

8 September 2011

Sent by email to: financial.reform@hmtreasury.gsi.gov.uk

Dear Sirs,

HM Treasury Consultation: A new approach to financial regulation: the blueprint for reform

The IMA represents the asset management industry operating in the UK. Our Members include independent fund managers, the investment arms of retail banks, life insurers and investment banks, and the managers of occupational pension schemes.

They are responsible for the management of around £3.9 trillion of assets, which are invested on behalf of clients globally. These include authorised investment funds, institutional funds (e.g. pensions and life funds), private client accounts and a wide range of pooled investment vehicles. As an example, our members manage client positions which in aggregate exceed 40% of the UK stock market.

We welcome the opportunity to comment on this consultation.

Overall

- The absence of competitiveness as a “have regard” is a serious flaw.
- The provisions relating to the FSCS, both governance and powers, and the scheme rules need complete revision;
- Certainty about which firms will be regulated by which regulator is essential, especially within groups and for asset managers with insurance subsidiaries;
- The suppression of details concerning the PRA veto should be a matter for HMT Treasury, not the PRA.
- The so-called product intervention clauses as drafted allow almost unfettered intervention in any business relationship;
- The importance of the client asset protection function at FCA requires it to feature in co-ordination and consultation obligations by PRA.
- The Regulated Activities Order and permission regime reflects out of date and unmappable provisions unfit for the single market.

Consultation Questions

In answering, we refer to clauses of the Bill as clauses and sections proposed to be inserted into FSMA by those clauses as “new Section”.

Box 2.A: Consultation question

1. *Do you have any specific views on the proposals for the FPC as described above and in Chapters 3 and 4?*

We do not have any specific comments about the objectives of the FPC as set out in section 9C. We welcome new section 9E(2), the duty to seek to avoid prejudicing the advancing by the FCA and PRA of their objectives. New section 9E(3)(c) is also welcome, the need to have regard to the international obligations of the UK; this is a concept we would like to see advanced to the FCA (and PRA).

Box 2.B: Consultation question

2. *Do you have any specific views on the proposals for the Bank of England's regulation of RCHs, settlement and payment systems as described above and in Chapters 3 and 4?*

We do not given it is now decided that RCHs will be regulated by the Bank of England. We agree that the regulation of CREST and the nature of the RCH regime compared to the European approach, especially under EMIR, will need review (your paragraph 2.38). We welcome the requirements under new Schedule 17A for a MoU between the Bank and the FCA and PRA.

Box 2.C: Consultation questions

3. *Do you have any comments on:*

- *the proposed crisis management arrangements; and*
- *the proposals for minor and technical changes to the Special Resolution Regime as described above and in Chapters 3 and 4?*

The crisis management arrangements are uncontroversial at such high-level; we await the outcome of the FSB and European Commission work in this area to which we are responding.

We do however note that the original separation of powers between FSA and the Bank of England secured under section 7 of the Banking Act 2009 are arguably diminished by the PRA and Bank now needing to consult one another and for the PRA to agree that the threshold conditions are no longer met. Given the policy behind section 7 to use FSA was a safeguard, Government ought at least to review any impacts from this now being transferred to a subsidiary of the Bank of England.

In similar fashion to concerns we have raised with the FSB, we think that the issue of recovery and resolution plans and other crisis management issues have not sufficiently considered the role of the FCA as the body principally responsible for client asset protection policy.

Otherwise, we support the SRR proposals.

Box 2.D: Consultation question

4. *Do you have any comments on the objectives and scope of the PRA, as described above and in Chapters 3 and 4?*

A significant issue for firms presently is uncertainty as to which of FCA and PRA will be their lead or only regulator. It is critical that this is made clear as soon as practicable and ahead of the Bill's consideration. We are informed that messages from FSA and HMT are not consistent. Firms should know where they might stand. The draft order on splitting responsibilities should be provided to the pre-legislative scrutiny committee.

