BANK OF ENGLAND
PRUDENTIAL REGULATION AUTHORITY

FCA FINANCIAL CONDUCT AUTHORITY

New Bank Start-up Unit Seminar

15 October 2019

Welcome

Arran Salmon

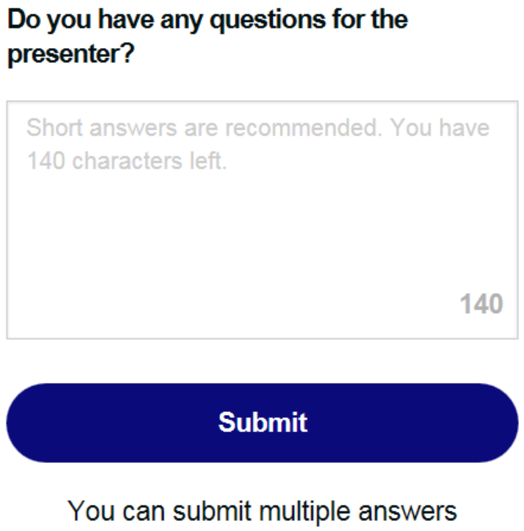
Head of New Banks, UK Deposit Takers Supervision, PRA

Agenda

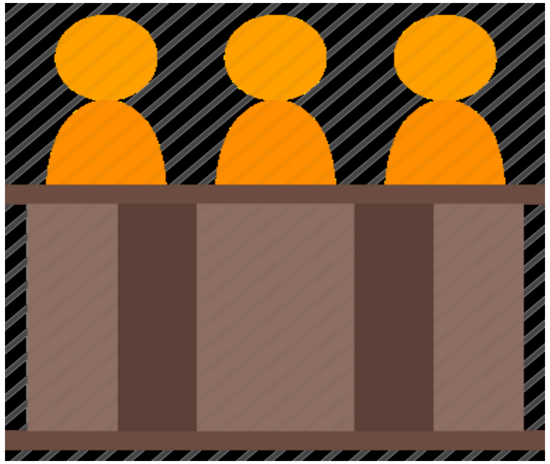
Time	Subject	Speaker
09.30 – 10.00	Arrival	
10.00 – 10.10	Welcome	Arran Salmon
10.10 – 10.30	Key note speech	Melanie Beaman
10.30 – 11.00	Becoming authorised	Arran Salmon
11.00 – 11.30	The Regulatory Business Plan	Jill Lough & Glenn Redemann
11.30 – 11.50	BREAK	
11.50 – 12.20	Governance	Jill Lough
12.20 – 13.00	Conduct Risk of Harm	Val Smith
13.00 – 13.45	LUNCH	
13.45 – 14.15	Firm observations	Monzo
14.15 – 14.45	The ICAAP	Chris Frank
14.45 – 15.15	Our supervisory approach	Russell Shotton & Peter Fox
15.15 – 15.45	Q&A	Panel
15.45 – 15.55	Closing Remarks	Arran Salmon

Got a question? Menti us!

Ask questions **anonymously, any time of the day**



Our panel will answer the most popular questions at 15:15.



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Key note speech

Melanie Beaman

Director, UK Deposit Takers Supervision, PRA

Becoming authorised:

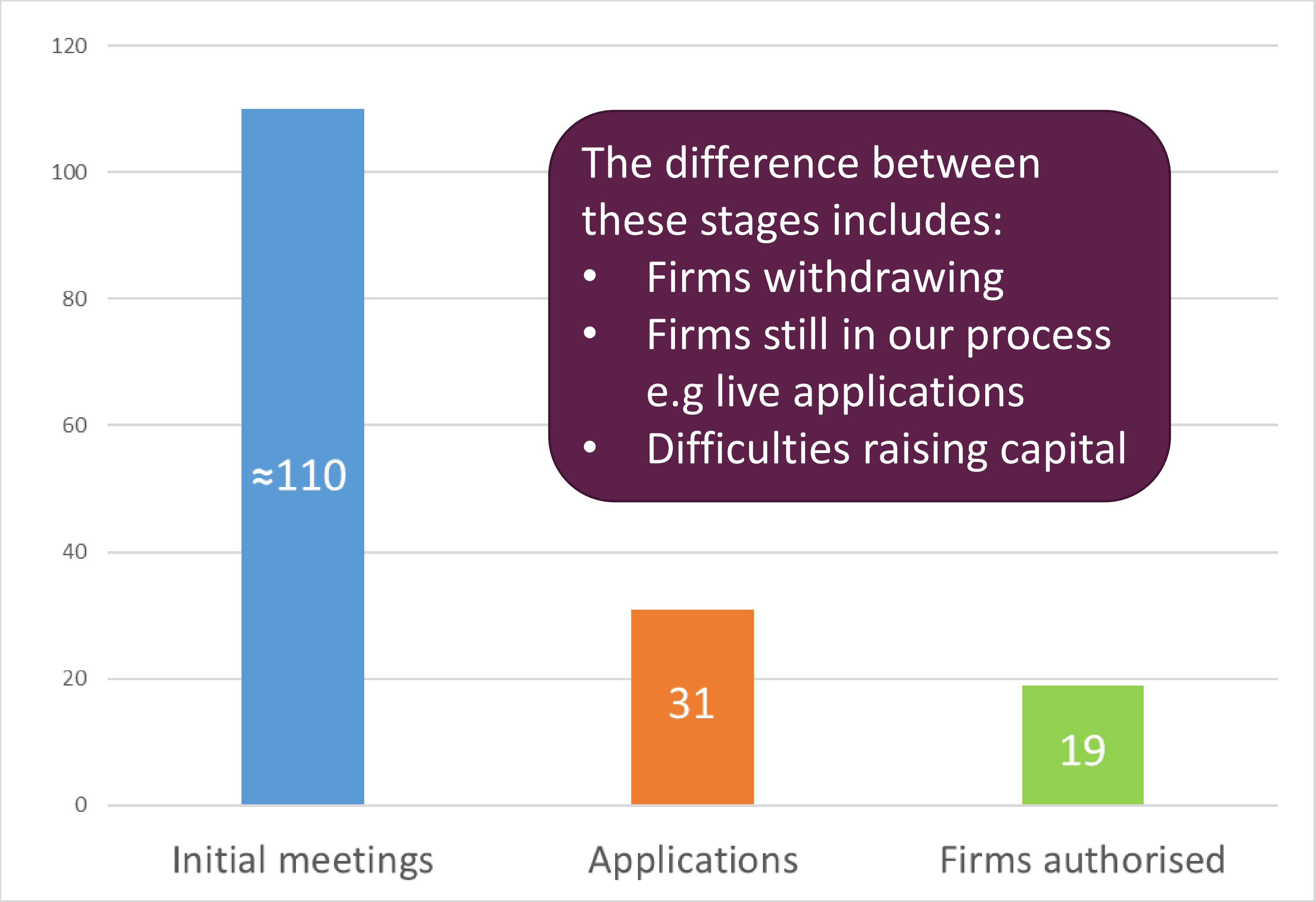
The evolution of your proposition

Arran Salmon

Head of New Banks, UK Deposit Takers Supervision, PRA

Some stats: New UK Banks

Since 2013 (until end of September 2019), there have been…

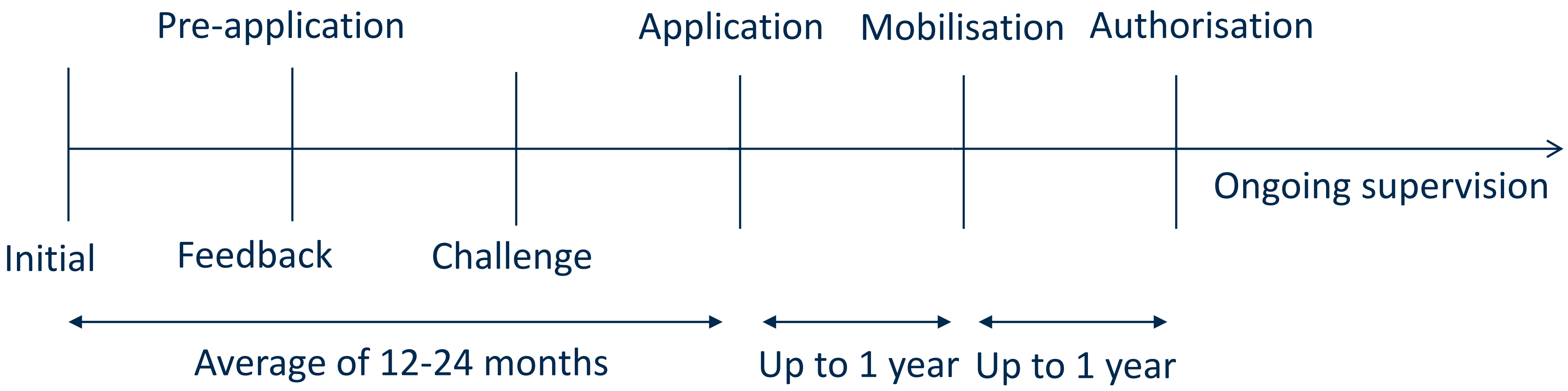


In order to navigate the process as **quickly** as possible to achieve your objective of becoming a bank, you should have:

- A **well thought through proposition**;
- Robust **challenge** and consideration of **threats/risks/harms**;
- **Clear and concise** documentation; and
- A good understanding of **regulatory requirements**.

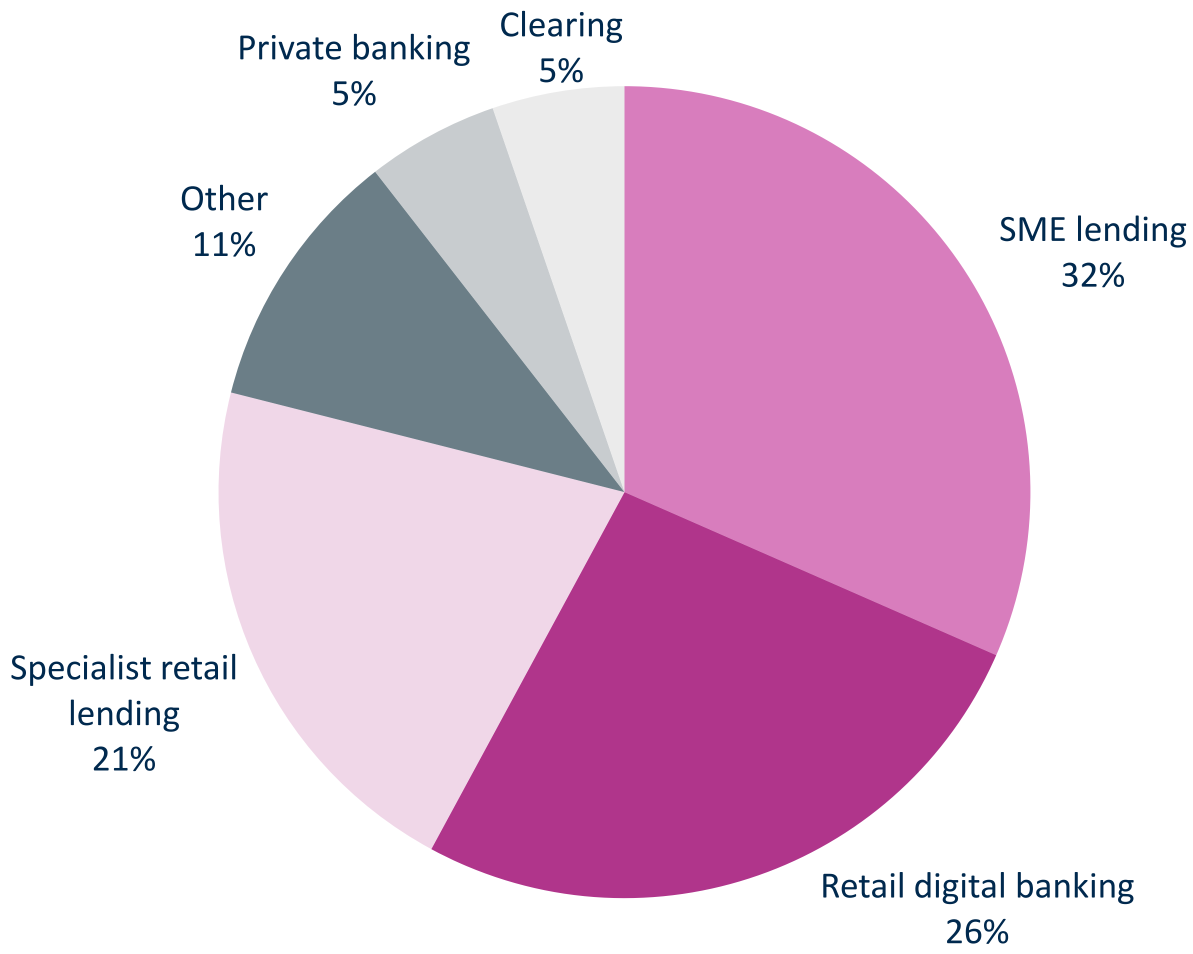
Time to authorisation

- Firms typically spend 12-24 months in pre-application before formally submitting an application.
- For firms which have used the mobilisation route, the average time firms spend in mobilisation is 8 months.



➢ **Authorisation is the <u>start</u> of your journey to being a fully established bank.**

Types of Business Model authorised since 2013



Interaction between firm and regulator objectives

We consider that firms and regulators have similar objectives

Firm objectives

- To be a **UK bank**
- To have a **viable and profitable business**
- **Treat customers fairly**

Regulator objectives

PRA

- To **promote safety and soundness** of the firms it regulates
- To **facilitate effective competition**

FCA

- To **protect consumers** and the **integrity of the UK financial system**
- To **promote effective competition in the interest of customers**

