Bank of England PRA

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15 January 2025

Dear Prime Minister, Chancellor and Secretary of State,

Thank you for your letter of 24 December regarding the Government's approach to regulation in the UK.

The PRA recognises and strongly supports the Government's focus on delivering a higher rate of sustainable economic growth in the UK, and on encouraging responsible risk-taking in support of that goal.

All of the PRA's objectives are designed to support economic growth. However, there is a distinction between our primary objectives, to promote safety and soundness of banks and insurers and protection for policyholders, and our secondary objectives to facilitate competition, competitiveness and growth.

Our primary objectives speak mainly to stability, which is the basis for a predictable economic environment that allows households and businesses to be confident in planning ahead and making investment and hiring decisions. Financial instability can lead to severe disruptions to the ability of households and businesses to make transactions, manage risks, and access credit, amplifying economic shocks and hindering growth.

But your letter speaks more to our secondary objectives – and in particular to our new secondary objective to facilitate the competitiveness and growth of the UK economy. I will therefore focus mainly on that aspect of our work in this response.

Actions the PRA has recently taken to advance competitiveness and growth

As you anticipate in your letter, we have already taken a number of actions in order to advance our competitiveness and growth objective since it came into operation on 29 August 2023. We have adopted a simple framework to guide our efforts in this area, in that we see our main impact on competitiveness and growth as being through three channels: the allocation of capital in the UK economy; how well UK banks and insurers are equipped to compete; and how attractive the UK is as a location for foreign banks and insurers. We have found that this framework provides a useful guide for us in thinking about how our activities can support growth.

Amongst the wide set of actions we have already taken I would highlight the following:

- We are currently in the process of implementing an update to banking regulation, known as '**Basel 3.1**', which aims to make bank capital requirements more reflective of the risks taken by firms. This is not a domestically-driven change, but an international reform in which we need to play our part in order to maintain both stability in the event of shocks and the UK's reputation as a responsible host of a very large global financial centre. These standards also provide a basis for effective international competition between banks. There is, however, scope to tailor the international rules for our market and we have used this scope to make important adjustments, including in response to industry feedback, to support competitiveness and growth – with the most material ones being changes to lower capital requirements in order to support lending to SMEs and infrastructure and to support trade finance. We have also ensured that the reform does not increase overall capital requirements for the UK banking system in any meaningful way.
- We have now implemented the new **Solvency UK prudential regime for insurers**. These reforms simplified overly complex and detailed EU requirements, while maintaining strong prudential standards. They also made material changes to the capital regime for insurers by reforming the Matching Adjustment rules in line with the legislative framework set by government, enabling the life insurance sector to play a bigger role in investing in the UK economy across a wider range of assets.[1]
- **Removing the 'bonus cap' for banks**. We have worked with the FCA to remove the so-called 'bonus cap', a measure we inherited from the EU which set a fixed

[1] The Matching Adjustment is an important part of the capital regime for insurers which provide pensions.

limit on the ratio between bankers' bonuses and salaries. This had the effect of inflating banker salaries which we considered unhelpful for safety and soundness, but was particularly damaging for competitiveness – both for UK firms and for foreign firms deciding whether to locate major banking operations in the UK. Removing the cap dealt with these problems and sent a strong signal to firms here and abroad about our willingness to make changes to rules to support competitiveness and growth in the financial services sector.

- Working with the FCA and HM Treasury to **review the Senior Managers and Certification Regime** (SM&CR). We have run an exercise in order to understand stakeholders' views on the functioning of the SM&CR and to identify ways to improve the regime and help it work better for firms and regulators, while preserving its underlying aims. Alongside steps announced by the Chancellor to replace the Certification Regime with a more proportionate approach, we will make additional changes to reduce bureaucracy and increase flexibility in the Senior Managers Regime.
- Driving improvements in our operational efficiency in order to support activity in the markets we regulate. This work had had a particular focus on the **timely handling of authorisation applications**, where we are now running consistently in line with our service standards – with 100% of cases meeting those standards across all categories in the most recent quarter, though more normally we would expect to have a few complex or difficult cases take longer and see this percentage in the high 90s.

Further actions the PRA intends to take

You asked what further actions we can take in the coming period to support growth. We are developing initiatives, in consultation with industry, in a number of areas that will contribute to growth once implemented:

- **Simplifying the prudential regime for small banks.** Since leaving the EU we have already simplified two key areas of our regime for small banks – liquidity and disclosure requirements. We are now consulting on the next leg of this package of reforms (known as 'Strong and Simple'), under which we have proposed a very material simplification of capital requirements for small banks. The aim of this work is to enhance effective competition and competitiveness by enabling a dynamic and diverse banking sector in the UK, without making the sector more fragile, thereby increasing the sector's efficiency and productivity. It will also lower costs for small firms without increasing riskiness, which will enhance their resilience and ability to support their customers and so the economy. Finalisation of the regime is dependent on the final implementation of the Basel 3.1 standards mentioned above, on which we are liaising closely with HM Treasury.

