Chair:** I did make Andrew the offer earlier.

**Andrew Bailey:** That is very kind of you.

**Rachel Reeves:** Jacob is not wearing a waistcoat, so that is pretty dressed down.

**Helen Goodman:** Mr Bailey, were you surprised when the Chancellor asked you to do this job?



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**Andrew Bailey:** Shall I tell you the story? That may be the easiest thing, because I knew this is going to come up. I have to start by saying that I was not looking for another job. That is very important, because I hugely enjoyed being chief executive of the PRA and the story is not negative about the PRA; I loved it. It was a great job. One or two journalists had speculated during the autumn about it and I had always said no, I was not thinking about it, because I was not looking for another job.

The second thing is that I would not in any sense have wished to be in the field, as it were, as long as Tracey McDermott was in the field, because I know Tracey very well. I have very high regard for Tracey and I am not going to compete with Tracey, because that has never been my interest. As you know, Tracey pulled out around mid-December. I was contacted and asked if I would see the Chancellor just before Christmas. I did not actually see him until just after New Year; I went away on holiday the day after I was contacted. I had an hour with him and he asked me if I would consider it.

I spent two weeks thinking about it, very hard. It was a very hard decision to make. In that sense, I was not expecting it. It was a hard decision because I loved the place I worked in. I get on famously with my former colleagues at the PRA; I loved setting up the PRA. But the Chancellor—I have to be honest with you—put back to me some of my own words: I had said a number of times that, for the twin peaks system to work, both peaks had to be firing. That is true. I am a strong believer in twin peaks and I am also a strong believer that the most important thing that those of us involved in regulation in this country have to do is do what we can to establish a stable institutional structure. I am in the 32nd year of my career and we are on the fourth system of financial regulation in this country, so you conclude that it has not been stable.

Given that, and the fact that I mentally asked myself whether I was up for the challenge and the answer was yes, I decided to say yes. I am really pleased I said yes, because the more I have thought about it, and having now done it for two weeks and a few days, I am hugely enjoying it. I hope that helps.

Q17 **Helen Goodman:** I am glad that you said what you said about Tracey McDermott, because it would look from the outside rather like an old boy's network kind of deal. Here we have a woman who is not a banker but a lawyer and from Rotherham. She is obviously outside the usual circle of appointments, so I am pleased you said what you said.

**Andrew Bailey:** I am from Leicester, so please don't—

Q18 **Helen Goodman:** I know you are. But it is interesting that the Chancellor felt the need to appoint somebody who had not even applied, isn't it?



**Andrew Bailey:** Yes. There are many things I cannot explain, because I was not on the other side of it.

Q19 **Helen Goodman:** Can I take you back to your previous job and something that happened there? I am going to read to you a speech that a Lib Dem Peer made on 15 December on the Bank of England and Financial Services Bill's Second Reading. He says in his speech, "Clause 22 alters the SM and CR that Parliament agreed to in the Financial Services Act (Banking Reform) 2013. This Act put into law the unanimous recommendation of the Parliamentary Commission on Banking Standards. The commission's report recommended [...] 'the full range of civil sanctions, including a ban, on an individual unless that person can demonstrate that he or she took all reasonable steps'", which would "make sure that those who should have prevented serious prudential and conduct failures would no longer be able to walk away" [...] 'The problem is the incentive for cheating markets is massive. If you can shift a rate fractionally you can make millions of dollars for your bank and then for bonuses.'"

He went on to say, "Over the course of the stages of this Bill and in discussion, the Government have offered a variety of justifications for reverting to a lighter-touch regime. [...] The third argument, put forward by Andrew Bailey, was that noise around the tougher regime has been distracting future senior managers from complying with the spirit of other important aspects of the regime. Mandy Rice-Davies would have known how to respond to that", said Lord Sharkey. He went on to say that there was a further argument about the specification of responsibility, which was advanced by you in a private meeting with Peers the previous week. My understanding from this is that you went to talk to peers who were unhappy about the Bill in private, not on the record, in order to explain the position.

He says, "As Tracey McDermott, the then director of enforcement [...] said [...] the inability to impose sanctions on senior executives was first and foremost due to the evidential standard required to prove their liability. That is why the old regime produced no penalties [...] and that is precisely why the regime proposed in Clause 22 will not do that either. It is absolutely no use having a detailed organisation and responsibility chain if there is no evidence." Then the Lord talked about the inequality of arms and contrasted it with the FCA, which is "underresourced", "overstretched" and "outgunned". He went on finally to say "The contest between the FCA and the banks is unequal, made more unequal by Clause 22. It is notable that the Government have fielded no one from the FCA to defend their proposed change. They have relied instead on Andrew Bailey, a Bank of England official."

I am wondering whether the Chancellor of the Exchequer felt that he could reply on you to persuade these opposition peers in a political environment of something on which he had been lobbied very hard, and because of that he felt that you were a more reliable person than Tracey McDermott to have this job.



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**Andrew Bailey:** I did meet with quite a number of peers. I can tell you from their voting records that I had no impact whatsoever on their voting, but let me explain. This question has come up in this Committee before so I will give a shorthand version of it. I reject completely the notion that the so-called duty of responsibility that we have today is light-touch versus the presumption of responsibility. That is just not true. The issue is that the so-called presumption of responsibility—

**Helen Goodman:** I am not particularly interested.

**Chair:** Can we just let Andrew Bailey answer this?

**Helen Goodman:** Okay. I am just trying to speed it up.

**Chair:** You did take a while to ask the question, Helen.

**Andrew Bailey:** This is germane to your point about whether you had to wheel in a Bank of England official to get the right answer. My view—and this is how the implementation of the presumption evolved—was that it was going to complicate the regime in ways that would be unhelpful to getting the results that you have very clearly stated you want and I want too by reversing the ways in which the previous regime had failed. That was because, in the way the presumption was evolving, we were getting very long checklists and tick-box procedures being developed to allow people to go through what they thought was the presumption exercise, which in that legislation involved, as you may remember, them demonstrating that they had taken reasonable actions.

We had people coming and saying, “Well, it is reasonable actions. I am sorry something went wrong, but we had a risk committee, a chief risk officer and a risk appetite statement. It all went wrong, but it is not my fault.” That is not acceptable, so the consequence in my judgment was that it was all going to come back to the regulators in that situation to say, “I am sorry; that is wrong. We are going to have to prove the case that you are responsible and you were responsible for what went wrong.”

If you take that line of argument, you may as well go straight to what we have now, which is the duty of responsibility—it is the same duty, the same responsibility; nothing has changed on the definition of responsibility—and say it is then the duty of the regulator to make the case. My view is that we were just going to end up there anyway, by a more convoluted route.

