BANK OF ENGLAND
PRUDENTIAL REGULATION
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Consultation Paper | CP5/13

Strengthening capital standards: implementing CRD IV

August 2013

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This Consultation Paper proposes changes to the PRA Rulebook, and introduces Supervisory Statements, to implement CRD IV

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1 Overview

1.1 This Consultation Paper (CP) sets out proposed changes to the Prudential Regulation Authority's (PRA's) rules in order to implement the package of European Union (EU) legislation known as CRD IV, consisting of the Capital Requirements Regulation(1) (CRR) and the Capital Requirements Directive(2) (CRD). This consultation is relevant to banks, building societies and PRA-designated investment firms, henceforth 'firms'.

Background

1.2 In June 2013, the European Union published legislation to implement within the EU 'Basel III', the international regulatory framework for banks developed by the Basel Committee on Banking Supervision. The legislation replaces the current capital requirements directives(3) with two new instruments: the CRD and the CRR.

Objectives of CRD IV

1.3 The financial crisis highlighted problems in banks' risk management practices and the regulatory framework. In general, banks failed to recognise the limitations of the level and quality of their capital and liquidity resources to deal with losses in certain risk activities and in periods of extreme stress and market disruption. Information problems also contributed to the mispricing of risks by financial institutions, regulators and the capital markets. The problems ultimately led to the breakdown in the ability of banks to carry out their critical economic activities, constraining intermediation and economic growth.

1.4 CRD IV aims to address these problems by:

- increasing the level and quality of capital held by banks;
- enhancing risk coverage;
- reducing procyclicality;
- expanding banks' disclosure requirements;
- providing a basis for EU liquidity standards; and
- introducing leverage disclosure requirements.

Level and quality of capital

1.5 The crisis showed that the level and quality of banks' capital was insufficient to deal with economy-wide shocks and financial stress. Proposals to enhance the quality of capital, and to raise the minimum amount of highest-quality capital banks must hold, address these issues.

Risk coverage

1.6 Banks' capital management practices did not consider the negative spillover their potential failure would have on the wider economy, especially during stressful periods. Proposals dealing with capital requirements for systemic firms, and expanded coverage of counterparty credit risks, help address these issues.

Procyclicality

1.7 Procyclical amplification of financial shocks throughout the banking system, financial markets and the broader economy was another source of instability. This amplification was facilitated by accounting standards for both mark-to-market assets and held-to-maturity loans, margining practices, and through the behaviour of leverage among financial institutions, firms, and consumers. The macroprudential measures and the countercyclical and capital conservation buffers in CRD IV help address these cyclical issues.

Disclosure requirements

1.8 The opacity of banks' activities prevented effective monitoring of bank risks and therefore the alignment of bank practices with the wider UK public interest. For example, heightened uncertainty about firms' exposures to complex structured products during the crisis disrupted funding markets as counterparties became increasingly reluctant to trade with banks. The CRD IV provisions introducing common reporting and enhancing disclosure standards help address these problems.

Liquidity

1.9 Many firms made excessive use of shorter-term liabilities to fund longer-term lending and assets, raising the level of liquidity risk on their balance sheets. Loss of confidence in firms' solvency rapidly raised the cost of short-term funding from wholesale markets and, at an extreme, led to widespread withdrawal of deposit funding, in effect bringing forward the likelihood of insolvency. Fire sales of assets, bank runs and the rapid onset of insolvency at some firms are evidence that

(1) Regulation (EU) No 575/2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms.
(2) Directive 2013/36/EU of the European Parliament and of the Council on the access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms.
(3) Consisting of two Directives: the Banking Consolidation Directive (2006/48/EC) (BCD), and the Capital Adequacy Directive (2006/49/EC) (CAD). Since its inception in 2006, the CRD has been amended several times, with major changes in 2010 (CRD II) and 2011 (CRD III).

liquidity positions left no room to manage underlying problems. The CRD IV provisions put in place a framework that, when implemented from 2015, will help address the liquidity risk problem.

Leverage

1.10 Excessive leverage at banks is another manifestation of the incentives for banks' management to take excessive risks. The use of aggressive modelling techniques to minimise measured balance sheet risks, facilitated by the opacity of the risks being measured, and the emphasis on capital minimisation exacerbate the risk of bank insolvency. The CRD IV leverage disclosure requirements will help to better expose firms' overall leverage.

Implementation

The legal nature of the CRR and the CRD

1.11 The CRR is the 'single rulebook' that gives effect to the majority of the provisions relating to Basel III: quality of capital, credit risk, counterparty credit risk, market risk and operational risk. The CRD contains, in particular, provisions concerning remuneration, enhanced governance and transparency arrangements, supervisory powers, supervisory review and evaluation processes and the introduction of new capital buffers. The different legal nature of the two instruments has implications for how the PRA will implement them in the United Kingdom.

CRR

1.12 The CRR is directly applicable in all Member States without the need for implementation by a national legal instrument. The PRA will not therefore transpose the text of the CRR into its rules. The PRA will, however, be required to delete any conflicting domestic rules. The PRA will therefore delete the Banking and Investment Firm Prudential Sourcebook (BIPRU) as this is substantially replaced by the provisions of the CRR, except liquidity rules in BIPRU 12.(1) The PRA will also disapply the General Prudential Sourcebook (GENPRU) to firms in scope of CRD IV as this is also covered by the CRR, except GENPRU 3 (cross-sector groups).(2) Amendments to the Supervision manual (SUP) and Systems and Controls (SYSC) chapters will be made as necessary to update existing provisions. The draft instruments to give effect to this are included in Appendix 1.

1.13 The PRA may give effect to CRR discretions and derogations through specific rules. In other cases the policy approach to case by case exercise of discretions is set out in supervisory statements. A brief explanation of the PRA's proposed use of such discretions and derogations, along with draft rules and supervisory statement text, is included in this consultation.

CRD

1.14 Unlike the CRR, the CRD is not directly applicable and must be transposed into UK law, including through PRA rules. A brief explanation of the PRA's proposed approach to this transposition, and the relevant draft rules text, are included in this consultation.

Powers

1.15 In implementing CRD provisions and relevant CRR discretions and derogations through PRA rules, the PRA acts as a 'competent authority' and will exercise its rule-making powers under the Financial Services and Markets Act (FSMA). In the exercise of 'supervisory powers' such as requiring firms to hold additional capital, the PRA may impose a requirement (i) on a PRA firm under section 55M of FSMA or (ii) on specified PRA firms as a general rule under section 137G of FSMA.

Issues to be addressed by other initiatives

1.16 Some requirements of CRD IV will be addressed by initiatives already under way; for example the requirement in CRD Article 74(4) regarding recovery and resolution planning will be addressed by planned amendments to the Financial Stability and Market Confidence Sourcebook (FINMAR) rules, as consulted on by the FSA in FSA CP11/16 and which the FSA provided feedback on in FS12/1. The CRD includes substantive new provisions on remuneration; remuneration issues are also raised in the Final Report of the Parliamentary Commission on Banking Standards(3) (PCBS). The PRA will consider its approach to remuneration in the context of the PCBS report. Those issues are not consulted on here.

EBA technical standards, guidelines and Q&A

1.17 The CRR and CRD provide for over 100 technical standards to be drafted by the European Banking Authority (EBA),(4) with varying deadlines for delivery by the EBA. Such standards are subject to adoption by the European Commission before entering legal force as directly applicable EU regulations. The EBA is also mandated to draft guidelines in specified areas. When adopted, these standards and guidelines may lead the PRA to adjust elements included in this consultation. Where particularly relevant, reference is made to the standards and guidelines in specific chapters of this CP. More information on progress with this work and consultations on the draft standards are available from the EBA.(5) The EBA has also launched a Q&A tool to facilitate common understanding of provisions related to CRD IV.(6) The PRA is engaged with this process but notes that, as made clear by the EBA, the Q&A

(1) National liquidity provisions may be retained for an interim period while the Liquidity Coverage Requirement (LCR) is phased in (see Chapter 12).
(2) GENPRU 3 transposes Directive 2002/87/EC and a provision of the BCD which is retained under CRD IV as Article 127 of the CRD. Consequential amendments to GENPRU 3, to reflect BIPRU deletion and CRR entry into force, will be consulted on later this year.
(3) www.parliament.uk/bankingstandards.
(4) In some cases in collaboration with other European Supervisory Authorities.
(5) www.eba.europa.eu.
(6) The 'Single Rulebook Q&A tool' covers questions on the CRD, the CRR, related technical standards, and EBA guidelines.

have no binding force in law, and are not subject to 'comply or explain' requirements. The PRA expects firms to develop an informed view of their obligations under CRD IV, related requirements and PRA rules, and to discuss issues with their supervisors where appropriate.

Process issues

1.18 Some of the rules consulted on in this CP and some provisions of the CRR give rise to new process requirements, such as a need for firms to apply to the PRA for approval to undertake a particular activity. Where necessary, information on such processes will be set out by the PRA in due course.

Co-ordination with other UK bodies

1.19 The PRA is co-ordinating with the Financial Conduct Authority (FCA) on CRD IV implementation where it affects the FCA's objectives.

1.20 Some provisions in CRD IV must be implemented by HM Treasury or other UK bodies. For example, CRD provisions on firms' disclosure of certain information on a country by country basis will be transposed by HM Treasury. HM Treasury will consult on this issue in due course. Further, HM Treasury must designate which authorities will be in charge of the application of the capital buffers for systemically important firms set out in the CRD. These provisions are therefore not included in the scope of this consultation.(1)

1.21 Article 458 of the CRR provides a mechanism for Member States to impose standards that are stricter than those set for microprudential purposes, when certain conditions are met and where this is necessary to mitigate macroprudential risks.(2) In the United Kingdom, the Financial Policy Committee (FPC) is charged with a primary objective of identifying, monitoring and taking action to remove or reduce systemic risks with a view to protecting and enhancing the resilience of the UK financial system.(3)

1.22 The FPC has powers to make recommendations on a 'comply or explain' basis to the regulators and to direct the regulators to adjust specific macroprudential tools. The UK authorities do not intend to use the process under the CRR immediately in order to introduce PRA rules to mitigate macroprudential or systemic risks already identified by the FPC. If and when such measures are necessary in the future, the PRA will consult on any required amendments to its rules to enact them.

The PRA's Policy Framework

1.23 The PRA has set out in the *PRA's approach to banking supervision* (henceforth the 'approach document')(4) its intention to replace the PRA Handbook (which contains material carried forward from the FSA Handbook) with a PRA Rulebook and to issue supervisory statements to provide additional general guidance. The aim is to set out clearly and concisely what the PRA expects of firms. To ensure use of the PRA's resources in the most efficient and economic manner, the PRA will phase in the transition to the PRA Rulebook.

1.24 The implementation of CRD IV is the first significant move towards establishing the PRA's new policy framework. The draft instruments in this paper exercising the discretions and derogations of the CRR and transposing new areas of rules from the CRD(5) are the first instruments to create the PRA Rulebook. They contain only rules, and firms should read these instruments and any accompanying draft supervisory statements together to understand the PRA's expectations. To support specific subject area rules, interpretative provisions and a central glossary are also necessary. These draft instruments are in Appendix 1.

1.25 These new instruments will be implemented into the current online handbook in PDF format, distinguishing the material from the PRA's legacy handbook provisions. The PRA will be reshaping the remainder of the PRA's rules and guidance over the coming years. The final supervisory statements and rules may be numbered or structured differently to the draft content. The PRA will include such changes in the final policy statement which will follow this consultation, alongside any substantive policy changes.

Structure of this paper

1.26 This paper consists of three parts. The first two are based on the structure of CRD IV: Part I: CRD and Part II: CRR. Discussion of the PRA's policy proposals is included in the part concerning the most significant relevant requirements.(6)

1.27 Part III: Economic analysis, considers the impact of CRD IV as a whole. The impacts of proposals that significantly change existing PRA policy are considered within each chapter.

1.28 Where relevant, related rules are attached in Appendix 1 and supervisory statements in Appendix 2.

Statutory obligations

1.29 In discharging its general functions of making rules and determining the general policy and principles by reference to which it performs particular functions, the PRA must, so far as reasonably possible, act in a way that advances its general

(1) However, the proposed interaction between the PRA's approach to Pillar 2 and the systemic buffers is set out in Chapter 2.
(2) Member States can set stricter standards in relation to the level of own funds, large exposures, disclosure, the level of the capital conservation buffer, liquidity, risk weights on residential and commercial property and intra-financial sector exposures.
(3) The FPC has a secondary objective to support the economic policy of the Government.
(4) www.bankofengland.co.uk/publications/Documents/praapproach/bankingappr1304.pdf.
(5) Ie all rules included in this CP apart from amendments to SYSC and SUP.
(6) For example, Reporting and Disclosure requirements are contained in both CRD and CRR, but as the most significant of these is the Common Reporting Framework as specified in the CRR, proposals are located in Part II.

objective to promote the safety and soundness of PRA-authorised persons.

1.30 The purpose of CRD IV[(1)] is to address problems highlighted by the crisis and so, among other things, promote the safety and soundness of firms in line with the PRA's objective. In implementing the CRD and exercising the discretions and derogations under CRR, the policy proposals being consulted on here advance the PRA's objective. Further information on the purpose and intent of the policies and proposed PRA rules is set out in each chapter.

1.31 In making its rules and establishing its practices and procedures the PRA must have regard to the Regulatory Principles.[(2)] In addition, when consulting on draft rules, the PRA is required to consider:

- the impact on mutuals;
- the impact on competition; and
- equality and diversity.

The PRA is also required to perform an economic assessment of the impact of its policy proposals (see paragraph 1.27 above).

Impact on mutuals

1.32 The PRA has a statutory requirement to state whether the impact on mutuals[(3)] will be significantly different from the impact on other firms. The provisions in CRD IV will affect mutuals. Mutuals are more constrained in their capacity to adjust, in particular to higher capital requirements. However, these constraints are generally factored into mutuals' business models and there are specific provisions for mutuals to issue instruments to meet requirements in Article 27 of the CRR. The impact on mutuals is discussed in more detail where appropriate within this document.

Impact on competition

1.33 The PRA has a duty to have regard to the need to minimise any adverse effect on competition in relevant markets. The provisions of CRD IV have the potential to change competitive conditions in the markets in which PRA supervised firms operate. More stringent capital requirements may raise the entry barriers to those markets that require firms to be authorised, which could have an adverse effect on competition. The CRR, over which the PRA has little discretion, contains the measures that are most likely to raise entry barriers in this context. The PRA's measures regarding barriers to entry will help to mitigate the possible adverse consequences.[(4)]

Equality and diversity

1.34 The PRA may not act in an unlawfully discriminatory manner. It is also required under the Equality Act 2010 to have due regard to the need to eliminate discrimination and to promote equality of opportunity in carrying out its policies, services and functions. As part of this the PRA assesses the equality and diversity implications of any new policy proposals considered. In general, the PRA's assessment suggests that the issues addressed in this CP do not give rise to equality and diversity implications.

1.35 The provisions on governance, set out in Chapter 4, include implementation of CRD requirements for firms and their nomination committees (where applicable) to put in place a policy promoting diversity on the management body; the nomination committee must also establish a target for gender representation on the management body. This is intended to improve diversity within firms' management bodies.

Responses and next steps

1.36 The implementation date for the majority of the CRD IV package is 1 January 2014.[(5)] To meet this date, this consultation closes on 2 October 2013. Views are welcomed on the issues raised in the CP. In particular respondents may wish to comment on:

- How the PRA is planning to operate discretions and derogations provided under the CRR.

- How the PRA is planning to operate the transitional provisions provided under CRD and CRR.

- How the PRA is intending to transpose the obligations in CRD into rules.

- The content of the draft Supervisory Statements.

- Existing PRA rules which will be deleted or disapplied as part of CRD IV implementation.

- Specific questions set out in individual chapters.

1.37 Respondents are requested to structure their responses on a chapter by chapter basis.

1.38 The PRA will publish a policy statement with feedback, finalised rules and final supervisory statements in December 2013.

(1) See paragraphs 1.3 to 1.10 above.
(2) FSMA 2H and 3B.
(3) Mutuals are defined as building societies, friendly societies, industrial provident societies and EEA mutual societies.
(4) See *A review of requirements for firms entering into or expanding in the banking sector*: www.fsa.gov.uk/static/pubs/other/barriers-to-entry.pdf.
(5) Specified sections are not required to be phased in until a later date, although in general the requirements must still be transposed into UK law (see the capital conservation buffer proposals, for example). Other elements of the proposal provide a delegation for the Commission to legislate further to introduce binding measures, such as the Liquidity Coverage Requirement. The United Kingdom may maintain its national rules in the area of liquidity until the LCR is fully implemented.

Part I Directive

2 Capital buffers

Articles 128-142, 160 CRD

2.1 This chapter sets out the proposed PRA implementation of the capital conservation and countercyclical capital buffer frameworks, and how they come together as a combined buffer.(1)

2.2 The buffer framework is intended to ensure firms maintain a sufficient amount of capital above their regulatory minimum, so that they can withstand periods of stress. This reduces their likelihood of failure and so contributes to the PRA's objectives.

2.3 New rules are proposed to implement these provisions; these rules are explained below and set out in Appendix 1.

Proposals

Combined buffer

2.4 The CRD creates a combined capital buffer that all firms will be expected to meet in addition to their Pillar 1 and Pillar 2 capital requirements (separately, the PRA may also impose a firm-specific buffer as described in the next chapter). The combined buffer must be met with CET1 capital and will include the capital conservation buffer and the countercyclical capital buffer, each of which is described in the sections below.

2.5 Firms that meet the combined buffer must not make distributions to shareholders or staff which would cause them to stop meeting it. Firms which do not meet the combined buffer must submit a capital conservation plan to the PRA explaining how they will meet the combined buffer within an appropriate timeframe. They will also automatically become subject to distribution constraints. These constraints prohibit firms from paying dividends or bonuses above a specified proportion of the profits after tax generated since their most recent distribution and which have not already been included in CET1 capital. Where firms are in the first quartile of their combined buffer (ie they meet between 75% and 100% of it), 60% of such profits can be distributed. In the second quartile, 40% can be distributed; in the third quartile, 20%; and in the fourth quartile, 0%.

2.6 Firms that cease to meet the combined buffer must inform the PRA of their maximum distributable amount (MDA), and the PRA proposes that they be required to do so within five days.

2.7 During any period in which firms do not meet the combined buffer they must inform the PRA of any intended distribution, and the PRA proposes that they be required to do so at least one month in advance of the intended date of distribution, unless exceptional circumstances justify a shorter timeframe. This notification should set out (amongst other matters) the firm's available capital, its MDA, and the details of the proposed distribution. To ensure a firm is able to meet its combined buffer within an appropriate timeframe, the PRA may consider exercising its powers under s. 55M of FSMA to prevent the firm from making an intended distribution.

2.8 Having regard to the regulatory principles, the PRA will take a proportionate approach to evaluating the capital conservation plans firms propose; for example, the PRA will use the discretion available to it to allow new entrants more time to build up their combined buffer.(2)

2.9 If the PRA does not approve a conservation plan, or a firm does not implement it, the PRA may impose supervisory measures such as requiring a firm to increase its capital to a specific level within a specific timeframe, or imposing more stringent restrictions on distributions than those imposed automatically.

2.10 Banks hold voluntary buffers over capital requirements for a number of reasons. One important reason often cited is the desire to avoid costly intervention stemming from a breach of the minimum regulatory requirements. The consequences of not meeting the CRD buffers, as set out above, are less severe than the consequences of breaching the legal minimum requirements. Banks may therefore choose to reduce their voluntary buffers over all regulatory measures in response to the introduction of the CRD buffers.

2.11 While the regulatory buffers have capital compliance cost implications, potentially raising the cost of capital for some firms, the increase will be offset to the extent firms reduce their voluntary buffers. Also, as discussed in Chapter 15 (Economic analysis), the benefits of the CRD IV package include a reduction in the likelihood of financial crises and the ensuing costs (expressed as a loss of GDP). Although this impact derives from the CRD IV as a whole, the required buffers contribute materially to this overall favourable

(1) As noted in Chapter 1, the systemic buffers set out in CRD are not in the scope of this CP.
(2) See *A review of requirements for firms entering into or expanding in the banking sector*, www.fsa.gov.uk/static/pubs/other/barriers-to-entry.pdf, pages 11 and 44.

systemic effect, which is expected to exceed the costs to individual firms.

2.12 The PRA recognises that it may be difficult for some firms, and particularly mutual societies, to build up their capital buffers in the short term given their more limited access to the capital markets. These firms, however, have other alternatives, including balance sheet restructuring and earnings retention, which are also viable options for all firms.

Capital conservation buffer

2.13 Within their combined buffer, all firms will be subject to a capital conservation buffer of 2.5% of risk-weighted assets (RWAs) at both group and solo level. The purpose of this buffer is to enable firms to absorb losses in stressed periods. The PRA proposes to introduce this buffer from 1 January 2016, in line with the transition timetable set out in the CRD (ie 0.625% in 2016, 1.25% in 2017, 1.875% in 2018 and 2.5% in 2019).

Countercyclical capital buffer

2.14 The countercyclical capital buffer (CCyB) requires firms to build up capital when aggregate growth in credit is judged to be associated with a build-up of system-wide risk. The buffer can then be drawn down to absorb losses during stressed periods. An increase in the CCyB provides a cushion to absorb losses that are larger than anticipated under the normal microprudential regime, as well as providing incentives for firms to avoid excessive or underpriced exposures. A release of the CCyB when threats to stability are judged to have receded could help mitigate a contraction in the supply of lending.

2.15 If effective, the CCyB may also result in smoothing the credit cycle and avoiding troughs similar to those a number of economies experienced during the crisis. As it is a new tool, there is an element of uncertainty around its success. However, it is clear that its effectiveness will be reduced if firms do not release capital and instead keep it within their voluntary buffer when the CCyB is reduced.

