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INTEGRATED FINANCIAL REGULATION:

LESSONS FROM THE UK'S FINANCIAL SERVICES AUTHORITY

I am asked to draw lessons from the British experience of establishing a single regulator and, in particular, to consider the relevance they might have for Germany.

In one sense, it is a very odd time to draw any lessons at all. Legally speaking, the FSA came into being as a single regulator at midnight last Friday. So we have had just 3 working days experience of integrated regulation, perhaps not quite enough experience on which to base rigorous conclusions. It is fair to say, though, that we have been operating, in practice, as a single regulator for about 3½ years – even if one or two pieces of the jigsaw have been inserted more recently. So there is some evidential basis on which to draw tentative conclusions. But I would be the first to acknowledge that any lessons drawn must be heavily qualified at this stage. It is hard to know precisely how long it would be appropriate to observe a structure of regulation before drawing conclusions on it, but it would certainly be advisable to watch how it performed through at least one significant economic downturn before doing so. That, of course, is happening to us in real time.

There will, in fact, be a more considered assessment of the FSA, prepared by an independent source, which will see the light of day in the Spring of 2003. The IMF are just beginning their Financial Sector Assessment Programme in the UK and are bound to assess the performance of the FSA in that context. So those who would prefer to wait for an independent assessment may do so. But since regulatory reform is on the agenda in Germany on an earlier timescale, you may have to make do with my provisional assessment as you design your own new regulator.

Before offering an assessment, however, it would be wise to explain just what we mean by integrated regulation in the UK. Because, just as there are different central banking models around the world, so there are different integrated regulators. They come in various shapes and sizes. They cover different combinations of functions, with different sets of powers and responsibilities. There is no single blueprint for a single regulator.

1. FSA: powers, scope and structure

By most standards the FSA is a very broadly based single regulator, with rather extensive powers within the regulator itself, albeit set within a rigorous framework of accountability, with many built-in checks and balances.

(a) Powers

First and foremost, the FSA is both a regulator and a supervisor. There are countries in which there is a clear distinction between the two. And, indeed, the FSA might even be called a legislator in some countries, including Germany.

The single Act which gives the FSA its powers, the Financial Services and Markets Act, is – in spite of its length – a piece of framework legislation. It includes a series of high level objectives, and gives the Authority considerable latitude to draw up rules and codes within that general framework. The legislation requires these rules and codes to be established within a set of what we call "principles of good regulation", on which the Authority may be judicially reviewed. But we can draw up, and amend many regulations ourselves, without further reference to Parliament. When we were looking at a potential merger between the London Stock Exchange and Deutsche Boerse last year, we discovered that a number of the market rules which were set in primary legislation in Germany, and could only be changed by the Bundestag and the Bundesrat, were part of the FSA's rulebook in the United Kingdom and could be changed by us, subject to consultation.

Furthermore, the objectives of the Authority are very broad. We are given four aims in the statute:

(i) To maintain confidence in the UK's markets. In some countries market confidence would be purely a central bank matter. In our case, the FSA's objective of market confidence sits alongside the Bank of England's responsibility for the stability of the system as a whole. I will explain later how this works in practice.

(ii) To promote public understanding of the financial system, which takes the Authority into the provision of information to consumers, and indeed financial literacy programmes. Relatively few other financial regulators undertake that kind of activity.

(iii) To protect consumers, bearing in mind their own responsibilities for their decisions – a relatively familiar objective internationally, though it is rarely accompanied by an explicit "caveat emptor" clause.

(iv) To reduce financial crime – a heroically-formulated objective. It is one which is gaining increasing prominence in the field of financial regulation, particularly since the events of 11 September.

It is the case, also, that the FSA carries the full responsibility for authorising and licensing financial institutions. In some countries the licensing function remains with the Ministry of Finance, even if the regulator prepares recommendations. And the Authority itself has a wide range of disciplinary powers. The Authority may levy fines, which may in principle be unlimited, may suspend authorisations or revoke them permanently, and may ban individuals from operating in regulated financial markets, again for indefinite periods. The Authority is also a prosecutor. We may bring either civil or criminal prosecutions for insider dealing offences or in relation to money laundering, for example. Again, that is a rather broad definition of the regulator's rôle. In many other countries the prosecution function would lie elsewhere.

