



## **SECURITIES & INVESTMENT INSTITUTE DIPLOMA**

**SUMMER 2008**

### **CHIEF EXAMINER'S REPORT - REGULATION AND COMPLIANCE**

The standard of the summer 2008 examination paper was strong. Candidates demonstrated a good command of many of the new changes that have come into effect recently and, in particular, under the MIFID. Trainers are to be commended for this.

Section A was answered well although candidates should answer the specific questions set. Section B was also dealt with well with the most commonly answered questions being 7 (financial promotion and ethics) and 13 (dispute resolution). A number of candidates also answered question 12 (sovereign wealth funds) with a smaller number attempting question 14 (short selling and market abuse). As in previous years, candidates must read the questions fully first and answer the various sub-parts in order to avoid wasting time or avoid losing unnecessary marks. Candidates should also attempt to complete all parts even if they are unsure of the answer. Some of the strongest sub-part answers were provided in papers that were not fully completed. Candidates should also look for ethical issues, in particular, in question 11 as ethics has become a core part of the Securities and Investment Institute syllabus.

The most commonly answered questions in Section C were 15 (accountability) and 18 (financial crisis) and then with question 17 (sovereign wealth funds) and 16 (financial capability). As always, the highest marks in Sections B and C were awarded on the basis of the most substantial amount of relevant detail provided.

#### **SECTION A**

**(1)** The threshold conditions set out in Schedule 6 consist of:

- (a)** legal status (body corporate or partnership);
- (b)** location (head and registered office must be in the UK);
- (c)** no close links that prevent effective supervision;
- (d)** maintenance of adequate resources;
- (e)** fit and proper (suitability).

EEA and Treaty firms must also comply with (a), (c), (d) and (e) in connection with an application for Part IV permission or additional permission. A non-EEA firm must also comply with any other additional conditions specified.

One mark for each correct response up to **three marks**.

(2) The main exceptions contained in the FPO include:

- (a) Generic promotions;
- (b) Investment professionals;
- (c) Overseas recipients;
- (d) Deposits and insurance;
- (e) One-off communications;
- (f) Certified high net worth individuals (net income of over £100,000 or net assets of over £250,000);
- (g) Certified sophisticated investors;
- (h) High net worth companies.

Half a mark for each correct response up to **three marks**.

(3) The following persons are authorised for the purposes of the FSMA:

- (a) a person who has a Part IV permission to carry on one or more regulated activities;
- (b) an EEA passport firm under Schedule 3;
- (c) a Treaty firm under Schedule 4;
- (d) a person otherwise authorised under the FSMA (s 31(1)).

One mark for each correct response up to **three marks**.

(4) The regulated activities listed in Schedule 2 FSMA include:

- (a) Dealing in investments;
- (b) Arranging deals in investments;
- (c) Deposit-taking;
- (d) Safe-keeping and administration of assets;
- (e) Managing investments;
- (f) Investment advice;
- (g) Establishing collective investment schemes;
- (h) Using computer-based systems for providing investment instructions.

Half a mark for each correct reference up to **three marks**.

(5) The Six General principles produced by the Takeover Panel were as follows although these subsequently cut to six:

- (a) all holders of the securities of an offeree company of the same class must be afforded equivalent treatment; moreover, if a person acquires control of a company, the other holders of securities must be protected;
- (b) the holders of the securities of an offeree company must have sufficient time and information to enable them to reach a properly informed decision on the bid; where it advises the holders of securities, the board of the offeree company must give its views on the effects of implementation of the bid on employment, conditions of employment and the locations of the company's places of business;

- (c) the board of offeree company must act in the interests of the company as a whole and must not deny the holders of securities the opportunity to decide on the merits of the bid;
- (d) false markets must not be created in the securities of the offeree company, of the offeror company or any other company concerned by the bid in such a way that the rise or fall of the prices of the securities becomes artificial and the normal functioning of the markets is distorted;
- (e) an offeror must announce a bid only after ensuring that he/she can fulfil in full any cash consideration, if such is offered, and after taking all reasonable measures to secure the implementation of any other type of consideration; and
- (f) an offeree company must not be hindered in the conduct of its affairs for longer than is reasonable by a bid for its securities

Half mark for each correct statement up to **three marks** although a full and exact reproduction of each principle was not required.