Many IMA members are within insurance-owned groups, some in bank-groups, but most are in neither. Of those not in insurance groups, many will have insurance subsidiaries for the sole purpose of writing unit-linked reinsurance contracts. We had asked for these to stay with FCA. We think the order should make provision to allow these connected companies to be FCA-regulated where they only write these unit-linked contracts.

We understand that each firm will be looked at separately and therefore no BIPRU 125K asset manager will be regulated by PRA even if a parent or sister company is a bank or insurer. This will mean that many FCA-regulated firms will have a single and subservient PRA-regulated subsidiary for contractual purposes. We consider the approach of the Bill and the draft documents on approach by the PRA and FCA presume that PRA's involvement will be where the group is by its nature PRA-regulated. It is important to note that the listing of numbers of firms said to be conducted and prudentially regulated by FCA may not tell the whole story for asset managers. Unless exempted, this use of reinsurance will permit PRA to have involvement in groups which in policy terms were probably meant for FCA alone. That alone will add to the complexity of running an asset manager in the UK and we would question the policy benefit in so doing.

In addition, PRA will have a power to designate other types of firm. It is not clear whether the PRA's statements about this proposed power and those of HMT are consistent. We have **annexed** an internal IMA note on the current statements about scope from the Authorities. Clarity through the publication of a draft order as the Bill proceeds is necessary. .

Clause 5, new section 2B: we question whether the PRA's objectives are overly focussed upon the UK. We would expect a provision such as at new section 9E(3)(c) for the FPC to be replicated here.

Clause 5, new section 3B: the regulatory principles are to include "responsibilities, in relation to compliance with requirements imposed by or under this Act, of the senior management of persons subject to those requirements". However section 2(3) of FSMA refers to the broader "responsibilities of those who manage the affairs of authorised persons." It is not clear whether there is a policy change here.

Box 2.E: Consultation question

5. Do you have any comments on the detailed arrangements for the PRA described above and in Chapters 3 and 4?

We have recorded in the previous consultation our concerns over the veto power and the risks that some banks will be over-protected; if not only through its use, but through FCA's perception of when it might be vetoed. Generally we think the FPC as well as FCA should be consulted; so section 3J(1) needs amending. As regards publication we think that it is for HM Treasury not PRA to judge the public interest. So section 3J (7) should refer to HM Treasury. Thus HM Treasury will lay a copy before Parliament and notify and publish as the public interest demands. More specifically, we propose that the power

under new section 3H should never be able to be exercised in relation to any power given to FCA to prosecute a PRA-authorized person or bring a market abuse action against the same.

We are of the view there should be a single independently-appointed complaints commissioner able to determine all FCA and PRA complaints; this would prevent coordination complaints falling between two stools (The Part 2 in each of New Schedules 1ZA and 1ZB). The appointment and removal should be by HM Treasury.

We note PRA has no power to make statutory general guidance (as opposed to guidance on objectives under new section 2H). It would be helpful to understand whether it is expected the PRA will ever issue anything other than a rule (our comments about FSA guidance and other material under section 7 is relevant).

There will be benefits in having a more formalised process of engagement with (but not accountability to) practitioners, particularly in the early years, at least to address overlap and underlap in regulation between the new twin peaks. The changes being made are complex and unforeseen impacts will arise; the Practitioner Panel could assist in this area and Government should re-consider its position in this regard.

Box 2.F: Consultation question

6. Do you have any views on the FCA's objectives – including its competition remit – as set out above and in Chapters 3 and 4?

We agree the objectives save as stated below.

We maintain our disagreement with Government over the absence of competitiveness as a particular issue to which the regulators must have regard. We have examples where the FSA has decided not to introduce rules to allow certain fund arrangements where these are available in Luxembourg or Dublin under European legislation. The obvious result is that funds are manufactured in those jurisdictions and passported into the UK. It may be that the judgement is correct but the point is that it should be made with an explicit regard to the position of other countries in the Single Market. We believe this issue links to our concern that the PRA's objectives are overly focussed upon the UK. We would expect a provision such as at new section 9E(3)(c) for the FPC to be replicated here.