2.16 The CRD requires each Member State to designate an authority which will be responsible for setting the CCyB rate for credit exposures in that Member State on a quarterly basis. HM Treasury has proposed that the Bank of England be the designated UK authority for the CCyB, with the responsibility for policy decisions on the CCyB delegated to the FPC.(1)

2.17 As set out in the draft rules in Appendix 1, firms will be required to calculate their firm-specific CCyB rate as a weighted average of the buffer rates that are being applied in jurisdictions to which they have a relevant credit exposure. By 1 January 2014, the EBA must draft regulatory technical standards on the method for identifying the geographical location of relevant credit exposures. In accordance with the CRD, the PRA proposes to make a rule requiring firms to identify the geographical location of a relevant credit exposure in accordance with those standards when they are adopted by the European Commission.

2.18 Each firm will also be required to disclose the geographical distribution of its exposures, as well as the amount of its CCyB, as set out in Article 440 of the CRR. The EBA must draft regulatory technical standards on disclosure requirements by 31 December 2014.

2.19 Parts of the regime for the CCyB in the United Kingdom will be determined by HM Treasury, including the authority responsible for setting the level of the CCyB for the United Kingdom, the timetable for implementation and transitional arrangements. HM Treasury will consult separately on these arrangements. Therefore, draft rules included in this CP may be subject to change.

2.20 The CCyB regime must be introduced by 2016, though Member States can begin to use it sooner. Draft PRA rules are included in this CP for the operation of the CCyB before 2016, though these may be subject to change depending on the precise powers given to the FPC by HM Treasury over CCyB rates (including powers to reciprocate rates set by overseas authorities) before 2016. These draft rules would require firms to apply the CCyB rate (if any) set by the FPC for exposures in the United Kingdom and CCyB rates reciprocated by the FPC for exposures located overseas.

2.21 From 2016, within the EEA, each firm will be required to apply the buffer rate set by the designated EEA or third-country authority to exposures located in the respective EEA state or third country, where the buffer rate does not exceed 2.5% of RWAs. For EEA or third-country buffer rates above 2.5%, the FPC must choose whether to recognise such rates for UK authorised institutions' exposures to those jurisdictions. The FPC has stated that it expects to reciprocate overseas authorities when such CCyB rates are judged appropriate.(2) For exposures outside the EEA, the FPC can set buffer rates where none has been set by the relevant overseas authority and set buffer rates that are higher than those chosen by the relevant overseas authorities.

2.22 CRD IV sets out transitional provisions which permit Member States to cap the firm-specific CCyB at 0.625% of RWAs in 2016 rising to 1.25% in 2017 and 1.875% in 2018 irrespective of the buffer rates set by individual jurisdictions. The extent to which this affects a firm will depend on the geographical distribution of its exposures, as well as the FPC's decisions on whether and when to activate the CCyB in the

(1) See HM Treasury's Financial Services Bill: *The Financial Policy Committee's macro-prudential tools*; available at www.gov.uk/government/uploads/system/uploads/attachment_data/file/191584/condoc_fpc_tools_180912.pdf.
(2) See the FPC's Draft Policy Statement, *The FPC's powers to Supplement Capital Requirements*, available at www.bankofengland.co.uk/financialstability/Documents/fpc/policystatement130114.pdf.

United Kingdom and the rate set. The draft PRA rules included in this CP do not set a cap, though this may be subject to change depending on the approach taken by HM Treasury to implementing the CCyB in the United Kingdom. HM Treasury will consult separately on this approach.

3 Pillar 2

Articles 73, 79–85, 87, 97–98, 102, 108–109, 110 CRD

3.1 This chapter sets out the implementation of changes to the 'Pillar 2' provisions, ie firms' internal capital assessments and the supervisory review of those assessments as set out in the CRD.

3.2 Pillar 2 is intended to ensure that firms have adequate capital to support all the relevant risks in their business, and that they have appropriate processes to ensure compliance with the CRR and CRD. It is also intended to encourage them to develop and use better risk management techniques in monitoring and managing their risks. Pillar 2 therefore acts to further the safety and soundness of firms, in line with the PRA's objectives.

3.3 Proposed rule changes are explained below and set out in Appendix 1, with supporting supervisory statements in Appendix 2.

Proposals

3.4 There are two main areas that the PRA considers when conducting a Pillar 2 review: (i) risks to the firm which are either not captured, or not fully captured, under the CRR (eg interest rate risk in the non-trading book or credit concentration risk respectively); and (ii) risks to which the firm may become exposed over a forward-looking planning horizon (eg due to changes in the economic environment).

3.5 The PRA refers to the first area as Pillar 2A and the second as Pillar 2B. In addition to the (Pillar 1) requirements of CRR, the PRA regards capital held under Pillar 2A as the minimum level of regulatory capital a firm should maintain at all times in order to cover adequately the risks to which it is or might be exposed. Additional capital held under Pillar 2B is a capital buffer which helps to ensure that firms can continue to meet minimum requirements (Pillar 1 and Pillar 2A) during a stressed period.

3.6 The proposals in this chapter implement the PRA's Pillar 2A regime and explain how the Pillar 2B regime will operate alongside the CRD buffers when they are phased in. The rules in Appendix 1, which give effect to this, are supplemented by two supervisory statements. One sets out the PRA's expectations of firms' ICAAPs[1] and the PRA's approach to the SREP.[2] The other sets out the PRA's expectations of firms' stress testing, scenario testing and capital planning capabilities, and the related microprudential buffer framework.

3.7 Firms should be aware that, independent of the CRD, the PRA is currently developing its approach to the treatment of risks under Pillar 2 and the application of associated supervisory measures. This may include the use of new supervisory powers referred to in the CRD such as requiring additional disclosures by institutions. The PRA already has the power to apply these new supervisory measures under FSMA. The PRA will communicate on the wider reforms of its approach to Pillar 2 in due course.

3.8 The CRD also mandates the EBA to produce guidelines on the conduct of the SREP. The PRA may, if appropriate, make amendments in future to reflect best practice identified in these guidelines.

3.9 In March 2013 the FPC made recommendations to develop regular stress testing of the UK banking system to assess the system's capital adequacy.[3] The Bank, including the PRA, is currently considering how to implement those recommendations. This work is likely to influence the PRA's expectations with regards to stress testing and the setting of the PRA buffer going forward. Further information on the approach the Bank and the PRA will take in responding to the FPC's recommendations will be communicated later this year.[4]

Pillar 2A

3.10 The CRD sets out requirements on firms with regard to their ICAAPs and internal procedures and control mechanisms, but does not directly change supervisory expectations in relation to Pillar 2A. The PRA proposes to implement these requirements through PRA rules.

3.11 The PRA believes that it is useful to provide high-level principles setting out its expectations of firms' ICAAPs and the PRA's conduct of the associated SREPs. A draft supervisory statement, building on the principles outlined in the PRA's approach document, is in Appendix 2.

(1) The ICAAP (the Internal Capital Adequacy Assessment Process) is undertaken by a firm to identify the risks to which it is or might be exposed, assess the amount and quality of capital it requires and ensure that as a whole it is adequately capitalised on a forward-looking basis.
(2) The SREP (the Supervisory Review and Evaluation Process) is the PRA's process to assess a firm's capital adequacy.
(3) www.bankofengland.co.uk/financialstability/Pages/fpc.
(4) As set out in the June 2013 *Financial Stability Report*, a discussion paper on stress testing will be published in Autumn 2013: www.bankofengland.co.uk/publications/Pages/fsr/2013/fsr33.aspx.

3.12 As with the existing Pillar 2 regime, the ICAAP will represent the first stage of the evaluation of the risks that a firm faces or might face in the future and will be reviewed by the PRA via the SREP. The PRA will advise a firm of the results of this evaluation and will set Individual Capital Guidance (ICG).

Changes to the quality of capital eligible for Pillar 2A

3.13 The PRA proposes that firms should meet Pillar 2A with at least 56% Common Equity Tier 1 (CET1) capital from 1 January 2015. Currently, Pillar 2A can be met with any regulatory capital, unless the PRA specifies a particular quality of capital. The CRD places greater emphasis on CET1 than the current regime. And consistent with that, the PRA is consulting on whether to move to firms meeting Pillar 2A in full with CET1 from 1 January 2016.

3.14 This proposal increases the quality of capital with which firms must meet Pillar 2A requirements. It does not change the magnitude of Pillar 2A assessments themselves.

3.15 This change may increase the cost of capital for some firms to the extent that existing, voluntary capital buffers are not of sufficient quality to support Pillar 2A. If they are not, then firms may elect to issue new capital, reduce dividend payouts or remuneration and/or alter the composition and size of their balance sheets.

The legal form of Pillar 2A

3.16 Pillar 2A is currently set as individual guidance on the capital that the PRA considers a firm should hold, in addition to meeting its Pillar 1 requirements, in order to comply with the overall financial adequacy rule. That rule requires a firm to hold adequate financial resources to ensure that there is no significant risk that it will fail to meet its liabilities as they fall due. Pillar 2A is therefore the PRA's quantitative view of what is required by that high level qualitative requirement. If a firm does not meet the guidance, this does not necessarily mean that it no longer meets the overall financial adequacy rule. The PRA will consider whether the firm is in breach of the rule and of the Threshold Conditions, but it will not reach this conclusion automatically.

Questions

Should Pillar 2A be set as:

(A) a firm-specific requirement under section 55M of FSMA to hold a specified amount of capital; or

(B) guidance on the capital the PRA believes a firm should hold to meet the overall financial adequacy rule?

What are the benefits and costs of a requirement to meet Pillar 2A risks with CET1?

Should this requirement be phased in by 1 January 2016? If not, over what period should it be phased in?

What implications are there of different minimum standards for the quality of eligible capital to be held against Pillar 1 and Pillar 2A risks?

3.17 The draft supervisory statement in Appendix 2 is drafted on the basis that the PRA will continue to set Pillar 2A as guidance. But the implications of the alternative approaches are set out below.

(A) Implications of setting Pillar 2A as a regulatory requirement:

- a firm that did not meet Pillar 2A would be in breach of a regulatory requirement, which would trigger the exercise of PRA powers to take disciplinary and other enforcement action; and

- although the 'soft landing' provided by a guidance-based Pillar 2A would be removed, this may become less necessary since a firm that no longer meets Pillar 2A will have crossed a number of restrictions on distributions as it used up its combined buffer.

(B) Implications of setting Pillar 2A as guidance:

- the PRA would retain discretion not to deploy formal powers against a firm for minor failures to meet Pillar 2A guidance (although it would ask the firm to remedy the position);

- before taking action in respect of failures to meet Pillar 2A guidance, the PRA would have an opportunity to revisit the supervisory judgements represented by a firm's Pillar 2A assessment, and to consider what supervisory actions are appropriate to the specific case; and

- failures to meet Pillar 2A which can be immediately rectified may be less likely to trigger disclosure obligations or the automatic termination or breach of funding agreements and other financial contracts.

Pillar 2B — the PRA buffer

3.18 The PRA expects that in some cases the CRD buffers will be sufficient to enable a firm to meet its capital requirements under stress, in line with the PRA's risk appetite. But for other firms (for example firms with particularly vulnerable business models) additional capital may be necessary.

3.19 In some circumstances, firms may therefore be expected to hold a firm-specific PRA buffer incremental to Pillar 1, Pillar 2A, any sectoral capital requirements and the CRD buffers. The PRA buffer will replace the current Capital Planning Buffer

(CPB). The PRA will set PRA buffers based on a range of factors including, but not limited to, firm-specific stress test results.

3.20 The PRA will provide more information on the transition to the PRA buffer in due course. Meanwhile, firms will continue to be subject to the current CPB policy as described in the draft supervisory statement on ICAAP and SREP, in Appendix 2.

Changes to the quality of capital eligible for Pillar 2B

3.21 PRA buffers, when introduced, will be set in CET1 capital, consistent with the CRD buffers, because buffers should be fully loss-absorbing on a going concern basis. The PRA will give consideration to the appropriate transition for the change in the quality of capital in Pillar 2B.

Relationship between the PRA buffer and the CRD buffers

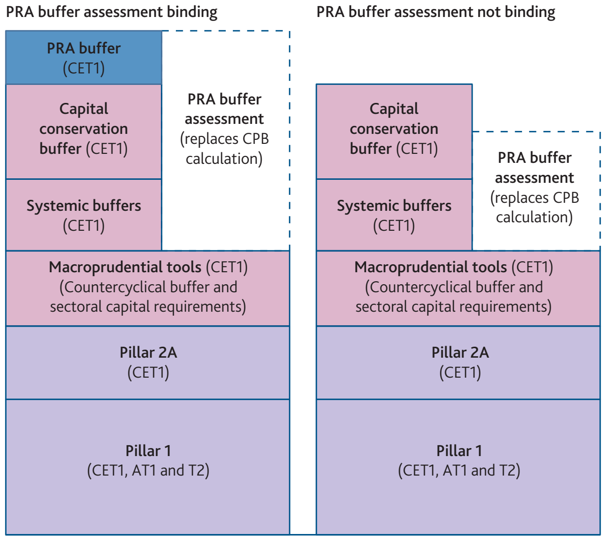
3.22 Capital used to meet a firm's CRD buffers may not be used to meet its PRA buffer. Quantifying the PRA buffer is a two stage process:

(1) the PRA will determine how much buffer capital a firm needs to achieve the purpose of the PRA buffer (hereafter the 'PRA buffer assessment'); and

(2) the PRA will then assess the extent to which the CRD buffers already address the risks identified in the PRA buffer assessment and will decide whether additional capital is required.

The PRA buffer is therefore a net amount.

Chart 3.1 The Pillar 2 capital framework[a]



AT1 = Additional Tier 1 capital; T2 = Tier 2 capital.

(a) Each chart should be read from the bottom up.

3.23 **Chart 3.1** illustrates a firm's total capital requirements and their relationship with the PRA buffer. In some instances, the PRA will not set a buffer if the CRD buffers are deemed sufficient, as illustrated in the right-hand column of the chart. This approach has regard for the differences in nature of the businesses of different firms, in accordance with the regulatory principles. Capital that firms use to meet their minimum requirements (Pillar 1 and Pillar 2A) cannot be counted towards meeting their buffers. All buffers are in CET1 capital.

3.24 The CRD buffers that appear in **Chart 3.1** are described in Chapter 2 (Capital buffers).[1]

3.25 The Capital Conservation Buffer (CCoB) has a similar purpose to the PRA buffer, so the PRA will deduct the CCoB from the PRA buffer assessment. Similarly, the PRA's intention is that the PRA buffer assessment will reflect a firm's systemic nature, and insofar as this is the case the PRA would expect to deduct the CRD systemic buffers (where applicable) from the PRA buffer assessment. For macroprudential policy decisions to be transmitted effectively, capital held to meet macroprudential tools (the Countercyclical Buffer (CCyB) and sectoral capital requirements) must be additive to the PRA buffer assessment.

3.26 The FPC will influence the total level of buffer capital in the system by setting the CCyB rate and sectoral capital requirements. The FPC will also be able to recommend to the PRA that it raise or lower the aggregate level of PRA buffer capital, and may make that recommendation on a comply or explain basis.

Consequences of not meeting the PRA buffer

3.27 A firm which does not meet its PRA buffer can expect enhanced supervisory action, and should prepare a capital restoration plan. If the PRA is not satisfied with the capital restoration plan or with the firm's reasons for using the buffer it may consider using its powers under section 55M of FSMA to require the firm to raise sufficient capital to meet the buffer within an appropriate timeframe.

3.28 The automatic distribution constraints associated with the CRD buffers do not apply to the PRA buffer.

(1) With the exception of the systemic buffers. As set out in Chapter 1, the PRA is not consulting on the introduction of the systemic buffers as part of this consultation paper. However, the intended future interaction between these buffers and the PRA buffer is set out here to provide greater clarity.

4 Governance

Articles 74–76, 88 and 91–96 CRD

4.1 This chapter sets out the PRA's implementation of changes relating to governance.

4.2 The CRD provisions on governance are intended to ensure that firms and their management organise and control their affairs responsibly and effectively. Sound governance practices and procedures enhance the safety and soundness of firms, in line with the PRA's objectives.

4.3 Although many of the rules in the CRD in these areas have been carried over from the current EU legislation, there are some significant changes. Proposed rule changes, which affect SYSC, are explained below and set out in Appendix 1.

Proposals

Governance arrangements

4.4 The PRA proposes to implement the revised CRD governance provisions by amending the relevant chapters of SYSC with copied out CRD text.

The management body

4.5 The CRD sets out the individual and collective responsibilities and requirements of the members of a firm's management body.(1) These will be transposed into Rules in SYSC 4.

4.6 The CRD introduces a new requirement that the roles of chairman and chief executive should not be combined, unless justified by the firm and authorised by the competent authority. Firms who wish to combine these roles should apply for a waiver of the relevant SYSC rule. Given that combining these roles is contrary to generally accepted principles of good governance, the PRA does not expect many firms to be affected by this requirement and would only expect to give such a waiver in exceptional circumstances. In deciding whether the statutory test for granting a waiver is met,(2) the PRA will need to be satisfied that the firm's governance arrangements will still ensure effective and prudent management of the firm, including the segregation of duties and the prevention of conflicts of interest.

4.7 Members of the management body must commit sufficient time to perform their duties at the firm. From 1 July 2014, directors of firms which are significant in terms of their size, internal organisation and the nature, scope and complexity of their activities should not hold more than the following combinations of directorships (including directorships held outside of financial services):

- one executive directorship with two non-executive directorships; or
- four non-executive directorships.(3)

4.8 The CRD permits the PRA to authorise a director to hold one additional non-executive directorship; this would be done through a modification of the relevant SYSC rule. A modification would only be granted where the PRA is satisfied that holding the additional position would not compromise the director's ability to commit sufficient time to his or her duties at the authorised firm(s).

4.9 Given that multiple directorships held within a group, or in an entity in which the firm holds a qualifying holding, count as a single directorship for these purposes, and directorships held in not-for-profit organisations are excluded, the PRA believes that these limits will not require any change to current practice in the vast majority of cases.

Nomination committee

4.10 Firms that are significant in terms of their size, internal organisation and the nature, scope and complexity of their activities must establish a nomination committee of non-executive directors. The nomination committee will have various duties regarding the composition and functioning of the management body. They include selection planning; identifying the qualities, competences and other factors to be taken into account when filling a vacancy; identifying and recommending candidates; and deciding on a target for the representation of the underrepresented gender on the management body and how to meet it. These requirements will be transposed into SYSC.

4.11 The PRA expects that the majority of firms who are 'significant' in this context will already have a nomination committee; however the requirement that it be composed solely of non-executive directors may require a change in some

(1) Articles 88 and 91 of the CRD.
(2) The test for modifying or waiving a rule is set out in section 138A of FSMA.
(3) The overriding requirement that members of the management body must commit sufficient time to perform their duties means that the PRA may wish to require a person to hold less than the maximum number of roles permitted.

cases, resulting in some additional time commitment by non-executives. The potential benefits of introducing such a committee are better consideration of the composition of the management body, and of the knowledge, skills and experience required of new members.

Risk management

4.12 The CRD has four main requirements in this area, which the PRA proposes to implement by adding a new section of rules specifically for CRD firms to SYSC 7:[1]

(1) A firm's management body is to approve and review periodically the firm's risk management policies and strategies, to devote sufficient time to consider risk issues and allocate adequate resources to considering and managing risk issues.

(2) Firms that are significant in terms of size, internal organisation and the nature, scope and complexity of their business are to establish a risk committee of suitable non-executive directors to carry out specified functions.

(3) Firms must have a risk management function that is independent from its operational functions, where appropriate and proportionate.[2] The function is responsible for assessing all material risks, with direct access to the management body. It is also to be involved in elaborating the firm's risk strategy and in all material risk management decisions. The function is to be headed up by a dedicated independent senior manager. If having a dedicated independent senior manager is disproportionate,[3] another senior person within the firm may be appointed, provided there is no conflict of interest. The function head cannot be removed without the prior approval of the management body, to which the head must have direct access when necessary.

(4) Firms that are not significant may combine their risk and audit committees, provided members of the combined committee have the relevant knowledge, skills and expertise for both.

4.13 The requirements in points (1)–(3) are substantially the same as the existing provisions in SYSC 4, 7 and 21. As such they will have minimal impact on firms already following those provisions. As regards point (4), non-significant firms can combine these two committees in the absence of a rule saying otherwise. This is because the rule requiring the establishment of a risk committee only applies to significant firms.

Remuneration

4.14 The CRD remuneration requirements are contained in Articles 75 and 92–96. These Articles incorporate and amend the remuneration provisions introduced by CRD III. They introduce technical changes to the CRD III provisions as well as a subset of substantive amendments. The PRA proposes to implement the technical changes, along with consequential amendments to update references throughout handbook text, requirements by amending SYSC 19A and the Remuneration Code with copied out CRD text. The proportionality framework in the Code is not affected by these changes. As noted in Chapter 1, the PRA will further consider the issue of remuneration in the context of its response to the PCBS report.

4.15 The EBA will develop by 31 March 2014 regulatory technical standards on the criteria for the identification of material risk takers within firms which are subject to the remuneration provisions and on the classes of instruments within the meaning of Articles 52 or 63 CRR or other instruments which can be fully converted to common Equity Tier 1 instruments or written down and could be used for the payment of variable remuneration.

(1) Article 76(2)–(5) of the CRD.
(2) In view of the nature, scale and complexity of their business and the nature and range of the investment services and activities.
(3) In terms of the nature, scale and complexity of the firm's activities.

5 Passporting and co-operation between Member States

Articles 33–52, 151–159 CRD

5.1 This chapter sets out the PRA's implementation of provisions on freedom of establishment and freedom to provide services, branches of non-EEA credit institutions, cooperation with non-EEA supervisory authorities and host-country responsibility for prudential supervision. In doing so, it outlines the PRA's approach to the transfer of responsibility for the oversight of liquidity of EEA branches from host to home authorities following the introduction of a liquidity coverage requirement within the EU as well as the approach during the transitional period.

