

# Being better informed

## FS regulatory bulletin

FS regulatory insights

April 2023

### In this month's edition:

- Government launches updated Green Finance Strategy
- Treasury and regulators kick start SM&CR review
- Ring-fencing reforms move forward
- FCA highlights risks in payments sector



# Executive summary



Welcome to this edition of 'Being better informed', our monthly FS regulatory bulletin, which aims to keep you up to speed with significant developments and their implications across all the financial services sectors.



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The regulators were as busy as ever as the first quarter of 2023 drew to a close, particularly on the topics of sustainability and banking prudential developments.

At the end of the month, the Government published its updated green finance strategy, which includes important updates on a range of topics, including the UK taxonomy and transition plan disclosure. The Government announced the UK taxonomy will be consulted on this autumn, and will be voluntary for two years, after which it may be made mandatory. Elsewhere, the Government said it will consult on requiring UK private companies to report transition plans (if they have them), to bring them in line with requirements of listed companies. Please refer to our [At a glance](#) briefing on the strategy for more information. The Government also published a consultation on bringing ESG ratings providers within the regulatory perimeter, and confirmed plans to establish a framework to assess implementation of the International Sustainability Standards Board standards this summer - further details can be found in this [At a glance](#) publication.

Meanwhile, HM Treasury (HMT) and the UK regulators kicked off their review of possible changes to the Senior Managers & Certification Regime (SM&CR). HMT issued a Call for Evidence, and the FCA and PRA published a Discussion Paper, seeking industry views on the effectiveness, scope and proportionality of the regime, and how it might be improved. The Government first announced it would be carrying out a review of the SM&CR in December 2022, as part of the Edinburgh Reforms. While a fundamental overhaul of the regime is considered unlikely, HMT and the regulators appear to be taking an open-minded approach to potential changes, asking a broad range of questions, and acknowledging that firms have raised some concerns about aspects of the regime. Our [At a](#)

[glance](#) publication looks at the papers in more detail.

The Bank of England (BoE), meanwhile, issued a report updating its analytical approach to assessing the treatment of climate risks within the regulatory capital frameworks for banks and insurers, and how these risks are potentially already captured in the current frameworks. The BoE's report builds on its 2021 Climate Change Adaptation Report and identifies areas for future work, although it does not propose specific policy changes. The report focuses on five main findings, highlighting gaps in the current capital framework, capability gaps in risk management and gaps in the capital regime. The BoE also commits to further work to develop its regulatory framework. Please read our [At a glance](#) briefing for further details.

Elsewhere, HMT progressed work on possible reforms to the ring-fencing regime for banks. It published a Call for Evidence (CfE), seeking input on the practicalities of aligning the ring-fencing and resolution regimes, and long-term options for reform. HMT launched the CfE in response to the recommendation of the Skeoch Review, which concluded that the resolution regime offered a more comprehensive solution to the 'too big to fail' dilemma. The CfE explores the benefits and costs of the ring-fencing regime and the options for aligning it with the resolution regime. Our [At a glance](#) briefing looks at the options in more detail.

Banks will also be interested in the PRA's proposal to remove the Common Equity Tier 1 (CET1) deduction requirement, regarding non-performing exposures (NPEs) that are treated as insufficiently covered by firms' accounting provisions. This requirement was introduced through the CRR and the PRA judges that it does not provide an objectively accurate measure of NPE-provisioning levels for PRA-regulated firms, and therefore might require deductions that are greater or lower than the level required to address

underlying risks. Instead, the PRA proposes to use existing supervisory tools to address potential shortfalls in firms' provisioning. The PRA plans to implement its proposed approach in Q4 2023. For more information, please see our [At a glance](#) briefing.

In conduct-related developments, the FCA issued a Dear CEO letter to payments and e-money firms, highlighting the regulatory risks and issues it sees in the sector, and the actions firms should take to address these. It remains concerned that many firms do not have sufficiently robust controls, and flags deficiencies in areas such as governance and regulatory reporting. The letter also stresses the need for firms to improve prudential risk management following failings identified in liquidity and capital risk management and lack of scenario planning and stress-testing. In addition, the FCA highlights increased evidence of financial crime in the payments portfolio and reminds firms of their obligations in relation to money laundering, sanctions and fraud. Our [At a glance](#) briefing considers the steps firms should take in response.

Read on to find out more about these and other developments in this edition of Being better informed. You can also visit our PwC [webpage](#) for further regulatory insights, including [analysis of the FCA's latest Business Plan](#).