It goes without saying that there are rigorous disciplines on the exercise of these powers. The significant enforcement powers must be exercised by a Regulatory Decisions Committee, appointed independently of the Executive of the Authority, and the Executive of the Authority are rigorously excluded from decisions on the penalties to be imposed in individual cases. There is, furthermore, an independent tribunal, in the judicial system, to which we must go if firms refuse to accept the penalties we seek to

impose. That tribunal hears the evidence anew, and we are the prosecutor in the tribunal; it is not an appeal body.

But, in bearing in mind those qualifications, one would have to conclude that the FSA is endowed with a considerable degree of power and responsibility.

(b) Scope

The FSA is also quite broadly-based in terms of the scope of integrated regulation, in other words the nature of the financial activities which come within its remit. The Authority incorporates the previous responsibilities of 10 separate regulatory bodies. We handle both prudential and conduct of business regulation for banks, insurance companies and investment firms. We cover a wide range of other bodies, including building societies, mutual societies of one kind or another, credit unions, financial advisers and fund managers. That brings around 10,000 separate firms into our authorisation. We also oversee all markets and exchanges in the UK, both cash markets and futures and derivatives, which takes us into commodity markets, including the oil and metal exchanges, and also increasingly into energy markets. And we are now the competent authority for listing and for the continuing obligations of firms to disclose information to the market. So in addition to the 10,000 financial firms we regulate directly, we also oversee the information disclosure of all listed companies in the UK.

But we do not regulate takeovers. There is a separate Takeover Panel with that responsibility, albeit its code must sit within our own regulatory framework. And we do not, as the SEC in the US does for example, oversee accounting standards directly, or audit the auditors. Those powers are handled elsewhere in the UK system.

It is always difficult to make direct comparisons between one country and another, but in German terms I would say that we undertook the banking supervision activities of the BaKred and of the Bundesbank and the Landeszentralbanken. The Bank of England does not have direct relationships with individual institutions for any supervisory purpose. We have the responsibilities of the German insurance regulator. We have almost all of the responsibilities of the BAWe, though as I have said we do not handle takeovers, which I understand the BAWe will in future do. And we carry out some of the functions of the economic ministries in those Laender where there are stock exchanges.

This is, therefore, a very broad definition of an integrated regulator, in terms of scope as well as powers.

(c) Structure

In terms of the structure of the Authority, we have adopted a highly integrated model. In deciding on the appropriate institutional shape for the FSA, we chose to pull together as many functions we could into the common areas of the Authority. So, for example, we have a single authorisation department, to which any organisation wishing to come into our fold must apply. We have a single enforcement division, and of course all the "back office" functions of the Authority, and all its operational staff, are fully integrated. We have also gone rather further, and now operate integrated supervision of complex financial groups. So you will not find a Banking Supervision Division in the FSA. Instead you will a Major Financial Groups Division, which looks after around the 50 largest financial groups operating in the UK, from Lloyds TSB through the Prudential Insurance Group to Goldman Sachs and Deutsche Bank. The teams are multi-functional, handling both prudential and conduct of business activities in the same teams. Elsewhere you will find a Deposit Takers Division which includes other banks, building societies and credit unions. Again, by international standards, we have chosen a highly integrated model and, indeed, this year we chose to increase the degree of integration in response to our early experience. This is a matter of choice. There is not a rule of which I am aware which tells you that financial regulation will be better carried out in an integrated way. But we believe it makes sense for us.

2. The rationale for an integrated national financial services regulator

That is, in broad terms, the nature of the beast we have created. But, again, before getting to the key question of the lessons we learn from it, we need to address the prior issue of why we created such a thing. What were the arguments which drove the new, incoming Labour Government to announce an integrated regulator as one of its very first policy initiatives, just two weeks after the 1997 election?

