



Financial Services Regulation Committee

Corrected oral evidence: The FCA and PRA's secondary competitiveness and growth objective

Wednesday 16 October 2024

10 am

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Members present: Lord Forsyth of Drumlean (The Chair); Baroness Bowles of Berkhamsted; Baroness Donaghy; Lord Eatwell; Lord Grabiner; Lord Hill of Oareford; Lord Hollick; Lord Lilley; Baroness Noakes; Lord Sharkey; Lord Vaux of Harrowden.

Evidence Session No. 7

Heard in Public

Questions 107 - 121

Witness

[I](#): David Postings, Chief Executive Officer, UK Finance.

USE OF THE TRANSCRIPT

1. This is a corrected transcript of evidence taken in public and webcast on www.parliamentlive.tv.

Examination of witness

David Postings.

Q107 **The Chair:** Welcome to this session of the committee. It is the seventh oral evidence session in the committee's inquiry into the FCA's and PRA's secondary competitiveness and growth objective. Thank you, David Postings, for attending. A list of Members' interests relevant to the inquiry is available online. The session is open to the public, it is broadcast live and is subsequently accessible via the Parliament website. A transcript will be taken of the evidence and put on the Parliament website. A few days after the session, you will be sent a copy of a transcript to check it for accuracy. It would be helpful if you could advise us of any corrections as quickly as possible. If after the evidence session you wish to clarify or amplify any points made during your evidence or have additional points to make, you are welcome to submit supplementary written evidence to us. Would you like to make a short opening statement?

David Postings: I can do, yes. Financial services is a high-productivity industry—banking and finance particularly—and offers high-quality jobs, well spread around the country, the majority outside London. It delivers £41 billion in tax revenues to the Government. Risk management is at the heart of what banking and finance do. To remain competitive, lending and investment need to be maintained and developed. The system-wide response to the global financial crisis was understandable, but I think we have reached a point where the pendulum of risk versus safety has probably moved a little too far and we need to rebalance that. That adjustment will allow us to grow and improve financial inclusion. In trying to avoid certain risks, there is a danger that we create other risks. We might want to expand on that as we go through the evidence later.

The Chair: I wonder if you could help me with a problem that I and the committee have. Many of your members want to have lunch with me, talk to me privately and tell me all the things that are wrong with the regulatory regime. When I say, "Would you like to come and give evidence to the committee?", they say, "Oh no, we don't want to do that because we don't want to upset our relationship with the regulators". Given that the Prime Minister has made it clear that he wishes our country to grow and that he sees good regulation as important but unnecessary and inhibiting regulation as a problem, what is your advice as to how we can move forward on this?

David Postings: We have good relationships with the regulators. It is tempting to think that we have only two, but we actually have lots. As well as the FCA and the PRA, there is the PSR and there are plenty of other bodies that have a big impact in terms of quasi or actual regulation, such as the CMA, the Lending Standards Board, the regulator for accounting, et cetera. So the landscape is quite diverse. The issue really arises from the fact that all those various bodies have tried to eradicate or reduce risk in the system over time. That is often driven by bodies such as this and the Treasury Select Committee, or a government crisis,

or the press. So there is not much in it for the regulators to take significant risk themselves because of reputational issues.

The Chair: Forgive me, Mr Postings, but you are not really answering my question.

David Postings: I am trying to. You get a system change that pushes everyone towards taking fewer and fewer risks. We need to rebalance the whole thing. I would not want to particularly criticise the regulators—the PRA and the FCA.

Q108 **The Chair:** What are the three top things the regulators could do to help us to get more growth and be more competitive in financial services?

David Postings: The secondary competitiveness and growth objective is really helpful. It is still early days for its implementation but I feel that that has the opportunity to help. I know that the PRA, for example, is really focused on that. That area is really important. If the regulators take that into account when they are considering new or existing regulation, that will really help.

The Chair: But what are the specific things you think could be changed? Is it about capital requirements? What are the specifics?

David Postings: The examples I would give of areas where we have problems are authorised push payment fraud and the consumer duty. They are two really significant ones which cause us to have a very risk-averse approach, with a lot of protection for consumers, which can actually end up with consumer detriment. I would focus on things such as that.