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# Cross sector announcements

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## Artificial intelligence

### Government outlines initiatives to regulate emerging technologies

The Government outlined key initiatives it will take forward to better regulate emerging technologies, in its [response](#) to Sir Patrick Vallance's review published on 15 March 2023. The review aims to establish the UK as the best regulated economy in the world in key growth sectors, including artificial intelligence (AI), drones, cyber security and the potential in the global space market. Financial services regulators will contribute to the implementation of some of the review's recommendations, and firms will be impacted by the outcomes of this programme.

The Government recognises the importance of a broad approach to regulating emerging digital technologies, as recommended in the review. Instead of regulating too early in their development, the Government and regulators will engage with industry to address issues related to safety, risk, and benefits of innovation. The review also called for the Government to build its own expertise to ensure that regulatory frameworks can be positively shaped at the right time.

The Government presents [the Quantum Strategy, Semiconductor Strategy, and Emerging Technologies Review](#) as an example of its long-term commitment to supporting the development of emerging digital technologies.

The review also includes two recommendations related to the deployment and use of AI which the Government, regulators and the Intellectual Property Office (IPO) will implement in the next six months:

- developing a multi-regulator sandbox for AI
- providing clarity in relation to the application of intellectual property law to the AI sector,

which will be supported by a code of practice the IPO will publish.

### Government sets out its approach to regulating AI

The Department for Science, Innovation & Technology (DSIT) outlined its cross-sectoral plans for regulating artificial intelligence (AI) in a [white paper](#) (WP) published on 29 March 2023. Building on the [National AI Strategy](#) and a [policy paper](#) published in June 2022, the WP describes a principles-based framework designed to manage risks associated with AI while promoting innovation and public trust.

The proposed framework will rely on a high-level definition of AI, a context-specific approach, cross-sectoral governance principles, and central functions to support coherent regulation.

DSIT expects to introduce a statutory duty requiring regulators to have due regard to the principles. Initially, regulators will have the discretion to apply the five following principles, enabling them to prioritise based on their sector's specific needs:

- safety, security, robustness
- appropriate transparency and explain ability
- fairness
- accountability and governance
- contestability and redress.

The WP emphasises the importance of assurance techniques and standards, with a layered approach to AI technical standards proposed. This includes sector-agnostic standards, standards addressing specific issues like bias and transparency, and sector-specific technical standards for compliance and performance measures.

Financial services regulators have already consulted the industry on the existing regulation in their [discussion paper](#) published on 11 October 2022. They will incorporate this new framework in their engagement with industry on AI, and any upcoming consultations.

For more information on the white paper, please see our [At a glance](#) briefing.

## Conduct

### FCA speaks on reforming UK capital markets

Nikhil Rathi, Chief Executive of the FCA, [spoke](#) at the Global Investment Management Summit on 29 March 2023 on the UK capital markets ecosystem. The speech touched on a number of areas, such as asset management (including proposed sustainable finance disclosures), equity markets (international and domestic), UK pension funds (e.g. their investments into UK equities) and the role of regulation (e.g. policy trade-offs and consequences).

The speech gives helpful context to, and principles behind, how the FCA is approaching amending the UK listing regime. Rathi states that the FCA plans to consult on replacing the current approach (standard and premium listing segments for shares in commercial companies) with a single listing category with one set of requirements and a focus on transparency. This would include, for example:

- removing the requirement to have a three-year financial track record as a condition for listing
- taking a more permissive approach to dual class share structures
- maintaining a disclosure regime while removing compulsory shareholder votes for large transactions and related party transactions.

Rathi said the regulator intends to keep a streamlined sponsor regime, a single set of Listing Principles, and rules to protect shareholders from the solvent cancellation of a listing without takeover offer or approval by a super majority of investors.

According to [The Regulatory Grid](#), published in February 2023, the FCA is due to issue a consultation paper in Q2 2023 on improving the effectiveness of UK primary markets. This would follow a discussion paper ([DP22/2](#)) published in May 2022.

### FCA issues latest Consumer Duty letters

The FCA published its latest batch of sector-specific Dear CEO letters on 3 March 2023 setting out its expectations on firms implementing the Consumer Duty. The letters build on the findings from the FCA's review of firms' implementation plans, and highlights sector-specific feedback. The regulator also sets out where it intends to focus its supervision ahead of the July 2023 implementation deadline.

The letters are addressed to credit brokers, credit unions, mortgage intermediaries, and providers of motor and retail finance. In line with the letters issued to other sectors, the FCA reminds firms of where they should focus attention during the remaining implementation period. For this portfolio of firms, the FCA notes that it will closely scrutinise firms' fees, charges and commission models throughout the distribution chain to ensure their products and services deliver fair value to customers. The FCA also draws attention to the current economic environment and states that firms should be alert to potentially higher numbers of customers in financial difficulty, and ensure that tailored forbearance and support options are available.