- (6) The general functions of the FSA with regard to listing are set out in s 73(2):
  - (a) issue rules with regard to listing under Part VI;
  - (b) issue general guidance with regard to listing;
  - (c) determine the general policy and principles governing the listing regime.

One mark for each correct reference up to **three marks**

The FSA is separately required to maintain the official list (s 70(1)) with applications for listing only being accepted where they satisfy the listing rules or any other requirements imposed (s 75(4)). Possibly one additional mark if necessary.

Reference may also be made to any of the other specific requirements imposed with regard to listing or prospectuses under the FSMA. Up to one mark if necessary.

- (7) In the event of breach of s 118, the FSA may either:
  - (a) impose an unlimited fine or financial penalty (s 123(1));
  - (b) publish a public censure (s 123(3));
  - (c) apply for an injunction (s 381); or
  - (d) apply for a restitution order (s 383).
  - (e) the FSA can also commence other disciplinary proceedings for breach of the High Level Principles or other provisions in the Handbook.

One mark for each correct response up to **three marks**.

- (8) The main supervisory tools set out in SUP include:
  - (a) desk based reviews;
  - (b) liaison with other agencies or regulators;
  - (c) management meetings or representative meetings;
  - (d) on-site inspections;
  - (e) reviews and analysis of periodic returns and notifications;

- (f) past business reviews;
- (g) transaction monitoring and
- (h) use of auditors and skilled persons (SUP 1.4.5 G).

Half mark for each correct reference up to **three marks**.

Specific risks may also be dealt with through a number of additional tools including@

- (a) making recommendations for preventative or remedial action;
- (b) providing individual guidance;
- (c) imposing requirements; or
- (d) varying a firm's permission including cancellation (SUP 1.4.6 G).

Half mark for each correct reference up to **three marks** if necessary.

- (9) This question has now become considerably more complex with changes made after the coming into effect of the MIFID. Half mark can be awarded for any correct reference (in summary) up to **three marks**.

The main requirements imposed under SYSC are as follows:

**(1) Senior Management Arrangements (SYSC 2)**

Firms must maintain clear and appropriate apportionment of significant responsibilities among directors and senior managers in respect of responsibility for each area of business and to ensure that the business is adequately controlled and monitored.

**(2) Systems and controls (SYSC 3)**

Firms must take reasonable care to establish such systems and controls as are appropriate to its business (SYSC 3.3.1).

**(a) Organisation**

There must be clear and appropriate reporting lines with outsourcing being properly monitored and firms having clearly documented business strategy plans that are tested and updated regularly to ensure effectiveness.

**(b) Systems and Controls in respect of compliance, financial crime and money laundering.**

Firms must take reasonable care to establish and maintain effective systems and controls for compliance with applicable requirements and standards under the regulatory system and for countering the risk that the firm may be used for financial crime.

**(c) Money Laundering Reporting Officer (MLRO)**

A firm must appoint an individual as MLRO with responsibility for oversight of its compliance with the FSA rules on systems and controls against money laundering.

**(d) Compliance Function**

Firms must maintain separate compliance functions where this is necessary having regard to their size with organisation responsibilities being properly documented and the department staffed with an appropriate number of competent and properly resourced staff with unrestricted access to the firm's records and governing body.

**(e) Risk Assessment**

The firm should consider whether it is appropriate to have a separate risk assessment function responsible for assessing risks.

**(f) Management Function**

The firm's arrangements should be such as to provide the governing body with adequate information to measure, manage and control the risks of regulatory concern.

**(g) Employees and Agents**

A firm must have adequate systems to ensure the suitability of anyone who acts for it and, in particular, ensure compliance by approved persons with the Training and Competence (T&C) sourcebook.