Q20 **Helen Goodman:** It is about the evidential base. In fact, the 2013 regime had not come into place at this point in December. It was not coming into place until this March. One of the reasons that the Chancellor wanted to get this piece of legislation through was that it would never be. I am not entirely convinced that a tick-boxy exercise happening under a previous regime is an argument against a regime that had not yet come into place.

**Andrew Bailey:** All I can tell you is that I was observing very closely—because we were implementing the regime, obviously, and we were



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observing what firms were doing—that that was the way it was going. That, to me, was a bad outcome.

- Q21 **Helen Goodman:** In the written answer to question 10 that you have sent to us, about enhancing your independence, you have relied on the fact that this is a five-year appointment.

**Andrew Bailey:** Yes.

- Q22 **Helen Goodman:** I am just wondering whether that is a sufficient condition to provide for your independence. Surely a more reasonable approach would be to look at the way you have in fact behaved on previous occasions.

**Andrew Bailey:** Sorry, do you mean in terms of my independence?

**Helen Goodman:** Yes.

**Andrew Bailey:** You can go back and look at how I behaved in the PRA. You can go back and look at the amount of capital we got the banking system to put on, which I cannot tell you they were happy about. If you want to do that, you can do that. The point about the five-year term and why it is important for me is this: I was not the only person who was pretty surprised, when Martin Wheatley stepped down, to find that he had not got a five-year term. Obviously, Martin and I were appointed at the same time to be the chief executives of the two regulators. I had assumed that he had got the same terms and conditions that I had at the PRA, which was a five-year term. It turned out, unbeknown to me, that he had not; he had got a more convoluted structure, which enabled the action that was taken to be taken. As you know, there was a further twist, as I understand it, in terms of his board term.

That, to me, was unacceptable. I made it quite clear. When I was approached, I said "If you are thinking about those terms and conditions, I am not in this, because that is not independence." The five year term that I have today is the same term and the same structure as I had at the PRA, which is the same structure as the Deputy Governor of the Bank of England has.

- Q23 **Helen Goodman:** I am just wondering why you, as head of the PRA, went to talk to opposition peers about government policy on the matter of FCA powers.

**Andrew Bailey:** It was PRA powers.

**Helen Goodman:** It is both, isn't it?

**Andrew Bailey:** This is very important. That was and is a PRA power, as much as an FCA power.

- Q24 **Chair:** Can I just clarify one other thing? We did take extensive evidence on this in the Committee at the time. I was concerned to get to the bottom of the reason for the change of view. It was significant and influenced this Committee that Tracey McDermott took the same view



that the presumption of responsibility or the reversal of burden of proof probably did need to be reversed. She was “relaxed” about it—I think that was the phrase she used—because she was weighing up the benefits of it against the unexpected or not wholly expected problems that had been created. Since I share part of the responsibility for the fact that this was in the legislation in the beginning in 2013, I felt I needed to say that, because there clearly had been unintended consequences.

That still leaves a point that Helen is making, quite reasonably, which could be answered more directly, and I would like a direct answer. Were you leant on or—I have not asked you this before—pressed in any way or requested to push off and do some secret lobbying on behalf of the Government to secure this change? If I do not have quite the right manner in which this might have taken place, I want my question to cover a whole raft of possible ways in which you may have been prevailed upon to do that. Isn’t that the key point that you are making, Helen?

**Helen Goodman:** Yes, absolutely, thank you.

**Andrew Bailey:** I understand the point you are making. I am pretty confident, because I have the dates roughly in my head, that the arguments I made on the question of the duty of responsibility were ones that I had made to this Committee, previously to any of those meetings. My position was, frankly, well known. It was not something that I was influenced to make up at all.

I just come back to the point I made at the start: what shaped my thinking was the experience of watching the implementation of it and the fact that, in my view, it was not going well. It was not going well at all. It was, frankly, in danger of taking us back into the world we were trying to get out of. To me, that would have been a desperately bad outcome. We all witnessed what went wrong in the previous regime.

Q25 **Chair:** I do not want to prolong this, or hog it either, but right at the heart of it is that there is going to be another episode, sooner or later, hopefully not as bad as 2008, but there will be another series of failings or failures and we will want to be able to discover where responsibility lies. It is conceivable that it does not lie with one particular individual, and it is a rare occasion when it really does lie with a group. The principle of individual responsibility has to be capable of being established with the new regime. By changing the presumption of responsibility, we have changed the terms of trade on that a little. It is essential, and I hope you can give us this assurance, that you come to this Committee if you have any concerns that you do not have the powers to ensure that, when that event occurs—it is not an if, but a when—you are capable of establishing how and that individual responsibility can, if appropriate, apply.

**Andrew Bailey:** I will of course do that, because the senior managers and certification regime is an absolutely fundamental reform to the system. We do not really have enough evidence yet, because it is still too early; it is only four months into the regime. If we get the evidence



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that it is not fulfilling our expectations or our wish list, we will of course do that.

**Chair:** We will certainly hold you to that.

- Q26 **George Kerevan:** Good afternoon, Mr Bailey. You come to the job with a certain amount of baggage. You were a senior manager at the old FSA when the two regulators were conjoined. Subsequently, in 2013, you were on the board of the FSA. Would someone be right in worrying, being concerned, that you have been a member of two organisations that have been less than successful?

**Andrew Bailey:** Well, let me explain. I spent the last two years of the FSA's life in the FSA, responsible for the prudential supervision of those firms that would go to the PRA. Essentially, the job we were doing there was running day-to-day prudential supervision, plus setting up the PRA to emerge into its current form on day one. That was why I went there. I was actually always employed by the Bank of England, but I held a management job, as you say, in the FSA, in order to do the job. You can judge me on that record, certainly. I have been a board member of the FCA since it was started, because, as you know, the legislation provides there is cross-board membership.

- Q27 **George Kerevan:** I am really teasing you to get an assessment of the responsibility you had and whether you discharged them on those previous occasions.

**Andrew Bailey:** I will give you one example. If you read the Davis review that was conducted on the whole briefing issue in relation to life insurance, you will find that there is a point in the review where it says that I was the board member who said to the chairman, "There has got to be a board meeting" on the day the thing blew up. If you want a bit of evidence that I took my job seriously, I would give you that as a piece of public evidence, because the Davis review is a matter of public record.

- Q28 **George Kerevan:** To press you further, what skillset do you bring to the new job? Apart from your understanding of economics, banking and the world of finance, what managerial skills do you bring that would allow you to take an organisation, which the Chairman has politely described as being in special measures, out of special measures?

**Andrew Bailey:** I have been involved in regulation on and off since the late 1980s. I inherited prudential regulation of banks and insurers in early 2011, when the banking system was coming out of its prudential crisis and, as you know, the FSA had substantially had its reputation damaged by its record on prudential supervision, so I had that task in respect of prudential regulation. I have been there before in terms of the need to build up a regulator.

