The City of London Law Society

4 College Hill
London EC4R 2RB

Tel +44 (0)20 7329 2173
Fax +44 (0)20 7329 2190
DX 98936 – Cheapside 2

mail@citysolicitors.org.uk

www.citysolicitors.org.uk

Angus Moir
Bank of England
Threadneedle Street
London
EC2R 8AH

By email: DatacollectionDP@bankofengland.co.uk

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Dear Angus

Bank of England Discussion Paper – Transforming data collection from the UK financial sector (the "Discussion Paper")

The City of London Law Society ("**CLLS**") represents approximately 17,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi-jurisdictional legal issues. The CLLS responds to a variety of consultations on issues of importance to its members through its 19 specialist committees.

This letter has been prepared by the CLLS Regulatory Law Committee (the "**Committee**"). The Committee not only responds to consultations but also proactively raises concerns where it becomes aware of issues which it considers to be of importance in a regulatory context.

We welcome the opportunity to comment on the role that technology can play in regulatory compliance in response to the Bank of England's Discussion Paper on transforming data collection. This letter builds on our previous response to the FCA's 2018 Call for Input on digital regulatory reporting.

Summary

We welcome the Bank of England's ambition to make data collection more efficient for firms and more effective for it and other regulators. We also welcome collaboration between the regulators and the industry to provide a clearer and more standardised reporting regime. We note that this work overlaps with other initiatives to improve data collection in financial services, in particular the FCA and Bank of England's digital regulatory reporting pilot.

The Discussion Paper considers several options for improving data collection. Some options – notably agreeing a common input layer and writing instructions as code – could support a switch from a "push" to a "pull" model for collecting regulatory data. This would involve providing the regulators with direct data access and the ability to extract this data to provide nearer real time monitoring.

The Discussion Paper acknowledges that writing instructions as code would have legal considerations and that the legal status of the code would need to be clarified. But the paper does not go into detail on the legal implications for adopting this approach or the other options it considers. Subject to further clarity on what the preferred option(s) might be, we have commented in this response on general legal considerations such as liability, access and transparency.

Background to the Discussion Paper

The Discussion Paper notes that, in its response to the Van Steenis "Future of Finance" report, the Bank of England committed to developing a "*world-class regtech and data strategy*" and said that it would launch a review of how the hosting and use of regulatory data could be transformed over the next decade.

The Future of Finance report recommended that requests for structured data should be machine-executable and that regular requests should be coded so that firms can automatically read the requirements and pull the data from their systems. In its response to the report, the Bank of England said that it would engage with industry to explore a range of options, including potentially pulling data directly from firms' systems.

Responsibility for interpreting regulatory requirements

Currently, most regulation – including reporting requirements – is written in a natural language which is not sufficiently standardised format to allow firms to automatically read the requirements and pull the relevant data from their systems. Terms may be defined broadly or not at all. Human judgement is required to determine whether and how rules apply to the facts. As the Discussion Paper says, "*firms interpret [the Bank of England's] instructions to make judgements on what they need to report*" and, in turn, that interpretation "*requires firms to make their own judgements at various points about how those requirements apply to their own business*". A "*further challenge of interpretation*" is translating "*reporting definitions and guidance written in natural language into unambiguous data and technology requirements*".

By contrast, nearly all the options in the Discussion Paper contemplate setting common data inputs and/or agreeing industry data standards in a way which would reduce the scope for interpretation.

The first step towards modernising reporting requirements therefore requires someone to review the current regulation and rewrite it in a more prescriptive way, reducing sufficient ambiguity from the rule. This is likely to require that person taking a narrower interpretation of the scope of that rule. Whoever takes on this responsibility for rewriting the rule also takes the risk that its narrower interpretation does not capture the full scope of the original rule. It is possible that someone adhering to the more prescriptive version of the rule might not comply with the original rule.

There is a range of approaches which could be taken to create and maintain more standardised interpretation of reporting rules and instructions. For example:

- *Regulator-led approach*: The Bank of England and FCA could replace existing requirements with more standardised rules and instructions which reduce the scope for interpretation. These could be presented as code for regulated firms to apply to the data they hold. Alternatively, code could be provided as guidance which would demonstrate compliance with the underlying rule.

