

Policy Statement | PS1/14

Responses to CP8/13 (No. 2)

January 2014



BANK OF ENGLAND
PRUDENTIAL REGULATION
AUTHORITY



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1 Introduction

1.1 This policy statement (PS) sets out the Prudential Regulation Authority's (PRA's) response to feedback received from the following chapters of CP8/13:⁽¹⁾

- Chapter 3 — Removal of the designated investment exchange regime.
- Chapter 6 — Related party transaction risk.

1.2 Chapter 3 is relevant to all PRA firms and Chapter 6 is relevant to banks and building societies. Firms should note the final rules set out in Annex A. For all chapters responded to in this PS, the analysis of costs and benefits and statutory obligations conducted at consultation have not changed following the responses received.

2 Consultation response

Removal of the designated exchange regime

2.1 No responses were received on this consultation. The PRA will remove references to designated investment exchanges from the PRA Handbook.

2.2 The PRA is also taking this opportunity to amend the definition of 'listed' used in Chapter 11 of the Supervision manual (SUP 11). This will address the defect that 'official list' may not include all the relevant EEA stock exchanges, because it only covers lists held by another competent authority, and not those held by stock exchanges. Potentially this will expand the population of PRA-regulated firms for which advanced approved applications can be made for acquisition or disposal of control. This change will ensure that the Handbook reflects existing practice.

Related party transaction risk

2.3 No responses were received on this consultation and this instrument comes into force on 1 February 2014.

(1) Occasional Consultation Paper (October 2013): www.bankofengland.co.uk/pru/Documents/publications/policy/2013/ocp8-13.pdf.

Appendices

1 Designated investment exchanges Instrument 2014

2 PRA Rulebook related parties Instrument 2014

DESIGNATED INVESTMENT EXCHANGES INSTRUMENT 2014**Powers exercised**

- A. The Prudential Regulation Authority makes this instrument in the exercise of the following powers and related provisions in Financial Services and Markets Act 2000 (“the Act”):
- (1) section 137G (The PRA’s general rules);
 - (2) section 137T (General supplementary powers);
 - (3) section 178 (Obligation to notify the appropriate regulator: acquisitions of control); and
 - (4) section 191D (Obligation to notify the appropriate regulator: dispositions of control).
- B. The rule-making power referred to above is specified for the purpose of section 138G(2) (Rule-making instruments) of the Act.

Pre-conditions to making

- C. In accordance with section 138J of the Act (consultation with the Financial Conduct Authority (“FCA”), the PRA consulted the FCA. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

Commencement

- D. This instrument shall come into force on 1 March 2014.

Amendments to the Handbook

- E. The rules and directions in the modules of the PRA’s Handbook listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2).

(1)	(2)
Glossary of definitions	Annex A
Principles for Businesses (PRIN)	Annex B
Supervision manual (SUP)	Annex C

Citation

- F. This instrument may be cited as the Designated Investment Exchanges Instrument 2014.

By order of the Board of the Prudential Regulation Authority

29 January 2014

Annex A
Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text.

<i>custodian</i>	<ul style="list-style-type: none"> (a) an <i>approved bank</i>; (b) an <i>approved depositary</i>; (c) a member <u>member</u> of a <i>recognised investment exchange</i> or designated investment exchange; (d) a <i>firm</i> whose <i>permitted activities</i> include <i>safeguarding and administering investments</i>; (e) a regulated <i>clearing firm</i>; (f) where it is not feasible to use a <i>custodian</i> in (a) to (e), and there are reasonable grounds to show that a <i>person</i> outside the <i>United Kingdom</i>, whose business includes the provision of custodial services, is able to provide such services which are appropriate to the <i>client</i> and in the <i>client's</i> best interest to use, that <i>person</i>.
...	
<i>exchange traded fund</i>	<p>a fund:</p> <ul style="list-style-type: none"> (a) which is an open-ended investment company; and (b) the units of which are traded on a regulated market or a designated investment exchange. [deleted]
<i>intermediate customer</i>	<p>(for the purposes only of COBS TP 1 (Transitional Provisions in relation to Client Categorisation)):</p> <ul style="list-style-type: none"> (1) (except in COB 3) a client who is not a market counterparty and who is: <ul style="list-style-type: none"> (a) a local authority or public authority; (b) a body corporate whose shares have been listed or admitted to trading on any EEA exchange; (c) a body corporate whose shares have been listed or admitted to trading on the primary board of any IOSCO member country official exchange; (d) a body corporate (including a limited liability partnership) which has (or any of whose holding companies or subsidiaries has) (or has had at any time during the previous two years) called up share capital or net assets of at least £5 million (or its equivalent in any other currency at the relevant time); (e) a special purpose vehicle;