The FCA reminds CEOs that the Consumer Duty should be a 'top priority for them personally' and that good customer outcomes should be at the heart of firms' strategies and objectives, with leaders playing a key role in delivering this. Where not done so already, firms are required to take action imminently to meet upcoming Consumer Duty implementation deadlines. In particular, firms should have completed all product/service reviews for new and existing products and shared relevant information with distributors by the end of April 2023.

## Finance

### Government launches Investment Research Review

The Government announced the launch of the Investment Research Review on 9 March 2023, publishing the Review's terms of reference and confirming Rachel Kent, Hogan Lovells Partner, as Chair.

First announced as part of the Government's Edinburgh Reforms package in December 2022, the Investment Research Review will examine the link between the levels of research and the attractiveness of the UK as a destination for companies to access capital, both in private and public markets. In particular, the Review will provide an international comparison to approaches in other jurisdictions and consider the quality and quantity of investment research and related investor demand. Further, the Review is expected to offer recommendations to improve the UK market for investment research. This may include legislative measures, changes to be made by the FCA, or industry action. As part of this, the Review will consider the impact of MiFID unbundling rules on the levels and quality of investment research and evaluate the likely impact of any proposed changes on investment and fees.

The Chair issued a call for evidence on 3 April 2023 requesting views from market participants on the features of investment research that are under review. Responses to the call for evidence are requested by 24 April 2023.

The review into investment research stems from Lord Hill's Listing Review which identified issues with the availability and market for investment research. The Investment Research Review will be conducted on an independent basis and is expected to report findings within three months.

## Financial crime

### HMT and FCA update on market abuse regime review

HM Treasury (HMT) and the FCA issued [a joint statement](#) on 24 March 2023, announcing they have completed a review of the criminal market

abuse regime (which sets out the UK's criminal sanctions for insider dealing and market manipulation) and identified a number of areas where updates would be appropriate. HMT says it will consider changes to the regime alongside any reforms to the Market Abuse Regulation made through the Future Regulatory Framework Review.

## Governance

### Government and regulators seek views on SM&CR changes

HM Treasury (HMT) and the UK regulators kicked off their review of possible changes to the Senior Managers & Certification Regime (SM&CR) on 30 March 2023. HMT issued a [Call for Evidence](#) on the legislative aspects of the regime, and the FCA and PRA published a [Discussion Paper \(DP1/23\)](#), seeking industry views on the effectiveness, scope and proportionality of the regime, and how it might be improved. The Government first announced it would be carrying out a review of the SM&CR in December 2022, as part of the Edinburgh Reforms.

While a fundamental overhaul of the regime is considered unlikely, HMT and the regulators appear to be taking an open-minded approach to potential changes, asking a broad range of questions, and acknowledging that firms have raised some concerns about aspects of the regime. These include the growth in expectations of Senior Managers in respect of new and emerging risks, and recent delays in Senior Management Function approvals. HMT is also seeking views on how the SM&CR compares with similar regimes in other jurisdictions - including where there may be opportunities for greater alignment, and to improve the UK's competitiveness.

Both papers close on 1 June 2023, and HMT and the regulators will then decide whether to propose any specific changes to the regime. Please see our [At a glance](#) publication for more information.

## Market infrastructure

### FCA targets wholesale data market

The FCA published the [findings](#) from its wholesale trade data review on 3 March 2023, alongside the [launch](#) of its Market Study into competition dynamics in the markets for benchmarks, credit ratings data and market data vendor services.

The wholesale trade data review explored concerns regarding the access and use of wholesale trade data and highlighted where competition is not working well and the implications this could have on the price and quality of trade data and on UK investors and savers. The review draws three main conclusions:

- Large trading venues have significant market share meaning there are few substitutes for the breadth and coverage of their data. As such, there is limited scope for users to switch or negotiate price
- Trading Venues' complex pricing, licensing design and unclear contract terms mean it is difficult for users to monitor trade data costs and compare alternatives.
- Many users pay for delayed data, despite rules for it to be distributed for free.

The FCA notes it will continue to work with Government to develop a Consolidated Tape that it believes could help improve overall cost, quality and accessibility of wholesale data. Further to this, the Market Study was launched to investigate competition concerns in other types of wholesale data markets (benchmarks, credit rating data, and market data vendor services), and how these impact investment decisions and costs. The Study will examine how firms compete to win and retain customers and the impact this has on the price, quality of data/services, and on market innovation. The FCA is due to publish its Market Study report no later than 1 March 2024. If it identifies concerns in the market, the FCA may consider rule changes or firm-specific remedies.