The Chair: What changes to the consumer duty would you like to see?

David Postings: I think it is in its interpretation. Nobody would argue that a good outcome for consumers is a bad thing; it is what everybody would seek to do. The problem is that good is something that is in the eye of the beholder and at a point in time. With a mortgage, for example, if you fixed a rate today, you might decide in a few years' time that a floating rate would have been a better outcome. So the concern is that that will produce the perversity of somebody potentially claiming in the future that they were mis-sold, and the ombudsman service would get involved at that stage. So financial institutions become risk-averse and try to mitigate that risk before it arises.

The Chair: You mentioned the ombudsman. Do you think there is a problem with the ombudsman operating almost as a quasi-regulator?

David Postings: In part, yes. It can operate above the regulation and even potentially with an eye to the law but not necessarily following it. I have talked to the ombudsman service and the FCA about the fact that they set precedents that are sometimes quite significant and can make firms unclear about where the boundaries lie.

Q109 Baroness Bowles of Berkhamsted: You say that everybody is too focused on eliminating risk, not just the regulator but businesses, and we have become overbound by that. Nikhil Rathi of the FCA has said that we need to have a more mature debate on risk. At the FCA's conference last week, he gave a long speech on that. What input would you give from your side on how to address allowing for more risk? How will firms take that to heart?

David Postings: Typically, when a regulation is put in place, most firms have some kind of buffer beyond the regulation to make sure that they do not breach it, whether that is capital or any other form of regulation.

Baroness Bowles of Berkhamsted: How do you have a behaviour buffer?

David Postings: They would try to anticipate the potential outcome down the line, either from the regulator or the ombudsman service, and attempt to make sure that their teams are fully briefed and, therefore, cautious.

Baroness Bowles of Berkhamsted: So how do they become less cautious? I am thinking about sitting in a risk committee. I am sure that, being in financial services, you would say that your tolerance for these kinds of things is zero, or next to zero. Would it change that?

David Postings: It is difficult. For example, some groups find it difficult to open accounts. Technically, they are allowed and the regulator does not say that they cannot open them, but the industry would view them as higher risk and they might find it more difficult to open them.

Baroness Bowles of Berkhamsted: So it might affect things like that?

David Postings: It can do. If the regulatory approach is for more risk tolerance and an understanding that perfection is not always possible and some outcomes may not be exactly as expected, there could be a loosening.

Baroness Bowles of Berkhamsted: Do you not think there are arguments already available to do that kind of thing, such as public interest and so forth, that the banks could make to the regulator to say that they will take these riskier options?

David Postings: They may be able to, but the reality is that, on occasion, that does not happen.

Q110 Lord Sharkey: I would like to ask about metrics. We have been told in this committee that there are no examples anywhere of meaningful assessments of performance on secondary objectives in financial services. Obviously, it is very important that we get the metrics right so that we can make a meaningful judgment about progress against the secondary objectives. In that context, what do you think about the proposed FCA and PRA metrics? What do they miss and how could they be improved?

David Postings: The Government issued some potential metrics that were focused on administrative speed and accuracy. My view is that we need more output measures, such as net lending, flow and stock, investment and things like that. It is difficult to link those back directly to the regulators, but I feel they must have metrics that align with that. Otherwise, we will just get a very efficient authorisation process, for example, that does not affect competition. There should be output metrics.

Lord Sharkey: Have you made suggestions of what these should be to the FCA and the PRA?

David Postings: Not so far.

Lord Sharkey: Do you intend to do so?

David Postings: We will attempt to do something like that, yes.

Lord Sharkey: When you do, we would be grateful if you could let us have a copy of the proposed changes or additions.

David Postings: Yes.

Q111 **Lord Hollick:** In your career, you have had experience of large banks and some very small banks. We have heard from quite a lot of small and medium-sized banks, as the Chair referred to, which are furious about the way they are treated and the poor service they get from the regulators. In particular, they take exception to the very heavy capital burden put on them and the cost of capital for SME lending in particular. As a representative of that group, what proposals have you put forward to move to a more mature risk regime so that those small and medium-sized banks, many of which you have personal experience of, could offer affordable lending to SMEs, which would meet the growth objectives pronounced by the Government only this week? What is your assessment of the impact that would have on the supply of credit to SMEs?

