Appointment Questionnaire for Jill May, to the Prudential Regulation Committee (PRC) of the Bank of England

17th August 2018

1. Do you have any business or financial connections, or other commitments, which might give rise to a conflict of interest in carrying out your duties as an external member of the PRC?

I have discussed my Board commitments, which are listed below, with the Secretary of the Bank (who is also the Bank's Conflicts Officer). He explored the role of NEDs at listed investment trusts and is satisfied that the NED role is focused on governance and does not have responsibility for asset class or stock selection, which is the responsibility of the trust's manager. He did not see my other business connections as likely to involve any conflict with the work of the PRC. I understand that the PRC endorsed these conclusions at a meeting ahead of my arrival, and the Court was informed.

These commitments are:

- Non-Executive Director, Ruffer Investment Company, a UK listed, Guernsey registered, investment company, which has an absolute return strategy
- Non-Executive Director, JPMorgan Claverhouse, a UK listed investment trust, invested in UK listed stocks
- Non-Executive Director, Sirius Real Estate, a UK listed company, invested entirely in German industrial property
- Non-Executive Director, ICAEW
- Member of Council, Durham University (term concludes 30/09/2018)
- Governor, Wellington College
- NED, Langham Industries, a private family engineering company

I am aware of the PRC Conflicts Code and the broader Bank Code and have adhered and will continue to adhere to them. I will of course report any potential issues to the Bank and take the Conflicts Officer's advice on how to manage them.

2. Do you intend to serve out the full term for which you have been appointed?

Yes

3. Have you taken on, or do you intend to take on, any other work commitments in addition to your membership of the PRC? If so, what impact will they have on your work at the PRC?

I have not taken on anything new since my appointment to the PRC. I have recently concluded my five year term as a Panel Member on the CMA and my NED investment trust roles for the most part involve quarterly Board meetings. The PRC role will be my primary focus and commitment for the next three years. I am not seeking but would not rule out an additional Board position during that period but only in the event that one of my existing commitments concludes and provided the nature of the role concerned would likely add to my knowledge of sectors and markets relevant to the PRC.

4. Please explain how your experience to date has equipped you to fulfil your responsibilities as a member of the PRC. To which areas of the PRC's work do you expect to make a particular contribution?

My executive career spanned some 25 years in financial services commencing with 13 years at S.G.Warburg & Co. Ltd where I worked in Corporate Finance, on a wide range of transactions for UK and international clients. This provided a good grounding in financial and business analysis in the context of assessing, executing and financing transactions for clients and familiarity with M&A

and capital markets. I spent a further 12 years at UBS as a Managing Director in group strategy roles which gave me a good knowledge of global international investment and wholesale banking.

I would also hope to be able to add value to the PRA's focus and interest in facilitating effective competition in the markets it regulates. It is clearly of importance to cultivate a competitive and dynamic financial services industry with proportionate and effective regulation that does not stifle innovation. I was a Panel Member of the CMA from 2013 until 2018 and worked on a variety of merger and market enquiries across different sectors, examining the competition issues arising, and making regulatory decisions as required.

The CMA Retail Banking Enquiry in 2015-16 furthered my understanding and stimulated an interest in retail banking in the UK as well as the SME banking and lending sector. The Panel's examination of the competition issues arising in that market included consideration as to the barriers and hurdles faced by smaller challenger banking institutions; the fragility, complexity and expense of the legacy IT systems of certain of the major retail banks, the consequent risks these might pose and highlighted the imperative of improving operational resilience at these firms. The work also involved examining new business models in retail banking and an appreciation of trends driving competition in the market, including the disintermediation of some of the more profitable activities of the big banks by new digital and Fintech operators.

My current Non-Executive roles in the investment trust and property sectors give me insight into UK and global asset management and into commercial property. I attend quarterly Board meetings with my fellow Board members to review business performance and to cover a range of governance issues.

I am experienced in working both in the private and public sectors and am familiar with different working cultures and expectations. I was a NED of the CMA for three years and a Member of Council of Durham University from 2012, sitting on its Audit Committee and Chairing the Student Appeals Committee.

I believe that my background and my business experience, particularly in financial services and competition regulation, will enable me to make a strong contribution to the work of the PRC.

