Written evidence submitted by OakNorth Bank

OakNorth Bank: view on the PRAs CP 5/22: The Strong and Simple Framework

These are the comments OakNorth Bank intends to submit to the PRA's CP. We, together with other mid-tier/challenger banks have also submitted comments through UK Finance.

Comments on the CP

- **Whilst it is good that the PRA is now looking to address this issue directly, we are particularly concerned about 1) the threshold size for challenger/mid-tier banks to qualify for such a regime (the proposal is set too low), and 2) the pace of delivery and the lack of detail of what a new regime would look like. If left unchanged, there will be a continued impact on the ability of challenger banks/mid-tier to scale and compete with the established incumbents successfully.**
- Although the PRA and FCA have done a good job in allowing the establishment of new banks in the UK, nothing discernible has been done to address the regulatory barriers to scaling that exist in the UK banking sector (and in some cases, like MREL, opportunities have not been taken). Since the financial crisis, there have been no credible scale competitors to the large established incumbent banks to emerge from this new bank cohort, suggesting some market failure or unnecessary regulatory barriers preventing growth[1].
- The policy proposals laid out to date do not yet include any detail on what such a new regime might look like in practical terms, e.g., in terms of the specific capital and liquidity regime, risk management requirements, operational resilience requirements and regulatory reporting etc.
- We understand that the PRA will not consult on this until next year, so it would be unlikely that any new regime would start until 2025 at the earliest. This would be six years since the PRA discussed the issue[2].
- Without the changes we have articulated below, we believe there will be little impact on banking competition in the UK. Together with the impact of MREL, it has led to less competition, higher prices for consumers and businesses, a lower flow of credit to the economy and lower UK economic growth.
- The £15bn threshold seems to bring in £15bn as the definition of systemic by the back door. With MREL being set at that level and now the strong and simple cut-off, it feels like that is the new level for the definition of systemic, even though the leverage ratio does not become a requirement until firms have £50bn of retail deposits.
- The £15bn threshold provides yet another barrier for firms to scale up and compete with the large banks truly.
- It is unclear why the simpler regime cannot be applied to larger firms (e.g., those with a balance sheet over £15bn), if they meet the other regime requirements, especially as the PRA has said they might extend it in the future. It seems odd that the development of this new regime, which will take up an enormous amount of policy-making time and will take a number of years to develop and implement, is targeted at those institutions least able to grow and provide real competition to the large, incumbent banks. While delaying the development of a streamlined/simplified regime for those challenger/mid-tier banks who are best placed to provide that competition.
- The regulatory regime has over 53 thresholds for deposit-takers. Many of these thresholds have been designed in isolation, and no one has stepped back to look at how firms scale from a smaller bank to get to the £50bn.
- The PRA should spend their time considering simplification of the regime for all firms. We have set out a number of areas below where it would be helpful for them to consider.

Areas where the regime could be further simplified for all firms, including those above £15bn

Being clearer on risk management expectations

- Bank's risk management should be enhanced and become more sophisticated as banks become larger and more complex. The PRA could helpfully set out in more detail the risk management capabilities they expect firms to have as they scale. Supervisory Statement 3/12 "Non-systemic UK banks: The Prudential

[1 and 2] As Sam Woods noted in his Mansion House speech in 2019, "it is notable that no new bank has successfully become a large bank" and nothing has changed in the intervening period.

Regulation Authority's approach to new and growing banks" does this for firms up to 5 years, and the Building Society Sourcebook does this for building societies. Having something similar for expectations on firms' risk management, moving from category 4-3-2-1 would be of benefit for all firms and hopefully also for the PRA.

Pillar 2a

The role of Pillar 2a capital should be reviewed. Capital held for these risks cannot be used to absorb losses from the crystallisation of pillar 2 risks as banks cannot go through their Total Capital Requirements (Pillar +Pillar 2a) without a risk of breaching Threshold Conditions. Therefore, the usefulness of Pillar2a capital should be considered. Instead, capital for these risks should be held as part of the buffer regime. We recognise this proposal would require a significant change to the capital regime and, in the meantime, have highlighted some areas where the PRA could take quick action that could be applied to all firms below £50bn, not just those below £15bn.

- Change the process for concentration risk to be calculated. Currently, this is set on a very mechanical basis by the PRA once every three years for challenger/mid-tier banks. As a bank grows, the concentration risk on its lending book usually decreases. However, the PRA will only commit to reviewing an ICAAP once every 3 years (vs every year for the larger banks), meaning that the concentration risk add on is quickly out of date, leading to a capital requirement that is not proportionate or risk-sensitive. This puts scaling challenger/mid-tier banks at a significant competitive disadvantage compared to their larger competitors.
- Remove or reconsider the concentration risk add-on for geographic exposure. The methodology penalises firms for being UK-centric when this is often preferable to firms having exposures in other countries, which introduces new risks. In addition, it is contrary for the strong and simple regime where firms have to have at least 85% of their credit exposures in the UK to be classified as simple.
- Remove the requirement to have external data for operational risk calculations. This is costly for firms and often data is not relevant. The PRA could provide aggregated data, or this requirement is removed and P2a operational risk is based on scenario analysis only.

Reporting

- The PRA could simplify reporting for all firms. Regulatory reporting has swelled from the introduction of COREP and FINREP. The PRA should undertake a review of what information they receive in FINREP/COREP, what they never use and what data they genuinely need.
- In addition, there is overlap with Bank of England statistical returns, Bank of England SMF collateral information, FINREP and ad-hoc regulatory returns. Again, the PRA should look to only gather information it actively uses and look for efficiencies and opportunities to de-duplicate regulatory reporting.
- For reporting that the PRA does need, more detailed worked examples and guidance should be provided to ensure accurate reporting.

Supervision

Along the lines of the new banks' supervision team, the PRA should create a specialist scaling bank supervisory area (including specialist and policy resources) and increase resources in this area, compared to the supervision of those firms with a static balance sheet and business model. This would better allocate resources to risk and would enable:

- A more dedicated supervisory resource focussed specifically on scaling banks, ensuring a consistent and detailed approach to scaling bank supervision.
- The ability for scaling banks to have a C-SREP or L-SREP more frequently than the 3–5-year cycle established challenger/mid-tier banks are currently subject to. More frequent capital and liquidity assessments would ensure a more proportionate capital and liquidity regime, benefiting both financial stability and competition.

- More precise articulation of regulatory expectations for this part of the banking sector (see the first point on risk management).
- Prudential policy that is more risk-sensitive and proportionate and that takes account of this peer group and can be developed and rolled in a timelier way.

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