David Postings: We have proposed that the MREL limit be raised so that banks that do not have to raise MREL can have a bigger balance sheet. That is the main proposal.

Lord Hollick: What impact would that have on the supply of credit? Could you quantify the amount of credit that could be offered?

David Postings: I cannot quantify the amount of credit it would create.

Lord Hollick: Have you done any work on that?

David Postings: I would have to check whether we have accurate data on that. I do not believe that we do.

Lord Hollick: In response to the FCA's call for more mature risk, surely it is an open door for an organisation such as yours, representing 300 banks, to come forward with clear proposals on how risk weighting should be done for different types of lending so that growth can take place

without calling a systemic risk in the event of some disaster. Is that not a central role that you can play?

David Postings: We can influence, and I think we have. That is why you saw the MREL changes announced yesterday. There has been some influence. However, just because a small bank lends to an SME does not mean it is any less risky than anybody else doing so.

Lord Hollick: Is it difficult to balance in your organisation the very large banks and the 280 or 290 smaller banks?

David Postings: No. Quite often there is a strong degree of alignment and consensus. Where there is not, we would often put forward more than one response to a consultation paper to evidence that. We have done that, and the Treasury and other bodies have said they value it, so we often put forward more than one view. But we do not have that much tension in the membership between those types of banks. Everybody is exercised about capital and everybody was exercised about Basel 3.1, but the advocacy we put forward was based on facts and we ended up with nine of the 10 things we asked for being acknowledged by the PRA and they will be implemented. We have been very successful there.

As I mentioned, the raising of MREL is another positive sign. It is not by as much as we would like, but it is a step in the right direction. We think it should be indexed at least to either GDP or inflation so that we do not end up with a smaller number over time. The cost of MREL varies between our smaller members, depending on their business model and the perceived risk the market gives to that debt. That has always been an issue. Some members find it very expensive and difficult to raise, and others find it much easier and cheaper. So there is no unanimity even among the smaller players. We work very hard to do that; the influence we have had with the PRA has been proportionate and sensible, and we have ended up in a good place.

Q112 **Baroness Noakes:** I would like to follow up on MREL. As I understand it, the proposals that came out this week merely keep the indicative MREL ranges in line with GDP growth from when they were originally set, so nothing has been achieved in the proposals other than to move off a historically set number. How can that be counted as some form of success?

David Postings: They were not moving before, with respect.

Baroness Noakes: Yes, but it is not changing the game in terms of allowing more banks to escape the cost of having to raise MREL.

David Postings: It does. I take your point about indexation; we have been talking to the PRA about it for two or three years. It is an improvement. Otherwise, as with some of the taxation burden we see, more and more businesses would have to raise it.

The Chair: Should you not be more ambitious?

David Postings: There comes a point where the public purse is at risk. That is why capital stacks are where they are. We would like to see a higher MREL ceiling for smaller banks. We have made that clear. We have been more ambitious than the outcome, but it is still a positive outcome that there has been some movement.

The Chair: Perhaps I should declare an interest as having previously chaired a small bank. On Lord Hollick's point, the larger banks among your membership basically set their own risk weightings because of their size and past performance, whereas the smaller banks are subject to risk weightings which, especially for housing developments, are quite penal. So the risk ratings on capital requirements to lend money for someone to buy a house for a mortgage are considerably lower than for someone to build a house. Are we therefore surprised that the effect is that house prices are pushed up because supply is limited and it is more profitable to lend money to people to buy a house than to build a house? Is it not central to the whole government growth objectives that we address these issues?

David Postings: It is important. It is the risk concentration that drives that view. I am not trying to defend the PRA here, because we disagree with it on some things, but the view that has been taken is that the concentration of risk in a particular portfolio and the capital stack that sits behind it needs to be stronger, and without the data to support an internal rating-based approach, a standard approach is the only way that can be implemented.

Q113 **Baroness Bowles of Berkhamsted:** There has been criticism of regulators that there is too much regulation. Does that fall mainly on the regulation side or the supervision side? What is the base of the problem? Is it the regulations, or is it the way they are applied, the frequency of the communications and all that kind of thing? If we are being told that we have to target the regulation, and that is not the fault, how do we target those other things?