Clause 5, new section 1D (the integrity objective) is critical in the absence of an explicit safety and soundness objective (such as for PRA's firms at new Section 2B(2)) since the FCA will have a role in ensuring safety and soundness in relation to critically important market infrastructure.

Clause 5, new section 3B: regulatory principles include "responsibilities, in relation to compliance with requirements imposed by or under this Act, of the senior management of persons subject to those requirements". However FSMA section 2(3) referred to the broader "responsibilities of those who manage the affairs of authorised persons." It is not clear whether there is a policy change here.

Box 2.G: Consultation question

7. Do you have any views on the proactive regulatory approach of the FCA, detailed above and in Chapters 3 and 4?

The New Section 137C is almost unlimited in its width. While we understand there is a need to consider product intervention on a much more proactive basis; the proposed clauses give unprecedented power to the FCA. We think there is still a need for greater thought about how it might operate especially in relation to authorised persons providing cross border services and with contracts formed under the laws of other countries. Alongside a legitimate concern to ensure that consumers do not suffer detriment, there is a need to provide some level of legal certainty so as not to disincentive any form of product innovation in the UK.

It is unclear whether the need to use resources in the most economic and efficient manner (new section 3B(1)(a)), will lead to more s.166 reports. These are very expensive mechanisms for supervision from the point of view of firms but probably relatively cheap from the point of view of FSA and their use appears to be on the increase. The FCA paper on supervisory approach does not address this and we are concerned that this may lead to many costs associated with the FCA supervision not being apparent on the balance sheet of FCA.

FCA must be much more open to learn both from FOS but also from FSCS. More generally for the proactive approach to occur, market practitioners will have to have confidence they can speak about concerns with the FCA. At present dialogue between the industry and the Bank of England is of a different depth and quality than with the FSA. In part this arises from the FSA being the regulator but it is also about an approach which needs to be much less insular in policy formation.

We would welcome far greater clarity from the FCA on the use of its powers compared to the FSA. The publication for years of documents which most viewed as guidance, but which were not subjected to the protections provided in FSMA should not be seen as acceptable in the new regulator. Although the FSA is now taking steps to correct these errors by issuing a large number of consultation guidances, it is doing so on very short notice no doubt to preserve the status of a variety of recommendations upon transition to the FCA. We would welcome a much clearer commitment from the FCA as to how it will identify guidance and other recommendations.

Box 2.H: Consultation questions

8. *What are your views on the proposal to allow nominated parties to refer to the FCA issues that may be causing mass detriment?*

9. *What are your views on the proposal to require the FCA to set out its decision on whether a particular issue or product may be causing mass detriment and preferred course of action, and in the case of referrals from nominated parties, to do so within a set period of time?*

We have no strong views on questions 8 and 9. Widespread confidence amongst consumers will be increased when widespread concerns have an outlet which is effective. Currently an important outlet is through the press and consequent reactions by regulators; in this way there will be an additional and more formalised mechanism for evincing a regulatory response to perceived mass detriment. The existence of the power ought anyway to incentivise early consideration by the FCA of such issues (so as to avoid the unwelcome perception that it was reactive rather than proactive). The nominated parties should command respect as independent and unconflicted bodies.

Box 2.I: Consultation question

10. *Do you have any comments on the competition proposals for the FCA set out above and in Chapters 3 and 4?*

We have no better ideas than the proposed model in new sections 140A to 140H. We see the sense in repealing section 164.

Box 2.J: Consultation question

11. *Do you have any views on the proposals for markets regulation by the FCA, described above and in Chapters 3 and 4?*

We support or have no objection to the proposed measures.

This is reference at several points (for example paragraph 1.40) to users of financial markets, such as institutional investors, being “consumers”. While we welcome the implicit acknowledgement that investors (the “buy side” of the market) are in a very different position from the “sell side” it is important that this should not translate into any suggestion that comparable levels of investor protection regulation are appropriate between retail individuals and institutional investors. Such institutional investors are in a completely different position from retail ones, and this needs to continue to be recognised.