There is no text to which one can refer for an authoritative answer to that question. Somewhat unusually, the Government did not proceed by means of a White Paper, setting out the arguments for change, and inviting debate on it. The announcement was rather short and to the point. There would be a single financial services regulator. (The name came later, chosen by me, the choice reflecting my lack of creative imagination). There had been considerable debate around different regulatory models in the UK for a number of years. And on one point, almost all commentators were agreed: our previous system was far too complicated. While no-one can hope to rival the United States in the diversity and complexity of its regulatory system, we had given it our best shot. We had a wide range of different sectorally-based regulators whose responsibilities were interlocking and overlapping in complex ways.

A second situational factor was the Government's plan for the Bank of England. The United Kingdom was one of the last developed countries to move to a fully independent central bank, with the power to set interest rates. The Government took the view that an independent monetary authority should not at the same time carry responsibility for government debt issuance or for the prudential supervision of banks. I am not personally wholly persuaded by the argument that there is a necessary incompatibility between monetary policy responsibility and responsibility for prudential supervision, and when I was at the Bank of England I did not observe the one corrupting the other. But I can see that, in the particular circumstances of the Bank of England in 1997, there was an argument for making an explicit change, to emphasise that the Bank would in future be making monetary policy decisions in the interests of the whole economy, and not simply in the interests of the City of London. I regard this as an optical point, rather than an issue of great substance, though I recognise that there are other strongly held views on the point. Indeed I will return to that argument a little later on.

The positive arguments for a single regulator are somewhat different.

In the UK, the rationale for an integrated national financial services regulator reflects 4 primary considerations. First, the increase in the number of financial conglomerates and the blurring of the boundaries between financial products make sectoral regulation increasingly less viable. In London there have, for many years, been few restrictions on the freedom for financial firms to acquire each other, across sectoral boundaries. In that respect our position is somewhat different from that historically of the US, which makes the arguments for integrated regulation rather stronger in London than they are in New York.

Second, we point to the availability of economies of scale and scope to an integrated regulator and the value of being able to allocate scarce regulatory resources efficiently and effectively.

Third, there are benefits from setting a single regulator clear and consistent objectives and responsibilities, and resolving any trade-offs between those objectives and responsibilities within a single agency.

Fourth, there is an argument for making the single regulator clearly accountable for its performance against statutory objectives, for the regulatory régime, for the cost of regulation and for regulatory failures where they occur – and they will.

(a) Financial Market Convergence

To amplify the first point, about convergence, I would say the following. "Convergence between sectors within the banking and insurance industries and the securities firms is growing in any case. As the markets change, there is a need for action on the regulatory level, with a view to securing the future stability of the financial system. When markets change and reconstitute on a cross sector basis,

government regulation of such markets needs to be reorganised. Universal financial regulation is the best way of reacting to the dynamics of changes in the financial markets".

I hope I find some support in Germany for those observations. They are translated from an annexe to the draft legislation creating the Allfinanz Authority.

After 3 years or so of practical operation of the single regulator model, how do these arguments look today? Have these theoretical advantages been borne out in practice? And are there any other lessons of the early years which alter the balance of the argument?

The first argument is essentially one about the way in which financial markets are expected to develop in the future.

My observation is that the hypothesis on which the FSA was based has, broadly speaking, been borne out in practice. We have seen an increasing number of cross-sectoral acquisitions in the financial sector, with the creation of financial hypermarkets offering a broad range of products to a wide spread of customers. In the UK, for example, Lloyds TSB acquired Scottish Widows, one of our largest life insurers. The Prudential Insurance Company bought M&G, an enormous fund manager, and has opened a bank, called EGG. Merrill Lynch acquired Mercury, a major asset manager, and have gone into partnership with HSBC in search of deposits and wealth management opportunities in the middle market of the personal sector. And in Germany, we have seen the Allianz/Dresdner merger.

I am not one of those who thinks that there will be one all-singing, all-dancing model of financial hypermarket which will dominate all financial markets in the future I suspect there will be a lot of competing models, for some time. Indeed I would hope there would be competing models to maintain a dynamic market characterised by intense competition. But I do not think that there will be competition based on single sectoral institutions matching the old regulatory boundaries. I therefore conclude that regulatory models based on old-style sectoral divisions will find it increasingly difficult to cope with the challenges posed by new corporate structures.