## Operational resilience

### BoE and PRA share Cyber Stress Test findings

The BoE and PRA shared the thematic findings from the 2022 Cyber Stress Test (CST) in a [letter](#) addressed to PRA-regulated firms and financial market infrastructures on 29 March 2023.

The CST was an exploratory test based on a data integrity scenario in retail payments. It tested firms' ability to quickly identify the nature of the disruption they faced, and the potential financial stability impacts of firms not meeting the impact tolerance in the case where data integrity had been compromised.

The supervisory authorities highlight five key themes with associated actions that firms must take:

- Industry coordination: leverage existing frameworks and review out-of-business-hours responses.
- Communication: align communication across entities/channels and consider how pre-scripted messages could help maintain public confidence.
- Contingencies: investigate available contingencies and assess their combined effectiveness during incidents. The BoE and PRA recommend identifying and prioritising critical payments.
- Mitigants: develop robust and scalable processes, such as emergency cash or extended overdrafts, and develop industry-wide frameworks for standardising mitigant application.
- Reconciliation: develop and test tools for automated data reconciliation and ensure clean data availability during incidents.
- Testing capabilities: undertake planning and testing to strengthen testing capabilities, including technologies and processes.

Although distinct from operational resilience policy, the supervisory authorities anticipate that

firms will draw on the CST's findings to maintain their important business services within impact tolerances under severe yet plausible scenarios by March 2025.

## Reporting

### FCA and BoE update on joint transformation programme

The BoE and FCA provided an update on progress of the joint transformation programme (JTP) on 23 March 2023. In their [communication](#) to firms, they cover progress of phase two use cases and the implementation of phase one recommendations.

The phase one recommendations update highlights progress made in implementing two recommendations:

- Quarterly Derivatives statistical return (Form DQ): the supervisory authorities have worked on improving reporting landing pages, restructured reporting instructions, and standardised counterparty classification.
- Financial Resilience Survey (FRS): the FCA has successfully implemented a redesigned consumer credit return and is working on improving another return (FSA038). It is also developing a prototype for a 'Firm View at a Glance'. Additionally, the FCA is conducting user research for a unified portal for external logged-in systems and testing a new data collection process to improve the overall data collection design.

The communication also provides an update to firms on phase two use cases:

- The commercial real estate, the strategic review of prudential data collection from solo regulated firms and the incident, outsourcing and third-party reporting use cases have entered the design stage, focusing on key deliverables.
- The JTP will deliver recommendations by summer 2023 for the retail banking business model data use case.

The BoE and FCA also highlight that further progress has been made on the data standards review, which will consider the work of the TNFD.

## Sustainability

### BoE assesses integration of climate risks into capital framework

The Bank of England (BoE) [published](#) a report on 13 March 2023, updating its analytical approach to assessing the treatment of climate risks within the regulatory capital frameworks for banks and insurers. The BoE's report builds on its 2021 Climate Change Adaptation Report and identifies areas for future work, although it does not propose specific policy changes. The report incorporates: the findings from the BoE's 2021 CBES exercise, the PRA's 2022 thematic observations of firms' management of climate risks and its 2022 review of audit reporting for major UK banks, and an international 'Climate & Capital' research conference hosted by the BoE in October 2022.

The BoE summarises five main findings in its report, highlighting gaps in the current capital framework, capability gaps in risk management and gaps in the capital regime. The BoE also commits to further work to develop its regulatory framework, and requests further climate-related research contributions in specific areas across the banking and insurance capital frameworks.

See our [At a glance](#) briefing for more information.

### EU authorities enhance climate change disclosures for structured finance products

The ESMA, EBA, EIOPA and the ECB published [a joint statement](#) on 13 March 2023 on supporting enhanced climate change disclosure standards for structured finance products.

For example, the statement calls for better reporting on existing climate-related metrics across securitised assets, as well as the need for additional tailored metrics for these assets. There are currently no mandatory disclosure requirements in place, but the ECB and the European Supervisory Authorities

(ESAs) are taking steps to improve sustainability-related transparency in securitisations, e.g. ESA templates for voluntary disclosures of sustainability-related information for securitisations.

Finally of note, the authorities call on issuers, sponsors and originators of securitised assets to collect better data on climate-related risks during the origination process.