There will be a need for close co-operation with the Bank of England in relation to its existing markets work (such as the Stocklending and Repo Committee) and its market intelligence activity and with the DMO.

Box 2.K: Consultation question

12. *Do you have any comments on the governance, accountability and transparency arrangements proposed for the FCA, as described above and in Chapters 3 and 4?*

There is a drafting error at new section 139A(5) - reference should be made in the text in subsection (3) to section 130J as well. It is an essential part of the duty of consulting on giving guidance that the regulator is obliged to have regard to any representations made to it

We would like to see a more public role for the non-executives. This could in part occur at the Annual Public Meeting but also we would like to see fuller discussions of the FCA Board’s reasoning for supporting or opposing specific rule changes. Dissenting comments should be recorded. Commonly we find the publication by the SEC of supporting and dissenting positions on regulatory issues very helpful.

It is essential that the power of HM Treasury to arrange an independent inquiry under clause 46 of the Bill extends to failures in relation to the co-operation and co-ordination duties in new section 3D. We think clause 46(2)(b)(ii) provides for this.

We note as regards annual reports the PRA must carry out a public consultation but have no annual public meeting, whilst FCA must have such a meeting but are not required to consult. Given transparency and confidence needs in society, is there a policy reason for such differences? Perhaps both should do both. (Schedule 3, paragraphs 12 and 20 refer.)

We are of the view there should be a single independently appointed complaints commissioner able to determine all FCA and PRA complaints; this would prevent co-ordination complaints falling between two stools (The Part 2 in each of New Schedules 1ZA and 1ZB). The appointment and removal should be by HM Treasury.

There are a number of legal protections which should be acknowledged by the FCA when publishing warning notices. We note the proposal to consult the person targeted by the warning notice (2.110 and new section 391(1)(c)) but there may be wider "maxwellisation" obligations. It is vital that court-made protections are not ignored or excluded without explicit intention so to act being announced by Government. In this regard we remain of the view that protections about fair comment ahead of any hearing should apply (we are unconvinced the Contempt of Court Act 1981 would provide such a protection).

We repeat our comments about the RDC and internal governance at the FCA; some of the Bill's clauses appear to reduce the level at which decisions would need to be made and the FCA paper has not explained how protections as provided by the present RDC will be preserved.

We would hope that the National Audit Office would look at the cost of data provision to the FCA very early on.

Box 2.L: Consultation question

13. Do you have any comments on the general coordination arrangements for the PRA and FCA described above and in Chapters 3 and 4?

In similar fashion to concerns we have raised with the FSB, we think that the issue of recovery and resolution plans and other crisis management issues have not sufficiently considered the role of the FCA as the body principally responsible for client asset protection policy.

We think it vital that the desire of the FCA to have better market intelligence does not lead to duplication by it (or the PRA) of work conducted at the Bank of England. We consider that the market intelligence unit of the Bank of England is likely to be the central place for a large part of the market intelligence that needs to be gathered.

Box 2.M: Consultation question

14. Do you have any views on the detail of specific regulatory processes involving the PRA and FCA, as described above and in Chapters 3 and 4?

As we stated in our response to the previous consultation, we think that the regulated activities order and the FSA register need to be fundamentally reviewed. There is no need for such a parochial and arcane system of permissions in light of European directives governing most activities of many firms. We remain to be convinced that the current system does anything other than add to costs and uncertainty. We cannot believe that consumers are assisted by having to consider several pages of permissions for a simple firm.

We consider work still needs to be done in relation to the role of the regulators in relation to firms exercising passporting rights and whether it would be more appropriate

for FCA to deal with all notifications and supervision (since prudential issues are matters for the home regulator not the UK host).

Box 2.N: Consultation question

15. *Do you have any comments on the proposals for the FSCS and FOS set out above and in Chapters 3 and 4?*

We support the involvement of the NAO in relation to FSCS and FOS.