5.2 In implementing these provisions the PRA will be acting in accordance with its responsibilities as an EU competent authority and its obligations under UK legislation.

5.3 The proposed rule changes are explained below and set out in Appendix 1.

Proposals

The freedom of establishment and the freedom to provide services

5.4 Schedule 3 FSMA and the *EEA Passport Rights Regulations*[1] currently implement requirements in various Single Market Directives, including BCD, in respect of the freedom to establish branches and to provide cross-border services. Additionally, the procedures, notification and reporting requirements to be followed by UK and EEA credit institutions seeking to make use of these provisions are set out in the Supervision chapters of the PRA Handbook, in particular SUP chapters 13, 13A, 14, 15, 16 and Appendix 3. The Handbook Rules relating to the freedom of establishment and freedom to provide services are principally procedural ones relating to notification and reporting.

5.5 These Handbook provisions need to be amended (i) to refer to CRD and any relevant amendments to UK secondary legislation and (ii) to take account of the fact that the requirements to use certain PRA notices will be replaced by requirements to use common notices in directly applicable EU regulations to be adopted under Articles 35, 36 and 39 CRD.

5.6 The EBA has already published Consultation Papers on draft Regulatory Technical Standards (RTS) and Implementing Technical Standards (ITS) relating to passport notifications under these Articles. The RTS specify the information required for a firm wishing to establish a branch in a Member State, while the ITS outline the procedure for notification (including common templates). The PRA will therefore need to delete its relevant notification and reporting requirements once these are replaced by directly applicable technical standards.

5.7 As the EBA identifies, its proposed notification requirements may impose some additional administrative costs on firms. However, greater uniformity in notifications may reduce burdens on firms seeking to passport into multiple EEA jurisdictions.

5.8 Articles 40, 41 and 43 CRD amend Articles 30, 31 and 33 BCD to reflect the fact that lead responsibility for supervision of liquidity for EEA branches becomes a home rather than host state responsibility. These provisions become operative only once a liquidity coverage requirement becomes applicable in accordance with the delegated act to be adopted under Article 460 CRR (see paragraphs 5.10 to 5.13 below).

Relations with third countries[2]

5.9 CRD Article 47 requires member states to refrain from applying to branches of credit institutions headquartered outside the EEA regulatory provisions more favourable than those applicable to branches of EEA credit institutions. It replaces a similar provision in BCD Article 38. The PRA currently sets out in guidance in BIPRU 1.1.10 the circumstances in which it accepts non-EEA credit institution establishment through a branch. Although most of BIPRU will be deleted, the liquidity provisions in BIPRU 12 will be retained, and will continue to apply to third country branches. The PRA will set out its approach to non-EEA credit institutions seeking to establish a branch in the United Kingdom in due course.

The principles of prudential supervision: competence and duties of home and host member states

5.10 Article 49 CRD provides that the prudential supervision of an EEA branch should be the lead responsibility of the home

(1) S.I. 2001/2511.
(2) The term 'third country' in EU legislation signifies non-EEA jurisdictions.

state competent authority. This is already the case for supervision of firms against capital rules, but will also apply to liquidity supervision. As a result, all Handbook provisions relating to the day-to-day prudential regulation of EEA branches will be disapplied.

5.11 However pursuant to Article 151, Article 49 together with Articles 50 and 51 (dealing with supervisory collaboration and significant branches) will not apply until the liquidity coverage requirement becomes applicable in accordance with the delegated act to be adopted under Article 460 CRR. The PRA is preparing for this to happen in January 2015. Until that point, as required by BIPRU 12.2.1R, the provisions of BIPRU 12(1) will continue to apply to EEA branches, as will the associated reporting requirements outlined in SUP 16.12; thereafter, these requirements will no longer be applicable. The PRA's powers to take action in relation to breaches of liquidity rules remain those contained in Part XIII FSMA during this transitional period. The government will introduce amendments to FSMA to reflect the changes to home and host state powers.

5.12 EEA branches in possession of a whole-firm liquidity modification granted and currently in force in accordance with BIPRU 12.8 will continue until the earlier of their expiry date (as specified in the direction) or the point at which the relevant BIPRU 12 provisions are disapplied in relation to EEA branches. The continuation of the whole firm liquidity modifications until that point will remain subject to the FSMA s138a statutory tests continuing to be satisfied.

5.13 The transfer of liquidity supervision from host to home authority is tied to the introduction of common EU liquidity requirements. Once these requirements are fully harmonised (due in 2018 in accordance with CRR) being supervised by one competent authority should not confer any additional costs or benefits as compared to being supervised by another. However, future common liquidity requirements may result in costs or benefits that arise from the new requirements diverging from previous national requirements.

(1) The PRA proposes to amend BIPRU 12 — see the approach to liquidity in Chapter 12.

Part II Regulation

6 Definition of capital

Articles 25–98, 465–491, 500 CRR

6.1 The CRR contains directly applicable provisions defining the tiers of required capital and the level of these requirements, which the PRA will supervise firms against. This chapter sets out the actions the PRA proposes to take to implement the CRR's definition of capital requirements.

6.2 The proposals in this chapter will allow the PRA to supervise effectively the quality of firms' capital, advancing the safety and soundness of firms in line with the PRA's objectives. For reference, paragraphs 117–120 of the PRA's 'approach' document set out the PRA's high-level approach and expectations on the areas covered by this chapter.

6.3 As explained below and set out in Appendix 1, the PRA proposes to make rules in a few specific areas to complement, where necessary, the CRR provisions on the definition of capital. A supervisory statement is also attached in Appendix 2.

Proposals

Deduction of holdings of own funds instruments issued by financial sector entities subject to consolidated supervision

6.4 Under the CRR, firms are required to deduct from regulatory capital their holdings in financial sector entities. However, where a holding is in an entity that is included in the same regulatory consolidation group as the firm, the PRA may decide whether or not to require deduction. In particular, the PRA has discretion under CRR Article 49(2) to require deduction for specific purposes, such as resolution planning and structural separation of banking activities.

6.5 As noted in the PRA's 'approach' document, capital resources are not always freely transferable around a group when it matters most. Experience has shown that, in a pre-resolution scenario, capital located elsewhere in a group cannot always be relied upon to be available to the entity facing the stress. To address this issue (among other things), and so improve the resolvability of the individual firms, the PRA intends to exercise the discretion provided in Article 49(2) to ensure that capital is located in the regulated entities where it is needed.

6.6 Under CRR, the value of all significant investments[1] in financial sector entities not subject to Article 49(2) are fully deducted from the firm's capital, where in aggregate these investments exceed thresholds set out in CRR Article 48. Any amounts not deducted are subject to a 250% risk weight. By requiring deduction for significant investments in financial sector entities included in consolidated supervision the PRA will apply the same treatment and require deduction where those investments exceed the Article 48 thresholds and a 250% risk weighting for those below the thresholds.

6.7 Deduction will apply to holdings of CET1, Additional Tier 1 (AT1) and Tier 2 (T2) own funds instruments and would be made from the corresponding tier of capital.

6.8 The PRA considers that a transition period is appropriate for firms to prepare for the full application of these deductions:

- from 1 January 2014, firms must deduct 50% of the significant investments, subject to the Article 48 thresholds, and risk weight the remaining 50% using the appropriate banking book equity risk weight in accordance with CRR Article 49(4);
- annually from 1 January 2015, firms must deduct an additional 10% (eg 60% in 2015) so that, by 1 January 2019, firms shall deduct 100% of the significant investments, subject to the Article 48 thresholds.

6.9 The degree to which the PRA requires deduction from CET1 will affect the incentives surrounding equity allocation. Deduction above the thresholds set out in Article 48 may lead some firms to restructure their groups, such that equity investments in subsidiaries by UK-regulated entities are minimised, or more equity is located in UK main operating companies rather than in holding companies. In formulating its approach the PRA has had regard to the regulatory principles: while such restructuring entails costs for firms, the broad outcomes would be positive for the safety and soundness of the individual entities the PRA regulates, with a reduction in the likelihood of firms' failure due to their greater resilience; the PRA therefore considers the costs entailed to be proportionate to the benefits.

(1) Significant investments are defined in Article 43 of the CRR.

6.10 The PRA considers that a requirement to deduct holdings in financial sector entities that are part of the same group would be disproportionate in the case of investments in venture capital vehicles.(1) Where these venture capital vehicles channel investment directly into non-financial sectors the PRA will not require deduction. As per the current regime, these exposures will continue to be risk weighted under the applicable credit risk provisions.

Treatment of banks' significant insurance holdings

6.11 As announced in its statement on 20 June 2013, the PRA intends to require firms to follow the default position in CRR Article 49(1); a firm will therefore be required to deduct holdings of own funds instruments issued by an insurer in which the firm has a significant investment from the firm's own funds. Deduction would apply to holdings of CET1, AT1 and T2 own funds instruments and would be made from the corresponding tier of capital. So, for example, a significant investment in the CET1 of an insurance company would be deducted from the investing bank's CET1. Deductions from CET1 are required only above a threshold allowance of 10% of the investing bank's CET1, as specified in CRR Article 48(1)(b). The amount below the threshold should be risk weighted at 250% as per CRR Article 48(4). The deduction would apply both to banking groups with an investment in an insurance company and to solo banks with an investment in an insurance company.

6.12 The PRA considers deduction necessary to prevent the multiple use of the same capital resources in different parts of the financial system. Deduction is the most effective way to ensure that banks with significant investments in insurance companies have sufficient capital of the right quality to support risks in both the firm and the insurer. The deduction of investments made by the firm in the insurer helps to ensure that both regulated entities are properly capitalised, limits the risk of contagion, and reduces reliance on the free transfer of capital, which may not be possible in practice.

6.13 CRR Article 49(1) permits national authorities to apply an alternative risk-weighting approach to deduction where the firm and insurer are supervised as part of a conglomerate. As a matter of general policy, the PRA does not intend to exercise this discretion to allow banks to use this alternative approach.

6.14 The existence of the threshold allowance under CRR moderates the impact of the deduction on firms by allowing a significant portion of investments in financial sector entities to be risk weighted. This threshold gives some allowance for diversification within the financial system, ensuring the burden on firms under the PRA's approach is proportionate to the benefits set out above, having regard to the regulatory principles.

Risk weight for qualifying holdings outside the financial sector

6.15 CRR Article 89(3) requires that competent authorities choose between two options with respect to 'qualifying holdings' that exceed the greater of two threshold criteria and to publish their choice. Under CRR Article 89(1) a 'qualifying holding' is a holding in a non-financial sector entity that is not: (i) a direct extension of banking; or (ii) ancillary to banking; or (iii) leasing, factoring, the management of unit trusts, the management of data processing services or any other similar activity.

6.16 The two options under CRR are:

- to apply a risk weight of 1250% to the excess qualifying holdings above the greater of the two threshold criteria; or
- to prohibit firms from having qualifying holdings above the greater of these two criteria.

6.17 Under the first option firms may also choose to deduct from CET1 the excess above the greater of the two threshold criteria, rather than risk weighting it at 1,250%.

6.18 The PRA, having regard to the regulatory principles, considers that prohibition is not proportionate, as the level of risk weighting proposed in the first option adequately discourages high concentration in a single firm and excessive equity exposures to non-financial sectors. Therefore, the PRA intends to apply the risk-weighting treatment contained in the first of these two options.

Connected funding of a capital nature

6.19 The PRA expects firms to comply with the purpose as well as the letter of the CRR. In line with this approach, the PRA expects firms not to structure transactions around the CRR capital regime. The PRA therefore proposes maintaining its current approach to connected funding of a capital nature (CFCN) under CRR.(2) CFCN arises when a firm lends a connected party funds that, directly or indirectly, behave like capital in the borrower, but the transaction is structured in such a way that it does not incur the treatment attached to investments in the capital of other entities. Such funding poses similar prudential risks; as a result the PRA currently requires such transactions to be deducted from firms' total capital.

6.20 The PRA intends to make use of the powers identified in CRD Article 104(1)(j) and (l) to make a rule requiring firms to report and disclose their CFCN. The PRA intends to make use of the power identified in CRD Article 104(1)(d) to make a rule requiring firms to deduct any CFCN identified.

(1) For example the UK Business Growth Fund.
(2) CFCN was previously called Connected Lending of a Capital Nature (CLCN).

6.21 Under CRR, a corresponding-tier approach is taken to the deduction of investments in the capital of other financial sector entities, which are deducted from the tier to which they have been credited. By its very nature CFCN is not assigned a tier of capital, therefore, the proposed rule will require firms to deduct CFCN from the most appropriate tier of capital, taking account of the behavioural characteristics of the CFCN in question. The PRA expects firms to be conservative in respect of their judgements regarding CFCN and the most appropriate tier from which to deduct. Firms should be aware that the PRA is committed to preventing gaming in relation to CFCN deductions.

Connected transactions

6.22 Under CRR capital instruments have to meet the eligibility criteria in Articles 28 (CET1), 52 (AT1) and 63 (T2). In coming to a view as to whether a capital instrument meets the CRR criteria, the PRA will assess the structure of the instrument holistically, taking into account not only the terms governing the specific instrument but also any connected transactions that may affect its nature. To help make this assessment and to prevent firms from structuring around the CRR regime, the PRA intends to make use of the power identified in CRD Article 104(1)(j) to make a rule requiring firms to report any connected transactions to the PRA.

6.23 This proposal to require firms to notify the PRA about any connected transactions addresses the loss of relevant supervisory information about the underlying quality of own funds and reported capital measures. Notifications will provide supervisors with data on the nature and extent of connected transactions, which will help inform supervisory judgements about capital adequacy.

Point of non-viability for instruments issued under foreign law

6.24 It is likely that instruments issued under foreign law will be outside the reach of the *Banking Act 2009*, making it unlikely that they would be of use in recapitalising a failing bank. To mitigate this risk and improve firms' resolvability, the PRA intends to make a rule. All new issuances of AT1 and T2 capital instruments by PRA regulated firms that are governed by the law of a non-EEA jurisdiction will need to include contractual terms that subject them to the possibility of being written down or converted in a way equivalent to instruments issued under English law. This rule will make firms responsible for convincing the PRA that any new issuances made under non-EEA law will be subject to the same degree of possible loss as instruments issued under English law.

Administrative provisions

6.25 In order to carry out its role as a competent authority under CRR effectively, the PRA will need firms to provide certain notifications and information about their capital instruments that go beyond the scope of standard regulatory returns.

6.26 As a result the PRA intends to write rules which will continue the current capital notification regime. The PRA aims to simplify this regime into three specific notification requirements. In most cases the PRA will require 30 days' notice, specific relevant information about the transaction, and a legal opinion stating why it complies with the CRR. The three types of transactions these rules will cover are:

(i) the issuance of a capital instrument;
(ii) the amendment of a capital instrument; and
(iii) the redemption of a capital instrument.

6.27 Only notification no later than the date of issue will be required for the issuance of ordinary shares and capital instruments under a debt securities programme, provided the PRA was appropriately notified prior to its first drawdown and the instruments have not changed. These rules will not act as an exclusive list; supervisors will be able to require other information as appropriate.

6.28 The PRA appreciates that there will be some costs to regulated firms as a result of this notification regime; however, these are outweighed by the benefits of supervisors having the appropriate time and information to understand capital instruments' issuance, amendment and redemption. As a result of receiving this information and having an appropriate time to review it, supervisors will be able more accurately to assess whether capital instruments meet the CRR criteria and provide appropriate loss absorbency; this will improve the safety and soundness of regulated firms.

Subordination of building societies' capital instruments

6.29 Currently, capital instruments issued by building societies must be contractually subordinated to senior creditors and retail depositors. CRR requires that AT1 and T2 capital instruments are subordinated to non-subordinated creditors. The PRA therefore proposes to write a rule to require that AT1 and T2 capital instruments are contractually subordinated to retail depositors in building societies.

Transitional provisions

6.30 Details of the overall Pillar 1 capital requirements are contained in CRR Article 92. However, Article 465 of the CRR provides for a possible one-year transitional period for Pillar 1 CET1 and Tier 1 capital requirements, which the PRA intends to implement. As a result, during the period from 1 January 2014 to 31 December 2014 the required Pillar 1 CET1 ratio will be 4%, rising to 4.5% from 1 January 2015 onwards. Similarly, during the same period the required Pillar 1 Tier 1 capital ratio will be 5.5%, rising to 6% from 1 January 2015 onwards.

6.31 In terms of the definition of CET1 capital the PRA intends to follow the CRR without following the transitional path; that is, 100% of all deductions and filters will apply from

1 January 2014. The only exception will be the deduction of holdings of own funds instruments issued by financial sector entities subject to consolidated supervision as noted in the appropriate section above.(1)

6.32 However, in terms of the definition of AT1 and T2 capital the PRA intends to follow the minimum CRR transitional path in all cases.

6.33 Finally, CRR also allows existing capital instruments to be grandfathered within certain limits if they do not meet the definition of capital criteria (CRR Article 486). Again, in this instance the PRA intends to follow the minimum CRR transitional path. This will allow 80% of the value of these instruments to be grandfathered during the period from 1 January 2014 to 31 December 2014, with this value decreasing by 10% per annum (eg 70% in 2015) until 0% is reached on 1 January 2022.

6.34 The PRA's approach to these transitional provisions is underpinned by its desire to improve prudential standards to ensure the continuing safety and soundness of the firms it supervises. However, the PRA also recognises the need to provide for as smooth a transition as possible to the new CRD IV regime and has therefore sought to implement transitional provisions where the PRA considers them to be appropriate and proportionate, having regard to the regulatory principles.

Basel I Floor

6.35 Until 31 December 2017, CRR Article 500 requires firms using an IRB approach for credit risk or an AMA approach for operational risk capital requirements to calculate their requirements in line with a floor against Basel I standards, in addition to the provisions of CRR Article 92. The supervisory statement in Appendix 2 sets out the PRA's expectations regarding the provisions in Article 500.

(1) The PRA recognises that for the transitional required by Article 468(4), the PRA rule as drafted (rule 11.5) sets out applicable percentages outside the ranges specified by the CRR in Article 478. This is because the PRA believes that Article 468(4) as drafted in the CRR contains a manifest error that is likely to be corrected by the Commission. Regardless of whether or not Article 468(4) is revised by the time the final rules are made, when making the rules the content of rule 11.5 will follow the CRR text as it is at that time. Similarly, the rule concerning CRR Article 478(2) replaces the ellipsis in the CRR text as published in the EU Official Journal with 1 January 2014, which is the date of application of the CRR and reflects the text and the April 2013 political agreement. Any final rule will, as above, follow the content of Article 478(2) as it is at the time the rule is made.

7 Credit risk

Articles 107–270, 404–410, 495, 496 CRR

7.1 The CRR contains directly applicable provisions on the capital requirements for credit risk; the PRA will supervise firms against these requirements. This chapter sets out the actions the PRA proposes to take to implement the CRR's credit risk requirements.

7.2 As explained below and set out in Appendix 1, the PRA proposes to make rules in specific areas to exercise the discretions afforded to it in the CRR in respect of the Standardised Approach to credit risk, the Internal Ratings Based (IRB) approach and securitisation. A supervisory statement is also attached in Appendix 2.

Proposals

Standardised approach

Exposures to UK regional governments

7.3 The CRR requires that exposures to EU regional governments are treated as exposures to the central government of the jurisdiction in which they are established where there is no difference in risk between them.

7.4 For these purposes, the PRA proposes to treat exposures to the following UK regional governments as exposures to the UK central government:

(a) the Scottish Parliament;
(b) the National Assembly for Wales; and
(c) the Northern Ireland Assembly.

7.5 The PRA took the same approach to implementing in the PRA Handbook the equivalent provision from the BCD.

Residential real estate exposures: buy-to-let

7.6 The CRR applies a 35% risk weight to loans that are fully and completely secured on residential real estate where certain criteria are met; a 100% risk weight applies where the criteria are not met. CRR allows the PRA to derogate from one of those criteria where the PRA publishes evidence of the long-established and well-developed nature of the UK residential mortgage market, and data showing loss rates on UK residential mortgages to be within specified limits.(1) The result of derogation from the criterion is that certain buy-to-let mortgage exposures would receive a 35% risk weight.

7.7 The PRA implemented in the PRA Handbook the equivalent derogation from the current BCD. Based on the available evidence, the PRA considers the continued implementation of the derogation to be warranted under the CRR. The United Kingdom has a well-developed and long-established residential property market: in 1987, the amount outstanding of total sterling net secured lending to individuals and housing associations (not seasonally adjusted) was £166 billion; in 2012, such lending stood at £1.3 trillion.(2) The write-off rate for UK residential mortgages in 2012, calculated using Bank of England data, was 0.05%.(3) The PRA considers this write-off rate to be a suitable proxy for loss rate in this case.

7.8 The CRR requires firms to report semi-annually to the PRA data on losses on certain UK residential mortgage exposures using uniform templates developed by the EBA. The PRA will publish those data annually on an aggregated basis, as required by the CRR. For the interim period between 1 January 2014 and the first publication of those aggregated loss data, the PRA proposes to publish the data currently reported to the Bank of England which provide evidence of the appropriateness of the derogation for the United Kingdom.

Commercial real estate exposures

7.9 The CRR applies a 50% risk weight to loans fully and completely secured on commercial real estate where specific criteria are met; a 100% risk weight applies where those criteria are not met. CRR also allows the PRA to derogate from one of the relevant criteria(4) where the PRA publishes evidence of the long-established and well-developed nature of the UK commercial mortgage market, and data showing loss rates on UK commercial real estate to be within certain limits. In addition, CRR permits the PRA to apply stricter criteria or a higher risk weight where appropriate on the basis of financial stability considerations; the PRA must consult the EBA where it does so.