- Q29 **George Kerevan:** Reading the answers to the questions that you gave us, there is one paragraph that jumped out at me, which is 'How to balance the duty of care towards consumers, the duty of responsibility of consumers for their decisions, the role of firms and the role of the



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regulator is an inherently difficult question to which there will be many potential answers. It lies at the heart of the FCA's mission. So far, I would say it has not been adequately answered." Then you do not quite answer it; it kind of stops there. I was going to give you a chance to answer that.

**Andrew Bailey:** The reason it is not answered is because I have been there a bit under three weeks. I have set the work in motion for what I want to be a very public piece of work. I hope, as I have said in the answers, we will be able to produce something for public discussion and consultation in the early autumn, if we can do that, to seek to put flesh on to that question and answer it. It is interesting, because one thing that is quite striking about this subject is that, particularly in the area of retail conduct supervision, there is not a lot of what I would call backing academic thinking that helps you get to an answer to these questions.

I have been involved in quite a few areas of public policy, in the Bank of England days. If you think about monetary policy, there was a big upsurge in the intellectual framework of monetary policy coming out of the high-inflation era of the 70s. If you think about prudential regulation and financial stability, there has been more recently a big upsurge. Interestingly, when you get to this question that you read out, which I think is fundamental by the way—I do not know whether you agree, but I think it is fundamental in this area—there is not a lot of what I might call outside thinking to fall back on and say, "How do we think about this question? How do we judge our duty towards our consumers?" I wish there was, because it would make the job easier. It also tells us something about the relative underdevelopment of, particularly, retail conduct regulation. It is a fundamental question.

We will see how good an approach we get to it. I am hopeful, but there is a lot of work for us to do in the next few months. Then we will put it out for very broad consultation and commentary. If you would like, I am very happy to discuss it with you at any time, in any form you like. That is what we will be doing.

Q30 **George Kerevan:** When will we get this work?

**Andrew Bailey:** As I say, I hope it is in the early-ish part of the autumn. The reason I am hedging a little is because we are in pretty early days, if you do not mind.

**George Kerevan:** We are just looking for a ball park

**Andrew Bailey:** It is a bit heroic to nail a date down at the moment, but I would like to do that.

Q31 **George Kerevan:** Before the end of the year?

**Andrew Bailey:** Yes. I would like to do that, because a whole number of things follow from that in terms of then embedding it into the FCA and putting it into the annual business plan cycle. That is the aspiration.



**Q32 George Kerevan:** There is an issue here on consumers. On your answer to question 9, when we asked you to assess the successes and failures of the FCA, there was one area that was missing, from my point of view as an elected Member, and I know this reflects the experience of a large number of elected Members, which is the sheer disquiet from small businesses going through the review process for FOS; this is very live. Now, there is an interconnectedness, a relationship, between FCA and FOS. I know it is slightly arms-length and FOS is deliberately there so you do not get involved in adjudicating cases, but nonetheless, given the relationship between the two agencies and the unhappiness, which is more than buyer's remorse—there is an extent of unhappiness with the operation of FOS—my question is really: how do you see the relationship developing between the FCA and FOS

**Andrew Bailey:** Can I answer that in two parts? I would slightly differ from your interpretation of the question in one respect, but let us talk about FOS to start with. The relationship has to be close. There is a constitutional independence of FOS, which has to be respected. I very much hope that we broadly have a relationship where we are on the same sort of wavelength, in terms of our basic attitudes towards the underlying issues, because, if we are not, it is going to be a problem.

The point I would differ on is this. Interestingly, the question about small firms, in my experience, is mainly not a FOS question, but a different question. Here I go to the point you made about the FCA and adjudication processes, and interest rate hedging products is probably the most controversial but not the only example of this. The FCA has found itself, for those areas that are outside FOS's role, creating adjudication processes. For interest rate hedging products, it has created a process by which the banks have a duty to do the process and there is oversight by a so-called skilled person, which is typically an accounting firm. That is enormously controversial. I can tell you that, because they are busy filling my inbox up as we speak with complaints. We had this at the annual public meeting of the FCA yesterday. They are, as you say, difficult cases.

If I step back from that, and this is an issue for the FCA's mission, I do not think the FCA was really established or conceived to be an adjudication body. It is a regulatory and supervisory body. Now, this is not a criticism, but it has found itself in that role, and it has found itself creating—I do not know how many, but there are quite a few—bespoke adjudication processes. Those processes are controversial. I watched the debate in the House of Commons earlier this year on no confidence in the FCA. Quite a bit of the debate was around cases that involve those adjudication processes.

The question that follows from that for me is: given that we have to have adjudication processes, how do we get to a point where we have better established processes with more authority and, frankly, where people can quite reasonably feel—I use this as a metaphor, not literally—"I have had



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my day in court.” The point is that the process has enough authority, in the best sense of the term, to it that I accept that it was a process that got me to a judgment, even if I do not like the end-point of it.

**Chair:** We will have to move on in a moment—just one quick question.

**George Kerevan:** I appreciate that. Everyone’s mailbag is full of this.

**Chair:** I agree—mine too.

Q33 **George Kerevan:** Indeed. My interpretation is that there is quite a deal of discontent with the adjudication process, beyond individual cases, because I filter those.

**Andrew Bailey:** One has led to the other.

Q34 **George Kerevan:** Are you suggesting to us that that is an area you are going to look at?

**Andrew Bailey:** Yes, I am going to look at this question. This is not the FOS, by the way; this is the non-FOS bit I am talking about now. This whole question about how to deal with these cases that sadly come up and how to deal with adjudication processes is one that I do want to look at, because I do not think this practice of creating—I use this term carefully, because it can be a bit pejorative, but you know the point I am making—ad hoc processes has been, frankly, in my view, a success.

Q35 **Chair:** That is very helpful guidance, because that is exactly what the FCA was trying to do in order to speed things up, with the best of intentions. We took evidence from Martin Wheatley on exactly that point.

**Andrew Bailey:** I do not yet know what the alternative is. If you do not mind, I need some time to think about it.

Q36 **Chair:** But you have decided that the model that was created only recently to deal with this is not the right one.

**Andrew Bailey:** Yes.

Q37 **John Mann:** I have four questions. I have just changed one of them entirely after your last answer, so I will start on that. You say that you want a system where people can have the equivalent of their “day in court”, but any system that goes in that direction is one that suits those people who have a case that is so bad that they want to simply use the system to have a shout and a scream, or those people who are sufficiently wealthy that they can always be going to court, as opposed to those who want transparency, fairness and justice. I would ask you to perhaps reconsider whether that is the appropriate concept of a consumer seeking justice and fairness, perhaps in difficult circumstances where the evidence base that they are trying to provide is not written down as clearly as they would hope. That may well be a key part of the problem. How are you going to manage that? Are we going to go to a system where it is only those who have a hopeless case or those who have money who are going to get justice?