5. What do you hope to achieve while on the PRC? What does success look like in this role?

My immediate focus is to understand better the current priorities of the PRA and to get to grips with a number of quite technical issues. I hope to be able to work with my fellow members to provide effective and constructive challenge to the executive, bring an outsider view to the debates of the Committee and contribute to sound decision making in the areas for which the PRC has responsibility, including regulatory strategy and supervisory issues.

I have considerable Board experience and can recognise good and effective Board practices, including how an individual's contribution helps shape and give rigour to decisions.

Success for the PRC would include completing the ring fencing of the UK banking system; in conjunction with the Bank, completing the 'gone-concern' preparations for resolution of banks; putting in place a comprehensive operational risk framework for banks; and making all necessary preparations for Brexit as well as reviewing and refining as required the regulatory reforms implemented since the financial crisis.

6. What have been the PRC's and before that the Board of the PRA's greatest successes, in your opinion? Where is there still work to be done?

The PRA has achieved a great deal in recent years. The strength and stability of the financial sector has been transformed and its ability to withstand shocks greatly improved. The UK banking system is much better capitalised now than it was before the financial crisis thereby making the UK financial system considerably more stable than 10 years ago. The results of the 2017 ACS stress test are testament to this, indicating that the major financial institutions are well capitalised and could withstand very serious shocks. The banking system is also much more liquid than it was; and it is much less interconnected than it was due to reductions in interbank lending and the rise of central clearing of OTC derivatives. Senior management accountability for their actions has been greatly improved by the introduction of the SM&CR. Structural reform, a huge programme of work for the financial institutions concerned and for the PRA, is largely complete. The introduction of a resolution regime by the Bank is also a major step forward. The PRA has successfully introduced Solvency II, a comprehensive set of reforms to prudential regulation for insurers.

The PRA has played an active role in international standard setting and is seen as a leading prudential regulator internationally. It will be important to maintain this reputation.

There is still some work to be done in refining the regulatory reforms of recent years, including ensuring that new capital rules do not cause unwarranted distortions and that the implementation of Solvency II in the UK for insurers is robust and any associated problems resolved appropriately.

There remain challenges and complexities ahead: Brexit presents significant uncertainties and a huge amount of preparatory work for international financial market participants. The PRA's role in providing stability and reassurance for the financial services sector at this time of upheaval is vitally important. The supervisability of new and complex structures arising from Brexit may pose challenges and underline the importance of retaining close relationships with regulators overseas.

The PRA and the PRC are turning attention to the many new and non-financial risks facing the UK financial sector which could threaten financial stability. There is much work to do - including ensuring firms' operational resilience and considering matters such as cloud outsourcing risks, the potential impact of climate change on financial institutions and a continuing focus on culture, accountability and governance.

7. What is your assessment of the public profile of the PRC, both within the industry and among the wider public? How important is it that the public understands the role of the PRC and the decisions it takes?

I think the profile of the PRC amongst the public at large is low. Whilst the PRC is a relatively new committee I am not sure that awareness of the predecessor Board of the PRA would have been very different. The profile amongst the financial community is certainly higher - regulation is such a major focus for all financial institutions that the work of the PRA and the decisions of the PRC are much better known.

It is important for the public to be confident that there is sound and competent financial regulation which can be relied upon to minimise the risks to UK financial stability and thus help ensure that the key economic functions that the public and business rely on in day to day life can continue. I am not sure that a more detailed appreciation of the remit and decisions of the PRC by the public is necessarily terribly important. It is vital though that the PRC has proper accountability and its regular TSC appearances are clearly a key element of this.

8. How do you intend to add to the public's understanding of the role and decisions of the PRC?

The external members of the PRC may not have the same public profile as those of the FPC or MPC and do not in general make public speeches on the work or policies of the PRA. Nonetheless once I am better acquainted with the organisation I would like to volunteer to take part in the Bank's outreach programme with schools and would also be interested to participate in any Bank or financial services diversity forums as this is an area of interest for me. I have been asked to participate in a roundtable/panel event at the Bank early in 2019 which aims to highlight what the PRA has achieved in terms of facilitating competition, and to take stock of where things currently stand.

9. What is your view of the transparency of the PRC? Is there any more that the Committee could be doing in this area considering that no formal minutes are published?

