Dear Andrew

Special Measures - PRA Statement of Policy

We have discussed the Parliamentary Commission on Banking Standards (PCBS) recommendation that regulators be equipped with a new “special measures” tool to identify and tackle serious failings in standards and culture within banks.

The Financial Services and Markets Act 2000, as amended by the Financial Services Act 2012, already enables us to take actions akin to those set out in the PCBS report, such as imposing requirements on a firm, requiring them to enter into formal commitments to take actions we think appropriate, and requiring them to appoint an independent monitor to ensure compliance. While this power was available in FSMA’s original form, it was linked to varying a firm’s permissions when a firm was failing or was likely to fail to meet its threshold conditions, or to protect consumers\(^1\) - a measure which would appear on the firm’s public register entry and which may damage public confidence.

The position of the PRA under the new FSMA is different. The requirements power is not linked to permissions, so we can easily frame requirements on a stand-alone basis – and we do not need to publicise requirements if we feel it would be prejudicial to the safety and soundness of a firm. We can also not only use this power to defend threshold conditions, but also to support “safety and soundness” in general. However to address the recommendations of the PCBS report the PRA will publish a statement of policy in 2014, which will explain in greater detail the tools available to us, and how the PRA’s expected use of its powers can respond to the scenarios envisaged in the PCBS report.

The statement will also describe the way in which the PRA will use its supervisory approach and statutory powers to pro-actively tackle failings in standards and culture in firms. The new (post 2012 Act) Threshold Conditions are central to our approach to supervision, and are now assessed on a continuous basis\(^2\), with consideration of “the manner of the firm’s compliance” with our requirements\(^3\). This includes the character of firms and addresses the need for compliance with the spirit as well as the letter of our Conditions. In order to address your concerns that dual regulation may overlook systemic cultural weaknesses, the statement will also explain the importance that the PRA and the FCA place on co-operation and co-ordination in this area.

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\(^1\) The Financial Services Act 2010 widened grounds to include “financial stability”

\(^2\) The Prudential Regulation Authority’s approach to banking supervision, para 15

\(^3\) FSMA, Schedule 6, Part 1E, para 5D
Finally, there are no cultural barriers in the PRA to imposing requirements to deal with a firm’s failings. We do not view using these powers as a sign of supervisory failure, and firms know that we expect them to have a culture which supports prudent management – we “expect firms not merely to meet the letter of the requirements… but to maintain sight of the overall principle of their safety and soundness and act accordingly”\textsuperscript{4}. Furthermore our proactive intervention framework (PIF) unambiguously sets out when and why firms can expect intensified supervision and formal action from us in line with the PCBS’ desire for a bank to “be subject to intensive and frequent monitoring.”

We look forward to the opportunity to address your recommendations and clarify our powers in the forthcoming statement of policy.

Yours sincerely,

Andrew Bailey

\textsuperscript{4} The Prudential Regulation Authority’s approach to banking supervision, para 36