

Rewriting the Rulebook

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Financial Services analysis: How will the Prudential Regulation Authority's (PRA) proposed changes to the Handbook affect financial services lawyers? Dr Rob Purves, a barrister at 3 Verulam Buildings in London, comments on the PRA's proposals.

Original news

PRA consults on changes to Handbook rules, LNB News 14/08/2015 79

The PRA is in the process of redrafting certain modules of its Handbook to create a Rulebook containing only current PRA rules. A consultation seeks views, among other proposals, on replacing guidance and rules relevant to financial conglomerates, third country banking and investment groups, group risk systems and control requirements, and general provisions on reporting. The deadline for comment is 13 November 2015.

What is the purpose of the proposals?

Many of the rules currently applied by the PRA and forming part of the current 'PRA Handbook' were made by the Financial Services Authority (FSA) and simply 'designated' as PRA rules (ie adopted by the PRA) at 'cutover' on 1 April 2014. This consultation paper is part of a planned series of consultations aimed at replace the PRA Handbook to create a new-look 'PRA Rulebook'.

What are the PRA's proposals?

Replacement of PRA Handbook rules and guidance applicable to financial conglomerates

The PRA explains that the main proposed changes to the legacy rules in this area are:

- o to replace them with equivalent references to the Rulebook or delete them where they are no longer relevant
- o to amend them to reflect the transposition of Solvency II (Directive 2009/138/EC)
- o to clarify their application in order to distinguish between rules which apply to members of a financial conglomerate for which the PRA is the co-ordinator, and members of a financial conglomerate for which the Financial Conduct Authority (FCA) or another EEA supervisory authority is the co-ordinator
- o to delete text where it is considered unnecessary, with no change to meaning or content, and
- o to make a consequential amendment to the notifications part of the Rulebook to reflect that firms must provide evidence to justify a change in financial conglomerate status

Specifically, the PRA proposes:

- o to replace GENPRU 3.1 (cross sector groups) and GENPRU 3 Annex 1 (Capital adequacy calculations for financial conglomerates) with a new Part of the PRA Rulebook entitled 'Financial Conglomerates'
- o to delete GENPRU 3.1.37R on the grounds that the relevant sectoral rules already apply group requirements at the level of a mixed financial holding company
- o to move to the PRA's website some existing guidance in GENPRU 3.1 and GENPRU 3 Annex 1 on the identification of financial conglomerates
- o to incorporate in the financial conglomerates part of the Rulebook, material relevant to financial conglomerates previously contained in (a) SYSC 12 (group risk systems and controls requirements) in particular SYSC 12.1.11R and 12.1.12R; and (b) GENPRU 3.2 (third country groups) in particular GENPRU 3.2.8R, and GENPRU 3 Annex 2
- o to move to the PRA's website some existing guidance on waivers and modifications under the Financial Groups Directive (the FGD) in GENPRU 3.1, in particular GENPRU 3.1.13G, and the form and explanatory notes on identifying a financial conglomerate in GENPRU 3 Annex 3, and

- o to move to the PRA's website some existing guidance in GENPRU 3.1 on waivers and modifications available under the FGD

The PRA indicates that:

- o the draft rules in the financial conglomerates part of the Rulebook are in substance the same as those currently detailed in GENPRU 3.1 and GENPRU 3 Annex 1, and
- o it does not expect that firms should need to amend their reporting practices as a result of the proposals in this consultation

Replacement of PRA Handbook rules and guidance applicable to third country banking and investment groups

The PRA proposes to replace the rules relevant to banking and investment groups in GENPRU 3.2 (third country groups) with a new chapter, 'Third country banking and investment groups', in the groups part of the PRA Rulebook.

The PRA indicates that:

- o the draft rules will apply to banks, building societies and PRA-designated investment firms, and
- o for insurance groups, the provisions of Solvency II regarding third country groups have been previously transposed into the PRA Rulebook

Replacement of PRA Handbook rules and guidance relating to group risk systems and controls

The PRA explains that the main proposed changes to the legacy rules in this area are:

- o to replace references to the Handbook rules with equivalent references to the PRA Rulebook, or delete them where they are no longer relevant
- o to delete text where it is considered unnecessary, with no change to meaning or content
- o to impose the requirement previously in SYSC 12.1.13 (CRR firms and non-CRR firms that are parent financial holding companies in a Member State) by applying specified Rulebook parts at the level of the consolidation group on a consolidated (or sub-consolidated) basis--general organisational requirements, skills, knowledge and expertise, and risk control
- o to delete without restating guidance on the responsibility for group systems and controls in SYSC 12.1.20G to 12.1.22G

As regards the deletion of the guidance in SYSC 12.1.20G to 12.1.22G, the PRA indicates that:

- o expectations that individual firms retain responsibility for functions outsourced to other group members are covered in the outsourcing part of the Rulebook', and
- o the fact that all PRA or FCA regulated entities have joint responsibility for group systems and controls where there are multiple regulated entities in the same group is a function of how the systems and controls related parts of the Rulebook have been applied at different levels within a group

Replacement of PRA Handbook rules and guidance relating to regulatory reporting

The PRA proposes to replace the rules in SUP 16.3 (general provisions on reporting) and SUP 16.6 (compliance reports) with new rules in the regulatory reporting part of the PRA Rulebook.