Whilst the PRC does not publish minutes of its meetings on account of the confidential information discussed at each meeting, it does publish significant numbers of consultation papers and discussion documents outlining its emerging thinking and proposed approach on all material matters affecting regulated firms. Senior PRA staff make many speeches, which are available on its website and some 150 documents are published each year. The PRA also runs an annual conference for banks and for insurers. The external PRC members have regular bilateral meetings with senior management of regulated firms to hear their views.

10. What are the main operational challenges now facing the PRC?

As I mentioned in the response to Question 6 Brexit presents great challenges. The situation remains unclear. Progress has been made, however, in clarifying the expected post-Brexit regime, including political agreement on a transition arrangement and the prospect of a temporary permissions regime in the UK. There will be a huge workload for the PRA given the need for large numbers of new authorisations of international banks and insurers who previously conducted business through the passporting regime. The PRA has indicated that EEA firms may (if they are not conducting material retail business) apply to be authorised as branches, assuming a cooperative relationship with the EU27.

A major challenge for the PRA relates to the supervisability of the new cross border structures. With additional complexity and fragmented markets come additional risks and effective supervision is more difficult. Potentially much more business will be conducted in branches of overseas banks and insurers rather than subsidiaries so cooperation with other regulators will be of paramount importance. There may also be related impacts on resolvability in the context of new banking structures with multiple regulatory resolution authorities.

Whilst the establishment of the post-crisis prudential regulatory framework is largely complete with only likely modest refinements to come, there are many new areas of potential risk to regulated institutions which require PRA attention. Ensuring firms have robust operational resilience is a major focus as new and elusive threats appear. These include cyber threats and outsourcing risks such as the use by regulated firms of cloud storage providers for firms' data.

Hand in hand with work on operational resilience must be continued focus on governance and on culture, incentives and accountability. So there is a great deal of work for the organisation which will require careful prioritisation to ensure best use of finite resources.

11. Which do you think are currently the greatest risks to the safety and soundness of the UK financial services firms, and how likely is it that those risks will crystallise?

I have addressed some of the PRA's challenges associated with Brexit in questions 6 and 10. The FPC judged in June 2018 that the UK banking system could support the real economy through a disorderly Brexit, and based on the results of the 2017 stress test, Brexit risks do not warrant additional capital buffers for banks.

Considering possible long term risks to retail banks, whilst competition in UK retail banking is welcome for the consumer, I think there is some concern about the future long term sustainability and resilience of the business models of some financial institutions. The sector is facing a rapidly changing competitive landscape - and while there has been increasing competition from challenger banks and from digital only banks for several years this may now accelerate with technological advances and the advent of PSD2 and Open Banking. This will make it potentially easier and cheaper for new entrants to enter the market and, with consent, to access customer data previously closely held by a dominant handful of banks.

Niche Fintech entrants are already focused on profitable parts of the incumbents' value chain including foreign exchange and payments, eroding margins. New banks may increasingly be able to capture entire customer relationships, potentially sucking deposits away from incumbents and impacting their lending ability.

More worrying for incumbents might be the comprehensive entry of a digital behemoth such as Amazon which would have the scale, resources, consumer trust and data advantages that might radically change the shape and profitability of the market.

Advances in technology and open APIs should also offer opportunities for the incumbent banks given their scale, customer ownership, brands and data together with vast low cost sticky deposit bases. Notwithstanding significant investment in redesign of business systems to reduce costs, a combination of interest margin pressures, higher capital requirements, structural upheaval, and conduct costs have weighed heavily on resources and profitability and large retail banks also may not have the necessary mindset and culture to embrace new ways of working and thinking. Legacy IT systems may be inflexible and fragile and not easily facilitate the grafting on of essential new technology and allow for the intelligent interrogation of big data.

The PRC and FPC are familiar with these risks and included these challenges in last year's Biennial Exploratory Scenario. The results did appear to give comfort that the financial institutions concerned were well protected notwithstanding very serious headwinds of this nature. Nonetheless this will be a continuing challenge looking ahead for Boards who will need to understand the main drivers of their business and profitability and how difficult it might be to reduce costs and respond to new competitive pressures that may be faster and more disruptive than they imagine.

There are also risks for smaller banks and institutions - challengers are finding life harder with a more competitive mortgage market and squeezed interest margins driving consolidation whilst building societies are also facing competitive pressure in mortgages and some are moving into higher risk asset categories. In general the low interest rate environment is contributing to strain on bank business models due to margin compression.