We have previously suggested that the role of the FSCS is such that its governance and powers should be reviewed. The size and nature of its role in compensation and resolution suggest that it should be seen as a stand-alone entity whose rules are made or approved by HM Treasury. We also consider that the FSCS could have its own rule-making powers to facilitate its activities, for example in relation to single customer views and other preparedness issues.

Above all these issues however we remain concerned that the Bill leaves at large questions over the structure of the scheme, its rules on funding and issues such as cross-subsidy. Leaving aside all the debates on cross-subsidy (cross-subsidies must end), it is fundamentally wrong that the maximum levy upon IMA firms is proportionately about twice what is imposed upon intermediaries.

We are unconvinced that the high-level co-operation duties will ensure the regulators will seek to learn lessons from the FSCS's experiences of defaults or how FSCS will be able to marshal the regulators to assist in ensuring the cost of failure is apportioned appropriately. In this regard, we have in mind the Keydata debacle; we would have expected that alongside investors being compensated, the FSCS could have required reviews to be carried out at firms who might contribute to the ultimate funding of the losses. And if FSCS itself could not have forced a review, it should have a formal power to require FCA so to act. It is wrong that the fund management industry had to find £223M but FSCS could not go direct to any firm to see if it should make a contribution, based on the firm's own liability for failure, despite them being regulated. Moreover FSA should have required a review and for investors to be told whether there had been any advice failures – to date many may think their intermediary has being wholly compliant (as some may have).

We think as well that it should be made clear that whilst the FSCS will commonly pay out investors upon a default, it would be within its powers (perhaps exceptionally) to "wait and see". This might involve a declaration that a person has suffered detriment but that payment of some or all of what might be the measure of damages can await what happens to a product. Thus if a person bought a 5 year bond and expected no payout till that 5th year, it may still do justice to see if the performance is as the person wanted (notwithstanding that an intermediary has defaulted and perhaps failed in making the right disclosures). We are not seeking to keep consumers from payment, we trust our approach to Keydata shows that ensuring investors were duly compensated was a real concern for our members, but we do think that the FSCS should be seen as a mature body in the regulatory system and not merely asked to act as a mechanical based upon rules made at a time when (as will always occur) some events were just not foreseen.

In case there is a risk that cross-subsidy might persist, we would note that many of our members are manufacturers of an approved product – a UK authorised fund (UCITS or

national) - they should be seen as a class ring-fenced from any liability to firms which intermediate securities. At present there appears to be better regulatory treatment in terms of FSCS risks of a firm if it manufactures a fund in continental Europe and passports it in to the UK than vice versa. The historic problem with the FSCS sub-classes partly arises because most classes are organised on a manufacturer/distributor basis – insurance and mortgages are such examples. The issue with investments is that most manufacturers are issuers (PLCs and SPVs) and so do not fall within the FSCS ambit. This has caused FSA previously to require fund manufacturers to be the sole subsidising body for distributors of a range of products unconnected with funds. This is patently unfair, in the sense not of moral outrage, but damaging to the attractiveness of the UK as a place to do business.

In relation to FOS, we have noted the proposed duty, in new section 230A (see Schedule 10) to publish a report of a determination unless the ombudsman deems it inappropriate. We consider FOS should be required to have regard to basic safeguards prior to publication - such as ensuring any individuals named have been consulted (we appreciate that compared to publishing a warning notice by FCA this is after determination – nevertheless some individuals may have had no opportunity to comment).

Conclusion

Government is right to review the regulatory system and the draft bill is a start. There are, as our response has shown, several other areas needing real reform to secure the UK regulatory regime's fitness for purpose.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'Guy Sears', written in a cursive style.

Guy Sears,
Director, Wholesale

Annex relating to question 4

Current thoughts on scope.

HMT's February paper described the Government's policy. Relevant extracts are annexed and should be read.

The June 2011 paper addresses scope at 2.54 to 2.59. It makes it clear that Government does not intend the face of the bill will define scope but rather the new section 22A will empower HMT to designate both what is a PRA-regulated *activity* and to confer functions on the PRA itself to develop designation criteria for identifying PRA-regulated *firms*.