(b) Economies of scale and scope

The second argument was that a single regulator would be able to achieve economies of both scale and scope, and would be able to allocate scarce resources more efficiently and more effectively.

It is always rather difficult to identify economies of scale in regulation, and altered structures of regulation of course operate against the background of a changing and expanding marketplace. So one might expect, whatever the regulatory structure, that the scale and cost of regulation would be likely to rise. Certainly, in the UK over the last few years, the volume of financial transactions has continued to expand, and indeed the number of firms has continued to grow in all parts of the market.

During this expansionary period, the FSA has also had to cope with the challenge of new responsibilities, and the cost of transition to the new régime.

Nonetheless, in spite of all of these pressures, our costs in real terms have been flat and, taking account of salary increases in the financial sector, have been falling. Indeed had the cost of the old régime expanded simply in line with wages in the financial sector over the last 4 years, our costs now would be some £15 million, or around 10% higher than they are. So there are clear signs of efficiency savings from a single regulator model.

Perhaps more important, though, are the economies of scope. A single financial services regulator should be able to tackle cross-sectoral issues more efficiently and effectively than can a multiplicity of separate or specialist regulators. This opportunity arises in three main areas: the setting of standards for regulated firms, the supervision of individual firms, and the analysis of industry and of market-wide developments. In the FSA we have a single set of principles for businesses and a single statement of requirement for high-level systems and controls. We also have a single set of regulatory manuals setting out the FSA's approach to authorisation, supervision and enforcement. I should emphasise that this is not intended to be a one-size-fits-all approach, and we have maintained appropriate differentiation by

taking into account the different degrees of protection required by different types of customers and the different ways in which the FSA's requirements can be met according to the nature and size of a firm's business.

Meanwhile, the supervision of each regulated firm brings together all of the regulatory requirements – prudential and conduct of business – to which each firm is subject. Since most firms are subject to both conduct of business and prudential requirements and since compliance with these requirements depends to a large extent on the quality of firms' senior management and controls, there are considerable advantages in integrating the two types of regulation in one institution.

As I have explained, for major financial conglomerates, a single team of supervisors monitors their adherence to all of the regulatory requirements applicable to the group. Similarly, although the other divisions remain organised primarily by sector, the same principle of integrated supervision applies, so for each firm a single team is responsible for monitoring all aspects of the business of that firm.

We have also found this integrated approach to be attractive in looking at the impact of market turbulence and industry-wide development on the financial sector. So, for example, we have been able to look across the whole financial sector in assessing the impact of the collapse of LTCM and the growth of hedge funds more generally. We have operated a cross-sectoral approach to the impact of the economic problems in South East Asia, Japan, Argentina and Turkey on London's markets. We have carried out analyses of the impact of other shocks on the financial markets, such as the problems of the telecoms industry or airlines. And, after 11 September, we were able to adopt an integrated approach to managing the fall-out from the events in New York.

We have learned that there is considerable benefit from this integrated approach. So, for example, we managed our Y2K work across the sector as a whole. We have undertaken a cross-sectoral analysis of the impact of a shift to a low inflation environment on financial markets and financial firms overall. We have done the same in relation to the development of e-commerce and indeed of money laundering, where it is right to impose the same disciplines on non-banks as traditionally have been imposed on banks.

There are a number of other, more specific areas in which risks have been transferred around the financial sector, and where there is considerable value in being able to monitor the effects of risk transfer. I think, for example, of the reinsurance market or, indeed, of credit risk transfer between banks and insurance companies often intermediated in the securities markets. There is huge advantage in being able to look at these trends from the perspective of both ends of the transaction.

As far as resource allocation is concerned we have found that, using a risk-based approach to regulation, we have already made significant changes in resource allocation within the Authority. Even in our short history to date, we have found it appropriate to switch resources between sectors in response to market developments. So, at the moment, we are switching resources into the insurance sector, where there are particular problems arising after 11 September. Following the LTCM collapse, we switched resources into looking at the hedge funds sector and derivatives markets. From a practical management point of view, it is enormously helpful to have the ability to deploy and redeploy scarce expert staff in this way.