Cyber risk is a major threat to financial institutions and may be exacerbated by digital advances and data sharing and could be a threat to financial stability. This is particularly challenging for organisations with legacy IT systems and a lack of familiarity on the part of management and Board members with the nature of cyber risks. This is an area of particular focus for the PRA.

I am more familiar with the banking sector than insurance so have focused primarily on the former. Risks though to UK insurers include some of those facing the retail banking sector - increasing digitisation, higher customer expectations and challenges with legacy systems, consolidation and the need for cost reduction, and cyber risk. Low interest rates are driving a search for yield in the form of higher risk and less liquid investments for life insurers.

Having highlighted certain possible areas of concern, I am not aware of material near term risks to the safety and soundness of the major UK financial services firms that would prejudice financial stability. The rigours of the annual stress testing process which applies very severe shocks to bank business models gives comfort that there is considerable resilience across the sector. There is also great breadth of experience across the PRC and FPC and whilst it is early for me to judge it appears that established and emerging risks are rigorously considered and addressed.

12. What is your assessment of prudential regulation in the UK, and do you think that the PRC has the tools it needs to ensure the safety and soundness of the firms it regulates?

The current state of prudential regulation in the UK - with much improved capital standards, structural reform which is largely complete and an improved ability to resolve troubled firms - is measurably stronger than the pre-crisis state of affairs and is arguably one of the most robust by global regulatory standards. Aggregate Tier 1 capital for the major UK banks has tripled since 2007 and was 17% of risk weighted assets in Q1 2018.

I understand that the PRA is satisfied with its current supervisory toolkit and indeed many elements of that toolkit are at the forefront of global regulatory standards, an example being the SM&CR. The PRA continues to evolve its approach, and can flex its supervisory toolkit to take account of new developments and emerging risks.

13. To what extent are you concerned with the operational resilience of UK financial services firms?

The challenges for firms of ensuring their businesses are resilient to operational disruption have become more complex and intense during a period of technological change and a more hostile cyber environment. Additional challenges occur where firms operate internationally or outsource a significant level of activity to third parties. The importance of addressing these issues has been underlined by the recent IT problems experienced by TSB as it migrated to Sabadell's systems and the consequent significant inconvenience experienced by its customers. Operational disruptions to products and services provided by UK financial services firms have the potential to cause harm to consumers and market participants and could potentially threaten the viability of firms and cause instability in the system.

Operational resilience is a major focus for the PRC and a discussion paper was published jointly with the FCA and the Bank of England only in July on this subject. Operational resilience is already a responsibility of firms but the supervisory authorities are considering the extent to which existing policies might be supplemented to improve the resilience of the system as a whole and to increase the focus on this area within individual firms.

The PRA will expect firms to set their own tolerances for key business services in the form of clear metrics indicating when a disruption would represent a threat to a firm, to consumers or to financial stability. Firms will be expected to test their tolerances and demonstrate that they have concrete measures in place to deliver resilient services. Boards will be expected to play a key role as they develop their operational and cyber resilience strategies. Firms will also need clearly to define and regularly test their approaches to incident management and have viable, tested contingency plans for the resumption of critical functions in order to be able to recover from an operational incident.

14. What is your assessment of the incentive structures in place at UK financial services firms? What more could be done to improve accountability at firms?

Incentive and remuneration structures at UK financial services firms have been subject to significant change since the financial crisis with the adoption of the CRDIV remuneration rules, Solvency II and additional rules under the Senior Managers and Certification Regime including the requirement for the variable remuneration of individuals subject to the regime to be deferred for up to seven years. It is the responsibility of remuneration committees to implement the rules, but the PRA is concerned that incentive structures for the most senior managers are aligned with its regulatory objectives.

These new rules have had a major impact on the way variable incentives are structured and seek to align performance and reward and reduce incentives for excessive risk taking. Recent findings suggest that LTIP structures include more risk-adjusted performance metrics than before the crisis and also evidence of the effective use of performance adjustment tools although there is variation amongst firms.

The bonus cap is not supported by the Bank as it has resulted in institutions raising fixed remuneration in compensation for capped variable compensation, limiting their ability to claw back income in response to misconduct or a risk management failure or to reduce costs in less favourable times.