#### FCA flags concerns with ESG benchmark providers

The FCA published [a portfolio letter](#) to ESG benchmark providers on 20 March 2023. Following a previous communication in September 2022, outlining its supervisory priorities and view on risks within the sector, the regulator now highlights the conclusions of a preliminary review of a sample of UK benchmark providers. Concluding that the disclosures made require improvement, it draws attention to:

- a lack of detail and accessibility on the ESG factors considered in methodologies
- providers not fully implementing ESG disclosure requirements
- methodologies not being implemented correctly.

The FCA plans further work in this area and may seek explanations from the firms affected. The UK Government is also planning to issue a consultation imminently on plans to bring ESG data and ratings providers within the FCA's remit.

#### Pensions regulator reviews occupational pension schemes' TCFD disclosures

The Pensions Regulator (TPR) [published a review](#) of the first round of climate-related disclosures made by occupational pension schemes on 23 March 2023. This reporting is driven by regulations that came into effect from 1 October 2021, with first reports being published from mid-2022. TPR considered gaps, areas for improvement and examples of good practice for each area of TCFD (governance, strategy, risk management, metrics/targets).

The review found that: data quality and coverage remains a challenge; governance was generally a strong section in reports; approaches varied widely regarding strategy and scenario analysis; most trustees used their existing risk management framework to meet requirements; at least three climate metrics were included in most reports, but it was not always clear how much of the scheme's assets were included in the metrics; and all reports included the required climate-related target disclosures.

TPR expects the quality of reports to improve year-on-year and trustees will need to consider TPR's wider findings and address any disclosure gaps in future reports.

#### TNFD publishes final beta framework

The Taskforce on Nature-related Financial Disclosures (TNFD) released its [fourth \(v0.4\) beta framework](#) for nature-related risk management and disclosure on 28 March 2023. This marks the final draft of the framework before publication of the finalised recommendations in September 2023.

The final beta version contains mostly minor adjustments and does not change any core elements of the framework. Based on v0.3 feedback, the TNFD reduced the recommended disclosures from 15 to 14, proposed a tiered approach to disclosure metrics, and adapted the notion of 'scope' used in climate reporting to make it more appropriate in a nature context.

As a result, organisations will now have to disclose on activities and assets in their 'direct operations', 'upstream and downstream value chain(s)' and, where appropriate, 'financed activities' rather than their scope 1, 2 and 3 emissions. The tiers proposed for disclosure metrics are:

- Core Global Disclosure Metrics relevant to global priorities, including the Global Biodiversity Framework and organisations across sectors.
- Core Sector Disclosure Metrics.
- Additional Disclosure Metrics particularly relevant to an organisation and its operations.

The TNFD also released draft guidance on the use of scenario analysis; engagement with affected stakeholders; sector-specific considerations for the first four sectors it intends to cover; and four biomes, including tropical forests. Additional sector and biome guidance will be released in the coming months on a rolling basis.

The TNFD's final recommendations will be published in September 2023, following a final 60-day consultation process on v0.4. The ISSB will consider the TNFD recommendations when designing its standards on nature.

#### FCA delays rules on SDR and investment labels

The FCA [announced](#) a delay on 29 March 2023 to its Policy Statement (PS) on the proposals in CP22/20 (see our [At a glance on CP22/20 here](#)) to account for the significant responses it received. The FCA now intends to publish the PS in Q3 2023 rather than June 2023. This will impact the proposed timelines for introduction of the rules, particularly the anti-greenwashing rule which is due to take effect as soon as the PS is published.

#### Government reveals updated Green Finance Strategy

The Government published an [updated Green Finance Strategy](#) on 30 March 2023. The strategy provides important updates on a range of issues, including:

- UK taxonomy: this will be consulted on in the autumn and will be voluntary for two years, after which the Government will explore making it mandatory. This is a departure from the previously announced plans to implement it on a mandatory basis.
- Transition plan disclosure: The Government will consult on making it a requirement for UK private companies to report transition plans. This is to bring them in line with requirements of listed companies.
- Embedding International Sustainability Standards Board (ISSB) standards: The

Government confirmed plans to establish a framework to assess implementation of the ISSB standards. This is expected in the summer (the ISSB has stated the standards will be published in June 2023, with an expected implementation date of 1 January 2024).

- Call for Evidence on the reporting of scope 3 emissions: To better understand the costs and benefits of requiring reporting on this and using this information (due Q3 of 2023).
- Embedding Taskforce for Nature Related Financial Disclosures (TNFD): The Government plans to explore how the TNFD framework can be reflected in UK regulation, once finalised.

Alongside the strategy, the [Government published a consultation](#) on bringing ESG ratings providers within the regulatory perimeter. The consultation is focused on providers of ratings, rather than data providers. The proposals would cover any service providing an ESG rating to be used by persons in the UK in relation to a FCA regulated investment.

