



Statement of Policy 1/13

Designation of investment firms for prudential supervision by the Prudential Regulation Authority

December 2021

Updating March 2013





BANK OF ENGLAND
PRUDENTIAL REGULATION
AUTHORITY

Statement of Policy

Designation of investment firms for prudential supervision by the Prudential Regulation Authority

December 2021

Updating March 2013

Contents

1	Introduction	1
2	Legal context	1
3	Designation policy	2
4	Withdrawal of designation	3
5	Periodic review of firms subject to designation	3
6	Procedural arrangements for designation decisions	3
Annex: Changes to Statement of Policy (SoP) - Designation of investment firms for prudential supervision by the Prudential Regulation Authority		5

1 Introduction

1.1 This statement of policy is issued under article 8 of the Financial Services and Markets Act 2000 (PRA-regulated Activities) Order 2013 as amended¹ (the PRA-regulated Activities Order).

2 Legal context

2.1 Under the PRA-regulated Activities Order, the Prudential Regulation Authority (PRA) may designate certain persons for prudential supervision by the PRA under CRR (other than those in article 4(1)(2AA) (a), (b) and (c) CRR). Before the PRA does so, the condition set out in article 3(2) of the PRA-regulated Activities Order must be satisfied. This is, broadly speaking, that the person has, or has applied for, permission to deal in investments as principal.

2.2 In this statement of policy, a person meeting the condition in article 3(2) is referred to as an 'Eligible Investment Firm'.

2.3 Provided this condition is met, the PRA may designate an Eligible Investment Firm if the PRA 'considers that it is desirable that the activity of dealing in investments as principal, when carried on by [the Eligible Investment Firm], should be a PRA-regulated activity' (article 3(1)(c)), so that upon designation taking effect the Eligible Investment Firm becomes a 'designated investment firm'. A designated investment firm is a PRA-authorized person and is subject to CRR. In taking designation decisions the PRA has regard to its statutory objectives and the matters set out in article 3(4) of the PRA-regulated Activities Order, which are:

- (a) the assets of the Eligible Investment Firm; and
- (b) where the Eligible Investment Firm is a member of a group:
 - (i) the assets of other Eligible Investment Firms within the group;
 - (ii) whether any other members of the Eligible Investment Firm's group have been designated; and
 - (iii) whether the Eligible Investment Firm's activities have, or might have, a material impact on the ability of the PRA to advance any of its objectives in relation to PRA-authorized persons in its group.

2.4 The PRA-regulated Activities Order also:

- (a) requires the PRA to keep under review all designations (article 5); and
- (b) provides for the PRA to withdraw a designation if the PRA considers it 'appropriate to do so' (article 6).

2.5 In taking designation decisions the PRA-regulated Activities Order requires the PRA to have regard to the factors set out in paragraph 3. It also requires the PRA to have regard to this statement

¹ Part 3, Section 15 of The Financial Services Act 2021 (Prudential Regulation of Credit Institutions and Investment Firms) (Consequential Amendments and Miscellaneous Provisions) Regulations 2021, which amends the PRA-regulated Activities Order, has been made by HM Treasury in exercise of the powers conferred by sections 22A and 428(3) of the Financial Services and Markets Act 2000. In accordance with section 22B(2)(a) and (3)(a) FSMA a draft of this Order was laid before Parliament and approved by a resolution of each House.

of policy in taking decisions to designate or withdraw designation or in reviewing designations. But these factors are not exhaustive. The PRA may also have regard to other considerations in deciding whether it is desirable for an Eligible Investment Firm to be designated or appropriate for a designation to be withdrawn.

2.6 In principle HM Treasury may add other PRA-regulated activities to the PRA-regulated Activities Order or make other changes to it under sections 22A and 428(3) of the Financial Services and Markets Act 2000 (FSMA).

2.7 Under the Bank of England Act 1998 (as amended by the Financial Services Act 2012), the Financial Policy Committee (FPC) can make recommendations to HM Treasury regarding the boundary between regulated and non-regulated sectors of the UK financial system – the regulatory perimeter. Such recommendations may concern what is a regulated activity under FSMA and also which particular activities are prudentially regulated by the PRA. The regime for designating investment firms for regulation by the PRA provides that the PRA may consult the FPC on any proposed revisions to this Statement of Policy.

3 Designation policy

3.1 The PRA has regard to each of the following factors in determining whether an Eligible Investment Firm should be designated:

- whether the firm’s balance sheet exceeds an average of £15 billion total gross assets over four quarters, as reported on regulatory returns; and/or
- whether the sum of the balance sheets of all Eligible Investment Firms in a group exceeds an average of £15 billion total gross assets over four quarters; and/or
- where the firm is part of a PRA group, whether the firm’s revenues, balance sheet and risk-taking is significant relative to the group’s revenues, balance sheet and risk-taking.

3.2 The first factor — that a firm is designated where it has **total gross assets over four quarters averaging more than £15 billion** — relates to the assets consideration in the PRA-regulated Activities Order. While an individual firm’s impact on the financial system is not only a function of its size, but also the complexity of its operations, the substitutability of the services it provides and its connectedness with the rest of the system, the use of a size threshold provides an objective reference point to indicate which firms are likely to be systemically relevant in this context. This does not mean that all firms above this threshold will be systemically relevant, nor that any firm below the threshold cannot be systemically relevant; it is simply indicative as to likely systemic relevance in this context. In deciding to designate a particular firm, the PRA will take account of its substitutability, interconnectedness and complexity using a range of metrics such as its market share in key markets, legal structure, intra-financial system assets and liabilities and leverage ratio.