(1) The relevant criterion, set out in the CRR Article 125(2)(b), is that, 'the risk of the borrower shall not materially depend on the performance of the underlying property or project, but on the underlying capacity the borrower to repay the debt from other sources, and as a consequence, the repayment of the facility shall not materially depend on the cash flow generated by the underlying property serving as collateral'.
(2) These data may be found in Bank of England data series LPQVTXH.
(3) The write-off rate was calculated using seasonally unadjusted data extracts from Bank of England series RPATBVX and RPATFHD.
(4) The relevant criterion, set out in CRR Article 126(2)(b) is that, 'the risk of the borrower shall not depend materially upon the performance of the underlying property or project, but on the underlying capacity of the borrower to repay the debt from other sources, and as a consequence, the repayment of the facility shall not materially depend on any cash flow generated by the underlying property serving as collateral'. The PRA considers this criterion to apply equally in where loans are secured on single or multiple properties.

7.10 The current BCD affords a similar discretion to that in the CRR, allowing the PRA to apply a 50% risk weight to loans fully and completely secured on commercial real estate. The PRA did not exercise that discretion, as it considers a 50% risk weight not to be adequate to capture the risk inherent in fully secured commercial property lending in the United Kingdom; consequently, a 100% risk weight is currently applied to such lending. Moreover, we consider that reducing the risk weight on such lending to 50% would be imprudent, could result in a significant increase in the extent of such lending at that lower risk weight by UK firms using the Standardised Approach for commercial real estate portfolios, and therefore gives rise to financial stability considerations.

7.11 To address this concern, the PRA proposes to introduce a stricter criterion for the 50% risk weight, in accordance with the ability to do so under the CRR. The relevant rule in Appendix 1 sets out the criterion the PRA proposes to apply. The criterion requires firms to assess whether annual average loss rates from lending secured by mortgages on commercial property in the United Kingdom did not exceed 0.5% over a representative period. The basis of this assessment would be the loss data collected and published by the PRA under Article 101 of the CRR. This additional criterion would ensure that any application of a 50% risk weight would be based on the loss experience. The PRA intends to consult the EBA on its proposed approach. An alternative means of addressing the PRA's concern would be to use the ability under CRR to vary risk weights for such commercial real estate exposures.

7.12 In respect of the derogation referred to in paragraph 7.9 from one of the criteria for the 50% risk weight, the PRA notes that the relevant commercial real estate lending would be relatively higher risk in nature. The PRA does not consider a 50% risk weight for such lending to be appropriately prudent. The PRA notes that sufficient data on loss rates — or a suitable proxy — for UK commercial mortgage loans are not currently available. Moreover, the stricter criterion that the PRA proposes to introduce would apply also to such lending.

Question

The PRA would welcome comments on what might constitute a representative period for these purposes. More broadly, the PRA would also welcome comments on the most appropriate means of addressing its concern on risk weights for commercial real estate exposures.

Covered bonds

7.13 The CRR includes the following:

(a) an ability for the PRA, after having consulted the EBA, to waive partly a limit on the extent to which covered bonds may be collateralised by exposures to institutions of a certain credit quality where specific conditions were met; and

(b) a transitional provision which, where certain conditions are met, would allow the PRA partially or fully to waive the limit on senior units issued by French *Fonds Communs de Créances*, or by equivalent securitisation entities, of 10% of the nominal amount of the outstanding issue.

7.14 The PRA proposes not to implement these discretions on the basis that we do not consider them to be necessary or beneficial for UK firms' safety and soundness. Similar provisions were included in the BCD; we did not implement them in the PRA Handbook.

Intra-group exposures

7.15 The CRR allows the PRA to permit firms to assign a 0% risk weight to certain intra-group exposures, provided that specific conditions are met. Where such permission is granted, the relevant exposures are also exempt from the large exposures limit. The PRA proposes to exercise this discretion as part of its approach to Core UK Groups, and sets out its expectations for assessment of compliance with the relevant conditions in the supervisory statement on Large Exposures (see Chapter 11 and Appendix 2).

7.16 The PRA's proposed approach is in line with that taken in the PRA Handbook to a similar discretion afforded under the current BCD.

Sovereign exposures

7.17 The CRR applies a risk weight of 0% to exposures to Member States' central governments and central banks, either on the basis of an appropriate external credit rating or where the exposure is denominated and funded in the domestic currency.

7.18 The PRA considers that risk weights should appropriately reflect the risk inherent in firms' exposures. The PRA will monitor developments in international and EU standards in respect of sovereign risk. In light of those developments, the PRA will take action as required to ensure firms' continuing safety and soundness.

Internal Ratings Based approach

Rating system approval

7.19 The CRR requires a firm's board, or a designated committee thereof, and its senior management to approve all material aspects of rating and estimation processes of IRB rating systems. Unlike in the BCD, 'senior management' is a defined term in the CRR.

7.20 Within the supervisory statement on IRB, the PRA is consulting on a supervisory approach that seeks to ensure the personal responsibility and accountability of a firm's senior executives in respect of the adequacy of its IRB rating systems. This approach involves an expectation that an individual in a Significant Influence Function (SIF) role would provide the

PRA with an annual attestation that the IRB rating system approvals required by the CRR have been carried out adequately.

7.21 The PRA's approach to transposing the current BCD requirement for rating system approval involves specifying that the designated committee must include at least one member of the board of the firm.

Question

The PRA would welcome comments on the appropriate level of individual in a SIF role for these purposes, and on whether such an approach would be warranted for all risk types for which models are used to calculate regulatory capital.

Definition of default — days past due

7.22 The CRR allows the PRA to replace 90 days in the days past due component of the definition of default with 180 days for exposures secured by residential or SME commercial real estate in the retail exposure class, and for exposures to Public Sector Entities (PSEs).

7.23 The PRA proposes to define a requirement, as set out in Appendix 1, specifying that the number of days past due for the purposes of the definition of default is 90. Within the supervisory statement in Appendix 2 as regards IRB, the PRA is consulting on allowing firms to apply for a waiver from the 90 day definition of default PSE rating systems and retail residential mortgage rating systems built after 31 December 2013. The PRA would expect to grant such waivers. A 180-day definition of default for such rating systems built prior to 1 January 2014 would be treated according to Chapter 14. Other retail rating systems that may use 180 days under the current PRA rules may not do so under CRR.

7.24 The implementation of the current BCD in the PRA Handbook applies a 180-day definition of default for Retail exposures, with the exception of Retail SME exposures, and PSE exposures.

Definition of default — materiality threshold

7.25 The CRR requires the materiality of a credit obligation for an obligor that is 90 or 180-days past due to be assessed against a threshold defined by the supervisor. CRR also requires the EBA to develop regulatory technical standards by 31 December 2014 specifying the conditions according to which the materiality threshold should be set.

7.26 For the period prior to implementation of those regulatory technical standards, the PRA proposes to apply on a total exposure basis a threshold of £100 for retail lending, and a threshold of £1,000 for non-retail lending. The PRA intends to review this approach, as necessary, in light of the outcome of the EBA regulatory technical standards.

7.27 The implementation of the current BCD in the PRA Handbook requires a firm to have a policy setting out how it will determine whether a credit obligation or, for overdrafts, the underlying amount, is material for the purposes of determining whether the days past due element of the definition of default is triggered.

Question

Comments are welcomed on the potential implications of the PRA's setting materiality thresholds for the definition of default upon implementation of the CRR which may require amendment following the adoption by the Commission of relevant EBA regulatory technical standards.

Equity exposures

7.28 The CRR allows supervisors to exempt from the IRB approach until the end of 2017 certain categories of equity exposures which firms held as at 31 December 2007. The PRA proposes not to apply this exemption.

7.29 This approach is aligned with that taken in the implementation of the current BCD in the PRA Handbook.

Securitisation

Notification of Significant Risk Transfer

7.30 The CRR allows the PRA to determine on a case-by-case basis that Significant Risk Transfer (SRT) to third parties has not occurred where the possible reduction in capital requirements that would result from securitisation is not justified by a commensurate transfer of risk to third parties.

7.31 In order to undertake the analysis required to establish whether commensurate risk transfer has been achieved, the PRA proposes to introduce a requirement for firms to notify it of securitisation transactions that they consider to achieve SRT to third parties. This requirement is set out in Appendix 1. The PRA's expectations regarding the information to be provided as part of such notifications are set out in the supervisory statement on securitisation.

7.32 This approach is in line with the implementation of the current BCD in the PRA Handbook, which requires notification of SRT transactions.

8 Counterparty credit risk

Articles 271–311, 378–386 CRR

8.1 The CRR contains directly applicable provisions on counterparty credit risk, including, exposures to a central counterparty; and credit valuation adjustment risk. This chapter sets out the PRA's approach to implementing these requirements. As explained below and set out in Appendix 1, the PRA proposes to make rules in specific areas to complement, where necessary, the CRR provisions on aspects of counterparty credit risk. A supervisory statement is also attached in Appendix 2.

Proposals

Standardised Method for transactions with a non-linear risk profile, or for payment legs and transactions with debt instruments as underlying

8.2 The Standardised Method can be used for the calculation of the exposure value of OTC derivative transactions to determine own funds requirements for counterparty credit risk. At present BIPRU states that for OTC derivatives transactions with a non-linear risk profile, or for payment legs and transactions with debt instruments as the underlying, a firm must apply the mark-to-market method where it has a CAD 1 permission but cannot determine the delta or the modified duration of the transactions.

8.3 Likewise, the PRA will require the application of the mark-to-market method under CRR Article 282, as set out in Appendix 1.

Communication of legal opinions to the PRA related to contractual netting agreements

8.4 Under CRR Article 296, recognition of contractual netting agreements requires that firms make available to the PRA written and reasoned legal opinions on all such contractual netting agreements. Firms should ensure that they hold these legal opinions and are able to provide them to the PRA if requested to do so.

Application of the Original Exposure Method for interest rate contracts

8.5 Firms within the scope of CRR Article 94 may use the Original Exposure Method (OEM) to calculate the exposure value of certain OTC derivative transactions' own funds requirements for counterparty credit risk. In order to determine whether the recognition of netting reduces risk, CRR Article 298(4) permits firms to use either the original or the residual maturity of the contract for the application of the OEM for interest rate contracts, subject to the consent of the PRA.

8.6 For all interest rate contracts, the PRA will require credit institutions that use the OEM to use the original maturity of the contract for the application of Article 298 to ensure a consistent application as set out in Appendix 1. This is the more prudent approach of the two set out in the CRR, which the PRA believes is appropriate to prevent use of the OEM leading to undercapitalisation of risk.

Permission to use an internal credit valuation adjustment model to estimate the maturity factor M

8.7 CRR Article 162 allows a firm to use its own one-sided credit valuation adjustment internal model ('Internal CVA model') to estimate the maturity factor 'M', if permitted to do so by the PRA. The PRA's expectations in relation to this discretion are set out in Appendix 2.

Permission to set the maturity factor M to 1

8.8 CRR Article 162 also permits a firm with permission to use the Internal Model Method (IMM) and an internal Value-at-Risk (VaR) market risk model for specific risk associated with traded debt instruments,[1] to set the maturity factor M defined in Article 162 to 1. To do so the firm must demonstrate to the PRA, as the relevant competent authority, that its internal VaR model captures the effect of credit rating migrations. The PRA's expectations in relation to this discretion are set out in the draft supervisory statement in Appendix 2.

Application of the own funds requirements for credit valuation adjustment risk for securities financing transactions

8.9 CRR Article 382 allows the PRA to include securities financing transactions (SFTs) in the scope of the own funds requirements for credit valuation adjustment (CVA) risk when the firm's CVA risk exposures arising from those transactions are material.

8.10 The PRA's expectations in relation to this article are set out in the draft supervisory statement in Appendix 2.

(1) In accordance with Article 361(1), paragraph (d).

8.11 SFTs are not defined in the regulation. However, the PRA considers that, for these purposes, SFTs should be taken as meaning repurchase transactions or securities or commodities lending or borrowing transactions.

8.12 The PRA's application of Article 382 is set out in the draft supervisory statement in Appendix 2.

Intra-group exemptions for the calculation of the own funds requirements for credit valuation adjustment risk

8.13 The scope of the own funds requirements for CVA risk contains an exemption for intra-group transactions under CRR Article 382. However competent authorities may disapply this exemption where laws requiring structural separation of banking groups are enacted in their country. The PRA will review this in due course in the context of structural reform legislation in the United Kingdom.[1]

Process for post-approval changes for counterparty credit risk advanced model approaches

8.14 The PRA propose to carry forward the existing supervisory statement LSS3/13 on post-approval changes for counterparty credit risk advanced model approaches. Consequential amendments will be made to reflect the deletion of BIPRU and entry into force of the CRR.

(1) See the Financial Services (Banking Reform) Bill, http://services.parliament.uk/bills/2013-14/financialservicesbankingreform.html.

9 Market risk

Articles 102–106, 325–377 CRR

9.1 The CRR contains directly applicable provisions on the own funds requirements for market risk; the PRA will supervise firms against these requirements. This chapter sets out the actions the PRA proposes to take to implement the CRR's market risk requirements.

9.2 As explained below and set out in Appendix 1, the PRA proposes to make rules in specific areas to complement, where necessary, the CRR provisions on market risk. A supervisory statement is also attached at Appendix 2.

Proposals

Material deficiencies in risk capture by a firm's internal approach

9.3 Where institutions are permitted to use internal models for market risk, these will be evaluated so that material deficiencies in risk capture by those models are identified, and may be rectified or mitigated by a requirement to hold additional capital (as set out in CRD Article 101).(1) The PRA considers that there is sufficient standardisation in this process to impose a consistent cross-firm framework to identify risks not captured in their market risk internal models. The PRA proposes to implement this uniform approach for VaR and stressed VaR models by utilising the current 'Risks not in VaR' (RNIV) framework. A rule and section in the market risk supervisory statement implements this continuation of the PRA's current policy.

Standardised approach for options

9.4 The current standardised approaches for the calculation of position risk for options in BIPRU will be replaced by an approach which requires use of the option's delta, in compliance with CRR Articles 329, 352, and 358. For OTC options, or where the relevant value of delta is not available from an exchange, the PRA may permit firms to calculate delta using their own pricing models. Institutions will only be permitted to use their own estimates of delta if the model they use for this purpose is appropriate.

9.5 In order to ensure that firms only use appropriately calculated own estimates of delta, the PRA expects that the model used should at least meet certain minimum standards for each type of option for which delta is calculated. These expectations are set out in the market risk supervisory statement.

9.6 A firm that is able to confirm to the PRA that its model meets the PRA's expectations would be permitted to use its own estimates of delta for the relevant option type.

9.7 If a firm is unable to satisfy these expectations with regard to a particular option type, measures may be taken to mitigate risks such as an additional capital charge and firms would be required to rectify the deficiencies through an agreed plan of action over a specified timeframe. If a firm is unable to meet the necessary standard to bring it into compliance with the CRR in respect of some or all of the categories of options in which it trades, then the PRA will consider further supervisory measures. This may include its permission to trade in the specific option types where the minimum standards are not met being withdrawn.

9.8 There is a transitional provision in CRR Articles 329, 352, and 358 which allows the PRA to continue to implement an existing national treatment applied prior to 31 December 2013 for the purposes of capturing non-delta risks of options until the RTS on this topic mandated by those Articles comes into force. The deadline for the required RTS is 1 January 2014. In case the RTS is not implemented when the CRR comes into force the PRA expects firms to use one of the approaches set out in the draft RTS published in EBA/CP/2013/16 until the final RTS comes into force.

Financial instruments where no treatment has been specified in the CRR

9.9 The situation may arise that a firm holds one or more types of financial instrument for which the capital treatment is not expressly specified in the CRR. In order to ensure that these positions are taken into account and that capital requirements are calculated in a consistent manner, the PRA proposes a rule stating that firms should, where appropriate, calculate their own funds requirements by applying by analogy the rules in CRR which are prescribed for positions in similar instruments. Otherwise firms should calculate an own funds requirement of an appropriate percentage of the current value of the position. This percentage should be either 100%, or a percentage that takes into account the characteristics of the position.

(1) The PRA is also required to review and evaluate the risks to which firms are exposed. Where firms have similar risk profiles, the PRA may apply the review and evaluation process across such firms in a similar manner (CRD Articles 97, 103).

Netting a convertible with its underlying instrument

9.10 No netting is allowed between a convertible and an offsetting position in the instrument underlying it, unless (as specified in CRR Article 327(2)) the PRA adopts an approach under which the likelihood of conversion is taken into account, or capital is held to cover any loss that conversion might entail. The PRA proposes a rule to implement this discretion to allow netting, so that a convertible instrument should be treated as a position in the equity into which it converts. This proposal represents a continuation of the PRA's current policy and therefore the PRA does not expect any material incremental costs or benefits.

Offsetting derivative instruments

9.11 CRR Article 331(2) states that firms may treat as fully offsetting any positions in derivative instruments covered in CRR Articles 328 to 330 which meet certain conditions.(1) One condition is that the reference rates (for floating-rate positions) or coupons (for fixed-rate positions) are 'closely matched'. The PRA's expectations in this area are set out in the market risk supervisory statement.

Exclusion of backtesting exceptions when determining a multiplication factor addend

9.12 CRR Article 366(4) states that competent authorities may in individual cases exclude backtesting exceptions (overshootings) when determining a VaR/sVaR multiplication factor addend, where the exceptions do not result from deficiencies in their internal model. The market risk supervisory statement describes the steps that a firm should take if it believes that a backtesting exception (overshooting) should be disregarded.

Derivation of notional positions for standardised approaches

9.13 For the purposes of the standardised approach it is often necessary to decompose relatively complex products into simpler notional positions that can be capitalised under the standardised approaches for each asset class. The CRR provides some high level instructions for deriving notional positions. However, the instructions provided are not sufficient in themselves to ensure a prudent and consistent application across firms for the derivation of positions in more complicated products. For the purposes of the standardised approach it is important that firms should treat positions in a consistent way.

9.14 The PRA therefore sets out its expectations in the market risk supervisory statement, consistent with the current PRA approach on the derivation of notional positions.

Qualifying debt instruments

9.15 CRR Article 336 states that positions listed on a stock exchange in a third country, where the exchange is recognised by the competent authorities, qualify for the specific risk own funds requirements in the second row of the table in Article 336. The market risk supervisory statement provides a list of those stock exchanges in third countries that the PRA proposes to recognise for the purposes of this rule. This list retains the pre-existing list of stock exchanges in third countries that are currently recognised for these purposes.

Question

Are there third country stock exchanges that should be added or removed from this list?

Expectations relating to internal models

9.16 CRR Article 363 states that permission for a firm to use internal models to calculate capital is subject to competent authorities verifying compliance with:

- the general requirements;
- requirements particular to specific risk modelling; and
- requirements for an internal model for incremental default and migration risk.

9.17 In order to meet the objective of minimising RWA variability arising from use of internal models the PRA proposes to complement the requirements of the CRR with information on the PRA's approach to verifying compliance with the above points, as set out in the market risk supervisory statement.

VaR and stressed VaR calculation

9.18 CRR Article 365 requires firms that use an internal model for calculating their own funds requirement to calculate at least weekly a 'stressed Value-at-Risk' (sVaR) of their current portfolio. When the PRA considers a firm's application to use a sVaR internal model it will consider compliance with the market risk supervisory statement as evidence that the standards required by the CRR have been satisfied.

Requirement to have an internal IRC model

9.19 CRR Article 372 requires firms that use an internal model for calculating own funds requirements for specific risk of traded debt instruments to also have an internal incremental default and migration risk (IRC) model in place to capture the default and migration risk of its trading book positions that are incremental to the risks captured by its VaR model. When the PRA considers a firm's application to use an IRC internal model, the PRA will consider compliance with the market risk supervisory statement as evidence that the standards required by CRR have been satisfied.

(1) See CRR Article 331(2) for details of these conditions.

10 Operational risk

Articles 312–324 CRR

10.1 The CRR contains directly applicable provisions on own funds requirements for operational risk; the PRA will supervise firms against these provisions. This chapter introduces a supervisory statement that clarifies the PRA's expectation of the proportion of a firm's operational risk exposure that should be captured by an Advanced Measurement Approach (AMA).

10.2 A supervisory statement is attached at Appendix 2.

Proposals

10.3 The supervisory statement applies to firms that intend to calculate their operational risk capital requirement using an AMA in combination with either the Basic Indicator Approach (BIA) or the Standardised Approach (TSA).[1]

10.4 The supervisory statement clarifies the PRA's expectation of the proportion of a firm's operational risk exposure that should be captured by an AMA:

(a) at the date of first implementation; and
(b) post implementation within a timescale approved by the PRA.

10.5 The proposal supports CRR Article 314(3)(a) and (b).

10.6 CRR Article 314(3) requires competent authorities to impose the following conditions when granting permission for institutions to use an AMA in combination with either the BIA or TSA:

- on the date of implementation of an AMA, a **significant** part of the institution's operational risk are captured by that approach;
- the institution takes a commitment to apply the AMA across a **material** part of its operations within a time schedule that was submitted to and approved by its competent authority.

10.7 The PRA's interpretation of the meaning of 'significant' and 'material' are set out in the Operational Risk supervisory statement. This is consistent with current practice, and therefore the PRA expects there to be no material impact on firms from this proposal.

(1) Article 314 CRR.

11 Groups and large exposures

Articles 6–24, 387–403 CRR, 111–113 CRD

11.1 The CRR includes directly applicable rules that define the arrangements for the application of prudential requirements to a consolidated group as well as the rules for defining the limits on the level of exposure between third-party and intra-group entities.

11.2 The proposals in this chapter explain how the PRA intends to apply prudential requirements to groups and how it will supervise the scale of exposures between different entities.(1)

11.3 The application of requirements to groups includes the PRA's approach to national discretions on the individual consolidation method, the methods of prudential consolidation and entities excluded under the scope of consolidation.