- (f) ~~a partnership or unincorporated association which has (or has had at any time during the previous two years) net assets of at least £5 million (or its equivalent in any other currency at the relevant time) and calculated in the case of a limited partnership without deducting loans owing to any of the partners;~~
- (g) ~~a trustee of a trust (other than an occupational pension scheme, SSAS, personal pension scheme or stakeholder pension scheme) which has (or has had at any time during the previous two years) assets of at least £10 million (or its equivalent in any other currency at the relevant time) calculated by aggregating the value of the cash and designated investments forming part of the trust's assets, but before deducting its liabilities;~~
- (h) ~~a trustee of an occupational pension scheme or SSAS, or a trustee or operator of a personal pension scheme or stakeholder pension scheme where the scheme has (or has had at any time during the previous two years):~~
 - (i) ~~at least 50 members; and~~
 - (ii) ~~assets under management of at least £10 million (or its equivalent in any other currency at the relevant time);~~
- (i) ~~another firm, or an overseas financial services institution, when, in relation to designated investment business, or related ancillary activities, conducted with or for that firm or institution, that firm or institution is an intermediate customer in accordance with COB 4.1.7R (Classification of another firm or an overseas financial services institution);~~
- (j) ~~collective investment scheme;~~
- (k) ~~a client when he is classified as an intermediate customer in accordance with COB 4.1.9R (Expert private customer classified as intermediate customer);~~
- (l) ~~a recognised investment exchange, designated investment exchange, regulated market or clearing house, except when it is classified as a market counterparty in accordance with COB 4.1.8AR (Classification of an exchange or clearing house);~~

but excluding:

- (i) ~~[deleted]~~
- (ii) ~~a client who would otherwise be an intermediate customer, when he is classified in accordance with:~~
 - (A) ~~COB 4.1.12R (Large intermediate customer classified as market counterparty); or~~
 - (B) ~~(except for the purposes of DISP) COB 4.1.14R (Client classified as private customer); [deleted]~~

inter-professional
business

(2) ~~(in COB 3) a person in (1) or a person who would be such a person if he were a client. [deleted]~~

~~the business of a firm:~~

(a) ~~when it carries on:~~

- ~~(i) regulated activities; or~~
- ~~(ii) related ancillary activities;~~

~~to the extent that the regulated activity that the firm is carrying on is:~~

- ~~(A) dealing in investments as principal; or~~
- ~~(B) dealing in investments as agent; or~~
- ~~(C) acting as an arranger; or~~
- ~~(D) giving transaction-specific advice or agreeing to do so;~~

~~but only if that activity is:~~

- ~~(i) in or in respect of an inter professional investment;~~
- ~~(ii) undertaken with or for a eligible counterparty; and~~
- ~~(iii) carried on from an establishment maintained by the firm in the United Kingdom;~~

(b) ~~but excluding the carrying on of the following activities:~~

- ~~(i) the approval by a firm of a financial promotion;~~
- ~~(ii) activities carried on between operators, or between operators and depositaries, of the same collective investment scheme (when acting in that capacity);~~
- ~~(iii) corporate finance business;~~
- ~~(iv) safeguarding and administering investments and agreeing to carry on that regulated activity;~~
- ~~(v) concluding a distance contract with a consumer;~~
- ~~(vi) activities relating to life policies;~~

~~in this definition, the exclusion in article 15 of the Regulated Activities Order (Absence of holding out etc) is to be disregarded in determining whether dealing in investments as principal or agreeing to do so) is a regulated activity. [deleted]~~

inter-professional
investment

~~any of the following investments specified in Part III of the Regulated Activities Order (Specified Investments) or, in the case of units in an exchange traded fund, defined in the Glossary:~~