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**Andrew Bailey:** I actually agree with you on this. I did use these words to Mr Kerevan: I was using that term as a metaphor.

Q38 **John Mann:** I think you agree with me. I am happy to accept that as an answer, so let me move matters on.

**Andrew Bailey:** I used it as a metaphor, because I agree with you, but that does not of course solve the problem. We have to solve the problem, because the current system is not delivering either.

Q39 **John Mann:** There are models out there that have been used that are more effective than the FCA's. I am sure you will be looking at other sectors to see such models.

**Andrew Bailey:** Yes.

Q40 **John Mann:** I have 2,000 cases I took to the Law Society. I am more than happy for you to wade through to see how adjudication systems can, if well devised, be very effective for a just outcome. That is for another day.

You are complaining about the inability of people to get the citizens they want from outside the EU into the country to work. That seemed to be your gripe, in part answer to the Chairman earlier, both from the bank and in the FCA. We have not heard before that these organisations have had problems recruiting the people they want, whom they wish to import from outside the EU, because of the visa system. Is there a specific problem there that we should be aware of?

**Andrew Bailey:** No. What I said—and I took this to be what the Chairman was saying—was that, in my time at the Bank of England and obviously my very brief time at the FCA, so far I have not heard that point made in respect of our ability to recruit. As I said, to give you the FCA situation, 14% of our staff are non-UK and about 6% are non-EU. I think what the Chairman said is that he hears it said by people from outside, and I hear the same things. I have never, frankly, had the time or the need to follow up those comments—I am not an expert on the visa system—to look at the substance of it. I merely said to the Chairman that I have heard the same comments that he has heard, probably from some of the same people.

Q41 **John Mann:** Fair enough. I have heard them from the banks but I have not heard them from either the Bank of England or the FCA. If it was a problem then we would, I am certain, want to know about it. You have clarified before today, and not demurred from it today, that, as a member of the FCA board, you were totally in the dark over the sackings, the non-appointments and then your own appointment. You had one chief executive booted out, another one temporarily appointed and then mysteriously withdrawing her application. There is still a haze over the circumstance in that. That is not your responsibility; you do not know about that, even though you were on the board at the time. Then you emerged from the ether without interview.



It is a very important organisation. You are in a very important role. Throughout that period, you have a chairman who has clearly been bypassed repeatedly on all issues. Is that the calibre and strength of chairman needed to give you the support that you will need in what is an increasingly important role in a very important organisation?

**Andrew Bailey:** He did know what was going on, because, after I engaged with the Chancellor, I had a conversation with John Griffith-Jones, actually more than once, so he did know what was going on. To be precise, my experience of major public appointments is there is usually a two-phase process. There is usually, as you said, an interview panel that conducts an interview, and then the Chancellor usually conducts some form of interview as well. In this case, only the second one of those occurred. Let me be clear. I just want to say one thing: I never declined to be interviewed. Let us be clear about that.

The thing I would say on the FCA, in the context, if you do not mind—to answer a broader question—is that it is very useful that we have had new people come onto the board. We still have a major gap on the board, because we do not have a person with a consumer background on the board. As you may know, unfortunately the person who was going to be appointed had to step out before they got on, if that makes any sense. Getting the board to a point where it is effective and able to play its part is a job for both me and the chairman, to ensure that we provide the board with the ability to do its job. I take that very seriously, having had a lot of experience of that in the Bank of England.

Q42 **John Mann:** What is your early view on the percentage of time that you and other senior people in the FCA will have to spend on Brexit over the foreseeable future—a year, two years, however many years? I do not mean the next few months, but let us say over the next year or two years. What is your rough early indication of the percentage of time required?

**Andrew Bailey:** It is a really good question. I do not know precisely. What we have done, let me tell you, is that we have set up a co-ordinating unit in the FCA to service me and the senior staff to play the role we are playing. Obviously we have not played much of that role yet, because Government are going to take the decisions. We are there to provide technical support.

Q43 **John Mann:** How many people are in that unit?

**Andrew Bailey:** We are probably aiming for a dozen or so at the start. The one thing I would say, which we have been very clear on, is that we will no doubt have to come back and do some adjustment as the thing goes on. If you asked me whether I think we have now got to a settled position in terms of what the demand on us will be, I would say almost certainly no.

Q44 **John Mann:** That is reasonable enough. My final question is this: when it comes to RDR and GRG, we have seen people hung out to dry over a



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long period of time. You may have an update on those. Is this what consumers can now expect from the FCA?

**Chair:** Briefly, if you can. I know they are both big subjects.

**Andrew Bailey:** The issue with the RDR was that it tackled two things at least. It tackled opaque commission and a general question of qualifications and training for the adviser population, but it contributed—it was not the only thing that contributed—to the advice gap. If you are a less well off member of the public, or you do not want lifetime advice but you want discrete event advice, it has left a gap. There is now a gap, and the so-called FAMR proposals have to actually fill that gap. We have to be very clear, I think, in implementing them and keep asking ourselves the question, “Will they do it or not?”

Q45 **Chair:** What do you reckon?

**Andrew Bailey:** They have the potential to do it but I do not think we can sign that one off with conviction.

Q46 **Chair:** Even after all this preparation with RDR, we still did not get it right, or, rather, the FCA did not get it right.

**Andrew Bailey:** A lot of it rests on, frankly, the question of whether we will get useful technology that can be put to work. The jury is out on that one, not because FinTech is bad, but can it do the iterative type processes that you need in that world? It is not straightforward: I ask you a question, you give me an answer and that is the end of it.

Q47 **John Mann:** Can we expect more reports on GRG to be forthcoming?

**Andrew Bailey:** Yes, you will get a report on GRG. I cannot tell you when at the moment. It is heavily underway.

Q48 **John Mann:** This year?

**Andrew Bailey:** I hope so.

Q49 **Chair:** It is another big issue we are keeping a close eye on in this committee.

**Andrew Bailey:** It is another one I have inherited. It is on the list of very big issues.

Q50 **Chris Philp:** Good afternoon, Mr Bailey. You mentioned earlier that there are a huge range of tools at the FCA’s disposal. Very briefly, could you outline which one or two areas of regulatory activity you intend to particularly focus the FCA’s attention on in the coming months and years.

**Andrew Bailey:** The biggest single issue we face in the financial services landscape, particularly the retail financial services landscape, is the long-term savings, retirement and pensions issue, by a long way. It obviously has quite a lot of elements to it. We have a number of major outside developments going on, such as the shift to near-zero interest rates. Just take what has gone on this year. If you look at the shift in



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the sterling yield curve this year, you see the issue writ large. We now have a 10-year gilt rate under 1%. That tends to suggest we are going to be in this environment for a long time. We have the question of ageing population and longevity. There is the question of care costs that go with it. To my mind, that is the biggest single issue. It is not to diminish other things, but, if you put them all together, I would put that one at the top.