Related to that, have you done any kind of survey of compliance cost per £1 million of turnover to see how it varies between larger organisations and smaller ones?

David Postings: I think it is a whole-system issue. I do not want to just blame the regulators for the fact that regulation is where it is, because that is driven by government policy as much as anything else and by public pressure. My point right at the start, which I tried to make, was that the whole system is looking to reduce risk. The whole system does not accept any outcomes that are deleterious.

As a consequence, the regulation ends up becoming tighter and more keenly supervised. So I could not really differentiate between whether it is through the supervision or through the regulation. My sense is that it is the regulation itself. But then you have the interpretation of it subsequently by the ombudsman service, for example, which often goes above and creates a different bar. So the water is very muddled.

As a consequence of that, what happens in all firms of all sizes is that they put a buffer in place. They have a contingency, and you see products withdrawn. We have seen that the sub-prime lending market has virtually been exited, and, as a consequence, there is greater financial exclusion. It is a whole-system problem. I do not want to sit here and just blame the regulators.

Q114 Lord Vaux of Harrowden: How do we change that? If it is a whole-system issue, what can we do? The committee is frustrated as we hear these fairly high-level comments, but what can we do about it?

David Postings: The secondary competitiveness objective is a good start. It is secondary, obviously. If that is taken into account every time regulation is considered and every time the regulator is pushed, that will help, especially if we have output metrics.

We have asked the Government to consider a competition and growth champion—somebody who can look at this in the round and try to help steady the ship and push the pendulum back a little. It will take political heft as well, because over the last couple of years there have been many incidences where a headline in the press has caused the Government to put pressure on the industry and regulators to do things. You will know that; you do not need me to tell you that. So it will need government to hold its nerve too in times of difficulty.

Q115 Lord Grabiner: Mr Postings, at the outset of the hearing this morning you will remember that the Chair said that there were regulated parties that were willing to talk to us privately and to make quite strong criticisms both of the rules and, indeed, of the way in which the rules are being applied by regulators. Does it come as a surprise to you that, although they are prepared to do these things in private, they are not prepared to tell us that publicly?

David Postings: We have to work as a system. We have to work with the regulators and they with us. Being publicly critical has its place, but it is challenging if you want to build relationships and get things changed. The way we approach it in UK Finance is to work closely, use data, use strong arguments and get things changed. I can point to a number of examples—I mentioned Basel 3.1—where we were listened to by the regulator. I think that is more effective than shouting at them through the press or through a public forum.

Lord Grabiner: So you are not surprised at all that, although people have criticisms of the system or the way in which it is being applied, they are not prepared to talk to us publicly about it. Is that your point?

David Postings: I cannot speak for them. I do not know.

Lord Grabiner: But you must know. They are your organisation, your members.

David Postings: Each member is different, so—

Lord Grabiner: But you must have a sense of how those members feel about those issues and why they are not prepared to talk to us publicly.

David Postings: I mentioned the fact that we have to have working relationships with the regulators, as we do with the Treasury and with other government departments. It is counterproductive to conduct a debate with them through the medium of something that is really public.

Lord Grabiner: Is that because of a fear of possible consequences of being critical of the regulator?

David Postings: UK Finance is not regulated, so I have no fear of that. The businesses would have to speak for themselves on that.

Q116 **Lord Lilley:** We are looking at the secondary growth and competitiveness objective. As far as growth is concerned—that is, the growth of the whole economy, not just the growth of the financial sector—does the degree of regulation that we now experience inhibit growth, for example through restricting investment? We have heard that the bulk of bank lending is now on mortgages. When I was a boy, which was centuries ago, most lending for mortgages came from building societies, and banks did not do much of it. What happens now? Most bank lending is now for mortgages. Who is lending the stuff that they used to? Or is that just not happening and people are having to finance it out of their own internal cash flow?

David Postings: Are you talking about lending to businesses?

Lord Lilley: Yes.

David Postings: I agree; when I started work, it was exactly as you described. Bank lending to SMEs is roughly 41% at the moment, with 59% of the total stock.

Lord Lilley: Forty-one per cent of bank lending is to SMEs?