(a) ~~share (article 76);~~

- (b) ~~debenture (article 77);~~
 - (ba) ~~alternative debenture (article 77A);~~
 - (c) ~~government and public security (article 78);~~
 - (d) ~~warrant (article 79);~~
 - (e) ~~certificate representing certain securities (article 80);~~
 - (f) ~~option (article 83); for the purposes of the permission regime, this is sub-divided into:~~
 - (i) ~~option (excluding a commodity option and an option on a commodity future);~~
 - (ii) ~~commodity option and option on a commodity future;~~
 - (g) ~~future (article 84); for the purposes of the permission regime, this is sub-divided into:~~
 - (i) ~~future (excluding a commodity future and a rolling spot forex contract);~~
 - (ii) ~~commodity future;~~
 - (iii) ~~rolling spot forex contract;~~
 - (h) ~~contract for differences (article 85); for the purposes of the permission regime, this is sub-divided into:~~
 - (i) ~~contract for differences (excluding a spread bet and a rolling spot forex contract);~~
 - (ii) ~~spread bet;~~
 - (iii) ~~rolling spot forex contract;~~
 - (i) ~~rights to or interests in investments in (a) to (h) (article 89)~~
 - (j) ~~units in an exchange traded fund. [deleted]~~
- listed*
- (1) (except in LR, SUP 11, INSPRU and IPRU(INS)) included in an official list.
 - (2) (in SUP 11, INSPRU and IPRU(INS)):
 - (a) included in an official list; or
 - (b) in respect of which facilities for dealing on a regulated market have been granted.
- ...
- ...
- market counterparty* {for the purposes only of COBS TP 1 (Transitional Provisions in relation to Client Categorisation)};

- (1) ~~(except in COB 3) a client who is:~~
- ~~(a) a properly constituted government (including a quasi-governmental body or a government agency) of any country or territory;~~
 - ~~(b) a central bank or other national monetary authority of any country or territory;~~
 - ~~(c) a supranational whose members are either countries or central banks or national monetary authorities;~~
 - ~~(d) a State investment body, or a body charged with, or intervening in, the management of the public debt;~~
 - ~~(e) another firm, or an overseas financial services institution, except in relation to designated investment business, and related ancillary activities, conducted with or for that firm or institution, when that firm or institution is an intermediate customer in accordance with COB 4.1.7 R (Classification of another firm or an overseas financial services institution);~~
 - ~~(f) any associate of a firm (except an OPS firm), or of an overseas financial services institution, if the firm or institution consents;~~
 - ~~(g) a client when he is classified as a market counterparty in accordance with COB 4.1.12R (Large intermediate customer classified as a market counterparty);~~
 - ~~(h) a recognised investment exchange, designated investment exchange, regulated market or clearing house when it is classified as a market counterparty in accordance with COB 4.1.8AR (Classification of an exchange or clearing house);~~
- ~~but excluding:~~
- ~~(A) a regulated collective investment scheme; and~~
 - ~~(B) (except for the purposes of DISP) a client, who would otherwise be a market counterparty, when he is classified as a private customer in accordance with COB 4.1.14R (Client classified as private customer). [deleted]~~
- (2) ~~(in COB 3) a person in (1) or a person who would be such a person if he were a client. [deleted]~~

...

private customer

~~(for the purposes only of COBS TP 1 (Transitional Provisions in relation to Client Categorisation)):~~

- (1) ~~(except in COB 3, COB 4.2 and COB 6.4) subject to (h), a client who is not a market counterparty or an intermediate customer, including~~
- ~~(a) an individual who is not a firm;~~