3.3 When considering a firm’s gross assets, analysing its balance sheet over four quarters prevents any large temporary movements in the balance sheet from distorting the view of a firm’s likely importance. In addition to looking at balance sheet size, the PRA will also consider a firm’s business model, including whether it is a clearing member of a central counterparty providing clearing services to other financial institutions who are not clearing members themselves, and booking practices to ensure that assets booked to the firm do not give a distorted view of the firm’s business and risk profile. Other assessments of asset values beyond those regularly submitted on a firm’s regulatory returns (both end-of-day and intraday) may also be considered in order to identify

whether a firm's assets, as disclosed in regulatory returns, provide an accurate representation of its risk-taking.

3.4 The second factor – **that the sum of the total gross assets of all investment firms in a group potentially subject to designation averages more than £15 billion over four quarters** – relates to the requirement in the PRA-regulated Activities Order to take into account, where the firm is a member of a group, the assets of the group members. This ensures that groups do not structure themselves in such a way as to avoid designation of a firm by spreading business across several investment firms within the same group which individually fall below the total assets threshold.

3.5 The third factor – **that the PRA analyses whether the share of a firm's revenues, balance sheet and risk-taking is significant relative to the group's revenues, balance sheet and risk-taking** – relates to the provision in the PRA-regulated Activities Order to have regard to the impact of an investment firm on any PRA-authorized person within the group. In some cases, an Eligible Investment Firm may pose risks to other PRA-authorized persons within the group even where the investment firm does not meet the total assets threshold. A firm's 'significance' to the rest of a group would be determined, among other things, through supervisory judgement gained through knowledge of the group and dialogue with the Financial Conduct Authority (FCA). The PRA would typically consider the materiality of a legal entity to its group with reference to its share of the group's revenues, balance sheet or risk-taking. Given that group structures vary significantly, the materiality of an individual entity requires specific knowledge of the group in question and will be a matter of judgement for the PRA.

4 Withdrawal of designation

4.1 In determining whether it is appropriate to withdraw a designation, the PRA will have regard to the same factors as it does when deciding to designate an Eligible Investment Firm.

4.2 The PRA would not normally be minded to withdraw a designation, however, unless the firm had been subject to prudential supervision by the PRA for at least one year after designation (except where there is a de-merger or a sale). This is also designed to guard against 'volatility in designation', where a firm switches between prudential supervisors on a frequent basis.

5 Periodic review of firms subject to designation

5.1 The PRA-regulated Activities Order requires the PRA to keep all designations under review. In reviewing designations, it is important to guard against volatility in designation. That is why the value of total assets is averaged over four quarters. PRA staff review the eligible population of firms against the designation criteria on a periodic basis to consider whether any additional firms should be designated, or their designation withdrawn. The PRA also discusses individual firms with the FCA as they approach the relevant designation thresholds. A summary of this analysis, plus any designation recommendations, is, where relevant, put to the Prudential Regulation Committee for decision.

6 Procedural arrangements for designation decisions

6.1 The PRA-regulated Activities Order requires the PRA to give firms notice of its intention to designate a firm and also confers rights on firms to make representations to the PRA and to refer designation decisions to the Upper Tribunal.

6.2 If the PRA decides to designate an investment firm, it will issue the firm with a notice stating the reasons for designation. The PRA will normally give the firm 28 days to make representations. The notice will also make clear the firm's right to refer matters to the Upper Tribunal. The notice will state the date that the designation decision would take effect which will usually be six months from the date of the notice being issued. The PRA-regulated Activities Order does provide for designation decisions to take immediate effect, in appropriate circumstances, but this will not normally be the case.

6.3 Where the PRA decides that a firm should no longer be designated, article 6 requires the PRA to follow the procedure for warning notices and decision notices. Should designation be withdrawn, the prudential supervision of the firm would pass to the FCA.

Annex: Changes to Statement of Policy (SoP) - Designation of investment firms for prudential supervision by the Prudential Regulation Authority

This annex details changes made to SoP 'Designation of investment firms for prudential supervision by the Prudential Regulation Authority' following its initial publication in March 2013.

December 2021

This SoP was updated in December 2021 following publication of Policy Statement (PS) 27/21 'Designating investment firms'.² The updates amended the SoP to:

- (i) reflect HM Treasury's amendments to the PRA-regulated Activities Order , including the change in the scope of the firms that can be designated;
- (ii) explain that there will usually be six months, rather than three months, between the Prudential Regulation Committee designating an investment firm and it becoming PRA-regulated;
- (iii) note that the PRA will take into account whether or not an investment firm is a clearing member of a central counterparty offering clearing services to other financial institutions (that are not clearing members themselves) when making a designation decision; and
- (iv) delete any obsolete text and make other minor textual and formatting amendments. This includes minor changes to the paragraph numbering as a result of the formatting changes.

To track the specific changes to each paragraph of the SoP, please see [Appendix 1 of CP15/21](#).

² December 2021: [PS27/21 – Designating investment firms](#).