David Postings: No. Of total lending to SMEs, 41% is provided by banks and 59% by non-banks. Arrears are at pre-low levels. That concerns me, and it is a combination of regulation and internal risk appetite that has brought it about.

Lord Lilley: It is a combination of regulation and internal risk appetite? So if regulation were different and you had the same risk appetite, you would get more lending by banks to SMEs?

David Postings: Potentially, yes. Some of it is to do with the cost of capital and some of it is to do with risk systems and a desire post 2008 to tighten up and avoid the problems that were encountered then.

Lord Lilley: They were very specific. They were not about SMEs much, were they?

David Postings: The interesting thing for me is that SME failures and insolvencies are at the highest level since 1993—not as a proportion of

the stock, because the stock is so much bigger, but in absolute numbers they are the same as 1993.

Lord Lilley: Is that a good or bad thing?

David Postings: It is an interesting thing, if you have got low impairment on the one hand and high failure on the other. It strikes me that there should probably be, as I said at the outset, some kind of rebalancing so that a bit more risk is taken. I would not advocate some massive swing, just a bit more risk to allow more growth.

Baroness Bowles of Berkhamsted: But surely it is not a higher failure rate. You said it was higher in absolute numbers but not proportionally to what it was. We have more businesses because we have more people. If it has just grown proportionately then that is not a deterioration.

David Postings: It is not at record levels as a proportion, but it is much higher.

The Chair: Could I pick up on the last thing you said to Lord Grabiner, who asked you about your members not being willing to engage about how we could improve the performance of the regulatory regime? You said they would not want to conduct a debate through the press and so on. This is not the press; it is a parliamentary committee, and the regulators are accountable to Parliament. Is that not quite different from asking your members to be open and honest about the constraints on their businesses?

David Postings: They have their own positions. I was postulating a potential reason, but I do not know. No one has said to me that they are not prepared to talk to you.

The Chair: Oh no, they are prepared to talk to us. It is about what they are prepared to say to us.

Q117 **Lord Eatwell:** The committee has had evidence that there are many countries and jurisdictions that have the secondary growth and competitiveness objective within their regulatory structures, and the academic evidence is that it makes not a jot of difference. Facing that evidence, the committee is very much attempting to identify practical measures that would make a difference—in other words, not simply relying on the secondary objective being there and just saying, “Okay, now we can sit back and the regulators will take it into account every time they think of doing something”, because the evidence is that nothing happens to the overall performance of the economy or indeed of the financial services industry. The committee is keen to have actual propositions that we could investigate regarding a different approach in respect of capital, customer duty, as you mentioned, or fraud, whatever it might be. We want practical examples that would make a difference to the growth and competitiveness both of financial services and of the economy as a whole. So what we would really like from your organisation—not necessarily right now; I appreciate that you would have

to have them in your back pocket, but perhaps you could write to us later—is specific things that could be done within the corpus of the whole regulatory system, which you have identified as the overall system, to change things and improve performance.

David Postings: I will try. It is a difficult subject, which is why some of my answers are frustrating you. If there were a silver bullet, I would have tried to lay it on the table already. As I have said, it is a whole-system problem; it is not just about regulation. I have seen government pressure on regulators that has caused a reaction that has then caused more risk aversion. So it is not just the regulators.

I wrote to the Chancellor of the Exchequer last week on this subject. I will be honest: the recommendations that we have put in place do not go as far as you have just asked—we do not postulate a series of detailed things that would have an impact—but we give some ideas. An example is the competitiveness and growth champion, someone to champion that. I mentioned earlier that the metrics for measuring it should be based on outputs rather than the efficiency of the process, which would help. Culturally, large regulators, plus others that are not subject to this and need to be, should have a good look at their culture internally, because you can get leadership at the top that wants to do something but that does not always permeate the whole organisation. It is a complex question, but I will do my best.

Lord Eatwell: We do not need a silver bullet but lots of little bronze ones. An issue that the Chairman referred to would be at least a starting point, as well as a warning signal for both government and regulators, is the comparative cost of compliance in the UK compared to the cost of compliance in our competitor jurisdictions. That would be very helpful.