- *Firm-led approach*: Alternatively, each regulated firm could adopt its own interpretation of the requirements and apply automated operations to them to the extent possible.

- *Industry-led approach*: Another option suggested in the Discussion Paper would be to take an approach based on industry-agreed data standards.[1] There are clear benefits to using them where they exist e.g. ISDA's Common Domain Model. However, where they do not exist, the Discussion Paper notes that agreeing them, and migrating to them, would not be a trivial exercise.

The legal consequences will depend on the detail of the model which is adopted (e.g. determining where the responsibility for the standardised rule interpretation lies).

Implications of crowdsourcing regulatory interpretation

Regardless of which model for agreeing a new stricter interpretation is ultimately preferred, we assume that the regulatory requirements would remain unchanged and individual regulated firms would continue to be held responsible for the reports that they submit to the regulators, even where an industry-standard interpretation is relied upon.

A significant risk for a regulated firm under this model is that the interpretation is deficient in some way and results in that firm submitting non-compliant reports to the regulator. We anticipate that regulated firms would need assurance that the industry-standard interpretation does in fact meet the relevant requirements for the data they submit.

A broader risk of this approach is that any deficiency in the interpretation would be shared across many regulated firms. Errors in interpretation which today may only affect single reports or single regulated firms could be magnified to affect the whole industry.

If an industry-led model is preferred, we recommend that a governance framework is established to manage the development of the standardised rules. This would necessarily be an approach that brings the industry and the regulators together. Under this framework the industry may take the lead on agreeing a standard interpretation of the rules but with the prospect of a sign-off or similar endorsement from the regulators that this interpretation is sufficient for compliance.

The role of the regulators in this framework should also be to ensure that all impacted regulated firms are represented in the future development of the technology and to act as a counterweight to regulated firms' vested interests. The regulators would need to ensure that a modernised reporting regime does not excessively benefit some regulated firms, such as those with the resources and IT infrastructure to benefit from such a change, and disadvantage others.

Such a governance framework could not end once the technology is established but rather crowdsourcing an industry-standard interpretation would require ongoing maintenance to reflect changes in that interpretation over time. Without this, the standards may ossify and increase the risk of gaps in compliance.

Moving from push to pull: straight-through processing

A key area under consideration in the Discussion Paper is moving from a "push" to a "pull" mechanism for data collection which would allow for near real time changes to reporting rules and reporting instructions. We assume that if the Bank of England were to adopt this model, it would also be followed by the FCA and so this model could potentially be applied widely to various categories of data.

[1] The Discussion Paper points out that an additional benefit to this approach is that it "*could in some cases help to overcome a collective action problem, which may arise since individual firms require an incentive to move to any standard that does not reflect their own existing approach*".

There are several legal considerations that such a move would raise, including:

- *Degree of access*: At present, a regulator has no general right of access to a firm's data. Instead, it may require a firm to provide data of a specified type (e.g. under the FCA Handbook, SUP 15.3 for emerging events, SUP 16 for routine reports and FEES 4.4 for fee calculations). Obtaining other information would ordinarily require the regulator to undertake a formal investigation, which bring into play the statutory limits and safeguards associated with that process.

- *Interplay with other requirements*: It is not clear whether a firm, or individual, would be relieved of a proactive disclosure obligation (e.g. under SUP 15 / Principle 11 of the FCA Handbook or PRA Fundamental Rule 7) in a scenario when the regulator had, or could have, access to the relevant data via the firm's systems.

- *Consultation process*: If the regulators can pull data from firms' systems, external consultations on proposed rule changes could be considerably shorter or even dispensed with on the basis that the regulators would have access to the data in any event and could produce the reports they need on demand (although this would likely need a change in the regulators' powers under legislation).

- *Customer data*: Customers and counterparties may have concerns about the confidentiality of their data if the regulator has ongoing access to it.

If this approach is adopted, we recommend that:

- There should be some clear and enforceable limitations in the regulatory rulebook around how regulators' access is exercised, in particular as to scope of access, preservation of client confidentiality and non-access to protected items.

- Legal safeguards are put in place on the use of this data and transparent processes to inform regulated firms of what data is taken, when, and how it is used. Where possible, this information should be disclosed before the data is taken.

- The regulators clarify how the power to pull data from firms' systems would interact with existing proactive disclosure obligations.