11.4 Being an entity within a group can be a source of prudential strength for a firm. But it can also change the nature of the risk that a firm is exposed to, for example through financial contagion due to intra-group exposures, pressure to extract capital through dividends, non-financial contagion through reputational damage, reliance on central functions, and risk concentrations.

11.5 As there is considerable overlap between the CRD IV group consolidation provisions and the legislation it replaces, there are no substantial changes to the current consolidation regime and the way in which it is applied.

11.6 The large exposures proposals relate to national discretions on the intra-group exposures, sovereign exposures and reporting requirements.

11.7 The PRA outlines below the approach to where changes have been made and national discretions used. Relevant rule changes are set out in Appendix 1 and a supervisory statement is also attached at Appendix 2.

Proposals

Groups

Structural separation

11.8 CRR Article 11 allows competent authorities the discretion to require structurally separated institutions to comply with certain prudential requirements on the basis of the sub-consolidation to which structural separation gives rise. The PRA will consider whether and how to exercise this discretion in the context of structural reform legislation in the United Kingdom.(2)

Individual consolidation method

11.9 CRR Article 9 gives the PRA the discretion, to permit parent institutions to incorporate subsidiaries when calculating individual capital resources subject to certain conditions being met. The PRA intends to continue to exercise this discretion in a similar way to the existing solo consolidation regime as set out in the Groups supervisory statement at Appendix 2.

Methods for prudential consolidation

11.10 CRR Article 18(3) requires the PRA to determine how consolidation is to be carried out for undertakings managed on a unified basis or with commonality of management as per Article 12(1) of the Seventh Company Law Directive.(3) In line with current practice, the PRA will continue to require proportional consolidation of the relevant undertaking. The relevant proportion will be as stated in the Part 4A permission of the firm.

11.11 CRR Article 18(5) requires the PRA to determine whether and how consolidation is to be carried out in the case of participations or capital ties not captured in the preceding paragraphs of CRR Article 18. One situation that CRR Article 18(5) could capture is an investment in a participation or capital tie that does not fall within CRR Article 18(4), because the liability is greater than the capital the firm will hold under proportional consolidation. For example, in the event that a firm has a participation in an undertaking, it may, either implicitly or explicitly, have arrangements in place that require it to provide financial support beyond the proportional share of capital it holds.

11.12 A prudent starting point, for the treatment of relationships captured in CRR Article 18(5), would be to require full consolidation. In the event that a firm can prove that a full consolidation treatment is disproportionate, they could apply to the PRA for permission to use proportional consolidation.

(1) For reference, paragraphs 65, 81 and 120 of the PRA's 'approach' document set out the PRA's high-level approach and expectations on the areas covered by this chapter.
(2) See the Financial Services (Banking Reform) Bill, http://services.parliament.uk/bills/2013-14/financialservicesbankingreform.html.
(3) 83/349/EEC.

11.13 The PRA is obliged under CRR Article 18(6) to determine whether and how consolidation is to be carried out in instances where (i) one institution exercises significant influence over another (but without holding a participation or other capital tie) or (ii) two or more institutions are placed under single management other than pursuant to a contract or clauses of their memoranda or Articles of association. The PRA will continue to require proportional consolidation of the relevant undertaking. The relevant proportion (if any) will be as stated in the Part 4A permission of the firm.

11.14 The approach to consolidation set out above is subject to regulatory technical standards; the EBA is required to submit the draft standards to the Commission by 31 December 2016.

Entities excluded from the scope of prudential consolidation

11.15 CRR Article 19 allows the exclusion of certain undertakings from the scope of prudential consolidation. Firms are able to exclude entities in cases where the cost of consolidation would exceed the benefits from mitigating the risks to the group. In particular, Article 19(2) permits discretion for the PRA, where it is the consolidating supervisor, to exclude undertakings from consolidation subject to specific conditions. Details of how the PRA intends to use this discretion are set out in the Groups supervisory statement in Appendix 2.

Large exposures

11.16 The requirements of the large exposures regime are located in CRR Part Four. The PRA does not envisage any significant change from its current large exposures regime where CRR provisions are either identical or similar to the provisions contained in the legislation it replaces.

11.17 The CRR sets out a number of national discretions in the application of the large exposure regime. The PRA will consider whether large exposure discretions on the limits and calculating credit risk mitigation techniques as set out in Article 395(6) and Article 401(1)–(3) respectively, should be exercised and will consult as necessary.

Large exposures limit

11.18 CRR Article 395(1) provides the PRA with the discretion to set a lower limit than €150 million in relation to the 25% large exposures limit. The PRA does not intend to use this discretion.

11.19 In the situation that a firm has breached the large exposures limit stipulated in Article 395(1) and where this breach is judged to have occurred in an exceptional case, CRR Article 396(1) enables the PRA to allow the firm a limited period of time in which to comply with the limit, where the circumstances warrant it. The PRA will consider whether to exercise this discretion on a case by case basis where the specific circumstances of the firm are judged as exceptional.

11.20 Where the amount of €150 million referred to in CRR Article 395(1) is applicable, the PRA will consider applications to exceed the 100% limit in terms of the institution's eligible capital on a case by case basis, where the specific circumstances of the firm are judged as exceptional.

11.21 The decision to exercise the discretions described in CRR Article 396(1) will not be a change to the current practice in the United Kingdom. Therefore, there should not be any additional costs incurred by firms who already apply current PRA rules.

Large exposures exemptions

11.22 CRR Article 400(2) allows the PRA to either fully or partially exempt certain categories of exposures from the large exposures limit specified in CRR Article 395(1). The PRA will apply the high-level principle that the large exposure regime is designed as a backstop to limit a firm's exposures to a single entity or group of connected entities. The probability of default of an exposure is not relevant in the application of the regime. In addition, the maturity or type of exposure should in general not matter when applying the large exposures regime. However, the PRA is proposing to allow for the exemptions specified in CRR Article 400(2)(c) and 400(2)(g)-(h), which are detailed later in this section. The PRA is not proposing to exercise any of the other discretions outlined in CRR Article 400(2).

Core UK group

11.23 CRR Article 113(6) permits the PRA to allow a 0% risk weighting in respect of intra-group exposures which fulfil the listed criteria. Provided that the provisions of CRR Article 113(6) are met, Article 400(1)(f) then requires that these exposures are exempted from the large exposures limit specified in CRR Article 395(1). Further clarification of how the PRA will exercise this discretion is provided in the supervisory statement on large exposures in Appendix 2.

11.24 The decision to exercise the discretion described in CRR Article 113(6) will not be a significant change to the current practice in the United Kingdom. Therefore, there should not be any material additional costs incurred by firms who already apply current PRA rules.

Non-core large exposures group

11.25 Article 400(2)(c) permits the PRA to exempt from the large exposures limit exposures incurred by a firm to specified counterparties that are subject to consolidated supervision in the same jurisdiction or in different jurisdictions but where equivalent standards of supervision are in force. The PRA proposes to exercise this discretion through a rule as set out in Appendix 1. Further information on the related process is provided in the supervisory statement on large exposures in Appendix 2.

11.26 The decision to exercise the discretion described in CRR Article 400(2)(c) will not be a significant change to the current practice in the United Kingdom in respect of the application of large exposure limits to non-trading book exposures. However the interaction with the concentration risk capital component (CNCOM) charge may result in an increased charge for some firms.

Question

The PRA invites comments on the approach set out to the non-core large exposures group, in particular the capital impacts for firms.

Sovereign exposures

11.27 Article 400(2)(g)-(h) allows the PRA to exempt exposures which constitute claims on central banks and governments. These claims can either be in the form of minimum reserves held at central banks and denominated in their national currencies, or statutory liquidity requirements held in government securities which are denominated and funded in their national currencies. The PRA proposes to exercise this discretion through a rule as set out in Appendix 1. Information on the related process is provided in the supervisory statement in Appendix 2 as regards sovereign exposures.

11.28 The decision to exercise the discretion described in CRR Article 400(2)(g)-(h) will not be a change to the current practice in the United Kingdom. Therefore, there should not be any additional costs incurred by firms who already apply current PRA rules.

12 Liquidity

Articles 411–428, 460 CRR, Articles 86, 105 CRD

12.1 The CRR introduces a new liquidity buffer; the Liquidity Coverage Requirement (LCR), and a stable funding requirement. This chapter sets out actions the PRA proposes to take to implement aspects of these requirements.

12.2 Neither requirement is fully harmonised at the commencement of the CRR in 2014. In the case of the LCR, from January 2014, all UK PRA authorised banks, building societies and designated investment firms are required to maintain levels of liquidity buffers that enable them to meet their liabilities during a period of stress. The Commission must adopt a delegated act to fully specify the definition, calibration, calculation and phase-in of the LCR for implementation in 2015. This chapter addresses national discretions provided for in the CRR and consequential amendments to BIPRU 12, including reflecting provisions set out in the CRD on liquidity risk. Relevant rule changes are set out in Appendix 1.

12.3 The PRA will conduct an impact assessment and an equality and diversity assessment when it considers the delegated act to implement the LCR which the Commission is to adopt in 2014. Until consideration of the delegated act, the PRA considers that its existing liquidity regime is in line with its statutory objectives. There is a longer timetable for the specification of the stable funding requirement. The Basel Committee on Banking Supervision and the EU institutions are considering policy options. CRR Article 521(2)(b) defers commencement of the general requirement for stable funding until 1 January 2016.

12.4 In 2014 the CRR introduces a mandatory reporting obligation for liquidity purposes, as required by CRR Article 415. The obligation applies to all firms within the scope of the CRR liquidity regime and they must meet this obligation at both the individual and consolidated basis, as specified in CRR Article 6(4) and Article 11(3). Firms are required to report by significant currency as specified in CRR Article 415(2). The reporting obligations require that relevant LCR data is reported not less than monthly and the data relevant to stable funding is reported not less than quarterly. The EBA will specify the uniform reporting forms and reporting portal that firms will use to provide the liquidity data required by the CRR.

12.5 Firms are also required to provide data for a number of additional liquidity monitoring metrics that are intended to assist supervisors in monitoring firms' liquidity risk profiles. The EBA is responsible for the development of these metrics and has consulted on its proposals.

Proposals

PRA liquidity regime

12.6 Until the LCR comes into force with the adoption of the Commission's delegated act in 2015, the PRA's liquidity regime, including liquidity reporting contained in BIPRU 12 and SUP 16 will continue to apply to PRA authorised banks, building societies and designated investment firms. In doing so, the PRA will be exercising the discretions contained in CRR Article 412(5) and Article 415(3).

12.7 The PRA will continue to have the power to undertake supervisory reviews of firms' liquidity arrangements in line with the provisions of CRD. The PRA will consider further how its liquidity regime will change upon the specification of the LCR. The PRA will consult on changes to its liquidity regime in due course.

Liquidity subgroups

12.8 From the commencement of the CRR until 1 January 2015, only domestic liquidity subgroups can be established. As permitted by CRR Article 8(2), the PRA will consider applications for the formation of domestic liquidity subgroups[1] for the purpose of reporting the liquidity data required by the CRR. The PRA will consider whether the circumstances and criteria specified in the CRR have been met by these applications. More information on the process for such applications will be provided by the PRA in due course.

12.9 Where a domestic subgroup is permitted, compliance with the CRR liquidity obligations at the individual level can be replaced with compliance at the sub-consolidated level of the liquidity subgroup. This proposal is in line with PRA's existing processes for deciding liquidity waivers and should not therefore impose additional costs on firms.

Investment firm exemption

12.10 The PRA has chosen not to exercise the discretions contained in Article 6(4) and Article 11(3) CRR which would

(1) ie where all member firms are authorised within the same Member State.

permit it to exempt the investment firms it supervises from the liquidity requirements set out in the CRR. In reaching this decision, the PRA took account of a range of factors, including those considered when designating the investment firms to be subject to prudential supervision by the PRA (for example, their potential risk to the stability of the financial system or to one or more PRA-regulated entities in their group).

Other national discretions

12.11 The PRA has chosen not to exercise the other competent authority discretions provided in the CRR liquidity requirements (relevant to reporting requirements, issuing of guidelines, the LCR and stable funding). The PRA will consider these national discretions alongside the Commission's adoption of the delegated act to harmonise the LCR in 2015. The PRA will also take into account technical standards to be developed by the EBA which will affect some of these national discretions.

Amendments to BIPRU

12.12 Amendments have been made to BIPRU 12 (set out in Appendix 1) as a consequence of the revocation of the rest of BIPRU and the transposition of the liquidity risk management requirements contained in CRD Article 86. The amendments do not give rise to a change in the standard and continue to be in line with the PRA's existing approach and should not therefore impose additional costs on firms.

12.13 The PRA does not expect these amendments to necessarily result in changes to modifications issued to firms. However, firms should review for themselves the amended Handbook materials and the CRR to ensure this continues to be the case for their circumstances.

13 Reporting and disclosure

Articles 99–101, 394, 415, 429–455, 499, 521 CRR, Article 90 CRD

13.1 The CRR introduces requirements for common harmonised reporting by institutions on own funds requirements, financial information and on other prudential requirements such as liquidity and leverage risk. Additionally the CRR and CRD require public disclosure of information relating to the activities of firms within scope of the legislation. This chapter sets out the PRA's approach to implementing these reporting and disclosure requirements.

Proposals

Implementing Common Reporting Framework (COREP) and Financial Reporting (FINREP)

13.2 As a result of the introduction of common reporting requirements under the CRR, the PRA proposes to delete and amend existing PRA reporting requirements.

13.3 This will involve the removal of the majority of PRA rules and guidance in the PRA Supervision manual Chapter 16 (SUP 16.12; and Annexes 24R and 25G). The implementing technical standards in CRR Article 99 require a number of new reports, where equivalents do not currently exist in the PRA Handbook. Firms should ensure they review the relevant technical standards, once published by the EBA, to understand these requirements.

Common Reporting (COREP)

13.4 CRR Article 99 requires firms to report data on own funds to the PRA as the competent authority. Other reporting requirements are in CRR Article 101 (losses stemming from lending collateralised by immoveable property); Article 394 (large exposures and other largest exposures); Article 415 (monitoring of the Liquidity Coverage Requirement (LCR)); and Article 430 (leverage ratios).

13.5 The rules and corresponding guidance on the following PRA data items are being deleted or amended:

PRA data item	Handbook treatment under CRD IV	COREP templates
FSA003 – Capital adequacy	Delete	COREP CA
FSA004 – Credit risk	Delete	COREP CR
FSA005 – Market risk	Delete except for data on Capital Add-ons for Risks Not in VaR	COREP MKR
FSA006 – Market risk	Retain	No equivalent
FSA007 – Operational risk	Delete	COREP OR
FSA008 – Large exposures	Delete	COREP LE
FSA018 – UK integrated group large exposures	Amend	No equivalent
FSA028 – non-EEA subgroups	Delete	COREP GS
FSA045 – IRB data	Retain	COREP CR IRB
FSA046 – Securitisation	Delete	COREP CR SEC
FSA058 – Securitisation	Delete	COREP CR SEC
SUP 16.16 – Prudent valuation	Retain until harmonised reporting templates come into force	Harmonised reporting will be required under CRR in future

13.6 Where data elements in the above returns are unchanged it is because they are not covered by the CRD or CRR Article 99 and therefore remain subject to the PRA's powers under FSMA.

13.7 This includes liquidity data items FSA047 and FSA049 to FSA056, which will remain as PRA supervisory returns until harmonised liquidity policy is introduced under the CRR (see Chapter 12).

13.8 FSA018 (UK consolidated groups) captures information on large exposures from the core UK group to the non-core large exposures group; that information is not collected in COREP LE. The PRA is therefore retaining FSA018 as a regulatory return. However, this reporting will only apply to firms that have both a core UK group and a non-core large exposures group. FSA018 guidance will be amended to this effect.

13.9 Firms will also continue reporting FSA045 (IRB portfolio risk) under the PRA rules. FSA045 collects data split between credit risk and counterparty credit risk. By contrast, the COREP CR templates combine counterparty and credit risk data when reported at grade level. Using the COREP CR data alone would prevent the PRA making like-for-like comparisons between counterparty credit risk and credit risk and identifying outlier firms.

3.10 FSA005 will largely be deleted as it is replaced by the COREP market risk templates. The PRA is retaining its 'Risks Not in VaR' (RNIV) framework. Part of the FSA005 data item captures data on capital add-ons due to RNIV, which is not captured in the COREP market risk templates. The data reported as part of FSA005 will enable the PRA to monitor the implementation of the RNIV framework and the PRA therefore proposes to retain it under the powers in CRD Article 104.

Financial Reporting (FINREP)

13.11 CRR Article 99 requires certain firms to report financial information. The PRA is therefore amending the rules and guidance for data items FSA001 (balance sheet) and FSA002 (income statement). This means that banks, building societies and designated investment firms meeting the criteria in CRR Article 99(2) and preparing accounts in conformity with international accounting standards will no longer report FSA001 and FSA002 at consolidated level. Rules and guidance relating to FSA001 and FSA002 continue to apply to those institutions at solo level, and also to any regulatory group not meeting all the criteria in CRR Article 99(2).

13.12 CRR Article 99(5) allows competent authorities the discretion to extend the scope of financial information reporting as prescribed in CRR Article 99(2) to firms other than those described in Article 99(2). The PRA is not exercising this discretion.

13.13 CRR Article 99(3) gives competent authorities the discretion to apply FINREP to consolidated groups required to use IFRS for regulatory reporting even though it is not used for published financial statements. As the PRA does not set such a regulatory requirement under its rules, this discretion is not applicable.

Public disclosures

13.14 CRD Article 90 and certain CRR provisions require institutions to disclose certain regulatory information publicly. As CRR imposes regulatory disclosure requirements directly on firms, the PRA Handbook rules and guidance in BIPRU Chapter 11 are being deleted. Any waivers of BIPRU 11 rules will end when the relevant CRR provisions enter into force. None of the CRR disclosure requirements can be waived.

Return on assets

13.15 CRD Article 90 requires institutions to disclose in their annual report among the key indicators their return on assets, calculated as their net profit divided by their total balance sheet. The PRA is introducing a rule to require this disclosure.

Leverage ratio

13.16 The CRR requires firms to disclose the leverage ratio from 2015, and a delegated act for the Commission to amend the ratio prior to disclosure if necessary to address shortcomings in its design. The interim FPC recommended that the largest UK banks publicly disclosure their leverage ratios; such disclosures began this year in respect of the 2012 financial year end. In June 2013, the PRA completed its capital shortfall exercise, which responded to the interim FPC's March 2013 recommendations on capital adequacy of major UK banks and building societies. This included requiring two firms to produce plans to meet capital shortfalls in respect of a 3% Common Equity Tier 1 leverage ratio after adjustments. The Basel Committee is currently consulting on revisions to the leverage ratio framework and disclosure thereof.

13.17 We have not included material on disclosure of the leverage ratio in this consultation. In due course, we intend to consider whether further PRA material is required to clarify our expectations of disclosure prior to 2015 and beyond.

14 PRA rule waivers — treatment under the CRR

Background

14.1 This chapter sets out the PRA's proposals in relation to the treatment under the CRR of rule waivers and modifications granted to firms in accordance with section 138A of FSMA and SUP 8. The proposals also apply to certain requirements imposed on firms in accordance with BIPRU 8.5.6(2)R. Rule waivers, modifications and the specified requirements will be jointly referred to in this chapter as 'waivers'. The proposals are contained in a draft instrument included in Appendix 1, which is also being consulted with HM Treasury. The legal instrument underpinning this proposal could change following consultation with HM Treasury, but we expect that the substance of our proposals as described in this chapter will remain the same.

Treatment for equivalent BIPRU rule waivers

14.2 As explained in Chapter 1 (Overview), the PRA is proposing to delete all the rules in BIPRU, except BIPRU 12, and to disapply GENPRU to firms in scope of CRD IV, except GENPRU 3. As a result, all waivers granted to firms under BIPRU and GENPRU rules (except those in BIPRU 12 and GENPRU 3) will cease to have effect by operation of law. However, where those rules are replaced by substantially equivalent requirements in the CRR, the PRA will have the power to grant an equivalent permission when exercising a national discretion given to it as a 'competent authority'.