**(h) Audit Committee and Internal Audit**

A firm should consider whether it is appropriate to have an Audit Committee to examine arrangements made by management to ensure compliance with the requirements and standards under the regulatory system with a separate internal audit function for the day-to-day monitoring of systems and controls.

**(i) Business Strategy and Continuity**

A firm should be able to plan, identify and manage regulatory risks and have arrangements to ensure that it continues to function in the event of unforeseen circumstances such as major IT failures which systems must be tested and updated.

**(j) Remuneration Policies**

A firm must manage appropriately any tensions between its ability to meet regulatory standards and personal advantage caused by its remuneration policies especially where employees are made on a commission basis.

**(k) General Factors**

The extent of the systems and controls to be maintained within a firm are dependent on a number of factors including the nature, scale and complexity of the business, the diversity of its operations, the volume and size of its transactions and the degree of risk associated with each of its operations; with firms always ensuring compliance with the Combined Code of Corporate Governance.

- (3)** Additional requirements are imposed in connection with common platform firms that have to comply with the Capital Requirements Directive (CRD) and the Markets in Financial Instruments Directive (MIFID):

- (a) **General organisational requirements including business continuity (SYSC 4);**
- (b) **Employees, agents and other relevant persons including senior management requirements (SYSC 5);**
- (c) **Compliance including internal audit (SYSC 6);**
- (d) **Risk controls including certain CRD risk-specific material (SYSC 7);**
- (e) **Outsourcing (SYSC 8);**
- (f) **Record-keeping (SYSC 9);**
- (g) **Conflicts of interest (SYSC 10).**

Half mark for any correct reference up to **three marks** if necessary.

**(10)** The TCF Consumer Outcomes are as follows:

- (a) Consumers can be confident that they are dealing with firms where the fair treatment of customers is central to the corporate culture.
- (b) Products and services marketed and sold in the retail market are designed to meet the needs of identified consumer groups and targeted accordingly.
- (c) Consumers are provided with clear information and are kept appropriately informed before, during and after the point-of-sale.
- (d) Where consumers receive advice, the advice is suitable and takes account of their circumstances.
- (e) Consumers are provided with products that perform as firms have led them to expect and the associated service is both of an acceptable standard and as they have been led to expect.
- (f) Consumers do not face unreasonable post-sale barriers imposed by firms to change product, switch provider, submit a claim or make a complaint.

Half mark for any correct reference up to **three marks** if necessary.

## **SECTION B**

**(11) Financial Promotion**

The fact pattern was concerned with the promotion of a range of new products offered by a small friendly society. This could have generally been answered on the basis of the core financial promotion provisions contained in the FSMA and COBS although ethical issues also arose in light of the importance and sensitivity of the products offered.

- (a) Candidates should have referred to the core requirements set out in s 21 of the FSMA including the need for financial promotions to be issued or approved by an authorised person and with such promotions being fair, clear and not misleading. Reference may also have been made to as many of the relevant provisions contained in COBS 4 (such as 4.1 application, 4.2 content, 4.3 enabling, 4.4 compensation and 4.5 communications, past performance, overseas promotions, off-the-page promotions and approval). Reference should also have been made to PRIN 7 (communications with clients), 6 (customers' interests), 3 (management and control) and possibly 1 (integrity).

- (b) Breach of s 23(1) may incur a 6 month or 2 year sentence with an unlimited fine subject to available defences. Contracts are also unenforceable under s 26 and compensation under s 28. Firms may also be separately disciplined by the FSA (including either warning or public censure s 205, unlimited fine s 206, injunction s 380, restitution s 382 and removal or restriction of permission or authorisation). Reference may also have been to damages under s 150 FSMA.
- (c) Relevant conditions with regard to comparisons are set out in COBS 4.6 (including application, past performance, simulated past performance and future performance as well as possible fees, taxes and charges, warnings, data source, risk and assumptions).
- (d) The core management requirements are, of course, set out in SYSC (including senior management arrangements, systems and controls – organisation, financial crime, MLRO, compliance function, risk assessment, management information, employees and agents, audit committee/internal audit, business strategy and continuity, remuneration policies and general factors – as well as additional provisions for common platform firms following MIFID). Reference may also have been made to COND, FIT and APER.
- (e) Sub-question 11(e) was more general in nature with the SII intending that this would include the FSA's Treating Customers Fairly (TCF) initiative and other more general ethical principles in addition to the high level standards in Block 1 of the Handbook to the extent not already referred to. Reference should specifically have been made to TCF which the FSA has highlighted continuously. Reference may also have been made to the SII Code of Conduct although this was not strictly necessary. Some marks were awarded for references to other additional parts of the Handbook to the extent relevant and not referred to in earlier parts of the question.