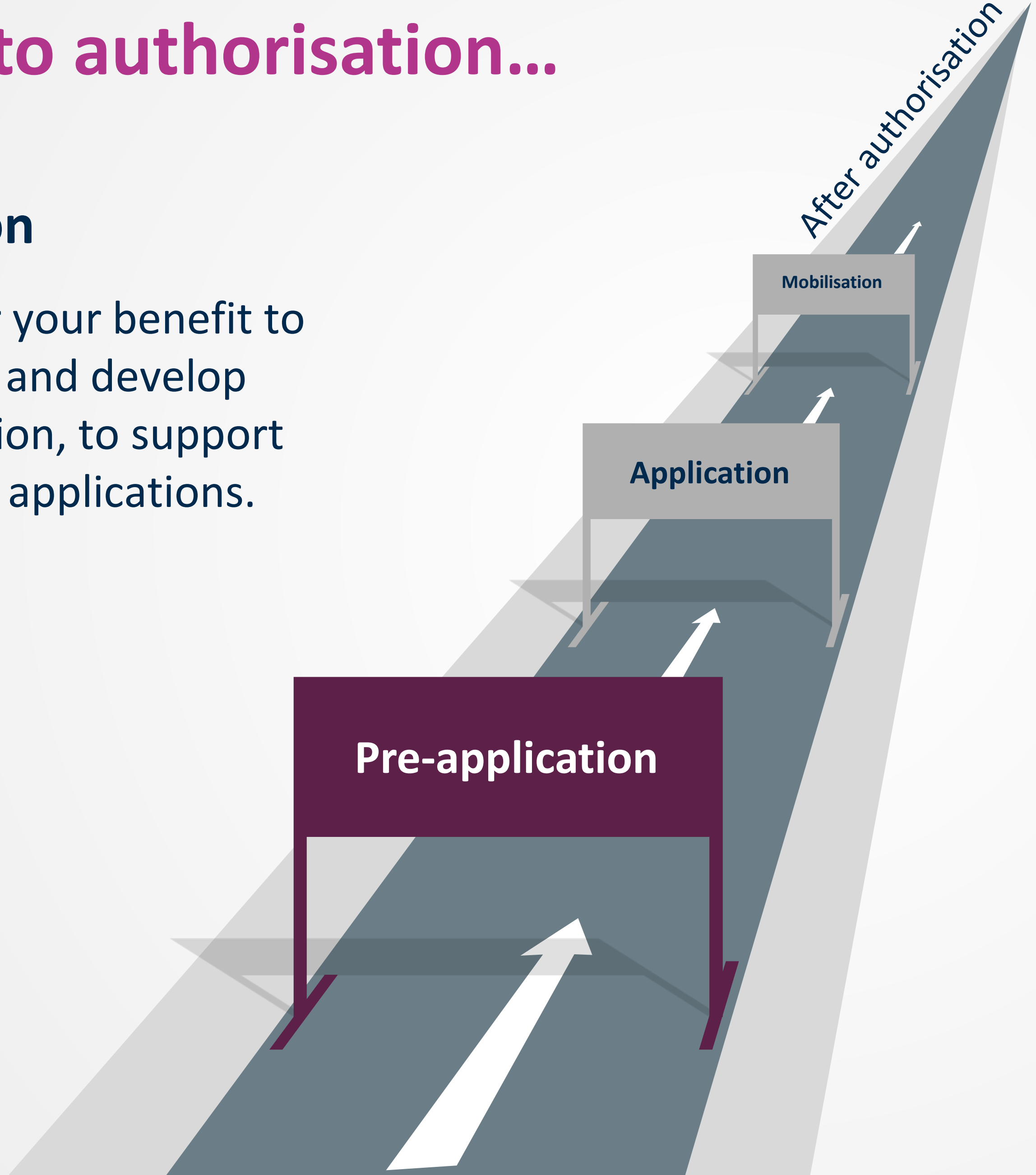
Threshold conditions

PRA	FCA
Legal Status – Deposit-takers must be bodies corporate or partnerships.	**Effective supervision –** The firm must be capable of being effectively supervised by the FCA.
Location of offices – A UK incorporated corporate body must maintain its head offices and, if one exists, its registered office in the UK.	**Appropriate non-financial resources –** The firm's non-financial resources must be appropriate in relation to the regulated activities it seeks to carry on, having regard to the FCA's operational objectives.
Prudent conduct of business – The applicant must conduct its business in a prudent matter, which includes having appropriate financial and non-financial resources.	**Suitability –** The firm must be a fit and proper person. The applicant firm's management have adequate skills and experience and act with integrity (fitness and propriety). The firm has appropriate policies and procedures in place and the firm appropriately manages conflicts of interest.
Suitability – The applicant must satisfy the PRA that it is a 'fit and proper' person with regard to all circumstances to conduct a regulated activity.	**Business model –** The firm's strategy for doing business is suitable for a person carrying on the regulated activities it undertakes or seeks to carry on and does not pose a risk to the FCA's objectives.
Effective supervision – The applicant must be capable of being effectively supervised by the PRA.	

The road to authorisation…

Pre-application

- Optional – for your benefit to better iterate and develop your proposition, to support better quality applications.



Evolution of your plans during pre-application

Early stages

Initial

- Why a bank?
- What are you going to do?
- How will you achieve this?

Feedback

- How do you plan to become profitable?
- What are the key risks and harms?
- How will you identify and mitigate these risks and harms?
- Priority areas to focus on

Challenge

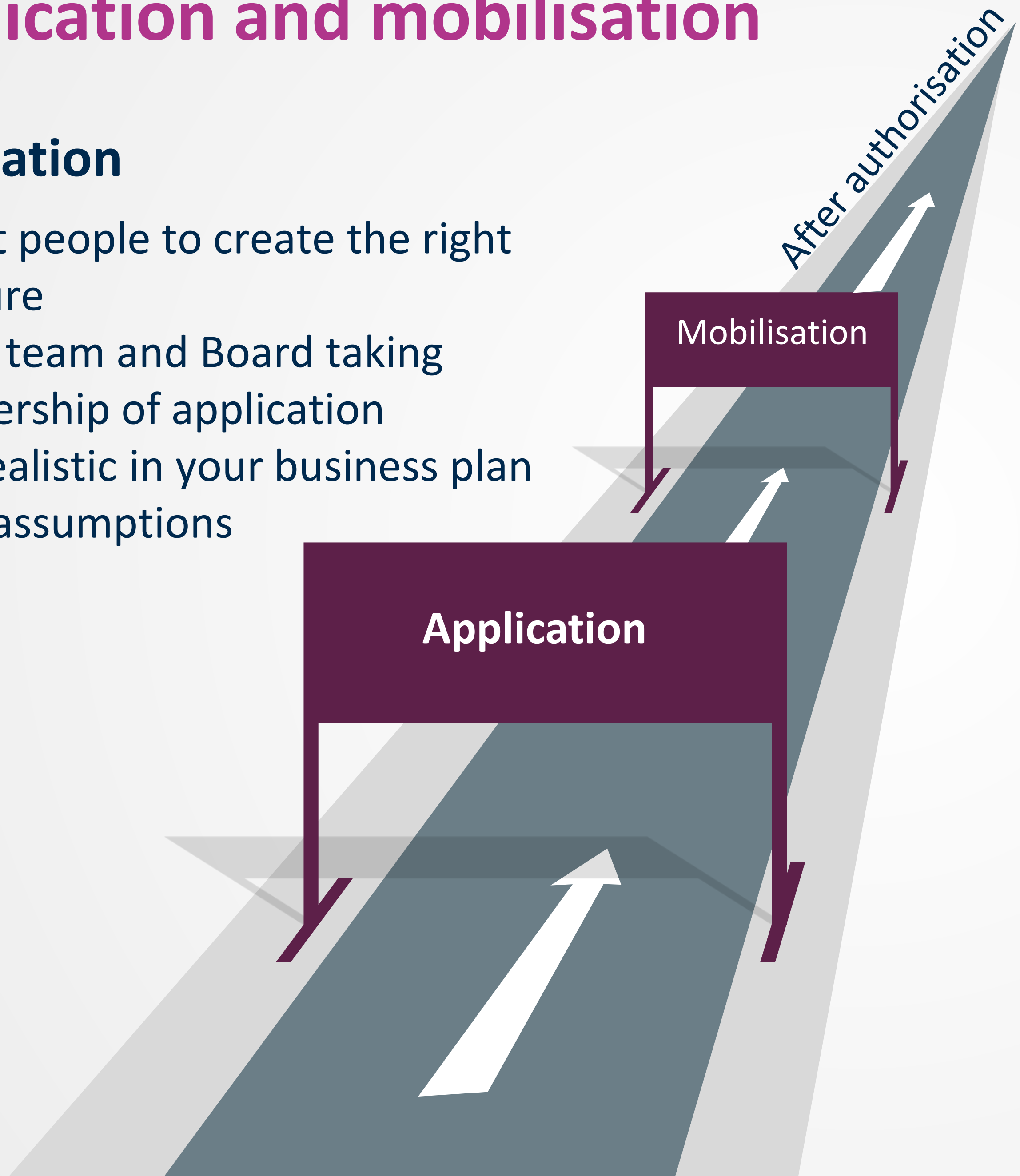
- Appraisal of near final RBP
- Won’t move to this stage if don’t address previous feedback
- Technical challenge on capital and liquidity

Submitting application

Application and mobilisation

Application

- Right people to create the right culture
- Exec team and Board taking ownership of application
- Be realistic in your business plan and assumptions



Mobilisation (optional)

- Authorisation with restriction

What are the benefits?

- Opportunity to build your bank as an authorised institution e.g.
  - Attract further investment
  - Develop IT
  - Recruit individuals

Exiting mobilisation

- Credible exit plan and Board attestation - are you ready to exit?
- Capital coverage for next 12 months
- Credible recovery plan
- Plan for how systems and controls are expected to develop

After authorisation

- The hard work does not stop there – **the end point is not getting authorised!**

- You need to continue to meet the threshold conditions on an ongoing basis.