(c) Reconciling conflicting objectives

The third argument was that a single agency is best able, within a clear frame of accountability, to reconcile the potentially conflicting aims of prudential and conduct of business regulation.

There are those who maintain that there is a fundamental incompatibility between the aims of the prudential regulator, and the aims of the monitor of market information and conduct of business. As we constructed the FSA, we sought to assess among ourselves, whether we believed that, with our different backgrounds and inheritances, we were in fact seeking to achieve different ends. Our conclusion was that we were not. We all wanted to ensure that the financial system operated effectively and fairly in the interests of its customers. The conduct of business regulator wants an individual consumer or market counterparty to be given fair information on which to base her decisions, and,

sometimes, compensation where that information was false or misleading. The prudential regulator wants to protect the depositor or investor by ensuring that the firms with which he deals are reasonably safe. Prudential regulation, and the pursuit of market confidence, is not a higher calling, unrelated to the interests of individuals. Financial stability is not a kind of platonic ideal divorced from the interests of economic actors. So the two forms of regulation are working towards the same end.

Nonetheless, it may be that, from time to time, there are apparent conflicts. A conduct of business regulator may wish to ensure that a bank gives its depositors up to date information on its financial position. But if that were to result in a bank run, because depositors jumped quickly to the conclusion that the bank was unsound, it could well be that all of the depositors were collectively disadvantaged. If there is a reasonable chance that the bank may be saved, there can be a case for maintaining depositors' confidence through a difficult period.

Similarly, in the case of a life insurance fund owned by the policyholders collectively, certain groups of policyholders may have a legal right to compensation. But if pursuing that compensation to the maximum extent destabilises the fund, such as it can no longer continue to accept new business and must close down, even those seeking compensation could be disadvantaged. So there is an argument for the regulator striking a balance between the interests of particular groups of policyholders, and the interests of policyholders as a whole.

We have already faced both these conflicts in the FSA's short life to date. They are extremely difficult issues to resolve. And I am not seeking here to defend the particular judgements we have made on individual cases up to now. But it is idle to pretend that there is not a balance to be struck, by suggesting that there are absolute interests which may be pursued single-mindedly by different institutions with different aims. Of course it may be argued that those issues can be best resolved in a public debate between different regulators. My experience is that that does not happen, and that what we see instead are private turf wars. So I would argue that these trade-offs are, in practice, best made within an institution with an appropriate framework of objectives and accountability, such as I believe we have in the FSA today.

(d) Clear accountability

That links with the fourth argument, in favour of clear regulatory accountability.

This is an area where there are different cultural norms from country to country. We live in a particular environment in which it is no longer possible for public authorities to decline to explain their judgements. It is not an environment in which the motto "never apologise, never explain" can safely be followed. It is necessary for regulators to explain the basis on which they take their decisions, and to be prepared to defend the trade-offs they make in the political and public arena. It is an environment in which politicians wish to hold an institution accountable for decisions and for the outcomes of difficult cases.

I have already had occasion to ask myself whether I am in practice so enthusiastic about this régime of accountability. But, abstracting from my personal position within it, I believe it to be preferable to the situation which we had before, where it was very difficult for Parliament and the public to understand just who was responsible for individual regulatory problems and their resolution. There is no doubt that, in the US and the UK, financial regulators now have a considerably higher profile than they do in many other countries, whether they seek it or not. I suspect this is an irreversible trend.

My conclusion, from the experience to date, is therefore that the arguments advanced for integrated regulation have, broadly speaking, been borne out in practice. Certainly I am sure that I can speak for the management of the FSA in its entirety when I say that we have become more convinced of the benefits of integrated regulation rather than less. It is for others to judge our success overall. But, in spite of our disagreements with parts of the market on individual cases, we have maintained broad support both from practitioners and from consumers who, in repeated surveys, have confirmed their support for the principle of a single regulator.