See our [At a glance](#) publications on the [Green Finance Strategy](#) and [ESG Ratings Consultation](#) for more information.

#### Treasury launches proposals to regulate ESG ratings providers

On 30 March 2023, HM Treasury (HMT) [consulted](#) on bringing ESG ratings providers within the remit of the FCA, where a provider's assessment is used in relation to a regulated investment, unless a specific exclusion applies. This would apply to information used in relation to activities within the UK, irrespective of the location of the provider.

The proposals do not extend to providers of raw ESG data as, although HMT acknowledges some risk associated with such providers, it believes this may be addressed by the implementation of the International Sustainability Standards Board standards. The proposals would apply to all services used in relation to FCA-regulated activities that provide an ESG rating (even if the

term is not used). The following exclusions are proposed: not for profits; ratings used solely by the entity that generated them; credit ratings that consider the impact of ESG on creditworthiness; investment research products; external reviewers, including third party verifiers; consulting services; proxy advisor services; academic research or journalism. The legislation would also not apply to proxy data providers.

The consultation seeks views on the best way to ensure proportionality, with a number of options being suggested on how smaller organisations should be considered. These options include: a complete exclusion from the regulation, different requirements for smaller organisations, or a voluntary opt-in. HMT also notes that it would expect a future regulatory regime to have considered international standards, such as [IOSCO's recommendations](#).

The consultation closes for comments on 30 June 2023. For more information, please read our [At a glance](#) publication.

# Banking and capital markets

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## Bank structures

### HM Treasury seeks input on ring-fencing reform

HM Treasury [published](#) a Call for Evidence (CfE) on 2 March 2023, setting out the Government's response to the Skeoch review of the UK ring-fencing regime (RFR). The review recommended in March 2022 that the Government consider ways of aligning the UK resolution and ring-fencing regimes, without undermining wider financial stability objectives.

The Government states that the purpose of the CfE is to explore the benefits and costs of the RFR and to inform how the regime could be reformed and aligned with the resolution framework. The CfE invites views on options for aligning the RFR with the resolution regime, as well as considering the benefits of the RFR (centring on resolution, supervision and future benefits) and the associated costs (focusing on operational costs and other business-related impacts).

On the range of potential options for reforming the UK ring-fencing regime, the Government proposes that these centre on retaining the current regime with no further changes; disapplying the regime; or further reform of the regime. In relation to potential disapplication, the CfE notes that the Government would also need to consider how to operationalise this option, should that be pursued. The CfE consultation will close on 7 May 2023. The Government will then issue a response to submissions received through the CfE and plans to publish a formal consultation paper later in 2023.

See our [At a glance](#) briefing for more information.

## Payments

### FCA calls out payments sector concerns

The FCA issued a [Dear CEO letter](#) to payments and e-money firms on 16 March 2023, highlighting regulatory risks and issues in the sector, and the actions firms should take to address these. Overall, the FCA remains concerned that many firms don't have sufficiently robust controls, and as a result, notes that some firms pose an unacceptable risk of harm to their customers and to financial system integrity.

The letter outlines three outcomes the regulator wants firms to take action to deliver. These are: ensure customers' money is safe, ensure firms don't compromise financial system integrity, and ensure firms meet customers' needs.

The FCA draws attention to failings identified in the sector, in particular noting issues relating to safeguarding, the appointment of auditors, prudential risk management, and wind-down plans. It also finds deficiencies in firms' know your customer processes, business-wide risk assessments, and sanctions screening solutions. Given the rising cost of living and potential increase in fraud, the FCA reminds firms of the need to regularly review and address weaknesses in fraud systems, as well as maintain ongoing customer due diligence controls.

The FCA also calls out significant issues with governance, oversight and leadership in the sector, and reminds firms of the Consumer Duty requirements to deliver good customer outcomes. This includes ensuring products and services meet customers' needs and that firms act in their customers' best interests.

The FCA expects firms' Boards to consider the risks in the letter and take prompt action to address any failings. Firms will be expected to

explain the actions they have taken in response to the letter.

See our [At a glance](#) briefing for more information.

## Prudential

### PRA adjusts approach towards non-performing exposures

The PRA [published](#) a consultation paper on 14 March 2023, setting out its proposal to remove the deduction requirement for provisioning shortfalls identified as 'non-performing exposures' (NPE). The PRA is also proposing to remove associated reporting requirements. The proposals would result in changes to the Own Funds and Eligible Liabilities (CRR) Part of the PRA Rulebook and the Reporting (CRR) Part of the PRA Rulebook.