14.3 Accordingly, the PRA proposes to grant all such CRR-based permissions with effect from 1 January 2014 to those firms which are currently holding an eligible waiver. A waiver will be eligible only if it meets the following conditions:

- first, the relevant waiver must relate to a BIPRU and, where applicable, a GENPRU rule with an equivalent article in the CRR. Waivers with equivalent CRR articles are shown in **Table 14.A** and **14.B** below;

Table 14.A Eligible advanced prudential calculations approach waivers

Advanced prudential calculation approach	PRA rule (rule waiver or modification)	CRR reference
Internal Ratings Based (IRB) permission for credit risk	• BIPRU 4 applies to a *firm* with an *IRB permission* • *Rules* waived or modified: (a) *GENPRU* 2.1.51R (b) *BIPRU* 3.1.1R	• Part Three, Title II, Chapter 3 • Article 143 • Article 178.1(b) (where a *firm* is authorised to replace 90 days with 180 days for exposures secured by residential or SME commercial real estate in the retail exposure class)
Eligibility of physical collateral under the IRB Approach	• *BIPRU* 4.10.16R (where authorised by the *firm's IRB permission*)	• Article 199.6
Master netting agreement internal models approach	• *BIPRU* 5.6.1R in accordance with *BIPRU* 5.6.12R	• Article 221
Supervisory formula method for securitisation transactions	• *BIPRU* 9.12.3R • *BIPRU* 9.12.5R • *BIPRU* 9.12.21R (where authorised by the *firm's IRB permission*)	• Article 259.1(b) • Article 262
ABCP internal assessment approach	• *BIPRU* 9.12.20R (where authorised by the *firm's IRB permission*)	• Article 259.3
Exceptional treatment for liquidity facilities where pre-securitisation RWEA cannot be calculated	• *BIPRU* 9.11.10R as modified in accordance with *BIPRU* 9.12.28G (where authorised by the *firm's IRB permission*)	• Article 263.2
Advanced Measurement Approach (AMA) permission	• *BIPRU* 6.5 applies to a firm with an *AMA permission* • *Rule* waived or modified: *BIPRU* 6.2.1R	• Article 312.2 • Part Three, Title III, Chapter 4
Combined use of different approaches for operational risk — AMA and standardised approach or basic indicator approach	• *BIPRU* 6.2.9R (in accordance with *BIPRU 6.2.10G* and the *firm's AMA permission*)	• Article 314, par. 2 and 3
Permission to use internal models to calculate own funds requirements for market risk (Value-at-Risk)	• *BIPRU* 7.10 applies to a firm with a *VaR model permission* • *Standard market risk PRR rules* as specified and waived or modified by the firm's *VaR model permission waiver* • *GENPRU* 2.1.52R	• Article 363 • Part Three; Title IV; Chapter 5; Sections 2, 3 and 4
Permission to use internal models to calculate own fund requirements for the correlation trading portfolio	• *BIPRU* 7.10.55T R to *BIPRU* 7.10 55ZA R (where the *firm* is authorised to use the *all price risk measure* in its *VaR model permission waiver*)	• Article 377

Table 14.B Other eligible waivers and requirements

National discretion	PRA rule (rule waiver or modification)	CRR reference
Individual consolidation method	• *BIPRU* 2.1.7R (*solo consolidation waivers*)	• Article 9
Application of requirements of Part Five (exposures to transferred credit risk) on a consolidated basis	• *BIPRU* 9.15.16A R	• Article 14.3
Methods of prudential consolidation — Article 12(1) relationship	• *BIPRU* 8.5.6(2)R (as required by the Part 4A permission of the *firm*)	• Article 18.3 as implemented by rule 2.1 of the PRA Rulebook CRR Firms: Groups Instrument 2013
Methods of prudential consolidation — significant influence or single management relationship	• *BIPRU* 8.5.6(2)R — 'Article 134 relationship' (as required by the Part 4A permission of the *firm*)	• Article 18.6 as implemented by rule 2.1 of the PRA Rulebook CRR Firms: Groups Instrument 2013
Entities excluded from the scope of prudential consolidation	• *BIPRU* 8.5.9R • *BIPRU* 8.5.10R	• Article 19.2
Permission to revert to the use of a less sophisticated approach for credit risk	• *BIPRU* 4.2.23R (as modified in accordance with *BIPRU* 4.2.25G) • *BIPRU* 4.2.24R (as modified in accordance with *BIPRU* 4.2.25G)	• Article 149
Traditional securitisation — recognition of significant risk transfer	• *BIPRU* 9.4.11R • *BIPRU* 9.4.12R (subject to conditions in *BIPRU* 9.4.15D)	• Article 243, par. 2, 3, 4 and 5
Synthetic securitisation — recognition of significant risk transfer	• *BIPRU* 9.5.1R (6) and (7) (subject to conditions in *BIPRU* 9.5.1B D)	• Article 244, par. 2, 3, 4 and 5
Securitisations of revolving exposures with early amortisation provisions — similar transactions	• *BIPRU* 9.13.11R • *BIPRU* 9.13.13R • *BIPRU* 9.13.14R • *BIPRU* 9.13.15R • *BIPRU* 9.13.16R • *BIPRU* 9.13.17R (subject to conditions in BIPRU 9.13.18G)	• Article 256.7
Permission to revert to the use of a less sophisticated approach for operational risk	• *BIPRU* 6.2.5R (as modified in accordance with *BIPRU* 6.2.6G) • *BIPRU* 6.2.7R (as modified in accordance with *BIPRU* 6.2.8G)	• Article 313
Combined use of different approaches for operational risk — standardised approach and basic indicator approach	• *BIPRU* 6.2.12R (as modified in accordance with *BIPRU* 6.2.13G)	• Article 314.4
Waiver of the three-year average for calculating the own funds requirement under the basic indicator approach for operational risk	• *BIPRU* 6.3.2R (as modified in accordance with *BIPRU* 6.3.9G)	• Article 315
Waiver of the three-year average for calculating the own funds requirement under the standardised approach for operational risk	• *BIPRU* 6.4.5R (as modified in accordance with *BIPRU* 6.4.8G)	• Article 317.4
Own funds requirements for position risk for options and warrants on: (a) interest rates; (b) debt instruments; (c) equities; (d) equity indices; (e) financial futures; (f) swaps; and (g) foreign currencies	• *BIPRU* 7.9 applies to a firm with a CAD1 model waiver • *Rules* waived or modified: (a) *GENPRU* 2.1.52R (b) *BIPRU* 7.6.1R	• Article 329
Own funds requirements for commodities risk for options and warrants on: (a) commodities; and (b) commodities derivatives	• *BIPRU* 7.9 applies to a firm with a CAD1 model waiver • *Rules* waived or modified: (a) *GENPRU* 2.1.52R (b) *BIPRU* 7.4.1R	• Article 358.3
Interest rate risk on derivative instruments	• *CAD1 model waiver* for the use of an interest rate pre-processing model in accordance with *BIPRU* 7.9.44G • *Rule* waived: *GENPRU* 1.2.52R	• Article 331 • Article 340
Waiver of 100% large exposure limit where the €150 million limit applies	• *BIPRU* 10.6.32R as waived in accordance with *BIPRU* 10.6.33G • *SUP* 15.3.11R	• Article 396 in relation to the 100% large exposure limit set out in Article 395(1)
Waiver of large exposure limits in relation to intra-group exposures: core group waivers	• *BIPRU* 3.2.25R(2) • *BIPRU* 10.8A	• Article 113.6 • Article 400.1(f)
Waiver of large exposure limits in relation to intra-group exposures: non-core group waivers	• *BIPRU* 10.9A	• Article 400.2(c) as implemented by rule 2 of the PRA Rulebook CRR Firms: Large Exposures Instrument 2013
Waiver of large exposure limits in relation to sovereign exposures	• *BIPRU* 10.6.34R as waived in accordance with *BIPRU* 10.6.37G	• Article 400.2(g) and (h) as implemented by rule 3 of the PRA Rulebook CRR Firms: Large Exposures Instrument 2013

- second, the firm holding a waiver must be fully compliant with the BIPRU and, where applicable, GENPRU rule, as waived or modified, and with any conditions relevant to the granting of the waiver (as such may be reflected on the direction given to the firm and in any separate notifications) on and before 31 December 2013. Compliance with the BIPRU and, where applicable, GENPRU rule will tend to show compliance with the equivalent CRR article, although specified requirements and conditions will apply to different types of waivers. This is explained further below.

14.4 Where a firm holds a waiver that relates to an advanced prudential calculation approach, it must expressly confirm to the PRA that it complies with the relevant requirements that apply to that approach. **Table 14.A** shows the applicable PRA rules and the equivalent articles in the CRR for all waivers relating to advanced prudential calculation approaches that will be eligible for the treatment described in this chapter. These do not include the Internal Model Method (IMM) for counterparty credit risk, which will be dealt with as entirely new permissions because the CRR will make significant changes to the requirements applicable to counterparty credit risk.

14.5 The PRA has already started contacting firms holding eligible advanced prudential calculation approaches waivers to inform them of the steps that will be followed ahead of the entry into force of the CRR. In short, the process will be as follows:

- first, the affected firms will have to submit to the PRA an attestation of compliance in relation to each relevant waiver by no later than 31 August 2013, unless they have done so already;

- at the same time, if the PRA has identified any instances of non-compliance, it will require those firms to remediate them before the end of 2013 or put in place a credible remediation plan where compliance cannot be fully restored within this time period;

- the PRA expects then to review the responses and engage in bilateral discussions with the affected firms during the Autumn. The PRA will in due course notify its decision to the affected firms on whether they may rely on the existing waiver direction as the equivalent permission under the CRR with effect from 1 January 2014 and if so whether:

(i) it will be subject to the same terms; or

(ii) it will be subject to certain modified terms. Among these, the PRA may decide to exclude certain models, exposures or products from the scope of the permission due to the firm's being unable to restore compliance before the end of 2013. As an alternative, the PRA may add an agreed remediation plan as a condition for the firm to maintain certain models, exposures or products within scope, or require the firm to hold a capital add-on or apply a floor in relation to a given model.

14.6 Where a firm currently holds any other eligible waiver, it may rely on the existing direction as the equivalent permission under the CRR with effect from 1 January 2014. For these purposes, eligible waivers are those specified in **Table 14.B**.

14.7 Firms will not be required to confirm expressly to the PRA that they continue to comply with any relevant rules and conditions applicable to each eligible waiver referred to in paragraph 14.6, except as described in relation to deemed solo consolidation waivers in paragraph 14.8. However, as stated above, firms must be fully compliant with all such rules and conditions on and before 31 December 2013 in order to be able to rely on the current waiver direction as the equivalent permission under the CRR with effect from 1 January 2014. Should a firm cease to comply at any time, they must notify the PRA immediately as per PRIN 11.

14.8 As an exception to the treatment described in paragraph 14.7, firms holding a deemed solo consolidation waiver under BIPRU TP 22.3R must notify the PRA prior to 31 December 2013 that the solo consolidation minimum standards continue to be met with respect to the relevant subsidiary undertaking. Where a satisfactory notification is provided, the PRA may allow firms to treat their deemed solo consolidation waiver as a permission to use the individual consolidation method in accordance with Article 9 of the CRR.

14.9 Waiver directions that remain in effect as equivalent CRR-based permissions in accordance with this chapter on 1 January 2014 will continue in full force and effect until the expiry date specified therein. Any waivers granted to firms under BIPRU or GENPRU rules which are repealed or disapplied on the 1 January 2014 and not otherwise listed as eligible waivers in paragraphs 14.4 and 14.6 will cease to have effect on that date.

14.10 The PRA will publish in due course its proposals for procedures to deal with applications from firms in relation to certain national discretions in the CRR, including those listed in paragraphs 14.4 and 14.6.

Transitioning eligible SUP 16 waivers

14.11 We are also proposing a number of amendments to SUP 16. The amendments are included in a draft instrument which is attached in Appendix 1. Any waivers granted under the SUP rules which we propose to amend will be deemed as granted under the equivalent SUP rules as shown in **Table 14.C**.

Table 14.C Eligible SUP 16 waivers

SUP 16 rule as in force until 31 December 2013	SUP 16 rule as in force from 1 January 2014
SUP 16.12.11R	SUP 16.12.11B R
SUP 16.12.12. R	SUP 16.12.12A R
SUP 16.12.15 R	SUP 16.12.15B R
SUP 16.12.16 R	SUP 16.12.16A R
SUP 16.12.22A R	SUP 16.12.22C R
SUP 16.12.25A R	SUP 16.12.25C R
SUP 16.12.26 R	SUP 16.12.26A R

Part III Economic analysis

15 Economic analysis

Summary of estimates[1]

15.1 This section sets out an analysis of the costs and benefits of introducing CRD IV in the United Kingdom. All numerical estimates should be treated as indicative, subject to substantial uncertainty and highly sensitive to the underlying assumptions.

15.2 The benefits of CRD IV accrue largely from the reduction in the probability that a crisis occurs as banks and building societies (deposit-takers) raise the proportion of capital on their balance sheets. Whilst it is possible to produce an estimate of combined benefits of all regulatory actions that raise capital ratios since the onset of the crisis, it is not possible to identify the individual benefits of CRD IV. However the PRA judges that the CRD IV package, given its role in the reform programme, is likely to have accounted for a substantial proportion of the overall benefits.

15.3 The costs to the UK economy of all actions taken in response to the crisis arise largely as deposit-takers adjust their balance sheets.

15.4 In contrast to the benefits, it is possible to estimate the contribution of CRD IV to the overall cost of the regulatory response to the crisis. Non-capital compliance costs, largely associated with new reporting measures (COREP/FINREP),[2] will add only minimally to the overall cost of CRD IV and are not expected to have a measurable impact on UK economic activity.

15.5 In addition to the inability to disaggregate the benefits (and therefore net benefits) of the CRD IV package in isolation, there is uncertainty around the measure of both the total benefits and costs. **Table 15.E** provides an indication of the statistical confidence intervals around the estimates of net benefits for the entire package.

Outline of policy changes considered

15.6 This analysis includes all CRD IV measures affecting firms that are anticipated to have an impact on activity in the UK economy. This involves largely those elements that raise capital requirements (both quality and quantity).

15.7 In line with the PRA's general objective of promoting the safety and soundness of firms, this analysis considers the implications of CRD IV on individual firms to the extent possible. The impact on individual firms is assessed through the implementation period and then aggregated to allow estimates of the macroeconomic impacts to be calculated. A key assumption in the analysis is that there is no significant disruption to firms' business models or the economy in future.

15.8 Given the scope of the changes considered, the analysis of the policy measures is necessarily approximate. Some elements of CRD IV are unable to be captured (eg group consolidation provisions, large exposures) although it is not expected that these elements will have a sufficiently large impact to invalidate the analysis.

15.9 **Table 15.J** (see page 58) contains a summary of all the policy elements and assumptions underlying this analysis.

Affected firms and markets

Firms

15.10 CRD IV changes prudential requirements for around 2,200 entities at both the solo and consolidated level in the United Kingdom. These include banks, building societies and investment firms. **Table 15.A** sets out the population of solo firms and consolidated groups by type and size subject to these rules. Most investment firms are prudentially regulated by the FCA. However, the PRA regulates a small number of designated investment firms whose size and scope of activities could present significant risks to the stability of the financial system.[3]

15.11 UK financial markets are highly concentrated. The ten largest deposit-takers in the UK account for almost 85% of UK banking sector assets and lending, and hold over 80% of deposit takers' retail deposits in the United Kingdom. Moreover of these, the largest five deposit-takers account for around 60% of total UK bank lending and retail deposits.

15.12 As activity is heavily concentrated, it is possible to approximate the impact on the economy by considering a smaller population of the largest firms. For the PRA's analysis, we have detailed quantitative information on the impact of

(1) The framework for computing these estimates is described in more detail in *FSA Occasional Paper No. 42*.
(2) Compliance costs of COREP are set out in Chapter 13: Reporting and disclosure.
(3) The PRA's statement of policy on the designation of investment firms is available at www.bankofengland.co.uk/pra/Pages/publications/designationinvestmentfirms.aspx.

Table 15.A Population of affected firms

Type of firm	Small[a]	Large[b]	Total
Banks	178	25	203
Building societies	50	1	51
Investment firms	1,709	213	1,922
of which:			
Limited activity	*109*	*24*	*133*
Limited license	*1,437*	*118*	*1,555*
Full scope	*163*	*71*	*234*
Total affected firms[c]	1,937	239	2,176

Source: FSA regulatory returns at 2012 Q4.

(a) Defined as banks and building societies with total assets under £100 billion, investment firms with total assets under £100 million.
(b) Defined as banks and building societies with total assets over £100 billion, investment firms with total assets over £100 million.
(c) Of the total affected firms that are regulated by the PRA, around 50 of these firms are mutuals (defined as building societies, friendly societies, Industrial & Provident societies and other EU mutual societies).

CRD IV for ten firms which represent approximately 64% and 70% of total UK banking sector assets and lending activity respectively. These ten firms also hold almost 60% of the total capital resources in the UK banking sector.

Markets

15.13 The markets in which the population of affected firms operate cover products most closely associated with the credit intermediation process, including: deposit-taking, retail and wholesale lending, and interbank lending. However, the affected firms also operate in a number of other markets for similar or complementary products such as: venture capital/private equity, securitisation, repos, securities lending and borrowing, OTC derivatives and asset management.

15.14 CRD IV will affect some markets directly (eg securitisation and OTC derivatives) given its broader risk coverage and higher counterparty risk requirements. These reforms will also create corresponding effects in related markets as firms adjust lending and deposit rates to manage profit margins and regulatory capital ratios to mitigate higher capital costs.

15.15 Previous research has shown that prior to the crisis, banks responded to higher capital requirements by reducing balances in relatively higher risk-weighted asset classes.(1) Deposit-takers do this by altering underwriting standards, including interest rates, which, in turn, affect the supply of credit in these higher-risk lending markets.

15.16 The PRA has not considered a strict definition of markets in this discussion. A more complete definition would include products that perform very similar functions whether currently used for this purpose or not ('imperfect substitutes'), and consider those firms not currently in the market that could supply these products. For example, the category 'wholesale lending' is identified as a market. A more complete market definition of 'wholesale lending' might include: wholesale borrowing by firms; corporate bond issuance; securitisation and collateralised debt obligations (CDOs) of firm debt; and repurchase agreements.

Impact on competition

15.17 The main transmission mechanism through which CRD IV is likely to affect UK economic output is through the effect that deposit-takers' funding costs have on their interest rate margins and the consequent impact on (non-financial firms) borrowing costs. Any change in interest rates on loans will be constrained to some extent as non-financial firms may choose to issue corporate bonds due to the relative increase in the price of loans.

15.18 To the extent possible, this analysis takes into account competitive interactions between lending and corporate bond issuance.(2)

Baseline for calculations

15.19 To analyse the costs and benefits of CRD IV, the PRA has identified a baseline describing the likely outcome if the policy package were not implemented. The baseline in this case is complicated by a number of factors.

15.20 First, there are a number of economic and regulatory factors that overlap with CRD IV which make a clear delineation of issues impossible:(3)

- Poorer economic conditions brought about by the crisis are not typical of the conditions banks face over the economic cycle. Estimates starting from current data will therefore be distorted as weak economic conditions will dominate the calculation.

- Banks have been subject to a number of regulatory actions since the onset of the crisis, some of which were in anticipation of higher capital requirements under Basel III. These actions have already moved banks towards the new CRD IV requirements. We will underestimate the benefits of CRD IV by ignoring these actions.

- The prolonged negotiation period for Basel III and CRD IV means that banks, driven by both internal management and market pressures, have already anticipated the higher capital requirements to some degree.

15.21 Second, market pressure on banks to pre-empt forthcoming regulation has affected firms' capital positions. Firms will need to raise a particular amount of capital overall, but it is impossible to predict accurately the timing of these moves. The analysis therefore assumes that capital is accumulated (and capital ratios raised) in a linear fashion over

(1) See *FSA Occasional Paper No. 36* for detail.
(2) See Section 5 of *FSA Occasional Paper No. 38* for discussion.
(3) These issues are discussed in detail in Section 6.1 of *FSA Occasional Paper No. 42*.

the implementation period (2014 to 2021). While this smooth profile for individual deposit-takers' capital ratios over the transition period is not entirely realistic, the estimates of overall costs and benefits are only affected by very large deviations, so this assumption will not alter the estimates.

15.22 Third, the net benefits of the policy package are likely to be underestimated if we choose a baseline that incorporates some increase in firm capital ratios that might be unwound in the absence of, or could otherwise be attributable to, CRD IV.(1)

15.23 Fourth, while it is possible to calculate the total benefits of all regulatory actions that raise banks' capital (and liquidity) requirements, it is not possible to calculate the incremental benefits of any particular element. This is because the marginal benefits, which arise from reducing the probability of a crisis, diminish as firms' capital requirements rise above previous levels. The incremental benefits of each policy element, while not affecting the total benefits, will change depending on the order in which they are assessed (regardless of merit).(2) The benefits therefore need to be calculated for all actions in total.

15.24 Given these considerations have a number of implications for calculating the costs and benefits of CRD IV, the following assumptions are made about the baseline:

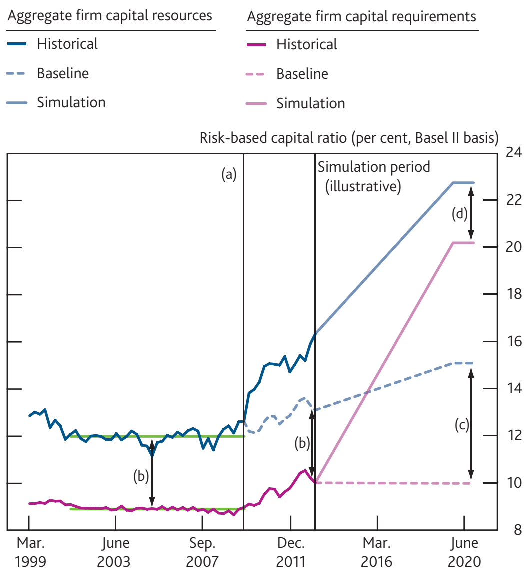
- Calculations start from a point immediately prior to the financial crisis to avoid the distortions brought about by the current atypical economic conditions and to ensure consideration of the full scope of the benefits of raising capital standards via CRD IV.
- The CRD III changes to the treatment of banks' trading book and resecuritisation exposures remain in place.(3)
- The FSA's enhanced supervisory programme, introduced in 2009 and which required increases in both the quantity and quality of capital for Tier 1 banks, is extended indefinitely into the future (see **Table 15.J**).
- The FSA/PRA capital planning buffers framework is maintained and deposit-takers either maintain their existing surplus over capital requirements or meet the capital planning buffer, whichever is higher.

15.25 **Chart 15.1** shows the path for firms' total capital requirements and resources both excluding (the baseline) and including (the simulation) the introduction of CRD IV. The baseline assumes that part of the increase in deposit-takers' capital ratios over the period from the March quarter 2009 to present is attributable to regulatory actions other than CRD IV (the blue dashed line). Deposit-takers' capital resources are then assumed to rise in a linear fashion to reach compliance with the final CRD IV requirements.