- (b) ~~an overseas individual who is not an overseas financial services institution;~~
 - (c) ~~[deleted]~~
 - (d) ~~(except for the purposes of DISP) a client when he is classified as a private customer in accordance with COB 4.1.14R (Client classified as a private customer);~~
 - (e) ~~a person to whom a firm gives basic advice;~~
 - (f) ~~(in COB 6.1 to 6.5) where the regulated activity (except for a personal recommendation relating to a contribution to a CTF) relates to a CTF and there is no registered contact, the person to whom the statement must be sent in accordance with Regulation 10 of the CTF Regulations;~~
 - (g) ~~(in COB 6.7) where the regulated activity (except for a personal recommendation relating to a contribution to a CTF) relates to a CTF and there is no registered contact, the child, via the person to whom the statement must be sent in accordance with Regulation 10 of the CTF Regulations;~~
 - (h) ~~a client who would otherwise be excluded as a market counterparty or intermediate customer if the client is within (e), (f) or (g);~~
- ~~but excluding a client, who would otherwise be a private customer:~~
- (i) ~~when he is classified as an intermediate customer in accordance with COB 4.1.9R (Expert private customer classified as an intermediate customer); or~~
 - (ii) ~~when the regulated activity relates to a CTF, any person other than (e), (f), (g) or (h).~~
- (2) ~~(in COB 3) a person in (1) or a person excluded under (1)(h)(ii) or a person who would be such a person if he were a client. (in COB 4.2 and 6.1 to 6.5) a person in (1) and, in relation to the conclusion of a distance contract, a consumer.~~
 - (3) ~~(in COB 4.2 and 6.1 to 6.5) a person in (1) and, in relation to the conclusion of a distance contract, a consumer. [deleted]~~

Annex B
Amendments to the Principles for Businesses (PRIN)

In this Annex, striking through indicates deleted text.

TP 1.1

	Material to which the transitional provision applies		Transitional Provision	Transitional Provision: dates in force	Handbook provision: coming into force
1.	PRIN 1 Annex 1 R 1.2(2) [deleted]	R	A firm need not comply with PRIN Ann 1R 1.2(2) in relation to an eligible counterparty if the client was correctly categorised as a market counterparty on 31 October 2007 and the firm complied with COB 4.1.12R(2) (Large intermediate customer classified as market counterparty). [deleted]	From 1 November 2007 indefinitely	1 November 2007

Annex C
Amendments to the Supervision manual (SUP)

In this Annex, underlined text indicates new text and striking through indicates deleted text.

11.3 Requirements on controllers or proposed controllers under the Act

...

Pre-notification and approval for fund managers

...

11.3.5B D The *appropriate regulator* may treat as notice given in accordance with sections 178 and 191D of the *Act* a written notification from a *firm* which contains the following statements:

- (1) that the *firm* proposes to acquire and/or dispose of *control*, on one or more occasions, of any *UK domestic firm* whose *shares* or those of its ultimate *parent undertaking* are, at the time of the acquisition or disposal of *control*, *listed*, or which are traded or admitted to listing trading on a ~~designated investment exchange~~ MTF or a market operated by a ROIE;

...

...

PRA RULEBOOK RELATED PARTIES INSTRUMENT 2014

Powers exercised

- A. The Prudential Regulation Authority (“PRA”) makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 137G (the PRA’s general rules); and
 - (2) section 137T (general supplementary powers).
- B. The rule-making powers referred to above are specified for the purpose of section 138(2)G (Rule-making instruments) of the Act.

Pre-conditions to making

- C. In accordance with section 138J of the Act (consultation with the Financial Conduct Authority (“FCA”), the PRA consulted the FCA. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

PRA Rulebook Related Parties Instrument 2014

- D. The PRA makes the rules in Annex A and Annex B of this instrument.

Commencement

- E. This instrument comes into force on 1 February 2014.

Citation

- F. This instrument may be cited as the PRA Rulebook Related Parties Instrument 2014.

By order of the Board of the Prudential Regulation Authority
29 January 2014

Annex A

PRA RULEBOOK – GLOSSARY

In the Glossary Part of the PRA Rulebook insert the following new definitions:

accepting deposits

means the *regulated activity* specified in article 5 of the *Regulated Activities Order* (Accepting deposits).

affiliated company

means (in relation to a *person*) an *undertaking* in the same *group* as that *person*.

body corporate

means any body corporate including a body corporate constituted under the law of a country or territory outside the *UK*.

director

means (in relation to any of the following (whether constituted in the *UK* or under the law of a country or territory outside it)):

(a) an unincorporated association;

(b) a *body corporate*;

any *person* appointed to direct its affairs, including a *person* who is a member of its *governing body* and (in accordance with section 417(1) of *FSMA*):

(i) a *person* occupying in relation to it the position of a director (by whatever name called);
and