This matches the proposal at 3.23 from the February paper – whereby two classes of firms will in effect be designated (and notwithstanding any individual firm's systemic significance). These firms will be all those with deposit-taking or insurance permission (a class-based activity designation). It also matches the proposal introduced at 3.23 and developed in 3.24-3.25 whereby PRA will set out criteria against which it will determine which additional specific firms will be PRA-regulated (an objective firm designation).

The power appears to envisage PRA designating firms in addition to insurers and deposit-takers as opposed to de-designating insignificant insurance companies or deposit-takers.

Formally at this stage the new section 22A to be introduced by clause 6 of the draft Bill is at large and provides no limit in practice to what might become a PRA-regulated activity (beyond limits arising from PRA's objectives). However the new s.22A may be seen as objectionable by the pre-legislative scrutiny committee as it allows HMT by order to confer powers upon PRA. If such powers allow *firms* to be designated as opposed to *activities* being designated, when s.22A only mentions activities, then this may be an excessive delegation from Parliament. If however PRA was obliged always to use criteria which linked back to an activity then that would likely narrow what they could ever designate – it is unlikely anyone would find it acceptable if PRA stated that the first criteria for deciding whether to designate was that a firm carried on any regulated activity; thus PRA will need to express a limited set of activities along with other criteria. This activity-linked approach to designating particular firms is consonant with the Government papers to date and Box 2 below which is from the PRA paper on its new approach to supervision.

In all these the activity mentioned is "dealing as principal". But this alone is still too wide since the policy expectation is that the designated firm "could pose significant risks to the stability of the financial system or to one or more PRA-regulated entities within their group". Introducing a qualification that limits the class to BIPRU 730K firms (see 3.25) would beyond doubt remove all IMA members – some do have "dealing as principal" permissions, though it is often historic or for very technical reasons. A BIPRU 730K firm is one that is not a BIPRU 125K, BIPRU 50K or UCITS investment firm.

IMA members are BIPRU 125K or UCITS investment firms. As regards the latter we might not expect that PRA has an interest in these even if technically some can deal as principal in box management.

A BIPRU 125K firm (most non-UCITS IMA firms) is one which it “does not deal on own account or underwrite issues of financial instruments on a firm commitment basis”.

Dealing on own account is not the same as dealing as principal.

It is often conflated and it may be that the shorthand of the HMT paper does the same (the former refers to a service of using one’s capital; the other a legal characterisation of a transaction). So whilst the paper refers to *limiting* the class of firms which deal as principal by reference to BIPRU 730K qualifications, it is by that proposing that the test is “dealing own account by a firm with a permission to deal as principal” – and the words “with a permission to deal as principal” are then otiose. HMT may therefore be proposing that designation is limited to firms which deal on own account. However although firms which “could pose significant risks to the stability of the financial system” might be expected to be large BIPRU 730K firms, the other policy purpose in having designation is to catch the firms which “could pose significant risks to one or more PRA-regulated entities within their group”. Here it is not so clear that such a firm would need to be a large BIPRU 730K firm – but it still might not need PRA to look outside the BIPRU 730K firms as a whole.

However there is a different emphasis between the PRA paper and the HMT papers. HMT sticks to the recognised prudential class of BIPRU730K, whilst PRA acknowledges that most firms which deal as principal “are not likely to pose sufficient risk to the stability of the financial system, however, and so the PRA will develop additional criteria for designation. These criteria are likely to include: the size of a firm; the substitutability of its services; the complexity of its activities; and its interconnectedness with the financial system and any PRA-supervised companies within its group.” It is unclear whether PRA really expects readers to take the reference to dealing as principal as a hard-edged legal term in distinction to deal on own account. In other words, PRA may not be challenging the concept that they would only ever designate firms which deal on their own account.

What may be more significant is that PRA flag that it is not content with section 22A as proposed – *“consideration will be given as to whether it is desirable to recommend changes to legislation, to ensure that the PRA will be able to regulate all firms posing potentially significant risks to the financial system because their activities are in substance analogous to deposit-taking”*. This points to a power to designate members of the shadow/parallel banking system and is worthy of note (at least) by operators of money market funds.