Principles of engagement

Our expectations of you:	What you can expect of us:
• <u>Be open and honest with us.</u> Provide all information that you think we should be aware of.	• <u>Be open, honest</u> and <u>clearly set out the requirements to become a bank.</u>
• <u>Develop your plans</u>, complete the necessary work, prepare and send materials in good time for meetings with us.	• Host pre-application meetings and <u>make the process as smooth as possible</u>.
• <u>Address or incorporate any feedback</u> provided by us into your RBP before moving to the next stage.	• Provide <u>you with clear feedback on your proposals</u> including through formal written feedback.
• Understand, consider and demonstrate <u>how you will meet the required standards at authorisation and on an ongoing basis</u>.	• Help you to understand the <u>standards required of being an authorised bank</u>.

Key takeaways

- The Board is expected to take **ownership** throughout the evolution of the proposition to demonstrate how the firm will meet the PRA and FCA's **threshold conditions** at authorisation and on an ongoing basis.

- The **pre-application** and **mobilisation** stages are **optional** but for your benefit:
    - Pre-application: to better iterate and develop your proposition
    - Mobilisation: to help build out operational capabilities whilst being authorised

- Authorisation is the **start** of your journey to being a fully established bank.

Regulatory Business Plan

Jill Lough (Senior Manager, UK Deposit Takers Supervision, PRA)
Glenn Redemann (Manager - Retail, Authorisations, FCA)

Agenda

Why have we chosen to discuss Regulatory Business Plans (RBPs)?

- RBPs have become of increasing length, but not necessarily of better quality
- Poor quality RBPs slow down the process for all firms

Agenda

1. What is an RBP and who uses it?
2. What does good look like?
    - Overall Principles
    - Examples by topic

What is an RBP and who uses it?

What is an RBP?

- The key document describing your business plan:
  - It contains **what** you want to do, **why** and ***how*** the bank will be set up and make money.
- It explains the **risks** your business poses and how you will look to mitigate them.
- It is **owned** by the Board who are accountable and responsible for the oversight of running the business.

Who uses it?

For you (primarily):

- Sets out the strategy and operational plan of the bank to your Board and other stakeholders e.g. investors

Our assessment:

- Core document that will support your application
- Demonstrates that you will meet minimum criteria for becoming a bank

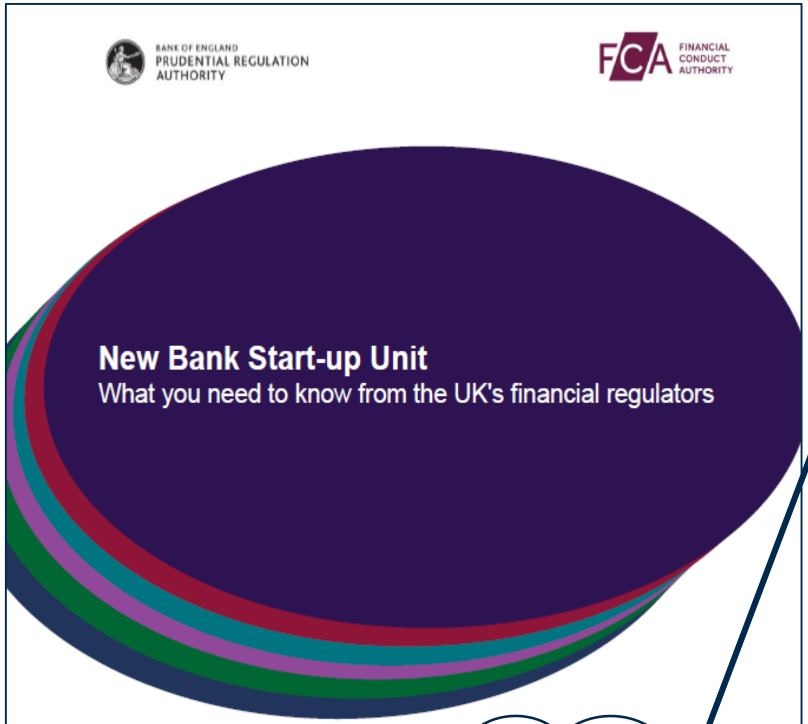
What does good look like?

Overall principles

- The RBP needs to be **owned** by the Board
- **Coherent and consistent** document
- **Quality** over quantity
- Presents a case for **viability** and **sustainability** of the proposal
- **Core assumptions** highlighted and how these were determined
- **Conduct risks** need to be considered throughout the document

What does good look like?

Extract from the NBSU guide



These topics will be discussed on the next few slides

Your fully developed RBP should include:

- ***business plan*** *– details of products, delivery channels and target market;*
- ***business viability*** *– competitive advantage, market research and how the bank will make money;*
- ***financial resources*** *– financial projections (for five years), capital (Internal Capital Adequacy Assessment Process - ICAAP) and liquidity (Internal Liquidity Adequacy Assessment - ILAAP), as appropriate;*
- *sources of funding – proposed funding model;*
- *owners and controllers –proposed owners and controllers;*
- *corporate governance – structure, board, senior management and governance arrangements;*
- ***risk management*** *– risk management and control framework;*
- ***customer journey*** *– products, pricing, complaint handling and on-boarding arrangements (including Anti-Money Laundering/Know Your Customer processes);*
- ***outsourcing*** *– details of key outsourcing arrangements;*
- ***IT*** *– IT infrastructure and systems and timescales for implementation and testing;*
- *recovery – recovery plans, if appropriate;*
- *policies and procedures – operational and regulatory policies and procedures;*
- *business continuity – business continuity plans, if appropriate;*
- *scope of permission – details of the regulated activities you wish to undertake; and*
- *mobilisation plan – project plan for mobilisation, if appropriate.*

Examples by topic: Business plan/viability

Outcome: To understand over what timeframe the business will be self-sufficient (i.e. not requiring capital injections) and if that appears plausible.

What does good look like?

1. **What are you going to do and why will this work?**
   - Clearly articulates your **USP** and **peer assessments**
   - Market research/surveys should be **specific** to your particular business
   - **Assumptions** evidenced for financial targets
2. **What are the threats that could throw you off course?**
   - Clearly demonstrates your **credit risk profile**
   - Considers how **conduct risks** could impact on the firm's viability
3. **What if things don't go according to plan?**
   - **Sensitivity analysis**/consideration of **downside risks** included
   - Consideration of **recovery** options

Examples by topic: Financial resources (capital)

Outcome: Capital structures will need to meet the Capital Requirements Regulation (CRR) Common Equity Tier 1 (CET1) eligibility requirements.

We pay particular attention to:

- Ability to absorb losses
- No barriers to recapitalisation

Firms will need to bear in mind that the pre-application process will take longer if there are more complex capital structures as the level of scrutiny and challenge will be higher.

Examples by topic: Risk management

Outcome: To understand how the key prudential and conduct risks in the business will be controlled through a practical risk management framework.

What does good look like?

Do you have sufficiently **skilled** individuals to identify risks?

What's your **risk appetite** and why? This will need to be monitored.

Clear **ownership** and **accountability** of Risk Management Framework so that risks are reported.

How will your operational model **evolve** as the business grows to manage risks?

Examples by topic: Customer Journey

Outcome: To understand the end to end customer journeys throughout the product lifecycle.

What does good look like?

- Customer journey set out clearly, identifying **risk of harm** and **mitigants**
- Clear articulation of **target customer segments** and **distribution channels**, on a product by product basis
- Clearly links the firm's **risk appetite statement** to products, thereby delivering **good customer outcomes**
- Evidence how the business model is **customer-centric** through demonstrating that potential harms and/or other conduct risks have been identified and mitigated throughout the customer journey
- Consideration of how the firm would deal with **consumer vulnerability**

Examples by topic: IT and outsourcing (1 of 2)

Outcome: Understand your IT strategy and architecture, including what is being outsourced (if anything) and how this will be managed.