David Postings: We have done that work, and the report is almost finalised. We have been working with Oliver Wyman on it for the last three months to try and come up with that comparison. We used bank data to do that. I will share that with the committee.

The Chair: Would you also share the letter you sent to the Chancellor?

David Postings: Yes.

The Chair: We had evidence from one person from an international organisation, who spoke openly, who pointed out that there were multiple additional costs in the UK compared to the next country in which they were dealing with.

Q118 **Baroness Noakes:** I want to explore the differences between the regulators. You said earlier that the PRA was taking the new objective fairly seriously in what it was doing. Could you comment on how you think the FCA is doing? A moment ago you mentioned other regulators that do not necessarily have the objective—for example, the Payment Systems Regulator. Could you expand a bit more on that?

David Postings: My view is that the PRA's independent review report was a good one. The FCA has a much broader remit, and it is possibly more difficult. There is definitely a focus now from it, but it could be more aligned with the PRA. The FCA could do more work, but I know definitely that it is trying. On the point about risk and consumer protection, the listing rule changes it made a few weeks ago are an example of where it has tried and succeeded, and of getting the balance right between risk and consumer protection.

I think the PSR should absolutely be subject to the secondary competitiveness objective. I was pleased to see that there is talk that the CMA might have some competitiveness objectives in its remit, too. I personally think there should be some scrutiny of how the FCA and the ombudsman service work together and how precedent is set. My view is that it was initially set up as a dispute resolution service but has morphed into something very different. Essentially, in some cases, it is the actual regulator because it is the body that sets the bar for firms to operate against.

Baroness Noakes: That is because the FCA has willed it to be so.

David Postings: I do not think that is the case. The constitution of the ombudsman service has caused it—the way that it is formed. It has that independence, so the FCA does not have control over it in that way.

Baroness Noakes: So what should be done about that, in practical terms?

David Postings: It needs to be looked at. I know that is not easy, because it would need primary legislation to change it, but it is very important.

Baroness Noakes: You mentioned the listing rules, which in some ways were low-hanging fruit, but in other areas, such as the consumer duty, what, in practical terms, would you want to see from a change in approach from the FCA that might have an impact on firms and affect their competitiveness?

David Postings: We could work with them on clarification of what a good outcome looks like. Obviously, it is supposed to be outcomes-based regulation. The problem with that is that the outcome is in the eye of the beholder, and it is at a point in time—if a product is a 30-year product, it is difficult. It would be really helpful to work with them through some examples of what a good outcome looks like.

Baroness Noakes: Was that not done extensively through the consultation period?

David Postings: Not in sufficient detail, no.

Baroness Noakes: Whose fault was that?

David Postings: I would not want to apportion fault.

Baroness Noakes: Why were those things not bottomed out during the consultation process?

David Postings: I personally, and we as an organisation, raised these issues throughout that process.

The Chair: The subject of listings takes us on to Lord Hill's question.

Q119 **Lord Hill of Oareford:** It was not quite such low-hanging fruit. You said at the beginning, or you gave the impression, that you think that perhaps there are too many regulators and there is overlap. Do you want to say anything about that? If one looked at that area and tried to clarify rules and reduce overlap, could there be benefits?

David Postings: There definitely could be, because there is overlap and inconsistency. I listed the majority of examples. The document that I will circulate contains what we think is close to the full list, with different remits. Some regulatory simplification would indeed be helpful.

Lord Hill of Oareford: Do you know how one should think about approaching that? Do you have thoughts on that?

David Postings: We are seeing the Competition and Markets Authority stray into areas which the FCA thinks it is in, so we could look at that. The PSR is supposed to be an economic regulator, yet it has moved into real detail on payments and price setting, in part. The new payment architecture, a piece of work that has been stopped, is an example of a project or system development that was constructed incorrectly from the outset. It was a big, centrally driven project with a taxation-based model, with limited involvement from the people who pay the bill.

The same is true in open banking, frankly. I do not think either of those are going to work as currently constructed. They need to be on a much more commercial basis, with the people paying the bill taking more of the lead and more of the risk. Those firms need to be able to make mistakes as well as succeed and have risk capital in it. As I said, some sort of centralist taxation-based model just does not work. Those are examples of where we could make some changes, and most of that leads back to regulation.