15.26 From **Chart 15.1** it is noted that the voluntary capital surplus over all requirements is assumed to be half the size in the simulation as in the baseline (footnote (d) in **Chart 15.1**) and that this surplus is reduced in a linear fashion over the implementation period. This is because: the CRD IV introduces new regulatory buffers that effectively reduce the need for firms to hold voluntary surplus capital above requirements; and CRD IV measures that constrain deposit-takers' risk-taking behaviour and improve transparency help reduce volatility of capital ratios.

15.27 We also note that **Chart 15.1** shows the path for the aggregate total capital ratio, measured on a consistent basis across the time period. That is, the calculations take account of changes to the composition of capital to provide a comparable measure. Similar profiles using the same assumptions (linear profile, reduction in voluntary capital surplus) are constructed at each level of capital required by CRD IV (CET1, T1 and Total capital).

Chart 15.1 Capital requirements and resources for the simulation and baseline



(a) March quarter 2009. The FSA Enhanced Supervisory programme was introduced in the December quarter 2008.
(b) Size of the average, pre-crisis capital surplus, defined as the difference between banks' capital requirements and resources.
(c) Size of the average capital surplus in the baseline, calculated as the average across banks of the larger of either individual banks' pre-crisis capital surplus or the capital planning buffer (calculation is illustrative).
(d) Size of the average capital surplus in the simulation, assumed to be half the average capital surplus in the baseline at the end of the period.

Changes in capital

Approach to calculating changes in capital

Deposit-takers

15.28 The UK deposit-taking sector is dominated by a small number of large but dissimilar institutions. The changes to regulatory requirements in CRD IV will affect these firms in

(1) See Section 6.1 of FSA *Occasional Paper No. 42*.
(2) See Section 6.2 of FSA *Occasional Paper No. 42*.
(3) See FSA CP09/29 for a description of these costs.

different ways, depending on each firm's business model. Treating the entire sector as a 'single representative agent' making decisions over an aggregate balance sheet, rather than as a number of heterogeneous firms acting according to their own business model, will most likely fail to capture properly aggregate behaviour.

15.29 The PRA has used an empirical analysis of UK deposit-takers' behaviour to create a model that approximates the different responses expected from individual firms.[1] The intuition behind the model is straightforward: deposit-takers react to differences between their desired future capital ratios (for each capital tier) and their existing capital resources by adjusting both (a) their levels of capital and (b) risk-weighted assets over time until they achieve their desired ratio. In this framework, changes to regulatory minima and buffers will change each firm's desired capital ratio. In contrast, changes to the definition of capital and risk coverage will change firm's existing capital ratios.

15.30 This model is applied to each firm considered in the analysis. The model provides an estimate of the likely difference in: CET1 capital; Tier 1 capital; total capital; total loans; risk-weighted assets; and total assets. There are a number of advantages to taking this approach to measuring the impact on deposit-takers capital ratios:

- The overlapping elements of CRD IV which interact with each other (eg higher minimum standards and definition of capital changes) can be taken into account.

- Different minimum regulatory requirements expressed in term of core, Tier 1 and total capital can be calculated.
- Changes in banks' balance sheets can be expressed in a consistent way, providing an quality-adjusted measure of capital ratios over time.

15.31 The responses from individual firms through time can be weighted to calculate a single series representing the firm's capital ratio that is consistent with their previous Basel II capital ratio using:

- Information on the expected changes to the composition of the balance sheet and capital.

- The expected cost to firms of different definitions of regulatory capital (see paragraphs 15.43–15.45 below).

15.32 The individual responses are then aggregated to derive an industry-wide response to the policy changes which can then be used in a macroeconomic model to determine the wider impact on the UK economy. Calculating the aggregate response in this way helps address the issue that changes to capital requirements affect individual banks in different ways and that calculations using aggregate balance sheet information are likely to be different (ie a fallacy of composition).

15.33 A key limitation of this approach is that it only calculates banks' responses to shocks and is not a model of the shocks themselves. Firms and markets do not respond solely to the published timing of changes in regulations. Rather, they respond pre-emptively and to market pressures (see paragraph 15.22). Consequently, this approach will only provide an approximation of the possible timing of any impacts.

Investment firms

15.34 Under CRD IV, investment firms will also face higher capital requirements. As profit-making firms, investment firms may look (a) to pass through the costs of adjustment to customers to the extent that competitive conditions in the market will allow, and (b) to adjust in the most efficient way possible while maintaining their profitability as best they can. Investment firms are therefore expected to adjust both the amount of capital and risk-weighted assets they have on their balance sheets in response to higher, and higher quality, regulatory capital requirements.

15.35 No clear empirical evidence of how investment firms might change their balance sheets in response to changes in regulatory requirements is available. In addition, consideration is only given to those designated investment firms regulated by the PRA in this analysis. The FCA will consult separately on the impact on other investment firms.

15.36 Consequently, calculations of both the additional capital that designated investment firms will hold if their balance sheets remained unchanged (current capital shortfalls), and the addition capital raised if these firms were to adjust their balance sheets in line with deposit-takers are provided. These calculations are unlikely to represent the actual capital raised by investment firms in response to CRD IV, although we expect the estimates to provide a range in which the actual response will lie.

Calculation of additional capital required

15.37 This section sets out the estimates of the change in capital for deposit-takers and investment firms. There are two parts to our calculations of the incremental capital required under CRD IV:

(1) The one-off incremental change in capital required to meet CRD IV requirements.

(2) The ongoing, annual charge to firms of remunerating the change in capital.

(1) See *FSA Occasional Paper No. 36* for the empirical analysis. *FSA Occasional Paper No. 42* also includes a discussion of how this analysis is used.

15.38 The analysis calculates the one-off change in capital by using outcomes from the approach described in paragraphs 15.30 to 15.32. First, an estimate is made of the change in the capital structure of deposit-takers' balance sheets over the long term, once all adjustments to the CRD IV requirements have been made. This adjusted capital structure is then applied to existing balance sheets and we calculate the implied incremental capital deposit-takers are expected to raise.

15.39 As it is expected that deposit-takers will meet the CRD IV changes by adjusting the risks on their balance sheets as well as raising additional capital, the increases in capital differ from that calculated by applying the CRD IV requirements to current balance sheet structures.

15.40 It is estimated that deposit-takers in the United Kingdom will need to raise, in aggregate, approximately £120 billion in additional capital fully to adjust to the CRD IV requirements based on the current size of their balance sheets. This capital will need to be raised over the course of the implementation period from 2014 to 2019. Total capital will need to rise by less than CET1 and Tier 1 capital reflecting the increasing quality of capital on balance sheets.

15.41 Capital is a riskier asset for investors to hold and requires higher remuneration than other forms of liability funding. That said, other things being equal, as the proportion of capital increases, there is a concomitant reduction in the risk attached to other liabilities and thus the return paid to investors. Any difference in the overall return to investors will represent the opportunity cost of measures taken.(1) However, an assessment of the impact is complicated by the degree to which in the past holders of bank liabilities believed that they were shielded from the risk of losses by the impact of 'too big' or 'too important to fail', among other factors.

15.42 The opportunity cost of debt and equity is not, therefore, fixed. As the proportions of debt and equity change on deposit takers' balance sheets, we expect that there will be changes in the relative prices. Prices could move such that there is no ongoing cost of holding additional capital. However, there are a number of factors (such as tax advantages of debt financing, risk opacity of deposit takers' balance sheets, short-term adjustment costs) that mean this outcome is unlikely to occur. We do not have clear empirical evidence of the extent to which debt and equity prices are likely to move. The presentation of the ongoing cost in **Table 15.B** is an upper estimate of the cost likely to be borne by firms.

15.43 The investment firms regulated by the PRA are estimated to have, in aggregate, a CET1 capital shortfall of between £36 billion and 43 billion once all CRD IV measures, including the regulatory buffers, are taken into account. If investment firms adjust their balance sheets in line with the estimated behaviour of banks used in this analysis, around £27–29 billion of capital will need to be raised over the CRD IV implementation period, based on the current size of balance sheets. The lower estimate reflects the reduction in risk, and therefore risk-weighted assets, that investment firms may hold once they have adjusted to the CRD IV requirements (**Table 15.C**).

Table 15.B Estimated change in capital resources: deposit-takers

	2012[a]		Estimated change	
	£ billions[b]	Percentage of total assets[c]	£ billions[b]	Percentage point of total assets[d]
One-off cost[e]				
Large deposit-takers[f]				
CET1	230	3.9	120	1.4
Tier 1	270	4.5	110	1.3
Total	330	5.6	30	0.3
Small deposit-takers[f]				
CET1	4¼	3.7	1½	1.2
Tier 1	4½	3.9	1¼	1.1
Total	6	4.9	½	0.3
Upper-bound ongoing cost[g] (£ billion per annum)				
Large deposit-takers	9.5			
Small deposit-takers	0.1			

(a) Data from December 2012 regulatory returns.
(b) Value of deposit-takers' capital valued in nominal 2012 pounds.
(c) Total assets held by deposit-takers in relevant size category.
(d) Percentage point change in composition of deposit-takers' balance sheets defined in terms of percentage of total assets.
(e) Change in capital resulting from the CRD IV package taking into account long-run adjustments made to the composition of deposit-takers' balance sheets.
(f) As defined in **Table 15.A**.
(g) Additional annual cost to deposit-takers of remunerating more and higher quality capital on balance sheets. Calculation is an upper limit as it does not assume any change to equity or debt prices as a result of changes to deposit-takers' balance sheet structure.

Table 15.C Estimated change in capital resources: investment firms[a][b]

£ billions[c]	
Current CET1 shortfall[d]	36–43
One-off CET1 increase[e]	27–29
Upper-bound ongoing cost	
(£ billions per annum)	
Ongoing capital cost[f]	2.1–2.3

(a) Includes only the investment firms regulated by the PRA. The approach to identifying which investment firms are regulated by the PRA is set out in 'Designation of investment firms for prudential supervision by the Prudential Regulation Authority', PRA Policy Statement, March 2013.
(b) Data are taken from *ad hoc* supervisory data collections. Collections include firms' own estimates of CRD IV (Basel III) impacts, made on a 'best efforts' basis which are used in these calculations. Assumptions on the calibration of CRD IV assumed are the same as for deposit-takers and set out in **Table 15.J**.
(c) Value of firms' capital in 2012 terms.
(d) Shortfall in capital from existing levels to new CRD IV requirements assuming no change in firms' balance sheets.
(e) Estimated change in CET1 based on expected adjustments to firms' balance sheets. The calculation is only indicative and assumes that investment firms adjust their balance sheets in line with banks' past behaviour.
(f) Assuming investment firms (a) adjust their balance sheet risks and (b) face the same cost of equity and cost of debt, as for deposit takers in **Table 15.B**.

(1) Crudely, the opportunity cost is estimated as the difference between the average cost of equity and non-equity funding for UK deposit-takers. Using the Capital Asset Pricing Model (CAPM), we approximated the long-term equilibrium cost of equity to be 10%, assuming a risk-free rate of 2% and equity risk premium of 5%. The risk-free rate is taken as the ten-year gilt rate and the equity risk-premium is the UK median from Fernandez, Aguirreamaloa and Corres Avendano (2013).

Impact on mutuals

15.44 The overall impact on mutuals of the CRD IV proposals will not be substantially different from that of other similar sized (non-mutual) institutions. However, there are some differences in the way in which mutuals are likely to respond to the new requirements.

15.45 Banks and other non-mutual firms can, in general, raise the proportion of equity on their balance sheets by retaining earnings, issuing new equity or a mixture of both. Mutuals cannot issue equity. However, mutuals will be able to issue common equity-like instruments to meet their core requirements (as allowed by Article 27 of the CRR) and they can meet some lower quality capital requirements with equity-like instruments. The extent to which mutuals will be able to issue these new instruments in markets, however, is not yet known.

15.46 Mutuals, like other firms, can retain earnings to boost their capital positions, although earnings need to be accumulated over time so retaining earnings is likely to take longer than raising equity-like instruments directly. Mutuals can also reduce their risk-weighted assets by adjusting their lending portfolios. It should be acknowledged, however that mutuals tend to have less diverse business models and any reduction in risk-weighted assets will be concentrated in particular business lines which may therefore affect profitability.

15.47 Nevertheless, mutuals' existing business strategies take this inertia in their ability to adjust their balance sheets into account by generally holding larger surpluses of capital resources over their total regulatory requirements than other types of firms and will help mitigate the cost of higher capital requirements.

Macroeconomic costs and benefits of CRD IV

Macroeconomic benefits of higher capital requirements

15.48 As noted in paragraph 15.2, it is not possible to disaggregate the benefits of the CRD IV package in isolation from other measures taken in response to the crisis that affect deposit-takers' capital ratios. However, the measured benefits of actions taken since the crisis to raise capital ratios are nevertheless in excess of the assessed costs of all measures. The PRA considers that the CRD IV package is therefore net beneficial to the UK economy.

15.49 We model the probability of a financial crisis using techniques developed by the early warning literature. This approach suggests that the likelihood of a crisis in any given year is influenced by both current and past policy and economic factors. In particular, crises are less likely as aggregate deposit-taker capital and liquidity ratios rise, and more likely as domestic asset prices accelerate or the United Kingdom's external balance deteriorates. It should be noted that while these factors can be used to estimate the probability of crisis, the model does not imply a causal relationship.

15.50 In the context of the crisis model used in this analysis, financial crises can have either a temporary or permanent impact on the UK economy.(1) For those crises that have a temporary impact, the subsequent recovery in economic activity following the crisis is expected to undo most, if not all, of the initial losses incurred. Consequently, these crises have little influence on the calculations of benefits.

15.51 Crises with permanent impacts, while generating significant, cumulative losses to UK GDP, do not occur with the same frequency as other crises. Examination of past crises suggests that permanent losses arose in only one in four crises in developed countries.(2) However, given the increased interconnectedness of the global banking system and the global capital mobility, it seems likely that a greater proportion of future financial crises will have a permanent effect on the economy. In the calculations, it is assumed that one in three crises have permanent effects. This assumption is a significant source of uncertainty for the calculations.

Table 15.D Estimate of costs and benefits[a]

	£ billions per annum[b]	Percentage of cost[c]
Total benefit[d]	15¼	
Introduction of the FSA's enhanced prudential regime[e] and CRD III[f]		36
Incremental costs of CRD IV[g]		
Minimum requirements[h]		56
Regulatory buffers		28
Pillar 2		7
Assumption: firms' voluntary buffers shrink		-26
Total cost of CRD IV	4½	64
Total cost of all prudential measures	7	100
Net benefits of all responses to the crisis	8¼[i]	

(a) Measured in terms of the impact on UK GDP.
(b) Annualised net present value of the chained-volume measure (2012) of GDP.
(c) Percentage of the total cost of all prudential measures taken in response to the financial crisis.
(d) The incremental benefits of individual measures are not meaningful as they are dependent on the order in which they are assessed.
(e) We define the financial crisis as the period following the collapse of Lehman Brothers in August 2008. The FSA's enhanced prudential regime was announced in 2008 Q4 and implemented in 2009.
(f) The implementation of these policies is discussed in detail in FSA (2009) and FSA (2011).
(g) See **Table 15.J** for detailed policy description.
(h) Includes changes to: minimum capital requirements, the definition of capital, and risk coverage.
(i) The net benefits should be considered in the context of annual GDP for the UK economy, estimated at £1.4 trillion per annum in chained volume terms for 2012.

15.52 Chapter 5 of *FSA Occasional Paper No. 42* contains a more complete discussion of the model and the approach to calculating benefits.

(1) See FSA *Occasional Paper No. 42* and Basel Committee (2010) for discussion.
(2) See Chapter 5 of FSA *Occasional Paper No. 42*.

Macroeconomic costs of CRD IV

15.53 Unlike the benefits, the costs of CRD IV, in terms of the impact of UK GDP, are largely linear and therefore additive. The breakdown of the cost estimates should be treated with great caution as they represent the net-present value of the reduction in GDP over the long run and are influenced by the assumptions made in this analysis.

15.54 We estimate the macroeconomic costs of CRD IV using outputs from the National Institute global economic model (NiGEM) of the world economy.(1) In this approach, the estimates are derived from long-run simulations that take account of the calculations of the change in capital ratios shown in **Table 15.B** aggregated for the UK economy over the full CRD IV implementation period. As the capital ratio calculations (derived from the same analysis used in **Table 15.B**) are undertaken for all tiers of capital, a single, quality adjusted series for the aggregate capital ratio that takes into account changes in both the quality and quantity of capital held can be calculated and used in the NiGEM model.

15.55 The NiGEM model has also been extensively modified to include a banking sector that reflects directly the impacts of prudential policy on aggregate lending margins in the economy. The intuition is that as deposit-takers are required to raise their capital ratios, they recover the costs they incur by increasing the spread between lending and deposit rates. The recovery of costs, however, is different over time and across sectors:

- It is more costly to adjust capital ratios in the short term than over the longer term as firms find it difficult to raise additional capital in markets at short notice, or require time to accumulate profits that could be retained to boost capital organically.

- It is more efficient to sell off, or slow the accumulation of, higher-risk assets as this reduces measured risk-weighted assets to a greater extent than lower risk assets.

15.56 As capital ratios rise initially, the model increases the spread between lending and deposit rates for higher risk (corporate) lending to a greater extent than lower risk (secured household) lending in the short term. Over time, this spread then narrows such that the increase is equalised across both high and low risk sectors. The model takes into account movements in debt and equity prices resulting from lower balance sheet risk to the extent that these prices have moved with balance sheet risk in the past economic cycle. Chapters 4 and 6 of *FSA Occasional Paper No. 42* contain a more detailed discussion of the empirical connection between capital ratios and bank margins and the general modelling approach.

Uncertainty of the estimates

15.57 As with all modelling approaches, there is a large degree of uncertainty around the estimates of costs and benefits of CRD IV. Two large sources of uncertainty arise from (a) the parameters of the models themselves, and (b) the estimates used as inputs into the model.

Model uncertainty

15.58 The NiGEM model contains a large number of equations which seek to represent the UK (and global) macroeconomic environment. Each of these equations is subject to statistical error, which are used to generate confidence intervals around the estimates of the net benefits using a stochastic simulation approach.

15.59 **Table 15.E** shows the confidence intervals around our central estimates of net benefits. Chapter 7 of *FSA Occasional Paper No. 42* contains a more detailed discussion of the approach to estimating the confidence intervals.

Table 15.E Confidence intervals around net benefits

	£ billions per annum[a]	
Interval	Lower	Upper
80% confidence	2	18
90% confidence	0	21
95% confidence	-2	23

(a) Annualised net present value of the chained-volume measure (2012) of GDP.

Data uncertainty

15.60 The analysis relies on quantitative impact study (QIS) data provided by firms. Estimates of the impact of CRD IV on firms' current balance sheets, used as inputs in the analysis, are made on a 'best efforts' basis. There is considerable uncertainty around these estimates, and it is possible that the impact of CRD IV on aggregate capital ratios has been underestimated.

15.61 In addition, supervisory assessments under the new regime will differ from previous judgements, reflecting the new approach and changing economic conditions. Judgements will be made on a firm by firm basis based on the individual risks taken at the time. To the extent that supervisors have made these judgements in the past, they are reflected in firms existing Pillar 2 requirements. However, it should be noted that such supervisory judgements cannot be pre-empted in the analysis so no further assumptions are made on whether Pillar 2 capital requirements will be higher or lower in the future.

(1) See FSA *Occasional Paper No. 38* for a description of the NiGEM model.

Table 15.F Impact of higher capital ratios[a]

Incremental change in:	
Firms' capital resources[b] (percentage point)	Net benefits (GDP,[c] £ billions per annum)
1	8¾
2	9
3	9¼
4	9¼
5	9¼

(a) Estimates are subject to the same degree of uncertainty as set out in **Table 15.E**.
(b) Capital ratio defined in terms of CRD IV capital and CVA definitions.
(c) The net present value of the change in the annual, chained-volume measure of GDP.

Table 15.G Median compliance costs per firm

	(£ millions)		
Type of firm	Small[a]	Medium[b]	Large[c]
Method 1: Sum of median one-off and ongoing costs			
Banks	0.4	2.6	9.0
Building societies[d]	0.2	0.8	9.0
Investment firms	0.5	0.8	2.7
of which:			
Full-scope firms	*0.1*	*0.6*	*2.2*
Limited license firms	*0.1*	*0.1*	*0.4*
Limited activity firms	*0.3*	*0.1*	*0.1*
Method 2: Medians of total costs			
Banks	0.6	8.5	14.0
Building societies[d]	0.2	0.8	14.0
Investment firms	1.0	1.3	2.7
of which:			
Full-scope firms	*0.4*	*0.9*	*2.2*
Limited license firms	*0.3*	*0.3*	*0.4*
Limited activity firms	*0.3*	*0.1*	*0.1*

(a) Defined as firms with total assets, or assets under management (asset management firms only), of less than £100 million.
(b) Defined as firms with total assets, or assets under management (asset management firms only), of between £100 million and £1 billion.
(c) Defined as firms with total assets, or assets under management (asset management firms only), of more than £1 billion.
(d) We received no survey responses for large building societies. The estimate for large building societies is based on bank responses.

Annex: Compliance costs of reporting and disclosure requirements

15.62 This annex discusses the compliance costs associated with the reporting requirements discussed in Chapter 13. Although the provisions of COREP and FINREP will be implemented via the CRR, the compliance costs are expected to be significant. Estimates of the overall compliance costs have been included to understand the possible scale of these costs better. That said, these costs are not expected to be large enough to have a macroeconomic impact but have been included here for completeness.

15.63 To estimate incremental compliance costs, we sent a survey to all relevant BIPRU banks, building societies and investment firms. The survey asked firms to provide a 'best efforts' estimate of the costs, both one-off and ongoing, they expect to incur in preparing for, compiling data under and reporting information according to the new rules. Approximately 270 (or 13%) of all firms completed the survey: 31 (or 18%) of all banks, 8 (or 16%) of all building societies, and 231 (or 13%) of all investment firms.(1)

15.64 Survey results of incremental, one-off and ongoing compliance costs per firm (based on estimates computed in two different ways to deal with outliers)(2) are reported in **Table 15.G**.