## **(12) Client Classification and Documentation**

The facts raised various issues in connection with the classification and documentation requirements that would apply in connection with the services to be provided for a sovereign wealth fund. Additional issues also arose in connection with confidentiality and national security as well as possible insider trading and disclosure of dealing commissions.

- (a) The fund would generally have been classified as a professional client following the coming into effect of the post-MIFID categorisation requirements (DP06/3 (August 2006) and CP06/19 (October 2006)) which corresponds with the former intermediate category under COB. Reference may also have been made to the right to request a different categorisation and the alternative classifications available.
- (b) Reference should have been made available to all general documentation and disclosure requirements imposed under COBS 8. The content and timing of a one-way terms of business should have been explained with relevant exceptions available. Services, fees and commission must also be disclosed under other matters under COBS 6. Reference may also have been made to

suitability or appropriateness under COBS 9 and 10 to the extent relevant or possibly other record and reporting requirements under COBS or CASS. Reference may have been made to the need to carry out due diligence for money laundering purposes.

- (c) The request made by the fund raised issues of conflicts of interest and client confidentiality which would have to be managed with some care. The matter should be referred to compliance who would consider how to respond. General non-client information may be available including through investment research documentation although the firm would have to avoid disclosing confidential information in connection with the activities or positions of other clients. Certain activities may also be subject to government directions in connection with areas sensitive to national security which would have to be confirmed separately. The firm must also clearly be careful not to disclose any inside information under CJA or s 118 FSMA.
- (d) This again raises issues of managing conflicts of interest under PRIN 8, SYSC 10 and SII 5. Reference may be made to the definition of investment research under the post-MIFID COBS (labelled or described as such or otherwise presented as the objective of independent research) as distinct from other ‘non-independent research’ or ‘marketing communications’. Specific care will have to be taken in that the post-MIFID rules apply to oral and written material. The research itself should contain all relevant information with the reference to ‘hidden gems’ presumably being dealt with separately within the report. The related issue that this raises is whether the information is based on inside information of any form contrary to CJA and s 118 FSMA (or possibly s 397 FSMA) which compliance should confirm.
- (e) The revised rules on dealing commission and restrictions on soft commission (or ‘softing’) should have been referred to including specifically COBS 11.6 (Use of dealing commission). Permitted uses of dealing commission should be explained and prohibited matters. Relevant disclosure and record keeping requirements should also have been noted. Reference may also have been made to the FSA papers on dealing commissions including PS05/9 (bundled brokerage and soft commission arrangements) and PS06/5 (bundled brokerage and soft commission arrangements for retail investment funds). The relevant positions were to be reviewed during 2008.

### **(13) Dispute Resolution**

The question raised a number of issues with regard to the management of complaints and redress available to private clients in dealing with UK authorised institutions. Candidates may have dealt with the question solely in terms of rights of redress and remedy although the best answers also referred to specific instances of breach of legal or regulatory obligation. Candidates should have read the question in full initially and dealt with each sub-part in turn.

- (a) The structure and operation of the internal complaints procedures that are required to be maintained within all financial firms should initially have been explained under DISP. Firms must maintain written procedures that are notified to and made available to all customers on request. Eligible complaints

must be dealt with under relevant policies with a senior independent member of staff considering the complaint fully and promptly and with appropriate redress being provided as necessary including compensation by the firm. Records of the decision and response must be kept for 3 years. The procedure must be carried out in accordance with the specified timetable with all of the relevant responses being carried out within the 5 business days, 4 weeks and 8 weeks as specified. Complainants must also be notified of their right to apply to the Financial Ombudsman Service (FOS) separately with firms also reported to the FSA on a 6 monthly basis of all complaints received or that no complaints had to be dealt with.