(ii) a *person* in accordance with whose directions or instructions (not being advice given in a professional capacity) the directors of that body are accustomed to act.

governing body

means the board of *directors*, committee of management or other governing body of an unincorporated association or *body corporate*.

incoming firm

means an incoming firm within the meaning of section 193 of *FSMA*.

management body

means a *firm's* body or bodies, which are appointed in accordance with national law, which are empowered to set the *firm's* strategy, objectives and overall direction, and which oversee and monitor management decision-making, and include the *persons* who effectively direct the business of the *firm*.

overseas firm

means a *firm* which has its registered office (or, if it has no registered office, its head office) outside the *UK*.

Part 4A permission

means a permission given by the *FCA* or *PRA* under Part 4A of *FSMA* (Permission to carry on regulated activities), or having effect as if so given.

Regulated Activities Order

means the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (SI 2001/544).

senior management

means those natural *persons* who exercise executive functions within a *firm* and who are responsible, and accountable to the *management body*, for the day-to-day management of the *firm*.

undertaking

means an undertaking within the meaning of section 1161(1) of the Companies Act 2006 (meaning of “undertaking” and related expressions).

Annex B

Part

RELATED PARTY TRANSACTION RISK

Chapter content

- 1 APPLICATION AND DEFINITIONS**
- 2 RELATED PARTY TRANSACTION RISK**

Links

1 APPLICATION AND DEFINITIONS

1.1 This Part applies to:

- (1) a *UK bank*;
- (2) a *building society*; and
- (3) an *overseas firm* that:
 - (a) is not an *incoming firm*; and
 - (b) has a *Part 4A permission* that includes permission to carry out *accepting deposits*.

1.2 In this Part the following definitions shall apply:

close family member

means in relation to a natural *person* (“A”):

- (a) A’s spouse or civil partner;
- (b) any other *person* with whom A lives as partner in an enduring family relationship;
- (c) A’s children or step-children;
- (d) any children or step-children of a *person* within (b) (and who are not children or step-children of A) who live with A and have not attained the age of 18; and
- (e) A’s parents.

related parties

means in relation to a *firm*:

- (a) any *person* that it *controls*;
- (b) its *affiliated companies*;
- (c) its and its *affiliated companies’ controllers*;
- (d) its and its *affiliated companies’ directors*;
- (e) its and its *affiliated companies’ senior management*;
- (f) its and its *affiliated companies’ key employees*;
- (g) *close family members* of any natural *person* listed in (a) to (f) above;
- (h) direct and related interests of any *person* listed in (a) to (g) above; and
- (i) any *person* that would fall into (a) to (h) above after the relevant *transaction* has occurred.

transaction

means any transaction or arrangement including:

- (a) any arrangement or circumstance that gives rise to or varies an on-balance sheet or off-balance sheet asset or liability (whether contingent or otherwise);
- (b) dealings such as service contracts, asset acquisitions and disposals, construction contracts, lease agreements, derivative transactions, borrowings and write-offs.

2 RELATED PARTY TRANSACTION RISK

- 2.1 A *firm* must enter into *transactions* with *related parties* at market value or on terms no more favourable than would be agreed if the *transaction* was not with a *related party*.
- 2.2 2.1 does not apply to beneficial terms that are part of an overall remuneration package such as favourable interest rates for employee loans.
- 2.3 A *firm* must establish, implement and maintain effective policies and procedures to identify, evaluate and manage risks arising out of *transactions* with its *related parties*.
- 2.4 In meeting 2.3, a *firm's* policies and procedures on *related party transactions* must:
 - (1) prevent a *related party* from taking part in the *firm's* decision making process in relation to any *transactions* with that *related party*;
 - (2) set a materiality threshold above which *transactions* with *related parties* receive prior approval from the *firm's management body*;
 - (3) ensure that the *firm* records and monitors the details and amounts of any *related party transactions* using an independent credit review or audit process; and
 - (4) only permit exceptions to those policies and procedures if reported to the *firm's senior management or management body* as appropriate.
- 2.5 A *firm* must provide the *PRA* with details on aggregate exposures to *related parties* if requested by the *PRA*. The details must be provided by the date set by the *PRA* at the time of the request.