**Q51 Chris Philp:** What action do you propose to take to address that?

**Andrew Bailey:** There are a number of things we can do, but of course this is where it is important to interpret independence. We have to work with other parts of public policy that have very big responsibilities. We are, frankly, trying to get people to have as clear and transparent a product as they can. We have a pretty complicated landscape these days, which is somewhat legacy. If you asked the question, "Do you think the future of long-term savings and retirement provision in terms of financial services is crystal clear in this country?", it would be a brave person who said yes.

**Q52 Chris Philp:** I would like to move on to commercial property funds. As we know, since Brexit, a number—I think with aggregate NAVs running into the tens of billions—have put the gate up and are not issuing redemptions.

**Andrew Bailey:** It is about £12 billion, I think.

**Q53 Chris Philp:** Yes, it is about £12 billion. Can I start by asking whether you think the FCA has any role to prevent those funds disposing of assets in a disorderly fashion and crashing the market? If you do think that is your role, what will you specifically do?

**Andrew Bailey:** Yes. This issue hit me on day one. This was the "welcome to the FCA" issue. The answer to your question is yes, for two reasons. One is because we have a responsibility in terms of treating customers fairly. The problem with these funds is that you have an open-ended fund with daily redemption with an illiquid asset that cannot be valued.

**Chris Philp:** You pre-empted my next question. Go on.

**Andrew Bailey:** Sorry. You have to take a view on the treatment of customers and investors fairly, between those who seek to exit quickly, those who seek to exit less quickly and those stay. That is the first thing.

The second thing is that no good comes out of inducing a fire sale of commercial property, and that is either from the point of view of the customers or from the point of view of the economy.

**Q54 Chris Philp:** Do you plan to intervene and instruct them to sell over a timescale of, say, three to six months rather than more quickly?



**Andrew Bailey:** I got the funds in on the third day I was in the FCA. I also had to do the press conference for the Financial Stability Review. The suspension mechanism is actually part of the design, and intentionally part of the design, because you have to have some sort of safety valve in that situation. The suspensions have been put in place.

Q55 **Chris Philp:** They were put in place because there was simply insufficient cash to meet redemption calls. The question then is how quickly you sell the underlying assets.

**Andrew Bailey:** Just to be clear, that is true, but the cash is a necessary but not sufficient condition. If you cannot value the assets, then you cannot pay out. You could have a lot of cash, but if you cannot determine the value of the payout it will not get you to that point. They need liquidity buffers, but on its own that does not solve the problem.

Since then, the latest evidence we have is that the position is stabilising. The pattern of withdraw requests versus investment requests has gone more into balance. One or two of them have introduced a form of swing pricing, which has a discount on exit. There are some interesting judgments in that as well on customers. We put some guidance out at the end of my first week there about treating customers fairly in these things. We are focused now, obviously, on the conditions and how they remove the suspension. Then we need to come on to the question of the design of these things and to look hard at the design.

Q56 **Chris Philp:** That is my next question. Do you think it is appropriate that you have a structure where you are offering essentially daily liquidity to investors, yet the underlying assets are inherently illiquid and, let us say, to dispose of them in an orderly fashion takes between three and six months?

**Andrew Bailey:** It is that and the fact that you cannot value them. You cannot value a commercial property daily. There is not a market that gives you a value. We are going to have to consult and discuss quite widely. The alternative is that you have essentially a closed fund, you trade and the market determines the price. There is a critique of that argument as well, which is, "Where does the market get the price from?", but you are right in saying there is a market generating price mechanism.

Q57 **Chris Philp:** There is a second mechanism, which is to use a structure that, for example, a private equity fund would use. You make an investment for a fixed term and you simply get paid from the liquidation proceeds at the end of a five or seven-year term.

**Andrew Bailey:** You can do that as well. That is a fixed-term fund. It is not something you could then particularly trade.

Q58 **Chris Philp:** It would be worth considering the appropriateness of the structure of these vehicles, and you might want to just do a piece of work in that area, because it strikes me that there is a fundamental mismatch between the liquidity offered to consumers, the pricing offered to



consumers and the underlying asset. That mismatch is something that would merit consideration.

**Andrew Bailey:** I agree with you and I have said something similar.

Q59 **Chris Philp:** Finally, I would like to explore an area about which I wrote to you two or three weeks ago. Have you received and do you recollect my letter?

**Andrew Bailey:** Yes, it was on peer-to-peer and crowdfunding.

**Chris Philp:** Very good, I am glad that you have paid attention to correspondence.

**Andrew Bailey:** I have. The Chairman wrote to me as well.

**Chris Philp:** Indeed he did. I was raising a concern in that letter that the consumers who are going onto peer-to-peer lending platforms, notwithstanding the disclosure they may receive, probably do not understand the risks that they are taking on. I am very concerned that there is an incentive mismatch. The people running these platforms get paid fees based on volume, on how many loans are written, but they do not take any balance sheet risk. That is exactly what happened with the origination and then syndication of subprime loans in the US in the run-up to 2008. First, do you share my concern that there is a misalignment of incentives currently at play in this sector?

**Andrew Bailey:** You may have seen that we put out a short piece in the last week or two essentially raising issues that we will be doing work on in this market. We cover some of your points, if not the gist of it, certainly. You are right. The place I would start, just to strip it back to basics for a moment, is that, in my world, at one of the end of the spectrum of how we invest our money, there is the deposit contract in a bank, in which I give you my money and I expect it all back, please, on terms that we agree. On the other end is an asset management contract. There is a famous Woody Allen quote that the stockbroker managed my money until it was all gone. You do not expect capital certainty on it. These things at that end of the spectrum are not capital certain.

However, let me say two or three things, because I agree with you on the risks. I am pretty worried about some of the things that are said about these funds when they are sold to people because some of the things you read get very near, but not quite there, to promising capital certainty.

Q60 **Chris Philp:** They do more than that. They come very close to promising a fixed return. Many of them have "fixed returns", with a little footnote saying, "By the way, this might not happen". In the marketing, it is a fixed return.

**Andrew Bailey:** "By the way, in fact, it is not". Some of them then say that they have so-called reserve funds.

**Chris Philp:** Sinking funds



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**Andrew Bailey:** That is fine, but there is of course no guarantee in that fund. That merely tells you how you have structured the investment.

Q61 **Chris Philp:** There is no guarantee that the sinking fund will be adequate to cover any loss.

**Andrew Bailey:** No, exactly. That is one aspect to it. You are also right; another thing that we want to work out is the fee structure. One of the things that would concern me about it is this: if you go back to the crisis, as you mentioned it, one of the problems—Northern Rock is the case in point here—is that you structure your lending and take the fees upfront. You capitalise the fees into your return in the year in which you grant the loan on the investment, and that creates all sorts of uncertainties about how you churn and manage the book. Now, I have to confess to you that I am not sure how they do it in this industry, in terms of fee accounting.