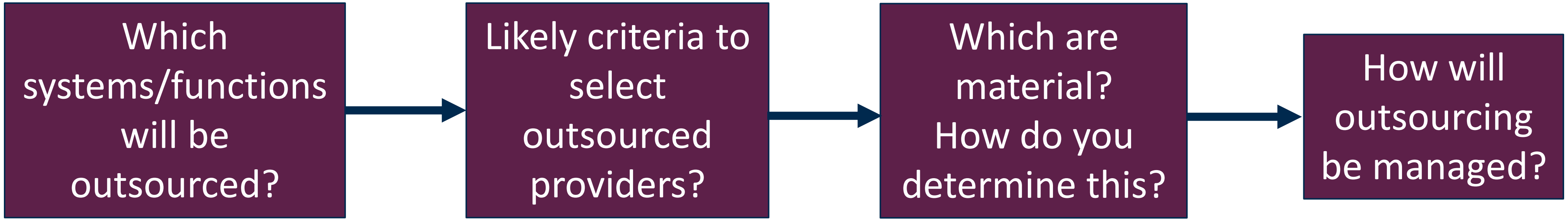
What does good look like?

IT

- Clear articulation of critical systems and processes
- Expected timelines for building and testing your IT infrastructure
- Strategy for operational resilience & cyber security

Examples by topic: IT and outsourcing (2 of 2)

Outsourcing



- Need to demonstrate adherence to regulatory expectations, including:
  - EBA guidelines on outsourcing
  - FCA's SYSC 8 requirements on outsourcing
  - The Outsourcing Part of the PRA Rulebook

Key takeaways

- **Quality** document which is **coherent** and **consistent**
- **Assumptions** evidenced and considers **downside risks**
- It is **your** business plan and should be **owned by the Board**

Break

Governance

Jill Lough

Senior Manager, UK Deposit Takers Supervision, PRA

Why does Governance matter?

What is governance?

- Corporate governance is the system by which companies are directed and controlled *(Corporate Governance Code)*.
- Key to this is the role of the board and its sub committees (also known as the governing body) in holding executive management to account effectively.

Why does it matter?

- It is **central** to any successful organisation. Its success is essential for a business to **achieve** its **objectives** and drive improvement.
- Poor governance is often a **lead indicator** of deeper issues e.g. capital/liquidity/business model/control.
- Board will **set the tone** and direction of the firm; **overseeing** and **supporting** management's efforts by **testing and probing** recommendations before approval.
- The right arrangements ensure all areas of the business have **appropriate oversight.**

What resources are available to new firms?

Senior Managers and Certification Regime (SM&CR)

- Rules and guidance aimed at increasing personal accountability of those in senior positions

EBA guidelines

- Consists of the EBA's view on appropriate supervisory practices

UK Corporate Governance Code

- Sets out standards of good practice regarding governance (comply-or-explain for listed firms only)

PRA Supervisory Statement (5/16)

- Sets out our expectations of firms and explains where we expect to focus our supervisory attention

PRA's governance rules and risk management rules

- In particular: General Organisational Requirements, Risk Control, Remuneration

FCA's Approach to Authorisation and feedback statement

- Explaining the purpose of authorisation and the approach

NBSU website

- Sets out what is expected at each stage of the pre-application stage and authorisation

Principles of good governance

- Clear roles and responsibilities
- Collective skills
- Promote transparency
- Independent oversight and challenge
- Clear policies and procedures
- Effective decision-making

What do we expect?

- The process is recognised as a journey:
    - **Pre-application** – "Guiding minds" in place and details of structure (including Board composition and other governance arrangements).
    - **Mobilisation (authorisation with restrictions)** – Independent Chairperson, CEO and one other senior executive in post as minimum. Recruitment plans and skills matrix readily available.
    - **Once authorised (with restrictions lifted)** – All key senior management in place - skills commensurate with business.

- **And remember…authorisation is the start of your journey to becoming a fully established bank.**

Common challenges for New Banks

Dominant individual(s)

Board member with material stake in business

Recruiting suitable individuals

Diversity of thought

Conflicts of interest

Appropriate MI for the Board

Key takeaway messages

Good governance is key to success

- You need to explain how the governance arrangements provide the **right oversight and challenge**.
- Recruit **suitable individuals** – particularly a **strong Chair**.
- Your governance arrangements should **evolve over time** to reflect the changing nature of your business.

Conduct Risk of Harm

Val Smith
Head of Retail, Authorisations, FCA

Purpose of this session

Understand better our thoughts around:

- The Conduct Risk of Harm Assessment.
- What harms are:
  - Our classification of harms;
  - An example of identified harms; and
  - Causes of harm.
- Conduct Risk of Harm.
- What good looks like.

Conduct Risk of Harm Assessment

Business model and strategy

- How significant could the impact of external factors be on the firm's business model?
- Is the firm's business model viable and sustainable?
- How significant are the inherent drivers of harm in the firm's business model?

Culture

- How effective is the firm in reducing the potential harm arising from the firm's business model in respect of the following:

Purpose	Leadership
People	Governance
Systems and controls	Oversight of the business

Harms

1. Pricing and quality
2. Sales and customer service / customer treatment
3. Meeting consumer needs
4. Wider effects on society
5. Market confidence and participation

If we take Sales and customer service / treatment, some of the sub-categories that we think about would be:

- Purchase of unsuitable products
- Loss of client assets / money
- Loss or misuse of personal data
- Failure to fulfil obligations to consumer
- Inappropriate treatment of consumers in financial difficulty
- Inappropriate treatment of vulnerable customers

Causes of harm

- Business model and strategy
- Governance and oversight
- Systems and controls
- Leadership and senior managers
- Operational
- Markets
- Consumers
- Anti-competitive behaviour
- External

If we take operational risks, some of the sub-categories that could cause harm are;

- Technological resilience
- Cyber resilience
- Information security (other than cyber events and attacks)
- Outsourcing of services
- Physical security

Conduct Risk of Harm

Mitigating potential harms to consumers and market integrity

Start thinking about **risk and harm mitigation** right from the start so it can:

- **Evolve** throughout your regulatory engagement.
- Help inform the structure and proposed **governance** of your business model.
- Cover the end-to-end **customer journey** for your products.
- Give consideration to how your firm would deal with **consumer vulnerability.**
- Clearly identify potential harms and **mitigants.**
- Show how your firm would create a **culture** that avoids consumer harm.
- Explain how the concept of delivering **good customer outcomes** will be embedded within your business, from culture to processes and governance link to employee remuneration.

What good looks like

Initial meeting	Feedback meeting	Challenge	Application/ mobilisation
The thinking behind conduct risk identification: • How would you define conduct risk to your business model? • How would you describe the harms in your business model?	• What are your identified conduct risks? • What are your identified harms and mitigation plans?	• Detailed assessment of identified conduct risks and accompanying mitigation plan • Near final RBP and, therefore, near final Conduct Risk Framework	• Fully formed Conduct Risk Framework embedded • Allocated SMF holder responsible

➢ **And remember… the conduct risks you face may change throughout your journey to becoming a fully established bank.**

Lunch

External Speaker

Tom Blomfield

CEO, Monzo

The ICAAP

Chris Frank

Senior Technical Specialist - Capital Assessment Team, UK Deposit Takers Supervision, PRA

Internal Capital Adequacy Assessment Process (ICAAP)

Today's Objective: To give an overview of unique ICAAP issues relevant to applicant and newly authorised firms.

Topics

1. What is the ICAAP, and how will the PRA review it?
2. How does the PRA set capital for the mobilisation period, what ICAAP issues does this create?
3. Capital Requirements at authorisation
4. Pillar 2B (P2B) Stress Testing – What is the 'Wind Down Approach' to stress testing and when / how should it be used?
5. What are some common weaknesses / pitfalls for newly authorised banks and how can they be avoided?
   a) Assessing Credit Risk under Pillar 2a (P2a)
   b) Data quality issues
   c) Risk appetite for new banks

ICAAP Overview and Expectations

What is the ICAAP?