But while the general principle of integrated regulation is not seriously challenged in London, there are loud debates under way elsewhere. So, before I conclude, I might offer a few observations on the main arguments which have been advanced against integrated regulation in the form we practice it, in countries where the question remains under debate.

3. The criticisms of integrated regulation

Five main criticisms have been advanced against the FSA model:

- (i) That there is the fundamental incompatibility between prudential and conduct of business regulation, making it appropriate to manage those strands of regulation in different institutions.
- (ii) That divorcing prudential regulation, particularly of banks, from the central bank is dangerous, reducing the central bank's ability to monitor financial stability and respond to threats to it.
- (iii) That the single regulator divorced from the central bank may adopt a purely domestic focus, driven by its conduct of business concerns, thus ignoring the important international dimension of regulation.
- (iv) That a single regulator responsible for the whole financial sector may be an over-mighty institution, inclined to act in a high-handed manner, which may perhaps damage the markets.
- (v) That a very broad regulator with an extensive reach, may lack expertise and focus on the problems of individual sectors, and may lose touch with the markets as a result.

On the first point, I have already given my view.

The second argument, about the impact on the central bank, is one which has generated considerable debate in many continental European countries, and also in the United States. Since I was, before I became Chairman of the FSA, the Deputy Governor of the Bank of England, and remain a director of the Bank, I do see both sides of this question myself. And indeed in 1996 I was happy to advance the arguments in favour of continued central bank involvement in banking supervision. Occasionally, I have been teased by commentators as a result. In response, I would advance the famous Keynes observation to the effect that when the facts changed, he changed his opinion. And, on this issue, I have certainly changed mine.

As I have said earlier, there are those who argue that there is a necessary incompatibility between a central bank's monetary policy responsibilities and the rôle of prudential supervisor. Interestingly, a key argument advanced in the Netherlands for their new arrangements, whereby the central bank will remain responsible for the prudential supervision of banking and be linked into prudential insurance regulation is that it is now reasonable to confirm the Nederlandsche Bank's regulatory functions, precisely because it no longer controls monetary policy. I can understand this argument, though I have to say that I did not see any examples, during my time at the Bank of England, of circumstances in which the Bank's view on monetary policy was distorted by its banking supervision responsibilities. My observation was that the functions were separately managed, with relatively little cross-fertilisation between them, rather than that one exerted an excessive influence over the other.

Most of the practical business banking supervision from day to day, month to month and year to year, is quite remote from the monetary policy process. The overall rules on capital must be set with an eye to financial stability, of course, but in practice what supervisors do is interpret and police those rules, and engage in a regular dialogue with individual institutions on the capital treatment of particular assets, the way the institution is managing those risks, the competence of its senior people etc. None of this activity is of any interest to those who determine interest rates or who manage the payments system.

There is an enormous overlap between this work and the work of other prudential supervisors in other sectors and between financial conduct of business regulation, as I have explained. There is almost no overlap with the work of the Monetary Analysis Division at the Bank of England.

That is not to say, of course, that the monetary policymakers are uninterested in what goes on in the banking system, or financial institutions and markets more generally. And our arrangements in the UK ensure that there are structural links between the FSA and the Bank of England, and a proper two-way flow of information. Our Memorandum of Understanding requires us "to establish information sharing arrangements to ensure that all information which is or may be relevant to the discharge of their respective responsibilities will be shared fully and freely". In particular, in the area of macro-prudential analysis, the Bank and the FSA share and discuss at all levels a large volume of information and analysis on economic and financial developments and the implications for financial stability. We also fully share information on potential problems emerging in the financial sector, which is especially important at the times of stress both for monetary policy and for risks to the payments system. There is no need for the central bank to collect this data directly. And, crucially, these information flows between the regulator and the central bank are set within the context of a tripartite arrangement to monitor financial stability, in which the Treasury is closely involved.

