HM Treasury

Financial Services (Banking Reform) Bill

Government Amendments: Regulators' powers over holding companies

Briefing for Peers **October 2013**

Rules to facilitate resolution

The Special Resolution Regime in the Banking Act 2009 is designed to give the authorities appropriate powers to deal with the failure of a bank in a way which minimises the effects on the wider financial system and financial stability, and protects access to critical services.

Banks may be organised in a number of different ways. It is common for large UK banks to have a structure where the bank (or banks), which is an entity regulated by the Prudential Regulatory Authority (PRA) or Financial Conduct Authority (FCA), is owned by a financial holding company. This holding company often is not a regulated entity itself. Banks may also be part of corporate groups that contain non-banking entities.

There may be significant interdependencies between entities within the same group. These may be financial in nature (for example, where capital and debt are issued out of a holding company and down-streamed to the bank subsidiary) or operational (for example, a service company in another part of the group may provide critical services to the bank, which are essential for its continued operation).

These interdependencies provide many benefits – however, they also have the potential for complicating a resolution of the bank or the banking group.

The PRA FCA already have powers to require regulated entities to take actions that would facilitate the resolution of the firm in the event of its failure. This may include, for example, requiring regulated entities to raise additional capital or issue debt to the market. It may also include requirements to make structural changes which ensure that the firm can be resolved effectively.

However, there may be cases where this is not sufficient – in particular where the regulated entity is not in a position of control and therefore cannot itself deliver the desired result. This may be the case in groups where group companies who provide services to the regulated entity concerned are not owned by the regulated entity but are owned by the parent undertaking, or where the banking subsidiary is dependent on capital and debt issued by a parent undertaking. Under the current law, the PRA and the FCA's powers to make rules in relation to parent undertakings which are holding companies of a regulated entity are very limited.

Therefore, this amendment will introduce a new power which will enable the appropriate regulator (either the PRA or the FCA depending on the firm in question) to impose rules on qualifying parent undertakings for the purposes

of requiring arrangements to be made that would, in the opinion of the regulator, allow or facilitate the exercise of resolution powers in relation to the qualifying parent undertaking or any subsidiary undertakings. A qualifying parent undertaking is a parent undertaking which is a UK company (or at least a company with a place of business in the UK) which is also an insurance holding company, a financial holding company, a mixed financial holding company or a financial institution.[1] It is not an authorised person itself (or a recognised investment exchange or clearing house).

This rule-making power will increase certainty for firms by introducing uniform arrangements in a transparent and consistent manner across a certain class of qualifying parent undertakings.

Group ring-fencing rules

Ring-fencing will require banking groups to make a number of structural changes to ensure the independence of the ring-fenced bank from other entities in its group for governance, operational and financial purposes. This insulates ring-fenced banks against the potential failure of group members. To make certain that the groups in which ring-fenced banks sit are structured and governed appropriately the regulator may in certain circumstances need to make rules applying to the parent company of a ring-fenced group. Parent companies can influence subsidiaries in a number of important ways, for example through their attitude to risk management throughout the group.

The Government is therefore giving the appropriate regulator the ability to make rules applying to UK incorporated parent companies of ring-fenced banks to support the objectives of ring-fencing. While the PRA already has the ability to direct individual parent companies to take certain actions, a rule-making power will enable the regulator to apply ring-fencing requirements consistently to all parent companies of ring-fenced bodies. The PRA will need to consult on these rules and publish a full cost benefit analysis. It will also have to report to Parliament about the way it uses these rules.

Further Enquiries

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2. For access to publications please go to www.gov.uk/government/policies/creating-stronger-and-safer-banks

[1] As defined in article 1(2) of the Financial Services and Markets Act 2000 (Prescribed Financial Institutions) Order 2013.