- (b)** The client's further rights of redress are to the FOS in the event that the firm's internal procedures fail to deliver a satisfactory response. As much information as possible should have been provided on the nature and operation of the FOS procedure. This includes the definition of 'eligible complainants' (essentially private individuals other than intermediate customers (professional clients) and small business, charities or trusts). Reference may also have been made to FOS investigation, hearings, representations and reporting as well as the power of the FOS to make an award of up to £100,000 and reasonable costs.
- (c)** The office manager may or may not have been an approved person carrying out a controlled function within the firm. If the manager was not properly approved, there may be a right of action under s 71 FSMA or a separate more general right of action against the firm under s 150 FSMA for breach of relevant rules under the FSA Handbook of Rules and Guidance. There may be a separate breach of the CASS rules. Other common law rights of action may also be available including damages for breach of contract, negligence or possible conspiracy.
- (d)** While the FSA will generally not become involved in individual client redress matters, it has power to require authorised firms to provide compensation or restitution without a court order or to apply for a court order for restitution requiring any person who has breached a rule or other requirement of the FSMA 2000 to provide compensation or restitution (ss 382-386 FSMA). The FSA would probably be unlikely to act in the event that adequate redress was already available under internal procedures or through the FOS ((a) and (b) above). It may nevertheless assist in the event that both of these options failed in the particular case. Action may then be available against the firm as an authorised person or against the manager individually assuming that he was still in possession of the funds misappropriated. Reference may also again be made to common law rights of action. Injunctions may also be available under s 380 FSMA if this may assist.
- (e)** In the event of the firm's collapse, compensation would be available from the Financial Services Compensation Scheme (FSCS) under COMP. Relevant entitlements (including the definition of 'relevant firm' and 'eligible claimant') should have been explained and the relevant compensation limits. Reference may also have been made to the current discussion on the extent to which the limits should be increased following the Northern Rock crisis.

## **(14) Short Selling and Market Abuse**

The fact pattern was specifically concerned with short selling on which the FSA has consulted recently and which has become of particular importance in light of the recent high levels of market volatility. While the FSA generally accepts that short selling is a legitimate trading technique that assists liquidity specifically, difficulties can arise with regard to market abuse although conflict of interest problems also arose in the question set. New definitions of 'disclosable short position' (0.25% of the issued shares or an equivalent economic interest) and 'rights issue period' have been incorporated within the FSA Handbook. The Market Conduct sourcebook (MAR) has also been amended to provide that a non-disclosed disclosable short position can constitute market abuse (misleading behaviour) under s118(8)(a) or market abuse (distortion) under s118(8)(b). The revised disclosure provisions were brought into effect on 20 June 2008 which candidates were not required to refer to specifically but they should nevertheless have been aware of the general issues that arise in this area.

- (a)** Acting against a research recommendation is not a problem in itself although issues may arise with regard to conflicts of interest and Chinese walls, release of research information and the need for the firm to comply with all relevant provisions within PRIN (including 1 and 8), SYSC (8 specifically) and APER (including 1 and 3). Independent research is also dealt with under COBS 12.2, non-independent research under COBS 12.3 and research recommendations under COBS 12.4. The decision not to follow the research recommendation made is not of itself a problem unless other suspicions arose although the research analyst maybe interested in the reason for not following the advice given.
- (b)** Shorting the stock subject to a buy recommendation is again not specifically a problem although concerns may arise with regard to either the market basis for the short position or the quality of the research being provided. Different positions may be taken by separate sections or desks within a firm. Provided that any conflicts are properly managed especially through the use of effective Chinese walls, no specific regulatory difficulties should arise. The position should nevertheless be monitored by compliance with any new disclosure obligations being complied with.