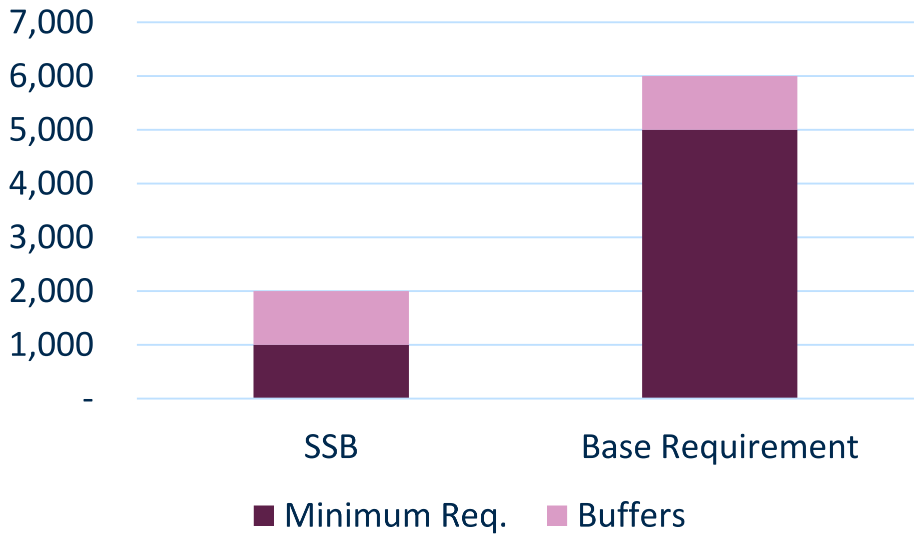
- Documented process by which **you** determine what constitutes adequate capital resources for **your** firm….
- It should be...
  - Subject to robust Governance and Board level challenge;
  - Suitable for your business model, size and risk profile (proportionate); and
  - Based on robust quantitative analysis.

In seeking and maintaining banking authorisation, firms can expect…

- To have their ICAAP assessed for adequacy as part of the application process;
- To be subject to a regular (annual) Capital - Supervisory Review and Evaluation Process (C-SREP) to ensure that the ICAAP remains adequate and proportionate to the firm's scale and risk profile;
- To be set minimum requirements for own funds and further capital buffers, based on the content of the ICAAP and the outcome of the C-SREP; and
- To be challenged on the Board's engagement with and understanding of the ICAAP risk quantifications.

Setting Capital in Mobilisation

- **The ICAAP submitted with the application should also consider the capital requirements of the bank during mobilisation separately to those required post mobilisation.**
- During mobilisation, firms may be classified as a **Small Specialist Bank (SSB)** with minimum capital requirements of the greater of £1mn or EUR1mn – so long as capital resources remain below EUR5mn (the base capital requirement) at which point EUR5mn becomes the minimum requirement.
- In addition, firms must also hold capital buffers of at least £1mn.



Capital Requirements at Authorisation

The Problem…

- The ICAAP should typically assess capital based on **actual balance sheet positions.**
- However, for many start-up banks / new authorisations: there are no material credit exposures and the balance sheet is not representative of the projected business model.

How do we determine capital requirements when no exposures exist?

The Solution…

- ICAAP undertaken on a 1 year forecast balance sheet basis at application only.
- Firms should hold sufficient capital to meet requirements at 1 year post-authorisation, throughout first year.

Key Takeaway:

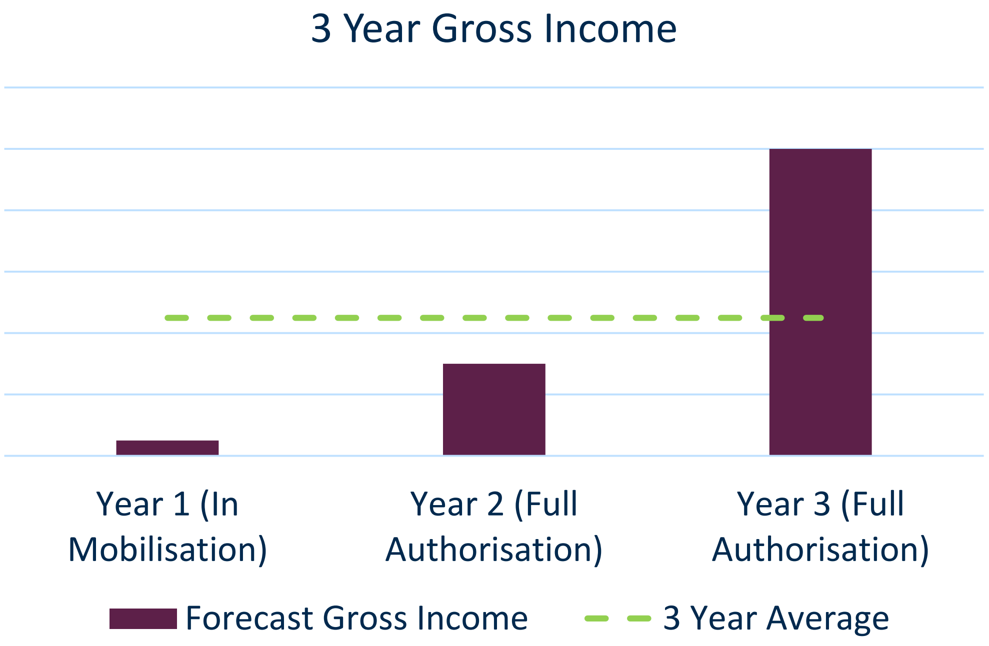
- **New bank ICAAPs should assess capital based on 1 year balance sheet forecast (in application ICAAP only) if they have no material exposures.**

Setting Capital in Mobilisation: Operational Risk Weighted Assets (RWAs)

- Pillar 1 Operational Risk Capital Requirements are based on a simple formula:
    - 15% of a 'Relevant Indicator of Operational Risk'

- This Relevant Indicator is based on the average of the last 3 years' income.

- If you don't have historical income data (i.e. because you are new), CRR requires a firm to use forecast data instead.



<u>This creates a problem…</u>

- New banks tend to grow rapidly, so forecast income in year 3 is often very large relative to the size of the firm during mobilisation.

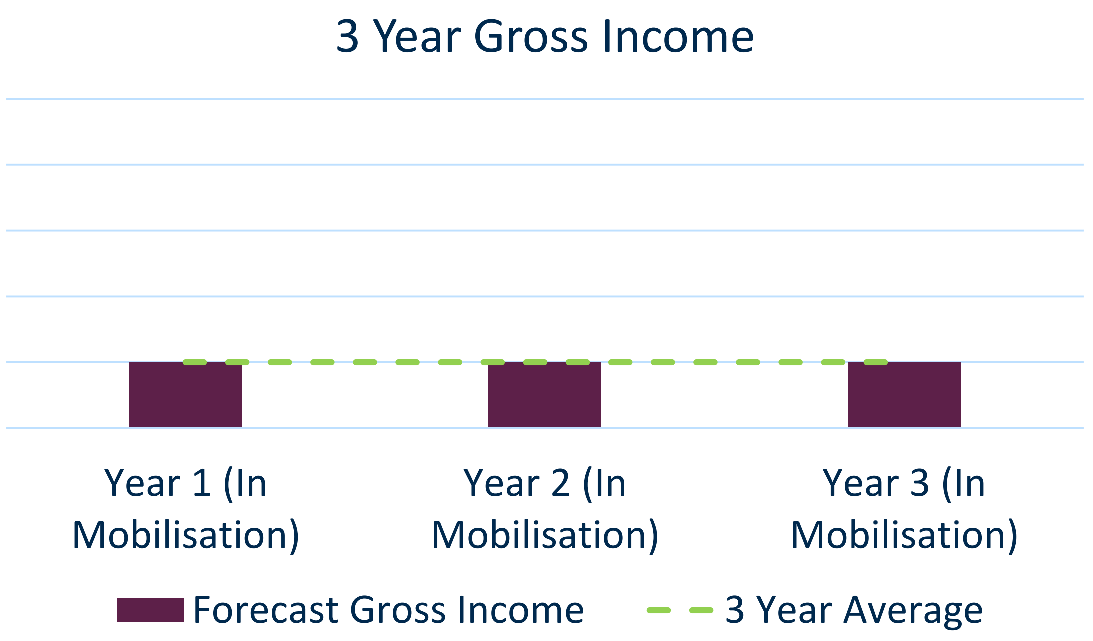
Setting Capital in Mobilisation: Operational Risk RWAs

A solution…

- **If firms are satisfied that the structure and operational risk profile that exists in mobilisation is materially different from that which would exist post mobilisation then**:

- They may consider that the post mobilisation income projections are not a **relevant indicator** of operational risks during mobilisation.