Lord Hill of Oareford: On a linked point, which also links to one you made earlier, the phrase you used was that it is a whole-system problem, which I agree with. You said that some of the incentives that politicians provide to regulators lead to risk-averse behaviour, and that needs to be addressed. That takes one to areas such as mission creep and to mandate letters that Ministers might provide to regulators to give greater clarity. Do you want to say anything about that?

David Postings: Emphasising the need for competitiveness and, in particular, growth, in those mandate letters is vital. It is a secondary objective, but it ought to be taken into account at every point in every decision, otherwise we will not see any changes, as you said. That is where I would focus. Clarification about the remit for each regulator

would be really helpful, so that they have boundaries that they are all aware of.

Lord Hill of Oareford: Do you think we should blow the pipes out on remit and boundary?

David Postings: Blow the pipes out?

Lord Hill of Oareford: You know what I mean. It has all been operating for quite a long time—

David Postings: I would just look to avoid overlap, because there is overlap. The FRC is another example of where the governance code impinges on the senior management regime. I do not want to be critical of either body, but there could be better dialogue to make it easier for firms to understand what they are supposed to comply with, and how. I do not want to use the phrase “blow the pipes out” but a review would be helpful.

Lord Hill of Oareford: It is the same thing. Is it helpful for the Government to keep adding new responsibilities to regulators, or is it unhelpful?

David Postings: It becomes a very long list and eventually, I guess, it becomes white noise.

Lord Hill of Oareford: So we should try to narrow that focus.

David Postings: Yes.

Q120 **Lord Vaux of Harrowden:** My question touches on what you said about open banking and the payment system. One driver of growth and competitiveness is innovation. When you talk about innovation with the regulators, the only thing they ever talk about is the sandboxes, which have been around for 10 years or so. Do you think the new objectives will help push the regulators to be more open to, and supportive of, innovation? What else could they do to support and allow innovation in financial services?

David Postings: Hopefully, yes. I have talked about the Payment Systems Regulator in particular. Most of our members would say that the mandatory change that is going through payments is roughly 100% of their total investment budget, so the appetite and ability to innovate is extremely limited.

There is a piece of work ongoing at the moment called the Regulated Liability Network, which a number of organisations, banks and technology companies are leading on. They are working with the Bank of England on an approach to a digital tokenised commercial money and, potentially, a CBDC hanging off the back of that, or being linked to it. That is an example of great innovation that is currently outside the regulatory purview.

As I mentioned before, though, things like open banking are sclerotic, because the commercial model is not there and because the system is based on billing people to develop something in the future, and that just does not work.

Lord Vaux of Harrowden: What has driven that?

David Postings: It was a Competition and Markets Authority remedy, which had a life of its own and which, to begin with and for a long period of time, was fairly unaccountable. It did not really report to anybody in particular, so its remit grew and grew, and the costs grew and grew, but the benefits were questionable. There is some benefit, and it could be exploited even more, but the desire of people to continue to invest in the system is very limited because they have little or no control over what actually happens with the money. That is at the heart of it. If that had a more commercial construct, where there was risk capital involved and people could make a return, the chances are that we would have a better outcome.

Lord Vaux of Harrowden: You have alluded to the fact that the industry itself is gold-plating the regulations and applying a risk buffer to what it does—I know I am not alone in this room in having experienced that as a PEP—and therefore the industry takes less risk than the regulators require. Why are they behaving like that? The FOS may be part of it, but what is driving that behaviour?

David Postings: With respect, they will have a board of non-execs, perhaps like the noble Lords around this table, who scrutinise them and do not want to fall foul of the regulators so they insist on a buffer. It is completely understandable. You see it on capital in every organisation all the time, and capital is not the only thing that people put a buffer on—it would be on the risk appetite for consumer duty, for example, if you take mortgages into retirement. Is that a good outcome for somebody over the age of 70 to have a mortgage in retirement? Some people would think it is and some would not, but the easy option is not to do it.

Lord Vaux of Harrowden: In the system you have talked about, how much of the problem is that behaviour, versus the regulators driving that behaviour?