- **Increasing the ability of the insurance sector to invest in the UK economy.** As noted above, the PRA last year made policy changes to enable life insurers to play an increased role in investing in the UK economy. As part of our consultation with industry on these changes, we have identified industry appetite for a new facility to allow firms to make investments more rapidly while waiting for full regulatory permissions. To this end, we plan to consult this year on establishing a 'Matching Adjustment Investment Accelerator'. This innovation would reduce barriers to investment by insurance firms, enabling them to deliver more quickly on their commitments to make additional investments in the UK and so support economic growth. We have also been taking part in discussions with HM Treasury, the National Wealth Fund and the insurance industry to help them explore whether the NWF can generate investment opportunities with an economic profile that works for insurers.
- **Improving the UK framework for Insurance Special Purpose Vehicles (ISPVs), including simplifying and accelerating the ISPV authorisation process.** ISPVs are specialised vehicles which allow investors to provide capital to insure a variety of risks, often used to cover losses from major catastrophes such as hurricane damage (sometimes called 'catastrophe bonds'). To date, the majority of such entities have been set up in other international jurisdictions such as Bermuda. This year we plan to make changes to the UK framework for ISPVs, which should contribute to the UK's international competitiveness and growth by making it more desirable to establish UK ISPVs, and providing more diversification opportunities for investors and additional sources of capital and reinsurance capacity.
- **Making further amendments to remuneration requirements to enhance competitiveness.** In addition to the removal of the bonus cap, we are now consulting on some other major amendments to our remuneration requirements for banks, which would enhance growth and competitiveness of the banking sector while maintaining its resilience. The changes would substantially reduce the period over which senior bankers' bonuses are deferred, in which area our current rules have become something of an international outlier.
- **Simplifying regulatory data reporting from banks.** As part of our Solvency UK reforms we have already cut reporting from insurers by around a third, leading to substantial efficiency gains and supporting the sector's competitiveness. We intend this year to identify opportunities to focus our data collections from banks, cutting little-used or duplicative data collections in order to reduce the burden on firms while still meeting the needs of day-to-day supervision and policymaking. We would also like to explore further whether there is scope and industry appetite for reforms to how we collect data (as distinct from what we collect), in order to drive potentially material cost efficiencies for firms. The aim of this work is to ensure that we get the data we need at the lowest possible cost to industry, but as per our conversations with HM Treasury it will require some upfront investment funded through the PRA

levy in order to realise these benefits and we intend to discuss this with the industry and FCA.

Beyond these five areas, we would like to explore with colleagues in HM Treasury and the Department of Business and Trade whether there are wider changes which could help to simplify and rationalise the UK regulatory regime or support UK growth in other ways. At this stage our thinking on these items is less developed than those above, but we would welcome a discussion with government on them to see if they are worth pursuing further:

- **'Concierge service' for new inbound foreign firms.** There has at times been some interest from industry in the idea of a 'concierge service' to help foreign firms navigate the UK when thinking about locating new businesses here – a comparison is sometimes made with the approach of the Monetary Authority of Singapore takes in this area, which we have examined closely. We could potentially work up a proposal for such a service this year, but would need to liaise with the FCA, the Office for Investment and potentially other stakeholders in thinking about how to approach this.
- **Rationalising the UK financial services regulators' 'have regards'.** The number of principles that the PRA is required to 'have regard' to has substantially increased in recent years, increasing the complexity of the analysis required when making or amending regulation. Depending on how they are counted, the PRA currently has around 25 such 'have regards'. Under the current framework we pay close attention to these 'have regards' and expect to be held to account for them when exercising our powers. However, there is scope to rationalise some of these 'have regards' where they form a cluster, for instance in the set of 'have regards' which relate to climate and the environment. By rationalising, we think there is an opportunity to simplify the length and complexity of the analysis underpinning future regulations, with consequential benefits for the cost of regulatory engagement by firms and the efficient use of resources by the PRA.
- **Looking for potential overlaps between the PRA's governance and disclosure requirements and those of legislation or other relevant regulators.** As we review our regulatory requirements on bank reporting, we will also be alert to any potential overlap between our requirements of banks and insurers and those of legislation or other regulators. With this in mind, we could explore with government colleagues and other relevant regulators whether there are any ways in which we might join up further or reduce overlap across new financial sector reporting requirements.

We look forward to continuing to work with the Government to help it achieve its mission of driving economic growth and stand ready to discuss this important topic as required.

Yours sincerely

Sam Woods

Deputy Governor and CEO, Prudential Regulation Authority