- There should also be clear internal processes at the regulators for the approval of rule changes within the standardised reporting regime. Proposed rule changes should be put before the FCA Board or a specific committee designed to consider changes to the regime.

- Once it is established, significant changes (e.g. where new inputs are required) should continue to be open to consultation as for the existing process. Individual regulated firms and/or any industry group setting the standard interpretation would then be able to comment on the feasibility of the proposed change and work with the regulators on the change that is required to the standard interpretation and/or the storage of regulated firms' data.

- The process for rule changes should be built into an ongoing governance framework. The regulators have an important role to play to ensure that any rule change does not excessively benefit some regulated firms to the disadvantage of others.

Liability for reports

Depending on the model which is adopted, we assume that individual regulated firms will continue to be held responsible for the accuracy of the reports that they submit to the regulators.

We recommend that the regulators provide specific guidance on the liability for an error in a report which has been pulled from firms' systems. Errors which result from an agreed prescriptive interpretation of a rule or a standardised code should be treated more leniently than errors which result from firms' data not being held correctly or failures in their systems and controls. While technology is being developed, we recommend that firms are given the option of participating in a sandbox environment which allows them to test the new technology under enhanced regulatory supervision.

Careful consideration should be given as to what status the prescriptive interpretation of a rule or instruction written in code would have in law. Subject to further clarity on what the preferred model is, we expect that the original rule which is retained in the regulators' rules continues to be authoritative and that this is what would be referred to in the event of any enforcement action.

Finally, it is also important to clarify what the responsibility of a firm should be where it does not agree with an industry-wide prescriptive interpretation of a rule (or rule change). The governance framework to develop the technology should take this into account.

Individual accountability

In addition to our assumption that regulated firms will continue to be held responsible for the accuracy of their reports, we also assume that any individual responsibility with respect to those reports will also remain unchanged.

We do not think that the application of technology for regulatory compliance changes the fundamentals of firms' governance arrangements. However, the relevant Senior Manager(s) responsible for this area would benefit from additional guidance from the regulators regarding how best to exercise their responsibilities when relying on a standardised interpretation of rules.

In particular, if the "pull" approach is adopted, the Chief Operations Function (SMF24) or equivalent would benefit from additional guidance on the practical aspects of how the regulators would have access to the firm's data (e.g. what technical safeguards a firm should have in place to ensure that the only the relevant data can be accessed and that only the regulator(s) can access it).

Monitoring reports

In the context of transaction reporting, regulated firms must have appropriate systems in place to check the accuracy of transaction reports that are sent to the regulators.

Similarly, we recommend that any regulatory reports that the regulators pull from firms' systems are made available to those firms to allow them to cross-check their accuracy against the data they hold.

Identifying suitable rules

It should be acknowledged that the vast majority of regulatory requirements, including possibly many reporting requirements, are not amenable to being reproduced in code or even standardised language without considerable change to their scope. This may be because the data inputs which are required for a given rule are not stored or storable (for example, the FCA's fair, clear and not misleading rule). It may also be because the rule has been written to include deliberate ambiguity or human judgment (for example, where catch-all language has been used because the draftsperson cannot itemise every possible outcome which the rule is intended to cover).

To ensure the success of this work, including the digital regulatory reporting pilot, we recommend that its future development recognises the limitations of the technology and continues to focus on the limited number of practically automatable regulations i.e. technical, data-driven requirements. We anticipate that transforming the way that data is collected under even only these rules would still have a significant benefit on the overall burden of regulatory compliance for the industry

If you would find it helpful to discuss any of these comments then we would be happy to do so. Please contact Karen Anderson by telephone on +44 (0) 20 7466 2404 or by email at Karen.Anderson@hsf.com in the first instance.

Yours sincerely

Karen Anderson
Chair, CLLS Regulatory Law Committee

THE CITY OF LONDON LAW SOCIETY
REGULATORY LAW COMMITTEE

Individuals and firms represented on this Committee are as follows:

Karen Anderson (Chair, Herbert Smith Freehills LLP)
Matthew Baker (Bryan Cave Leighton Paisner LLP)
Peter Bevan (Linklaters LLP)
Chris Borg (Reed Smith LLP)
Simon Crown (Clifford Chance LLP)
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