**Chris Philp:** They charge a 1% or 2% fee based on the volume of loans written and they take it on their books at the beginning. Let me ask one final question, if I may, Chairman.

**Chair:** You had your final question a moment ago, but this will be your final question.

Q62 **Chris Philp:** It will, Chairman. I have a specific suggestion I will like to make to you and get your response. Why not require these platforms to co-invest, say, 10% of the loan value on their own balance sheet, either pari passu or even the first-loss piece? If their own money was on the line alongside that of consumers, that would concentrate their minds when it came to making good credit decisions. I would like your response to that.

**Andrew Bailey:** That is what I am looking at. The only thing I would say is that I presume, from what you have said before—you can tell me, but you would probably agree with this—you do not want that to start looking like bank capital and therefore a promise to the investor that they will get all of their money back. Providing you structure it in that way—which you can do, by the way; I am not disagreeing with you—it is certainly an idea worth thinking about because it puts skin in the game.

Q63 **Mr Rees-Mogg:** Good afternoon. I must begin with a declaration of interest because I am chairman and founding partner of Somerset Capital Management, which is regulated by the FCA. In that sense, I report to you. Can I first of all ask you a question on the Lloyds Bank enhanced capital notes and the FCA's role in this? I am not after a specific answer now, but would like to raise the point with you that regulation of prospectuses is with you as the FCA, and that the legal judgment in the Supreme Court is on the interpretation of contracts, not on the regulatory suitability of the prospectus. I think 123,000 retail customers received this prospectus which then turned out to be wrong.

**Andrew Bailey:** We will reply on the subject. This is a slightly déjà vu moment because I have been involved in this issue in my former life and



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I am now involved in it in another capacity in my current one, but there will be a reply from the FCA, yes.

Q64 **Mr Rees-Mogg:** In your new role, it is a very different hat.

**Andrew Bailey:** The question is a different one, yes.

**Mr Rees-Mogg:** In the old role, you wanted Lloyds to have the capital and in the new role you are the champion for retail investors.

**Andrew Bailey:** Yes, but if I step back into my old role for the moment, it does not do any good to put capital into banks on an unsound basis. It is not a great move.

Q65 **Mr Rees-Mogg:** I just wanted to highlight that, but we would be very interested in what comes out of that. I was going to go on to the relationship between your old and new roles. In your questionnaire, you said that the relationship between the two had become “deeper than was originally envisaged” and you mentioned, I think in answer to Ms Goodman, the twin peaks. Do you think it is a good thing that they are getting closer together or do you risk recreating the FSA?

**Andrew Bailey:** It is interesting. This is the reason it has happened, more than any other; and I say this quite honestly. If we had been having this hearing five years ago—I cannot remember exactly, but a number of years ago—and you had asked me as a prudential regulator, “Do you think that conduct risk is going to become one of the biggest risks for a prudential regulator in the future?”, I would have honestly said no, and I would have been wrong. It has turned out to be.

If you look at the stress-tests that the PRA and the Financial Policy Committee do each year, and you look at the significance and therefore the amount of time and effort that is put into putting a stressed estimate of conduct risk into the stress test, that gives you an example of why those sorts of thing has become closer. Conduct risk is a bigger issue now for prudential supervisors than we would have envisaged.

Q66 **Mr Rees-Mogg:** So the two come together.

**Andrew Bailey:** They come together, but let me say that it is not—and I always try to be scrupulous about the PRA—because the prudential regulator is trying to influence the FCA to somehow compromise conduct regulation. It is because we have been in a position where we have had to tap the expertise of the FCA and say, “Can you help us get the best estimate of what this could be sized at?” PPI is the biggest example of this, at £24 billion.

Q67 **Mr Rees-Mogg:** On a mis-selling thing, which is a conduct thing in the first place. Does it worry you that your very senior role in the PRA and your move to the FCA can appear to be bringing the two together, with you still having a strong affiliation with how the PRA did things, or are you creating Chinese walls?



**Andrew Bailey:** That is a good question. I have gone to the FCA with a self-denying ordinance that I do not go around saying, "This is how we do things in the PRA" because they are different. They have a very different set of objectives. It would not work.

Q68 **Mr Rees-Mogg:** You say in your questionnaire, very interestingly, that the FCA has more important challenges than the PRA. Is that because the FCA has not really been working as well as an organisation and the PRA has, or is it that the level of regulation that one does is more important than the other?

**Andrew Bailey:** There is a job to do at the FCA in that respect because of some of the well known incidents. However, if you go back to the pension issue for a moment, the FCA is actually heavily involved in some of the most fascinating public policy issues that are around. Do not get me wrong; it would be lovely to think that prudential supervision was done and finished and we could put it on auto-pilot; sadly it will never go there. But three weeks in, it is already fascinating; I can tell you that there are some truly fascinating issues.

Q69 **Mr Rees-Mogg:** Moving on to how you will operate at the FCA, you said that the level of intensity of regulation should not vary over time and distanced yourself from the very unhappy comment of your predecessor about shooting first and asking questions later. Are you looking at quite a different approach to enforcement?

**Andrew Bailey:** You would have to ask him this. Whether Martin regretted the comment, I do not know, but it got a lot of notoriety; put it like that. Honestly, as a public authority, if you try to analyse that comment and say, "Can you really shoot?", no. It would be quite honestly contrary to public law. It is a metaphor. In terms of enforcement, no: as I said, the FCA has a set of tools. Enforcement is clearly one of them. The FCA, as you probably know, has just completed its first major insider dealing trial, Operation Tabernula, which goes right back to the FSA days, when I was in the FSA previously.

It is very important that these things happen because, in terms of the overall cleanliness and conduct of markets, these things are very important. They are very complex to do, but it is very important. So, no, that is not true. By the way, the FCA has recruited a new head of enforcement, who has experience in many other parts of the world. He originally came from Australia. I am very pleased we have that expertise in the building.

Q70 **Mr Rees-Mogg:** How selective do you have to be in your enforcements? They are very complex actions. How do you decide on them?

**Andrew Bailey:** We have to make choices; that is true. Choices are made, because they have to be things where you can say, "Pursuing that case will help us pursue the objectives of the FCA." Again, this is where I hope the mission will help, because I would like you and the rest of the public to have a better sense of how we do it. I do not think you can



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sustain having a closed book in terms of how you do it. That has probably contributed to some of the things you hear said about the FCA: that they are just trigger-happy on enforcement.

**Q71 Mr Rees-Mogg:** The Treasury was pushing you down an enforcement route of doing lots of early deals, which you have resisted.

**Andrew Bailey:** Yes.

**Mr Rees-Mogg:** Personally, I think that is absolutely right. Plea bargaining is against most forms of justice. You are absolutely right to do this. On the other hand, it means you end up being more selective because the hurdle for enforcement becomes higher.