In my view, and I speak both as Chairman of the FSA and as a director of the Bank of England, these new arrangements have created a much better flow of information around the system, and have given the authorities a better insight into important part of financial markets than they had before. Of course the Bank of England had a privileged position in the banking system when it was a banking supervisor, but it had no formal relationships with the then separate securities and insurance regulators. With the new arrangements the Bank's perspective through the information provided to it by the FSA gives it a broader view of financial market developments. And as risks are transferred around the system, particularly between banks and insurance companies, this broader perspective assumes particular significance.

I would note, too, that the Bank of England's financial stability work has developed enormously in the last 4 years. The work done in the context of the Bank's Financial Stability Review is widely acknowledged as influential both domestically and internationally. Certainly we find the Bank's perspective, unclouded by the needs to manage the grubby day to day supervisory relationships, to be a crucial input into our own work.

The third argument which has been advanced as a criticism of the UK system is that a single financial services regulator has an exclusively domestic mandate, while central banks are more internationally focused and therefore better able to take account of the cross-border implications of difficulties arising in the financial system in a particular country. The point was made in an ECB paper last year.

As I look at the FSA's travel budget, and at the number of international committees and working groups of which we are the UK member (somewhere north of 100) I find it difficult to take this argument seriously. We play a substantial rôle in bilateral and multilateral co-operation with financial services regulators and other authorities throughout the world. Indeed it can be argued that the FSA is a considerably more effective contributor than was ever possible when the regulatory responsibilities in the UK were split between 10 separate financial services regulators.

Another variation of this argument for the central bank as supervisor, also advanced by the ECB, is that a central bank can be a more effective banking supervisor because it is more independent than non-central bank regulators. There may be some justification in this argument in some developing and transition countries, where the central bank stands (almost) alone as an institution with independence from political interference, with status and reputation, and with the resources to recruit and retain high calibre staff. In these circumstances the effectiveness of regulation could be compromised if the function were removed from the central bank. But the argument has little or no validity in most developed economies, where the independence of non-central banks financial services regulators can be achieved (as, for example, in the UK) through legislation that draws an appropriate balance between independence and accountability.

Indeed, it is the opposite argument which is more often heard in the UK, where the FSA has at times been characterised as over-mighty and as a law unto itself. We have not typically been described as under the Treasury's thumb – indeed I cannot recall that point being made.

The "over-mighty subject" argument is, in my view, one with potentially more substance. There is inevitably some risk that a very broad regulator, will be seen to represent too large an agglomeration of power and responsibility. This is a point to which a regulator must give serious attention. I hope that our structures, with separate decision-making bodies for all disciplinary cases, with statutory consultation processes and statutory consumer and practitioner panels, will help us to preserve a reputation as a balanced and reasonable exerciser of our powers. But the only proof of that will be in our record.

The last argument, which is perhaps a second cousin of the "over-mighty" charge, is that a very broad regulator may lose focus on the problems of individual sectors, and may lose targeted expertise.

Once again, I have to acknowledge this as a risk. Certainly we need to ensure, in our recruitment and training policies, that we maintain centres of expertise on the full range of regulatory disciplines within the organisation.

So far, I would see little evidence that it is becoming more difficult to do so. Indeed the FSA is attractive in the marketplace, partly because it is, for those with an interest in regulation, the only game in town, but also because it allows people to achieve useful cross-fertilisation between their own areas of expertise and others which may relate to them.

Conclusion

It would be idle to pretend that these debates on regulatory structure will quickly be resolved in one direction, or another. I would certainly acknowledge that there are well-functioning examples of a wide range of different regulatory systems in operation around the world today. It is perfectly possible to run the functionally-based system well, it is possible to run a "twin peaks" system satisfactorily. There are excellent central bank regulators, and excellent non-central bank regulators. I am comfortable with our own new model, and in the particular circumstances of the United Kingdom and the City of London. But far be it for me to argue that it is the only workable solution. And I am sorry when institutions, in defence of their own particular structure, seek to demonstrate fundamental flaws in models which do not happen to be their own. That has not been my approach tonight. And, indeed, it is crucial that, as supervisors, we respect each others' expertise and each others' systems. The international regulatory network depends crucially on good co-operation and good collaboration across borders, between institutions with respect for each other.