Firms are currently required to deduct the 'applicable amount of insufficient coverage for non-performing exposures' from CET1 capital - the actual NPE deduction is calculated as the difference between the gross value of an NPE and the total value of the accounting and regulatory adjustments specific to the same NPE. The PRA has assessed that the NPE deduction does not provide an objectively accurate measure of NPE provisioning levels for PRA-regulated firms, given that it was originally designed and calibrated on an EU-wide basis. In particular, the PRA is concerned that the application of the NPE deduction might require deductions that are greater or lower than the level required to address actual underlying risks.

Instead, the PRA proposes to exercise supervisory judgment in deciding whether to address firms' expected losses from NPEs, rather than relying upon an automatic capital deduction. The PRA is also proposing to amend the associated NPE deduction reporting requirements by removing certain references from the relevant reporting templates. The deadline for comments is 14 June 2023. Once the PRA has confirmed its policy proposal, it anticipates implementation of the removal of the NPE deduction in Q4 2023.

See our [At a glance](#) briefing for more information.

## Retail products

### TSC questions banks on savings rates and executive pay

The Treasury Select Committee (TSC) [wrote](#) to the CEOs of the UK's four largest banks on 1 March 2023, asking them to provide information on their savings rates and executive pay. The letters follow the CEOs' appearance before the committee in February 2023, and ask for details on how the banks determine what proportion of interest rate rises they pass onto their customers. Harriet Baldwin MP, Chair of the TSC, said banks have a responsibility to offer 'reasonable savings rates' and said it is 'difficult to avoid the conclusion that our biggest banks are taking advantage of their most loyal customers to increase profits and CEO pay'. In the letters, the TSC also asks a number of follow-up questions from the February 2023 session, including on basic bank accounts and branch closures, and requests a breakdown of the revenue and profits generated by the banks' savings products.

### FCA finalises guidance on support for mortgage borrowers

The FCA published [FG23/2: Finalised Guidance](#) on 10 March 2023, setting out how mortgage lenders should support borrowers impacted by the rising cost of living. The guidance aims to clarify how firms can comply with existing FCA rules, guidance and principles, rather than introducing new expectations. Apart from some minor amendments, the guidance is unchanged from the draft guidance which the FCA consulted on in December 2022 and is effective immediately. The regulator seeks to remind lenders of the range of options they have to support customers, particularly those facing higher interest rates alongside the rising cost of living.

The guidance focuses on: providing forbearance, offering contract variations to support customers who would like to reduce their monthly payments, and exceptions to the requirement to provide

advice. The regulator reminds firms they can use automation or digital tools to meet the operational challenge of large numbers of customers requiring support at the same time. In the context of the rising cost of living, the FCA says this could include automating support for a group of customers with similar needs and circumstances. However, it notes that firms need to have controls in place to ensure forbearance arrangements are appropriate.

The regulator says it will continue to review how firms are delivering against its expectations. It reminds firms to consider what impact the incoming Consumer Duty will have on the range and nature of customer support measures they offer.

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## Advice

### FCA updates on investment advice regime

FCA Director of Consumer Investments, Therese Chambers, delivered a [speech](#) on 21 March 2023 providing an update on the FCA's work on the investment advice regulatory regime.

In the speech, Chambers gave an overview of the feedback to the FCA's November 2022 [consultation](#) on a simplified core investment advice regime, noting that there is a strong appetite for a market for cheaper and more simplified financial advice and that firms are supportive of the premise of the proposals. Chambers also highlighted firms' feedback regarding the limitations of the proposals, including how the regime is not applicable to certain businesses and how target market is defined. Chambers confirmed the FCA is currently considering the best way to respond to the feedback and take forward any simplified advice regime.

Chambers also updated on the FCA's proposed holistic review of the boundary between advice and guidance. The review is aimed at understanding how the boundary is operating in practice and where the current regulatory regime is too burdensome and detrimental to consumer outcomes. Chambers confirmed that accumulation products, including General Investment Accounts, ISAs and pensions wrappers, and decumulation assets, including pensions decumulation, will be in scope of the review. Defined Benefit transfer advice and other pensions that have safeguarded benefits, such as Guaranteed Minimum Pension or Guaranteed Annuity Rate, will be excluded from scope of the review.

Timings on the review remain undefined, but the FCA is working with HM Treasury to organise its engagement with industry as part of the review.

## Sustainability

### TSC raises concerns with FCA on sustainability proposals

Harriet Baldwin MP, Chair of the Treasury Select Committee, sent a [letter](#) on 9 March 2023 to the FCA's CEO Nikhil Rathi concerning the Sustainability Disclosure Requirements (SDR) and sustainable investment labelling proposals in the FCA's consultation CP22/20. The letter raised several issues that follow on from the evidence given by FCA officials to the Treasury Sub-Committee on Financial Services Regulations on 22 February 2023. On 23 March 2023, the FCA [published its response](#).