The PRA indicates that the proposed rules are in substance the same as those currently detailed in SUP 16.3 and SUP 16.6 of the Handbook, with no change in the scope of firms to which the rules apply. Therefore, the PRA does not expect that firms should need to amend their reporting practices 'in any substantive way' as a result of the proposed changes.

Consequential changes to and deletions from the PRA Handbook

The PRA proposes amendments to the PRA Handbook Glossary, the Credit Unions Sourcebook and the Senior Management Arrangements, Systems and Controls Sourcebook as a result of, and to come into force at the same time as, the deletion of GENPRU 3 and SYSC 12.

In addition, the PRA proposes to delete the following parts of the PRA Handbook at the same time as and for the purpose of 'the final move away from the PRA Handbook':

- o chapter 1 of COBS--this application provision is no longer required as the rest of COBS has been deleted from the PRA Handbook
- o the transitional provisions and schedules of SUP, GEN and SYSC--all the provisions to which these transitionals are relevant having been deleted from the PRA Handbook
- o chapters 16.1 (application) to 16.3 (general provisions on reporting) of SUP--the relevant reporting requirements in SUP have been, or are proposed to be, transposed into the Rulebook
- o GEN 2 (interpreting the Handbook)--this relates to interpreting the Handbook which will no longer be relevant when all existing Handbook content has been rewritten or deleted, and
- o the glossary, as this will no longer be relevant when all existing Handbook content has been rewritten or deleted

A new provision on Rulebook interpretation

The PRA proposes to insert the following rule into the interpretative provisions part of the PRA Rulebook:

'2.2A In the PRA Rulebook an expression in italics that has no meaning given in any of the relevant Part, the PRA Rulebook Glossary, FSMA or the Interpretation Act 1978 but that was defined in the PRA Handbook as at [DATE] has that meaning.'

The intended effect of this provision appears to be to preserve the PRA Handbook meaning of a defined term (at a specified date), but only if there is no definition elsewhere.

How should lawyers and their clients prepare for the proposed changes?

As originally conceived, the PRA intended that its Rulebook (which now appears online in a relatively user-friendly form) would be clearer, more concise and (unlike the FSA Handbook, which was replete with embedded guidance) consist only of rules.

Specifically, the PRA indicated that it did not intend to issue detailed guidance to clarify its policy. The intention was that if, in the PRA's judgment, guidance material was required, the material would be issued in and the form of 'supervisory statements'.

The PRA's expectation was that supervisory statements would be 'focused on the PRA's expectations, aimed at facilitating firms' judgement in determining whether they meet these expectations, and will not be overly detailed'.

This consultation paper neatly demonstrates the difficulties inherent in the reshaping of the PRA Handbook along those lines. Although the vision was for a Rulebook stripped of guidance and accompanied only by concise supervisory statements, the PRA now preserves some of the old FSA guidance material outside of the Rulebook, on the PRA website. For example, in relation to the preserved guidance on financial conglomerates the PRA indicates that it 'expects that firms will find this guidance helpful when assessing themselves against the criteria laid out in the Financial Conglomerates Part as part of the identification of the firm as a financial conglomerate'. Firms might legitimately reply 'quite so'. The FSA Handbook may have been wordy in places, but guidance was generally given for good reason, not simply out of a desire to be unnecessarily prolix.

Perhaps ironically, the PRA seems to be on the way to replicating in part the outcome under the FSA, in which Handbook provisions were accompanied by a vast array of 'non-Handbook normative material'--that is, material relevant an understanding of the regulator's policy or approach, but published outside the Handbook.

As a matter of public law, however, all such material is and remains relevant to any challenge to regulatory policy or action.

The PRA say that the draft rules accompanying this consultation paper do not represent a policy change. However, firms and their advisers would be well advised to consider whether their understanding of particular rules rested on guidance that is now deleted, and if so, to document the basis for continuing to hold that understanding.

Interviewed by David Bowden.

The views expressed by our Legal Analysis interviewees are not necessarily those of the proprietor



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