The SM&CR seeks to strengthen individual accountability and improve corporate governance through a clear allocation of responsibilities for senior management and those who have significant influence or the ability to cause significant harm to a firm's business. It also gives stronger powers of approval, supervision and enforcement to the PRA and FCA and is seen by firms and supervisors as a very positive step, already producing good outcomes in terms of greater clarity of responsibilities and enhanced accountability. This is now being extended to insurance companies in the UK by the end of this year although the PRA has already put the main elements of it in place.

Whilst the SM&CR is a clear step in the right direction culture change takes time. It is notable though that there have been encouraging market led initiatives such as the FMSB which will help reinforce change.

15. How is the PRC ensuring that climate related risks are sufficiently factored into firm's business models?

The consideration of weather-related risks has long been part of the PRA's approach to supervising general insurance firms. As the financial risks become apparent banks and insurers are increasingly considering climate change as a core financial and strategic risk rather than a CSR issue. The PRA has an important role in ensuring that regulated firms take a long term view and fully consider climate related risks in their governance and risk management frameworks and that proper disclosures are made. The PRA published a more specific review of the impact of climate change on the UK insurance industry in 2015, and routinely includes weather-related shocks in the scenarios for its biennial general insurance stress test. More recently, the PRA has extended its focus to climate-related financial risks faced by the UK banking sector, and will publish the results of this review shortly.

The banking review will highlight examples of good practice and the PRA intends to articulate its supervisory expectations for both banks and insurers later this year. More broadly, the PRA also recognises the value in sharing expertise and best practice, and participates in a number of related international initiatives, such as the Sustainable Insurance Forum and the Central Banks and Supervisors Network for Greening the Financial System.

16. What is your assessment of the competitive landscape in the UK financial services sector?

There have been well articulated concerns in the past about a lack of competition in retail banking. The CMA market enquiry into Retail Banking and SME lending concluded that there were competition problems and in particular that the lack of customer engagement and of switching by consumers made it difficult for new entrants to gain critical mass and thus effectively challenge the incumbents. A number of remedies have been implemented including Open Banking, enabling customers and SMEs to share current account information securely with other third party providers. The FCA is further investigating retail banking business models and how competition in the sector is working.

Whilst current account switching remains low, not least reflecting the lack of charges for many consumers, perceived homogeneity amongst major banks and lack of trigger points for review, the market for retail banking products is becoming measurably more competitive with multiple new entrants, many with new business models including digital-only banks eschewing expensive branch networks. The advent of PSD2 and Open Banking will likely accelerate change and drive further competition although it remains to be seen how quickly new entrants and challengers can gain necessary market share. The PRA has played a part in facilitating a more competitive landscape including through its joint work with the FCA in making it easier for new banks to be authorised and by implementing policies to address concerns that smaller banks were disadvantaged by the capital requirements of standardised risk models compared to internal ratings based models.

SME lending was also an area where the CMA had concerns about competition in the market. The implementation of the Banking Competition Remedies in the course of the next two years is designed to stimulate competition in this area and build critical mass amongst challenger banks.

In UK mortgage lending, there is currently strong competition, driven in part by new entrants and the need for ring fenced banks to find suitable assets. Consumer credit is also an area where there is strong competition between banks.

My understanding of the UK general insurance market is that it is highly competitive and for the most part functioning well. Some concerns have been expressed though that the competitive pressures in wholesale insurance markets are resulting in firms writing business on terms that would be unprofitable in an average catastrophe year and that risks are therefore heightened. On the life side there appears to be a competitive market for both savings business and for annuity business. More generally Solvency II should facilitate effective competition in the insurance industry as it provides a consistent framework for all participating firms based on market consistent balance sheets and risk based capital.

As regards the international competitiveness of the UK financial services sector the PRA is working to support the government's commitment to effective regulation of the sector, securing the right balance between a financial sector that is globally competitive yet secure. Concerns have been expressed that if UK regulation is too tough relative to other financial centres UK competitiveness will be diminished. In view of the PRA's objectives though, the primary focus must be on the benefits to all parties of a stable financial system as backdrop to a competitive business environment.

In insurance some have expressed concerns that our international competitiveness is being impaired by some aspects of the Solvency II rules, especially the risk margin, making some life business in the UK unattractive. The PRA is alert to this and has acknowledged some problems in the calculation of the risk margin and will work to rectify these.