**Andrew Bailey:** I have to say, from some exposure to this, that one of the things I do not like about the US system is that it is very hard to challenge some of those processes, if not impossible. The odds are so much stacked against them that you do not do it, which, like you, I think is a problem in natural justice.

**Q72 Mr Rees-Mogg:** It is a very important point: you have a duty to natural justice, as much as you do to enforcement. Do you have the resources that you need in terms of people and quality of people?

**Andrew Bailey:** The FCA is quite a large organisation. It has grown quite a bit. It has had to do that because it has taken on some big things. The biggest thing it has taken on is consumer credit. I think I am right in saying the current turnover rate of staff is 11.5%, which is down from where it was; it was around 14% at one point. It needs to come a bit lower. You do not want it too low, because then nothing turns over, but it needs to come down. We have had a heavy turnover of senior staff, so one of my big tasks is to build the executive committee and the people in senior management that we have into an effective senior management team because, like me, a lot of them are new.

**Q73 Mr Rees-Mogg:** Finally, in your questionnaire, you mentioned the importance of establishing public understanding of the FCA and increasing its profile. Millions of people are watching this session and that is, no doubt, helping. People all over the world, probably, are tuning in to see your responses. It is quite difficult to make regulation exciting, unless you do a bit of shooting first and asking questions later.

**Andrew Bailey:** Yes.

**Chair:** Jacob will help you find a way.

**Mr Rees-Mogg:** I can only do that if I start being rude to you, which I do not want to do.

**Andrew Bailey:** I have to confess: I do not know whether, when you get older, you become sadder as a person. I actually do watch Parliament TV sometimes in the evenings. That is a pretty sad comment. It is quite exciting, really. The problem with it becoming so exciting is that it is just headline grabbing, and that is not the thing. Let us be



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serious: public accountability in hearings like this is really very important. It has been a huge benefit to the Bank of England in its various activities over the years, relative to where it used to be. The FCA needs to benefit from the same thing. I hope that one of my objectives would be that we can have a stable accountability regime in which the FCA gets into the same position and you feel that you are holding us to account constructively, which is absolutely to our benefit. There is no doubt about that.

Q74 **Mr Rees-Mogg:** I was just going to say that some stability will help.

**Andrew Bailey:** Absolutely.

**Mr Rees-Mogg:** I have been in the City almost as long as you and therefore have gone through almost as many regulatory regimes. It gets quite hard to remember what all the initials stand for in the end.

**Andrew Bailey:** That is true.

Q75 **Chair:** The turbulence in politics just now provides the clearest possible case for bodies with statutory independence like yours to get on with the job in the meantime.

**Andrew Bailey:** Indeed, I agree. We need stable institutions.

Q76 **Chair:** There is just one other point that Jacob raised there about resources. There is also the question that we were very firm on wanting to see a cap on resources, unless there was a good reason for there not to be, on the existing responsibilities and not for the new responsibilities. Are you going to continue to deliver that?

**Andrew Bailey:** That is my aim. I wanted to spend a bit of time getting into and looking under the bonnet of the budget. It is a sensible aim.

Q77 **Chair:** Perhaps in the autumn you could commit to sending us a letter setting out how you are going to do that.

**Andrew Bailey:** I can do that.

**Chair:** It could include some numbers and the areas that you consider to be new and existing, so that we can track this over time. After all, this is cost to the consumers in the end.

Q78 **Rachel Reeves:** Thank you very much, Mr Bailey, for coming along this afternoon. I want to return to one of the issues that the Chairman raised earlier, and that is overdraft charges. That probably will not surprise you because I have written to you on this subject. You said in your answer to the Chairman that the CMA has a competition aspect to look at, but the FCA's remit is broader and it can look as well at consumer detriment. You will know that the CMA, in its report on unauthorised overdrafts, said, "We have provisionally decided to make an order to require all personal current account providers in the UK to specify the maximum total charge that a consumer could incur in any given month as a result of exceeding or attempting to exceed an arranged borrowing limit." The



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important thing there is that it is the bank or the personal current account provider that will specify the maximum charge, rather than a regulator. Do you think that the CMA has gone far enough, and, if not, do you believe that the FCA, under your leadership, could impose a cap?

**Andrew Bailey:** It is a question that I want to examine when the CMA delivers its final remedies to us. The reason I raised the point about us having more powers was deliberate because it was exactly to this point. The FCA could decide to do more. I want to take that very seriously. You know, obviously, what has happened on payday lending, which I was a strong supporter of, by the way, as a board member because I thought the practices were very poor.

This is early days. There is an interesting balance here, because we are talking about unpredicted overdrafts, not the approved sort. There is a balance, frankly, between getting to a point where there is not gross overcharging of people and having some sensible incentive structure in there, of one sort or another, to say that relying on unpredicted overdrafts is not a particularly good way of going about business. How you do that we need to spend more time on, but I start in the same place. Any form of very high cost credit has to have the question asked of it: "Is this really consistent with the risk of the product?"

Q79 **Rachel Reeves:** Let us unpick a couple of those things: first of all, the difference between arranged and unarranged overdrafts; secondly, the issue that you raised, Mr Bailey, of payday lenders. It is my view that there should not be a distinction between authorised and unauthorised overdrafts. If a bank is aware that accepting a payment request would take a customer over a pre-arranged limit, then the bank is explicitly authorising the customer to extend their overdraft. It could and can disallow a payment, but, if a bank decides to offer additional flexibility, it should be on the same terms as the arranged overdraft. What are your views on that distinction?

**Andrew Bailey:** I would like to examine that quite carefully. Look, you may be right. Do not get me wrong, but I want to be confident that, for all of the circumstances in which a bank could say, "We are only going to provide arranged overdrafts, and therefore we are going to put mechanics in place to do that", it would not leave some parts of the population adrift in terms of their ability to access credit in emergencies. I do not know the answer to that question. I have not spent enough time on it yet; I am sorry. With that caveat, I take the point, but I would like to look at it more thoroughly before we jump one way or the other on that.

Q80 **Rachel Reeves:** There are obviously already fees, charges and interest attached to having overdrafts. It would be interesting to examine whether personal current account providers would continue to offer overdrafts above the level. At the moment, you could be going into an unauthorised overdraft without, perhaps, knowing it, and incurring very high fees and charges for a transaction that would not really matter and



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that you certainly would not do if it was going to cost £35 in fees and charges.

**Andrew Bailey:** My only point there—and it is true in all these areas—is that we have to try to do our best to assess the behavioural consequences of any action we take. I would just caveat it with that.

Q81 **Rachel Reeves:** You mentioned, Mr Bailey, the issue of payday lenders. I, too, welcome the decision that was taken, introducing a price cap in 2014. You will have seen that new research from Which? compared the cost of borrowing £100 for 28 days, and found that charges at some high street banks for unauthorised overdrafts were as much as £90, which is up to four times higher than the maximum charge of £22.40 that would be allowed on a payday loan. It is now the case that the cost of borrowing on an unauthorised overdraft is higher than on a payday loan. Will you at least ensure that there is a consistency in approach towards lending from different types of lenders?