Extracts from existing policy statements

“3.23 In addition to deposit-taking and insurance, the PRA will be able to designate certain investment firms for prudential regulation by the PRA where it determines that they could pose significant risks to the stability of the financial system or to one or more PRA-regulated entities within their group. These risks are likely to arise through the scale or complexity of such a firm’s operations and its interconnectedness with other firms or the system as a whole.

3.24 In order for PRA designation to have value, the risks posed by the firm must be of a kind that can be mitigated through prudential regulation. It is therefore envisaged that designation would apply only to firms which have permission to ‘deal in investments as principal’ and are therefore subject to substantive prudential requirements. As there are a large number of firms who have permission to carry out this regulated activity,

objective criteria will be set out in secondary legislation to refine the number of firms that are capable of being designated for prudential regulation by the PRA. Ultimately, this will be a matter of judgement for the PRA to ensure that, where it is desirable and appropriate, the PRA is responsible for the prudential regulation of certain investment firms.

3.25 It is currently proposed that investment firms that are classed as 'BIPRU €730k'² firms will be capable of being designated by the PRA. Further minimum capital requirements may also be appropriate, as well as a set of indicators for assessing whether the firm's systemic importance or interconnectedness with PRA regulated group companies require it to be prudentially regulated by the PRA. Further development of the appropriate additional criteria for firms dealing in investments as principal will form part of the PRA's development of its supervisory approach, and will be subject to consultation with firms."

Box 2 - "Other firms designated for supervision by the PRA"

Under statute, a number of firms that are neither deposit-takers nor insurance companies will be eligible to be designated for supervision by the PRA rather than the FCA, if the PRA determines that the firm could present significant risks either to the stability of the financial system or to one or more PRA-supervised entities within the firm's group.

It is currently envisaged that investment firms authorised to deal in investments as principal on their own account will be eligible for PRA designation. ('Investment firm' is a term used to describe, among other things, a firm undertaking investment banking activities.) Most of these firms are not likely to pose sufficient risk to the stability of the financial system, however, and so the PRA will develop additional criteria for designation. These criteria are likely to include: the size of a firm; the substitutability of its services; the complexity of its activities; and its interconnectedness with the financial system and any PRA-supervised companies within its group.

The PRA will consult on its proposed policy in this area in due course.

In addition to establishing clear designation criteria for firms dealing in investment as principal, consideration will be given as to whether it is desirable to recommend changes to legislation, to ensure that the PRA will be able to regulate all firms posing potentially significant risks to the financial system because their activities are in substance analogous to deposit-taking. If necessary, following consultation, the authorities will make recommendations to HM Treasury.

It will also be possible for the FPC to propose revisions to the regulatory perimeter when a particular type of unregulated activity is considered likely to pose potentially significant risks to the stability of the financial system as a whole."

Extract from PERG on Dealing on own account under MiFID

"Dealing on own account is trading against proprietary capital resulting in the conclusion of transactions in one or more MiFID financial instruments. In most cases, if you were a firm who was dealing for own account under the ISD, the FSA would expect you to be dealing on own account for the purposes of MiFID if you continue to perform the same activities.

Dealing on own account involves position-taking which includes proprietary trading and

positions arising from market-making. It can also include positions arising from client servicing, for example where a firm acts as a systematic internaliser or executes an order by taking a market or 'unmatched principal' position on its books.

Dealing on own account may be relevant to firms with a dealing in investments as principal permission in relation to MiFID financial instruments, but only where they trade financial instruments on a regular basis for their own account, as part of their MiFID business. We do not think that this activity is likely to be relevant in cases where a person acquires a long term stake in a company for strategic purposes or for most venture capital or private equity activity. Where a person invests in a venture capital fund with a view to selling its interests in the medium to long term only, in our view he is not dealing on own account for the purposes of MiFID.

In our view, where you are a firm which meets all of the conditions of article 5.2 of the recast CAD (see Q61), you will not be dealing on own account.”