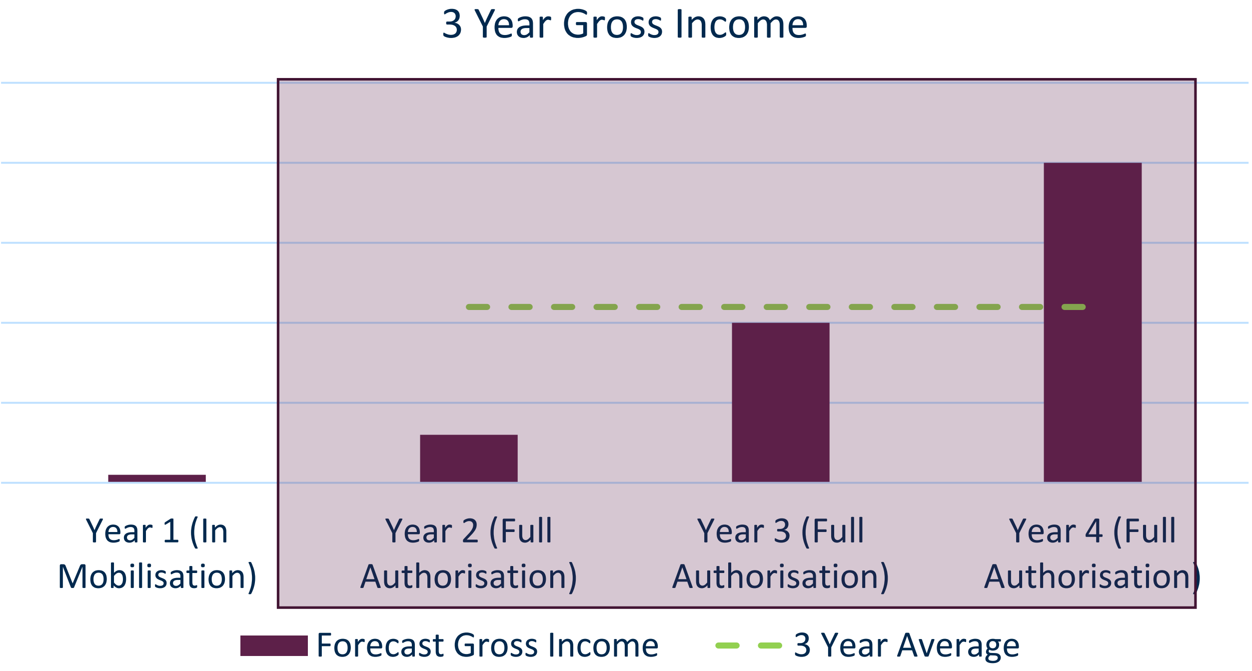
- Forecast income on the assumption that they stay in mobilisation indefinitely…



Setting Capital in Mobilisation: Operational Risk RWAs

After mobilisation…

- Firms should not include historic gross income from their time in mobilisation within the historic gross income data as it is not a relevant indicator of the firm's risk profile.



Key Takeaway:

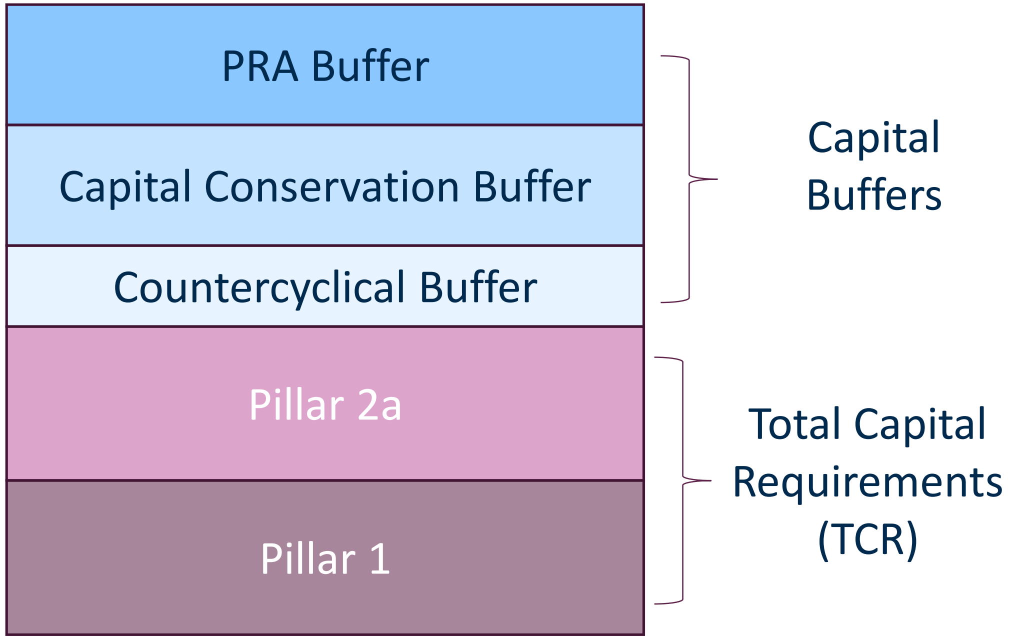
- **Operational risk profile for banks in mobilisation may differ substantially from those an authorised bank with restrictions lifted. So, when calculating operational risk pillar 1, avoid use of operational risk indicators which are not relevant by:**
  - **For mobilisation firms: forecasting income based on an assumption of staying in mobilisation**
  - **For fully authorised firms: excluding historic mobilisation income**

PRA Buffer (PRAB) for Start Up Banks

- The capital buffers sit above regulatory minima (Total Capital Requirements or TCR). They are intended to be **usable in a stress** and their purpose is to protect the bank in the event of a ‘severe but plausible’ stress.

- Some buffers (Capital Conservation & Countercyclical) are set on a formulaic basis to all firms.

- PRAB is a firm specific top-up to the formulaic buffers above: it is typically **quantified using stress testing**.



Key Takeaway:

- **Capital buffers are calibrated to protect the firm in a severe but plausible stress.**
- **Riskier business models require larger capital buffers to achieve this.**

Assessing P2B for Start Up Banks

Traditional Approach to setting PRA Buffer: **A problem**

- PRA is often sceptical of management actions or stressed projections which rely on raising capital during a severe but plausible macroeconomic scenario.

- Many new banks cannot deploy a reduction in growth rate as a strategic management action in response to stress as they are loss making and do not have a ‘break-even scale’.

- **Rapid growth rates combined with heavy losses under stress produce very large buffer requirements in stress tests.**

PRA Buffer (PRAB) for Start Up Banks

A solution…

- Stress testing shows new banks typically need very large buffers to survive a severe but plausible stress without external capital support.

- We developed the ‘wind down approach’ to PRAB setting to **ensure firms had sufficient resource to safely wind down, rather than survive, in a severe but plausible stress scenario.**

- Intended to generate lower buffers for new banks than the traditional approach, and reduce barriers to entry, whilst continuing to support the PRA objectives.