**Andrew Bailey:** I agree with you. We will come to look at this question of overdrafts when the CMA delivers its package to us. I agree with you; I think the Which? thing is pointing to a very powerful point.

Q82 **Rachel Reeves:** What sort of turnaround would you be looking at once you get the full report and recommendations from the CMA? Do you have an expected exact date for that?

**Andrew Bailey:** No, I do not have an exact date, I am afraid. It is going to come in the autumn and I believe that it will not be too late into the autumn. I do not have an exact date for when they will deliver at the moment. I will let you know if I can find one out.

**Rachel Reeves:** Thank you. Then from getting that—

**Andrew Bailey:** We will do it as quickly as we can. One of the questions we probably will face is whether we implement their recommendations or whether we bring some other things into play. If we do bring some other things into play, we will have to go through the consultation process.

Q83 **Rachel Reeves:** Let me finally ask you about that. I am sure that what they recommend will be better, even if marginally, than the current situation that we have. At least there would have to be a maximum monthly charge and text messages, or something, would be sent to people if they were going to go over their overdraft limit, etc. One possibility would perhaps be to introduce what they recommend, but then, if you wanted to go further, Mr Bailey—I do not know, and maybe you do not know at this stage—how lengthy a process of review would you have to go through?

**Andrew Bailey:** I am afraid that, two and a bit weeks in, I do not know the answer to that question. What I would say is that, instinctively, I start in the same place as you do on this. It seems to me that it helps but it still leaves important questions outstanding. You are right to point



to the relative differential in the cost of borrowing, and I do not feel particularly comfortable to leave that thing out there, as it were. It comes back to the point I was making about how we approach consumer detriment for different groups in society. You pose a reasonable question that we will have to address, which is, "Is it better to do it in stages, or is it better to do it all as one? If we do it all as one, how long will it take?" I do not know the answer to that question, but we will tell you the answer to that question when we have a sensible view on it.

**Q84 Mr Baker:** You take up the reins at a time when the FCA has had appalling experiences in the public sphere, which you do not need me to rehearse, but including the extraordinary step of a confidence debate in Parliament. After two and a half weeks or so in post, what is your assessment of morale at the FCA?

**Andrew Bailey:** My focus in my first month has been on meeting as many members of staff as possible, because that is very important. There is a very committed staff who want to do the right thing; they really want to do the right thing. It is incumbent on those of us in leadership to organise a place to do that. Actually, I am very encouraged. I would be telling a different story, frankly, if I was encountering an organisation where there was deep resistance, or where they were so ground down that it was too difficult. I have done quite a bit so far, and I am off to see the Edinburgh office tonight. What I have encountered so far is a staff who really want to do the right thing. Like a lot of people in public policy, they are very enthused by the challenges that come their way, but it is an organisation that has taken a battering. Your description is correct entirely.

I would have to tell you that it was very motivating. I had been appointed for about a week when that debate happened. I watched it on television and my wife said to me, "You want to do this job, do you?" I said, "Absolutely." It was an interesting experience.

**Q85 Mr Baker:** You obviously take up your task with buoyancy and hope, as Churchill might have put it, when facing hideous odds. You have said in your questionnaire that it is imperative that the FCA becomes confident of its capacity and ability to put into effect its mission. It sounds like that confidence in its capacity and ability is very much about how the staff feel about their work. Given the experience you have just described, what is your level of confidence that you can lead the organisation to meet that imperative? Also when do think it can be achieved?

**Andrew Bailey:** I would not have gone there if I did not think I could make a difference. I really want to make a difference. That is why I did it. I could have stayed in the PRA; I would have been happy to stay in the PRA, this was an opportunity to do something that would make a difference. I am very motivated by public policy and trying to improve things. How long it will take I honestly do not know. It would be rash of me to put a time estimate in terms of the things that we need to do. I



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just hope that we will be able to come back and progressively show that we are making a difference. I am optimistic on that front.

**Mr Baker:** But you are not willing to put a figure on it. Are you willing to say that you expect to see morale substantially improved within a year because the organisation knows that it is effective?

**Andrew Bailey:** I hope so. I have had the message that they are looking to have a management that provides leadership. I have come to do that and I will do that. I have experience of doing it. It is a big challenge. We have a lot of complex and quite difficult issues to deal with, which are going to be noisy. We have touched on a number of them this afternoon. There is quite a bit of challenging legacy, whether it is interest rate hedging, GRG or Connaught. These are all difficult issues that we are dealing with and have to deal with in the legacy.

**Mr Baker:** I hope the Chairman will not mind me saying that I am sure we all wish you a great deal of success.

**Andrew Bailey:** Thank you. That is very kind of you.

Q86 **Chair:** The charge sheet of what you are having to deal with is pretty long.

**Andrew Bailey:** Thank you for reminding me.

**Chair:** We may as well get that down at the start. The breach of the listing rules that the FCA was responsible for was extremely concerning. The cancellation of the culture review seemed extraordinary to this Committee. There are the leaks that pour out of the FCA; 15 were identified last year alone. The strategy document, frankly, was an upmarket picture book of eight pages and virtually content-free and could scarcely be dignified with the word "strategy". Then there is the SME Alliance issue about treatment as whistle-blowers. It is difficult to get to the bottom of that one, but it does not look very good on the basis of the information that we have.

**Andrew Bailey:** I know that you and Tracey have exchanged letters on a number of occasions. The moral of the story was that, when that sort of thing happens, you have to be very clear and upfront with people and say "Are we in whistle-blowing or are we not in whistle-blowing?"

**Chair:** That clearly did not happen.

**Andrew Bailey:** No, because unfortunately both sides had a slightly different interpretation ex post.

Q87 **Chair:** I have one last thought for you. You said at one point today that you will only ever be able to investigate a fraction of all of the instances of misconduct, and that you will always be dealing with this huge volume, which you will not be able to cope with. In that case, you are going to have your work cut out managing the expectations of consumers, aren't



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you? The consumer sees the FCA—and indeed some of the language used about the FCA by your predecessor created or furthered this impression—as an all-powerful body that effectively provides an all singing, all dancing consumer protection body, which you are not.

**Andrew Bailey:** It is another reason why we need to have those mission statements, so that we can be very clear what we do. We have to use all of our tools, because they can contribute different things and some tools are more effective in some situations than others to achieve those aims.

**Chair:** We have been going for almost an hour and three quarters, and no doubt we will hear a lot more from you in the future. We are looking forward to receiving several documents, which you have kindly agreed to send us. We will bring the hearing to an end there, colleagues. Thank you very much for coming.