Relevant provisions include PRIN 1 (integrity), 2 (skill, care and diligence), 3 (management and control), 6 (customers' interests) and 8 (conflicts of interest). Reference may also have been to SYSC 2 (senior management arrangements), 3 (systems and controls) and 10 (conflicts of interest) as well as APER 1 (integrity), 2 (skill, care and diligence), 3 (proper standard of market conduct), 5 (proper organisation of business), 6 (skill, care and diligence in management) and 7 (regulatory compliance). Reference may also have been made to SII Code of conduct 1 (acting honestly and fairly at all times), 2 (integrity), 3 (compliance), 4 (market integrity), 5 (conflicts of interest), 6 (professional competence) and 7 (highest personal standards).

- (c)** The proprietary desk and institutional sales desk may also take the same or different positions. This is again not a problem provided that the proprietary desk has no information with regard to retail or wholesale client orders and the

firm's original investment research (above). The investment team should nevertheless not be provided with information concerning specific client investment objectives or positions and the trading desk should not deal with clients directly. The operation of the Chinese wall should be reconfirmed and other internal communications within the firm to ensure that there has been no 'crossing of the wall'. The timing of the proprietary and wholesale trades may be reviewed specifically. Reference may also have been made to COBS 2.3 on client order handling and COBS 12.2 on investment research. All of the other specific provisions within PRIN, SYSC and APER would also apply. Compliance would also specifically want to ensure that there had been no insider trading (CJA), market abuse (s 118 FSMA) or market manipulation (s 397 FSMA).

- (d) The same general concerns would arise with regard to systems and controls and the management of conflicts of interest as above. The specific new issue highlighted is one of insider trading, market abuse or possibly market manipulation. Reference should have been made to all relevant possible offences and defences as well as penalties. The large short position may simply have been taken in light of the prevailing market conditions and market volatility although compliance would want to confirm this. Any breach should be reported to the FSA as soon as possible under PRIN 11 and SII 3.

## SECTION C

### (15) Accountability

The question was concerned with the effectiveness of the accountability regime set up under the FSMA against the extensive powers conferred. Candidates could have initially referred to the enforcement powers available to the FSA (including investigations, independent reports, unlimited fines, injunctions, restitution orders, private and public censure and insolvency applications). The FSA can revoke or suspend permission and authorisation or impose directions and has a separate power to pursue criminal proceedings in a number of cases.

This then has to be set against the accountability regime created which is essentially based on statutorily based duties and functions and supporting regulatory objectives and principles, HM Treasury board appointment and removal, executive director appointment and oversight, maintenance of appropriate oversight and disciplinary measures, complaints procedures, annual reports and annual general meetings. The FSA has to take into account the opinions of the Consumer and Practitioner Panels and the Small Business Practitioner Panel.

The Treasury may separately conduct reviews or set up independent investigations. Supervisory decisions are taken by the Regulatory Decisions Committee (RDC) on appeal to the Financial Services and Markets Tribunal and to the courts on a point of law. Judicial review is also available as well as possible liability under misfeasance in public office with possible reference being made to the *Three Rivers* action which was eventually abandoned with costs of up to £83 million being awarded in favour of the Bank on an indemnity basis.

## **(16) Financial Capability**

Candidates were asked to explain the work undertaken by the FSA in promoting 'Financial Capability' which is based on its consumer education objective. The FSA's policy in this area is intended to ensure that consumers are better able to manage their financial affairs and take informed decisions in their best interests. The difficulty that arises is concerned with the need to ensure that full information is made available in all cases (essentially through transparency and disclosure requirements) as well as provide consumers with the necessary tools and support to allow them to make informed decisions with regard to financial matters.

Reference could specifically have been made the consumer awareness and protection objectives set out in s2(2)(b) and (c) and ss 4 and 5 FSMA. The series of discussion papers issued by the FSA in this area may have also been referred to. The FSA has undertaken a number of separate further initiatives in connection with this especially with regard to the maintenance of a dedicated website function, the production of a number of 'Key Facts' documents and other fact sheets and information packs, the conduct of road shows, its disclosure policy more generally and the more recent work in connection with 'Treating Customers Fairly' (TCF).