David Postings: It is difficult to quantify that. It is part of the issue, but that is human nature. You see that cascade down through an organisation. It does not stop at the board; it carries on throughout the organisation. All organisations operate like that, and you end up with compound safety. The regulator sets the bar and it sets the environment in which you operate. Regarding the de-banking issue that came up a year or so ago, an initial review said there was not that much to see, so we moved on, and then the regulator decided to ask individuals to personally attest to the detail behind that. Can you imagine what that would do inside an organisation in terms of the manpower needed, the double-checking and so on? It is that kind of thing. We have got them to

soften their approach, so it is less draconian, but it is things like that that drive the idea of a bit of a buffer—a bit of extra caution.

Lord Hill of Oareford: On that point, do you think the regulators care about the knock-on consequence of human behaviour on the framework? You have just explained eloquently that what they do gets you so far and then what humans do takes you further. Do you think the regulators are cognisant of that and care about it as a factor?

David Postings: I sense that at the senior level they really do care, but they do not necessarily always understand that, if you pull a lever, it might be connected to the thing you see but it is also connected to 10 or 15 other things that you do not see. I have talked to both regulators about that, and, for example, the PRA always expresses surprise that people do not use their buffers in times of crisis. They just do not, and never will—or very rarely. I think they appreciate it, but how they resolve that is difficult.

Lord Vaux of Harrowden: Can they change their behaviour to encourage people to behave differently? Is there something to encourage people? The PEP issue is a really good example where they could be saying, “Don’t do that”.

The Chair: On the PEP issue, they have just completed their consultation, which took more than a year. The main recommendation for change is that non-executive directors of government departments should no longer be classed as PEPs, which is straight out of “Yes Minister”. I apologise for interrupting.

Lord Vaux of Harrowden: That was just an example. Can and should the regulators behave slightly differently to try to prevent the gold-plating of regulations they put in place, and encourage people to behave?

David Postings: I was asked earlier whether it was supervision or regulation, and I think you can see that it is both. It is about how people are supervised and the threat of enforcement—what would happen if X happened? That is quite significant, too.

Q121 **Baroness Donaghy:** Compliance departments have been a growth industry for the past 15 years. I remember asking somebody 10 years ago what they would recommend if there were openings in the finance industry, and the unanimous view was to get a job in a compliance department. Yet the ordinary consumer has little or no trust in banking, so it has not led to any increase in trust, particularly among female potential investors and savers.

To come back to Lord Sharkey’s metrics, you said it was important that they were based on output. Do you think it might help to have a few more facts and figures about how far we can trust the industry? Do you think the FCA in particular has been used as a political dustbin over the years so that it has way too much to do on the macro and the micro, and that perhaps a bit of streamlining might help to promote its culture of being flexible at the top level and bring it down to the rest of the

organisation?

David Postings: On the trust issue, I do not have the stats to hand, but my belief is that trust in banking has been rising. It might not be where we want it to be, but it has certainly risen and stands up well against a number of other industries. I promise to share the latest data with you so that you can see that.

I think banking is trusted, but the regulatory burden on the FCA in particular—or the burden from the Government on the regulator, the FCA—is very significant. It must be very difficult to manage such a diverse group of regulated firms and with such a broad remit.

Baroness Donaghy: The facts and figures would be most interesting; I am sure the committee will want to see them. People are more likely to put their money into a cash ISA than a stocks and shares ISA, although the potential for getting more income over a longer period is greater with the latter. Do you not think that is something to do with the amount of trust there is?

David Postings: No, I do not. I think the fact that they are leaving it in cash tells you they trust the banks. What I think you are seeing there is an example of regulation some years ago that saw the end of advice being offered because of the impact it had. As a consequence, not enough people have had advice about where to invest their money, which is at the heart of the work that Lord Hill did.

We reap what we sow. That is a cast-iron example of cause and effect, as I tried to describe earlier. The same will be true of our pension schemes, where they are heavily invested in fixed income rather than equity. That is a product of the same kind of thing—where regulatory push, because of a crisis or an incident, results in overreaction, less risk-taking and a worse outcome. All it does is crystallise a different risk somewhere else, and that different risk is that people are not getting the return they should get. But they are safe, and I think they trust.

The Chair: On which note, we have run out of time. Thank you for answering the questions.