Key Takeaway:

- **ICAAP for new banks, reliant on rapid growth, should include an assessment of the capital required to wind down the business under stress.**

Assessing P2B for Start Up Banks

Best practice: thinking about wind down costs…

- Timing: think about the **triggers** that would identify that a stress had begun and when the wind down would actually begin and when would it finish?
- Costs: what **savings** could be achieved during a wind down? Staff? Marketing?
- Costs: what **additional costs** might be incurred? Legal? Severance? Contract termination?
- Credit exposures: what happens to **impairments** or loss rates during the stress?
- Disposals: where fixed assets or loan portfolios are disposed, consider what assumptions should be made for the **market valuation and haircut** for a distressed sale?

Assessing P2B for Start Up Banks

Transitioning to full stress test based approach to buffer setting

- The expectation is that, by year 5, capital buffers are set on the same basis as incumbent firms (reduction in capital surplus under stress).

- New banks often experience difficulty in transition to full stress testing regime where we hold higher expectations for:
  - Scenario design and calibration
  - Impairment modelling
  - Identification of triggers and impact of strategic management actions

- New firms should be prepared for the transition away from ‘wind down cost’ buffers and the impact this may have on capital requirements.

New Bank ICAAPs: Good Practice & Common Pitfalls

Pillar 2A - Credit Risk

- New banks are frequently over-reliant on PRA published benchmark risk weightings from Internal Ratings Based (IRB) models but….
  - Are these appropriate for your business exposures, and if so, how can you demonstrate this?
  - What supporting analysis / stress testing have you done to verify the adequacy of benchmarks or the standardised Pillar 1 risk weights?

New Bank ICAAPs: Good Practice & Common Pitfalls

Data Quality

- PRA frequently encounters issues with data quality in ICAAPs for example:
  - Inconsistent statement of key capital measures (RWAs, CET1, Total Capital) across ICAAP
  - Risk quantification in Pillar 2 returns, submitted as part of the C-SREP, differs from ICAAP.
  - Inconsistency in reference date (e.g. forecast vs actual)
  - No clear statement of the firm's view of its actual capital requirement and buffers

New Bank ICAAPs: Good Practice & Common Pitfalls

Risk Appetite & Capital Management

- ICAAPs should set out an overarching risk appetite for capital: for example:

  Our capital ratio will not fall by more than x% of RWAs under a Board approved stress scenario

- Capital survival days under growth:
  - How many days' growth should your capital surplus support?
  - What actions to preserve capital does this time allow?
  - Note: delays in capital raising is not a valid reason to breach capital requirements or buffers!

Our supervisory approach

Russell Shotton (Senior Manager, UK Deposit Takers Supervision, PRA)

Peter Fox (Senior Manager, Retail Banking Domestic Portfolio Supervision, FCA)

The FCA's Supervisory Approach

- The FCA supervises retail banks on either a relationship managed or non-relationship managed basis.
- Once a new bank is fully authorised (i.e. restrictions lifted), it will enter the New Banks Start-Up Unit which sits within our Domestic Portfolio. New banks remain in the New Banks Start-Up Unit for two years.
- While we generally **do not relationship manage firms within our Domestic Portfolio, we recognise that newly authorised banks may require more support in the early years.**
- Outlined below is our supervisory approach:

FCA supervisory approach

An **introductory meeting**	**Proactive Engagement Meetings** every 6-12 months	The **Supervision Hub** will act as the first point of contact	The **innovation hub** enables firms to test innovative financial products/services	**Limited involvement in multi-firm work** in the early years while you reach critical mass.

In line with Principle 11, firms should contact the FCA to report an crystallised/crystallising risks promptly

The FCA's Firm Assessment Model

Assessment Category	Assessment Group
Business Model & Strategy	How significant could the influence of external factors be on the firm's business model?
	Is the firm's business model viable and sustainable?
	How significant are the inherent drivers of harm in the firm's business model and strategy?
Culture	How effective is the firm's purpose in reducing the potential harm arising from the firm's business model?
	How effective is the firm's leadership in reducing the potential harm arising from the firm's business model?
	How effective are the firm's people policies in reducing the potential harm arising from the firm's business model?
	How effective is the firm's governance in reducing the potential harm arising from the firm's business model?
	How effective are the firm's systems & controls in reducing the potential harm arising from the firm's business model?
	How effective is the oversight of the business in reducing the potential harm arising from the firm's business model?

PRA’s Supervisory approach

We consider the potential impact a deposit-taker or designated investment firm could have on financial stability, then how the external context and business risk it faces (together, its risk context) might affect the firm’s viability. This gives us an assessment of gross risk.

We then consider mitigation, first a firm’s operational mitigation covering management and governance and its risk management and controls.

We next consider financial mitigation and its financial strength, specifically capital and liquidity.

Finally, we consider structural mitigation and the firm’s resolvability.

The PRA's Risk Framework

Gross risk			Mitigating factors				
Potential impact	Risk context		Operational mitigation		Financial mitigation		Structural mitigation
Potential impact	External context	Business risk	Management and governance	Risk management and controls	Capital	Liquidity	Resolvability

Scope of PRA supervision

What does this mean in practice?

Key messages	• The control environment remains appropriate for the size and complexity of the bank. • Banks should continue to invest in the support, operating and control infrastructures to ensure they keep pace with their business ambitions.
Business Risk	• Firms need to demonstrate that their business model is viable and sustainable in the long term. • Recovery plan is fit for purpose, with viable recovery options. • Changes to business strategy are approved by the Board. Regulators informed in advance of any significant changes to a firm’s business proposition or material issues affecting it.

Management & Governance	• Senior management and Board appointments need to have appropriate skills and experience to lead the bank given its current (and expected) size and complexity. • Sufficient independent challenge provided. • The skill sets of both the Executive and Board should be kept under review as the business develops and grows, and for the Board to provide effective challenge to the business.
Risk Management	• ICAAP and ILAAP documents are fit for purpose. • Regulatory reporting is accurate. • Firms need to demonstrate they have sufficient resilience to be able to continue providing services after unexpected events, including both operational incidents, or market wide stresses.

Capital	• The firm needs to demonstrate that (i) it is able to organically generate capital or (ii) there are no material concerns about the ability to raise additional capital as necessary. • Firms should have an appropriate capital risk appetite, and if ongoing investment is needed, we expect firms to proactively plan in advance to avoid any risk of going into their buffers due to planned events such as business growth. • Capital continues to meet Capital Requirements Regulation (CRR). • Moving from Pillar 2B (P2B) calculated on the basis of wind-down costs to stress analysis, as appropriate.
Liquidity	• The firm has a treasury function appropriate for its liquidity risk profile.

Common challenges for new banks

- Viable and sustainable business models
- Risk management keeping pace with business growth
- Operational resilience
- Additional capital injections and sufficient liquidity
- Financial Crime
- Clear and timely customer communications
- Governance and Board independence
- Oversight of 3rd parties
- Regulatory engagement
- Quality of senior management
- Appropriate level of MI

Some tools we use: PRA/FCA

Specialist reviews	Peer analysis	SM&CR interviews	Thematic work	Continuous assessment
Solvent wind-down plans	Skilled person reviews	Capital scalars	Changes to permission	Attestations

Key takeaway messages

- The PRA and FCA will look to assess how you are **managing the key prudential and conduct risks** to your business through our supervisory approaches.

- Your operating and control environment should **evolve over time** and develop in line with your business and associated risks.

- Authorisation is the **start** of your journey to being a fully established bank.

Q&A Panel using Menti.com

Melanie Beaman, Arran Salmon, Val Smith, Jill Lough, Glenn Redemann, Russell Shotton, Peter Fox, Chris Frank, Stephen Senior

15:15 – 15:45

Closing remarks

Arran Salmon

Head of New Banks, UK Deposit Takers Supervision, PRA

Key takeaways

- We remain ‘**open for business**’.
- Please make use of our **feedback**, it is there to help you.
- Firms that have a **well thought through proposition** navigate the regulatory process more quickly.
- **Good governance** is key.

➢ **Authorisation is the <u>start</u> of your journey to being a fully established bank.**