The FSA has most recently announced a *Money Guidance Summit* to provide free, impartial information and guidance on money matters following the Thoresen Review of Generic Financial Advice in January 2007. The FSA will lead the initiative although participants from the Government, the financial services industry and voluntary organisations will also participate in partnership with HM Treasury. The conference on 'Money Guidance Pathfinder: Issues considered how best to reach and engage those that could benefit from such guidance, the provision of tailored guidance especially using telephone and face-to-face channels, digital technology and evaluation mechanisms within the Thoresen Review roadmap.

The FSA is separately continuing with its 'Delivering Change' strategy to improve the financial capability of UK consumers over a 5-year period with the specific target audience including schoolchildren, young adults, Not in Education, Employment or Training (NEETs), university students and Further Education (FE), workplace employees and new parents. Information is also made available through the FSA's Moneymadeclear consumer website and other publications. The FSA reports that it has already reached almost 4 million people against a total target of 10 million people by 2011.

Reference may also have been made to the review of the work undertaken in connection with financial capability in any of the most recent FSA *Annual Reports* and *Business Outlooks*.

## **(17) Sovereign Wealth Funds**

The question was concerned with Sovereign Wealth Funds (SWFs). SWFs are among the largest single investors at this time and despite the down turn in many aspects of legal work, are still generating a substantial amount of transaction activity within the major law firms.

There is no standard definition of ‘Sovereign Wealth Fund’ at this time although reference may be made to any of the major funds including in the Middle East as well as Scandinavia and the UK and China (each of which generally has its own website). Reference may also have been made to the current work being undertaken in this area by various organisations and committees including the Committee of European Securities Regulators (CESR) and the International Organisation of Securities Commissions (IOSCO) as well as the Basel Committee and the European Commission. The issue has also been discussed within the US Congress.

The specific regulatory issues that arise include the following:

- (1) Disclosure and transparency;
- (2) Corporate governance;
- (3) Management autonomy within target firms;
- (4) National security (although specific definition issues arise in defining relevant interests with this possibly extending to include energy companies, transport and freight (such as the New York Port Authority) in addition to military and armaments interests);
- (5) Money laundering;
- (6) Possible market distortion or disruption;
- (7) Moral hazard (with the implied sovereign support or guarantee provided); and
- (8) Potential corruption and political interference in certain countries.

Reference could also, for example, specifically have been made to the FSA’s statutory objectives and the extent to which SWFs could cause specific difficulties for the FSA in regulatory terms.

## **(18) Financial Crisis**

Reference could initially have been made to any of the recent crises in UK or international markets that have affected the UK. These include BCCI and Barings, Enron and WorldCom and Sumitomo. The structure of the new regulatory regime set up under the FSMA could have been referred to briefly with specific reference to the role and function of the FSA as an integrated or single regulator and the scope of coverage of the FSMA as well as key FSA policies such as supervision by risk, the new operating framework and ARROW, the better regulation agenda and the move to principles based regulation.

The cause and nature of the most recent credit crisis following the tightening of liquidity on inter-bank markets in August 2007 could then have been described and the circumstances following the financial support for Northern Rock and its subsequent public acquisition (nationalisation).

The various Tripartite and Treasury papers published since Northern Rock could then have been referred to and possible lessons learned outlined. This could have been restricted to the banking markets (such as with the new Special Resolution Regime (SSR) proposed) or extended to include all financial markets and the system of

financial regulation set up under the FSMNA more generally. Further comment could have also been made on the most recent proposed institutional changes to the structure of financial stability management in the UK and the relationship between the FSA, the Treasury and the Bank of England especially under the revised MOU entered between them and the Bank's role with regard to SSR.

Candidates should have attempted to refer to some of the main lessons learned as this was the specific purpose of the question. No specific answer was nevertheless expected and the question could have been dealt with in a number of different ways.