In its letter, the Committee requested a new cost-benefit analysis (CBA) of the proposals, including the costs posed to consumers who, following the provision of new sustainability information, elect to switch their investments. The FCA states in its response letter that this cost was not included in the CBA because the proposals do not require consumers to switch but rather look to inform that decision, which will ultimately depend on consumers balancing their individual preferences, including the cost of switching.

In response to the Committee's concerns regarding enforcement action, the FCA notes that it already monitors the market for sustainability-related claims that are not 'clear, fair and not misleading'. Once the proposed rules come into force, the FCA says it will be undertaking proactive, targeted reviews of compliance and will use all of its tools, including supervisory and enforcement action, to tackle misconduct.

Responding to the Committee's concern that certain proposed requirements are too onerous and diverge from other jurisdictions, the FCA states that the proposed rules were designed to be compatible with requirements in other jurisdictions. It also notes its work to help shape common international standards through IOSCO.

The FCA is expected to publish its Policy Statement containing final rules in Q3 2023

# Insurance

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## Conduct

### FCA publishes final business interruption claims data

The FCA [published](#) on 31 March 2023 the final set of business interruption (BI) claims data it has collected. The FCA has been collecting data from affected insurers on the progress of their non-damage BI insurance claims since March 2021. This was following the Supreme Court judgment on the FCA's BI test case in January 2021. Recent headline figures include 341 BI claims now pending a decision on validity by the insurers, and £1.4bn paid in aggregate in final settlement for 36,904 claims.

The FCA states that it has been closely monitoring firms' handling of BI claims since it started collecting this data. And that going forward, while it will not be collecting any further BI claims data, firms should continue to ensure they handle claims promptly and fairly, and act in their customers' best interests. The FCA also reminds firms that they should provide reasonable guidance to help a policyholder make a claim. The FCA signposts firms to its earlier [review](#) on how firms handled BI insurance claims, which includes good practices and areas where firms fell short of its expectations. The FCA emphasises the findings of its review are relevant to the claims handling function of all product lines, and not just BI.

## Prudential

### PRA speech on risk management, stress testing and ease of exit

Shoib Khan, Director of Insurance Supervision at the PRA, delivered a [speech](#) on the current risks to the UK's insurance sector at the Westminster Business Forum policy conference on 27 March 2023.

Recognising the current uncertain economic climate, including the liquidity challenges faced by some international banks, Khan explains models play a critical role in the way insurers manage their risk. Beyond internal models, the models insurers use include third-party natural catastrophe models used in pricing and reserving, economic capital models used to make business decisions, and models used to carry out stress testing. Given models drive business decisions made by boards and executives, Khan reminds insurers to reassure themselves of the continued validity of their models in the face of market stress.

Khan emphasises the importance of stress testing to understand vulnerabilities to severe scenarios. Khan states insurers should extend stress testing exercises to check the continued viability and availability of corresponding management actions. Additionally, reflecting on the PRA's Insurance Stress Test 2022 exercise, Khan confirms that the Bank of England plans to run a cross-sector stress test exercise, using severe financial markets stress scenarios. Banks, central counterparties, insurers and funds will be included in this exercise.

Finally, Khan explains that insurers should recognise where recovery is no longer the best option for policyholders, and at which point insurers should instead seek to exit the market in an orderly way. Khan confirms the PRA will issue a consultation on its approach to exit planning and its expectations from insurers later this year.

## Sustainability

### IAIS consults on climate risk supervisory guidance

The International Association of Insurance Supervisors (IAIS) [consulted](#) on proposed changes to supervisory guidance on climate-related risk on 29 March 2023.

The IAIS has performed a gap analysis of its existing supervisory material to assess how climate risk is already captured. As a result of this, IAIS intends to undertake a number of consultations over the coming 18 months on changes to the guidance related to various Insurance Core Principles (ICPs).

This consultation is the first and is seeking views on:

- proposed changes to the text of the ICP Introduction, highlighting climate risk as an example of an interconnected risk
- whether existing materials relating to ICP 7 (Corporate Governance) and ICP 8 (Risk Management and Internal Controls) remain appropriate
- whether the planned consultations should include consideration of transition planning or other issues.

The document also provides a general update on some of the IAIS's recent activity on climate risk, and notes that it intends to release an Application Paper later in 2023 that outlines supervisory considerations and good practices on scenario analysis.

The consultation closes on 16 May 2023

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