15.65 Total staffing and internal information technology (IT) costs are expected to comprise the majority of costs at mid-size and large banks, while small banks and building societies believed costs to be heaviest for external consulting and IT-related services related to new data capture data verification processes.

15.66 Extrapolating these costs to the entire set of affected BIPRU firms (roughly 2,200) and across firm types and size classes revealed total compliance costs ranging between £1.7 billion (based on the sum of extrapolated median costs of one-off and ongoing compliance costs, see **Table 15.H**) and £3.1 billion (based on extrapolation of median total compliance costs, see **Table 15.I**), with over 70% falling in the banking sector.

(1) The vast majority of the investment firms that responded to the survey were those for which the Financial Conduct Authority is prudentially responsible.
(2) To deal with outliers we computed cost estimates using two methods. Under Method 1, we estimated per firm costs as the sum of the sum of the medians of one-off and ongoing costs, while under Method 2, we used the median of total costs.

Table 15.H Extrapolation based on sum of medians of one-off and ongoing compliance costs[a]

Type of firm	Small[b]	Medium[c] (£ millions)	Large[d]	Total
One-off costs				
Banks	1.9	112	485	599
Building societies[e]	0.1	6.6	80	87
Investment firms	19.2	8.2	9.9	38
of which:				
Full-scope firms	*3.1*	*6.9*	*9.1*	*19*
Limited license firms	*15*	*0.9*	*0.6*	*17*
Limited activity firms	*1.1*	*0.4*	*0.2*	*1.7*
Ongoing costs				
Banks	5.1	92	507	604
Building societies[e]	0.6	18	84	103
Investment firms	157	30	61	249
of which:				
Full-scope firms	*9.5*	*18*	*53*	*81*
Limited license firms	*119*	*12*	*7.8*	*139*
Limited activity firms	*28*	*0.4*	*0.2*	*29*
Total costs				
Banks	7.0	204	992	1,202
Building societies[e]	0.7	25	164	189
Investment firms				
of which:				
Full-scope firms	*13*	*25*	*62*	*100*
Limited license firms	*134*	*13*	*8.4*	*156*
Limited activity firms	*29*	*0.8*	*0.4*	*31*
Total costs	184	267	1,226	1,677

(a) Estimates derived using Method 1 from **Table 15.G**.
(b) Defined as firms with total assets, or assets under management (asset management firms only), of less than £100 million.
(c) Defined as firms with total assets, or assets under management (asset management firms only), of between £100 million and £1 billion.
(d) Defined as firms with total assets, or assets under management (asset management firms only), of more than £1 billion.
(e) We received no survey responses for large building societies; consequently, the median estimate for this size class of firm is based on large bank responses.

Table 15.I Extrapolation based median total compliance costs[a]

Type of firm	Small[b]	Medium[c] (£ millions)	Large[d]	Total
Banks	9.5	665	1,530	2,195
Building societies[e]	0.7	25	252	278
Investment firms				
of which:				
Full-scope firms	*59*	*43*	*58*	*160*
Limited license firms	*37*	*2*	*0.4*	*40*
Limited activity firms	*397*	*32*	*8.2*	*438*
Total costs	504	767	1,849	3,111

(a) Estimates derived using Method 2 from **Table 15.G**.
(b) Defined as firms with total assets, or assets under management (asset management firms only), of less than £100 million.
(c) Defined as firms with total assets, or assets under management (asset management firms only), of between £100 million and £1 billion.
(d) Defined as firms with total assets, or assets under management (asset management firms only), of more than £1 billion.
(e) We received no survey responses for large building societies; consequently, the median estimate for this size class of firm is based on large bank responses.

Table 15.J Detail of policy calibrations used for estimation of costs and benefits of prudential policy measures

Measure	Calibration/description	Implementation date
Existing responses to financial crisis		
FSA's enhanced prudential regime and capital planning buffers	– Minimum core capital ratio of 4% under stressed conditions, Tier 1 capital ratio of 8%, total capital ratio of 10%.	December 2008
	– Changes to the definition of regulatory core Tier 1 capital (most notably the deduction of intangible assets from the definition) from the Basel II definition.	May 2009
	– Firms are assumed, by the end of the implementation period, to meet the higher of their capital planning buffers or their average, pre-crisis capital surplus.	
	– Minimum ratios and changes to definitions of capital assumed to become permanent.	
European Capital Requirements directive (CRD) changes to the treatment of banks' trading book and resecuritisation exposures	Firms required to: – calculate additional market risk capital requirements for interest rate and equity positions in their trading books and all commodity and foreign exchange positions; – apply more capital to resecuritisation positions to reflect the higher risk of 'unexpected impairment losses' (see FSA (2009) and FSA (2011)). The size of the impact was calculated using data from an FSA QIS exercise.	January 2012
CRD IV response to the financial crisis		
(a) Expected to have a macroeconomic impact		
Changes to the definition of capital	Changes to: definitions of CET1 capital (including all deductions from CET1); eligibility criteria of AT1 and T2 instruments. Instruments that become ineligible under the new definitions are assumed to be replaced at each capital tier through the implementation period with higher-quality eligible instruments. For significant investments, data is available for the holdings above 10% of a firm's CET1. Where applicable, we assume a risk-weight of 400% to calculate the appropriate RWA treatment over the transition period. In such cases the total deduction is made 50% from CET1 and 50% is risk-weighted from January 2015, with the composition changing annually to 100% from CET1 and 0% in RWAs by January 2019 in a linear fashion. The size of the impacts is calculated using FSA QIS data from December 2012.	Phased implementation from 2014 to 2019
Changes to risk coverage	Revised metrics to calculate: – credit risk: credit valuation adjustments is expected to raise capital requirements materially; – market risk: no major changes expected; and – operational risk: no major changes expected. The size of the impacts is calculated using FSA QIS data from December 2012.	January 2014 (most proposals)
Change in the minimum capital ratios under Basel III	Minimum CET 1 ratio of 4.5%, Tier 1 capital ratio of 6%, total capital ratio of 8%. The definition of these ratios reflects the CRD IV changes to the definition of capital and risk coverage.	January 2015
CRD buffers comprising:	Regulatory buffers are treated as a new minimum by firms. Market pressure is expected to push firms to hold sufficient resources to prevent them from breaching buffers over the cycle.	
Capital conservation buffer	The capital conservation buffer is 2½ percentage points for all firms.	
Countercyclical buffer	The size of the countercyclical buffer (CCyB) is assumed to be ½ percentage point on average over the cycle. The average, over-the-cycle estimate of the CCyB reflects (a) the expectation that the buffer will be at zero through most of the cycle and increasing to the maximum 2½ percentage points only at the peak of the credit cycle; and (b) the cycle is beginning at a very weak point following the financial crisis.	January 2014 (representing an over-the-cycle average beginning immediately)
Pillar 2	Pillar 2 requirements may have some impact on firms' capital requirements. The changes will differ from firm to firm and will depend on the supervisory judgements. We assume that the aggregate level of the new capital requirement remains unchanged from existing Pillar 2 Individual Capital Guidance (ICG). We assume that Pillar 2 requirements, which were met with a mix of capital proportionate to the capital tiers held in total, will now be met entirely by CET1 capital.	Phased implementation from 2014 to 2016
Shrinkage of banks' voluntary capital surplus	Banks' capital surplus over their overall capital requirements (including CRD buffers) is expected to shrink from pre-crisis levels as (a) banks reduce risk levels as the capital ratios rise which reduces volatility; and (b) the introduction of regulatory buffers reduces the need for voluntary buffers. Banks' voluntary capital surplus is assumed to fall by 50% from December 2012 levels.	Phased in between 2016 and 2019
(b) Not expected to have a macroeconomic impact or cannot be estimated		
Group consolidation provisions & Large exposures	There are a number of changes to the treatment of Groups and large exposure requirements. These changes may result in some changes to individual firms' requirements. The expectation is that CRD IV is not materially different from existing practice so a disproportionate effort would be needed by policymakers to estimate a firm by firm impact.	
Liquidity measures	There are no changes to requirements for holding liquid assets at this time. The current ILG regime will be retained until changes are made in a future consultation. We assume that firms do not change their current liquidity ratios from existing ILG requirements going forward.	–
Governance and remuneration	Some impact from higher fixed remuneration at firms. Assume changes don't affect net interest margins.	–
Reporting and disclosure	Compliance with COREP/FINREP is expected to add to firms' overall operational costs. We expect firms to attempt to recover these costs from customers.	

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Appendix 1

PRA RULEBOOK CRR FIRMS: – CAPITAL BUFFERS INSTRUMENT 2013

Powers exercised

A. The Prudential Regulation Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137G (The PRA's general rules); and
(2) section 137T (General supplementary powers).

B. The rule-making powers referred to above are specified for the purpose of section 138G (Rule-making instrument) of the Act.

Pre-conditions to making

C. In accordance with section 138J of the Act (consultation with the Financial Conduct Authority) ("FCA"), the PRA consulted the FCA. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

PRA Rulebook CRR Firms: Capital Buffers Instrument 2013

D. The PRA makes the rules in Annex A to this Instrument.

Commencement

E. The following rules in Annex A of this instrument come into force on 1 January 2014: Rules [1.1 to 1.3, [3.2], [3.3], 4.1 to 4.5, 5.1 to 5.6].

F. The following rules in Annex A of this instrument come into force on 1 January 2016: Rules [2.1; 2.2, 3.1].

Citation

G. This instrument may be cited as the PRA Rulebook CRR Firms: Capital Buffers Instrument 2013.

By order of the Board of the Prudential Regulation Authority
[DATE]

Annex A

In this Annex, the text is all new and is not underlined.

Part

CAPITAL BUFFERS

Chapter content

Links

1 APPLICATION AND DEFINITIONS

1.1 This Part applies to every *firm* that is a *CRR firm*.

1.2 In this Part the following definitions shall apply:

capital conservation buffer

means the amount of *common equity tier 1 capital* a *firm* must calculate in accordance with Chapter [2].

combined buffer

means the sum of

(a) the *capital conservation buffer*; and

(b) the *countercyclical capital buffer*.

countercyclical buffer rate

means (in accordance with point (7) of Article 128(1) of the *CRD*) the rate:

(a) expressed as a percentage of *total risk exposure amount* set by the [Bank/FPC] or an *EEA countercyclical buffer authority*; or

(b) expressed in terms equivalent to a percentage of total risk exposure amount set by a *third country countercyclical buffer authority;*

that a *firm* must apply in order to calculate its *countercyclical capital buffer.*

countercyclical capital buffer

means the amount of *common equity tier 1 capital* a *firm* must calculate in accordance with Chapter [3].

distribution in connection with common equity tier 1 capital

includes (in accordance with Article 141(10) of the *CRD*):

(a) a payment of cash dividends;

(b) a distribution of fully or partly paid bonus shares or other capital instruments referred to in Article 26(1)(a) of the *CRR*;

(c) a redemption or purchase by an institution of its own shares or other capital instruments referred to in Article 26(1)(a) of the *CRR*;

(d) a repayment of amounts paid up in connection with capital instruments referred to in Article 26(1)(a) of the *CRR*; and

(e) a distribution of items referred to in points (b) to (e) of article 26(1) of the *CRR*

EEA countercyclical buffer authority

means the authority of an *EEA State* other than the *UK* designated for the purpose of Article 136 of the *CRD* with responsibility for setting the *countercyclical buffer rate* for that *EEA State*.

MDA

means maximum distributable amount calculated in accordance with [4.3(4)]

parent financial holding company in a Member State

means (in accordance with point (26) of Article 1(1) of the *CRD*) a *financial holding company* which is not itself a *subsidiary* of an *institution* authorised in the same *EEA State*, or of a *financial holding company* or *mixed financial holding company* set up in the same *EEA State*.

parent institution in a Member State

means (in accordance with point (24) of Article 1(1) of the *CRD*) an *institution* authorised in an *EEA State* which has an *institution* or *financial institution* as *subsidiary* or which holds a *participation* in such an *institution* or *financial institution*, and which is not itself a *subsidiary* of another *institution* authorised in the same *EEA State* or of a *financial holding company* or *mixed financial holding company* set up in the same *EEA State*.

parent mixed financial holding company in a Member State

means (in accordance with point (28) of Article 1(1) of the *CRD*) a *mixed financial holding company* which is not itself a *subsidiary* of an *institution* authorised in the same *EEA State*, or of a *financial holding company* or *mixed financial holding company* set up in the same *EEA State*.

relevant credit exposures

means (in accordance with Article 140(4) of the *CRD)* exposures other than those referred to in points (a) to (f) of article 112 of the *CRR* that are subject to:

(a) the *own funds* requirements for credit risk under Part Three, Title II of the *CRR*; or

(b) where the exposure is held in the *trading book*, *own funds* requirements for specific risk under Part Three, Title IV, Chapter 2 of the *CRR* or incremental default and migration risk under Part Three, Title IV, Chapter 5 of the *CRR;* or

(c) where the exposure is a *securitisation*, the *own funds* requirements under Part Three, Title II, Chapter 5 of the *CRR*.

third country countercyclical buffer authority

means the authority of a *third country* empowered by law or regulation with responsibility for setting the *countercyclical buffer rate* for that *third country.*

total risk exposure amount

means the total risk exposure amount of a *firm* calculated in accordance with Article 92(3) of the *CRR*.

1.3 Unless otherwise defined, any italicised expression used in this Part and in the *CRR* has the same meaning as in the *CRR*.

2 CAPITAL CONSERVATION BUFFER

2.1 A *firm* must calculate a *capital conservation buffer* of *common equity tier 1 capital* equal to 2.5% of its *total risk exposure amount*.

[**Note: Art 129(1) (part) of the *CRD***]

2.2 This rule modifies [2.1] for a transitional period between 1 January 2016 and 31 December 2018:

(1) from 1 January 2016 until 31 December 2016 for 2.5% there is substituted 0.625%;

(2) from 1 January 2017 until 31 December 2017 for 2.5% there is substituted 1.25%; and

(3) from 1 January 2018 until 31 December 2018 for 2.5% there is substituted 1.875%.

[**Note: Art 160 (part) of the *CRD***]

3 COUNTERCYCLICAL CAPITAL BUFFER

Calculation of the countercyclical capital buffer

3.1 (1) A *firm* must calculate a *countercyclical capital buffer* of *common equity tier 1 capital* equal to its *total risk exposure amount* multiplied by the weighted average of the *countercyclical buffer rates* that apply to exposures in the jurisdictions where the *firm's relevant credit exposures* are located.

[**Note: Art 130(1) (part**) **of the *CRD***]

(2) In order to calculate the weighted average referred to in (1), a *firm* must apply to each applicable *countercyclical buffer rate* its total *own funds* requirements for credit risk, specific risk, incremental default and migration risk that relates to *the relevant credit exposures* in the jurisdiction in question, divided by its total *own funds* requirements for credit risk, specific risk, incremental default and migration risk that relates to all of its *relevant credit exposures.*

(3) For the purposes of (2), a *firm* must calculate its total *own funds* requirement for credit risk, specific risk, incremental default and migration risk in accordance with Part Three, Titles II and IV of the *CRR.*

(4) The *countercyclical buffer rate* for an exposure located in the *UK* is the rate set by the [Bank/FPC] for the *UK*.

(5) The *countercyclical buffer rate* for an *exposure* located in an *EEA State* other than the *UK* is:

(a) the rate set by the *EEA countercyclical buffer authority* for that jurisdiction; or

(b) if that rate exceeds 2.5% and has not been recognised by the [Bank/FPC], 2.5%.

(6) The *countercyclical buffer rate* for an *exposure* located in a *third country* is the rate set by the [Bank/FPC] for that jurisdiction.

(7) If the [Bank/FPC] has not set a rate for a *third country*, *the countercyclical buffer rate* for an *exposure* located in that jurisdiction is:

(a) the rate set by the *third country countercyclical buffer authority* for that jurisdiction; or

(b) if that rate exceeds 2.5% and has not been recognised by the [Bank/FPC], 2.5%.

(8) If the [Bank/FPC] has not set a rate for a *third country* and either there is no *third country countercyclical buffer authorit*y for that country or the authority has not set a rate for that jurisdiction, *the countercyclical buffer rate* for an *exposure* located in that jurisdiction is zero.

(9) If the rate for the *UK* is increased, that increase takes effect from the date specified by the [Bank/FPC].

(10) If the rate for an *EEA State* other than the *UK* is increased, subject to (5)(b) that increase takes effect from:

(a) the date specified by the *EEA countercyclical buffer authority* for that jurisdiction, if the rate applied under this Chapter does not exceed 2.5%;

(b) the date specified by the [Bank/FPC] if the rate applied under this Chapter exceeds 2.5%.

(11) If the rate for a *third country* is increased by the [Bank/FPC], that increase takes effect from the date specified by the [Bank/FPC].

(12) If the [Bank/FPC] does not set a rate for a *third country* and the rate for that *third country* is increased by the *third country countercyclical buffer authority* for that jurisdiction, subject to (7)(b) that increase takes effect from:

(a) the date 12 months after the date on which the increase was published by the *third country countercyclical buffer authority* in accordance with the relevant law the *third country*, if the rate applied under this Chapter does not exceed 2.5%;

(b) the date specified by the [Bank/FPC] if the rate applied under this Chapter exceeds 2.5%.

(13) If a rate is reduced, that reduction takes effect immediately.

[**Note: Art 140 (part) of the *CRD***]

3.2 A *firm* must identify the geographical location of a *relevant credit exposure* in accordance with Commission Regulation (EU) […/…insert reference to regulatory technical standards adopted in accordance with article 140(7) of the *CRD*.][1]

[**Note: Art 140(5) of the *CRD***]

3.3 This rule applies until 31 December 2015

[1] This rule will not be made until the Commission has adopted regulatory technical standards in accordance with article 140(7) of the CRD.

(1) A *firm* must calculate a *countercyclical capital buffer* of *common equity tier 1 capital* equal to its *total risk exposure amount* multiplied by the weighted average of the *countercyclical buffer rates* that apply in the jurisdictions where the *firm's relevant credit exposures* are located.

(2) In order to calculate the weighted average referred to in (1), a *firm* must apply to each applicable *countercyclical buffer rate* its total *own funds* requirements for credit risk, specific risk, incremental default and migration risk that relates to *the relevant credit exposures* in the jurisdiction in question, divided by its total *own funds* requirements for credit risk that relates to all of its *relevant credit exposures.*

(3) For the purposes of (2), *firm* must calculate its total *own funds* requirement for credit risk, specific risk, incremental default and migration risk in accordance with Part Three, Titles II and IV of the *CRR.*

(4) The *countercyclical buffer rate* for an *exposure* is the rate set by the Bank/FPC for the jurisdiction in which that *exposure* is located.

(5) If the [Bank/FPC] does not set a rate for the jurisdiction in which an exposure is located, the *countercyclical buffer rate* for that *exposure* is zero.

(6) If the rate for a jurisdiction is increased by the [Bank/FPC], that increase takes effect from the date specified by the [Bank/FPC].

(7) If a rate is reduced, that reduction takes effect immediately.

4 CAPITAL CONSERVATION MEASURES

Combined buffer

4.1 A *firm* does not meet the *combined buffer* if the *common equity tier 1 capital* maintained by the *firm* which is not used to meet the *own funds* requirement under Article 92(1)(c) of the *CRR* does not meet the *combined buffer*.

[**Note: Art 129(1) (part) and 130(5) (part) of the *CRD***]

Restrictions on distributions

4.2 A *firm* that meets the *combined buffer* must not make a *distribution in connection with common equity tier 1 capital* to an extent that would decrease its *common equity tier 1 capital* to a level where the *combined buffer* is no longer met.

[**Note: Art 141(1) of the *CRD***]

4.3 (1) A *firm* that does not meet the *combined buffer* must:

(a) calculate the *MDA* in accordance with (4); and

(b) report the *MDA* to the *PRA* in writing no later than 5 working days after the *firm* identified that it did not meet the *combined buffer*.

(2) A *firm* that does not meet the *combined buffer* must not undertake any of the following actions before it has calculated the *MDA*:

(a) make a *distribution in connection with common equity tier 1 capital*;

(b) create an obligation to pay variable remuneration or *discretionary pension benefits* or pay variable remuneration or *discretionary pension benefits* if the obligation to pay was created at a time when the *firm* did not meet the *combined buffer*; and

(c) make payments on *additional tier 1 instruments.*

(3) If a *firm* does not meet the *combined buffer*, it must not distribute more than the *MDA* calculated in accordance with (4) through any action referred to in points (a) to (c) of (2).

(4) A *firm* must calculate the *MDA* by multiplying the sum calculated in accordance with (5) by the factor determined in accordance with (6). Any of the actions referred to in point (a), (b) or (c) of (2) shall have the effect of reducing the *MDA.*

(5) The sum to be multiplied in accordance with (4) shall consist of:

(a) interim profits not included in *common equity tier 1 capital* pursuant to Article 26(2) of the *CRR* that have been generated since the most recent decision on the distribution of profits or any of the actions referred to in points (a), (b) or (c) of (2);

plus

(b) year-end profits not included in *common equity tier 1 capital* pursuant to Article 26(2) of the *CRR* that have been generated since the most recent decision on the distribution of profits or any of the actions referred to in points (a), (b) or (c) of (2);

minus

(c) amounts which would be payable by tax if the items specified in points (a) and (b) were to be retained.

(6) The factor referred to in (4) shall be determined as follows:

(a) if the *common equity tier 1 capital* maintained by the *firm* which is not used to meet the *own funds* requirement under Article 92(1)(c) of the *CRR* expressed as a percentage of the *firm's total risk exposure amount*, is within the first (that is, the lowest) quartile of the *combined buffer*, the factor shall be 0;

(b) if the *common equity tier 1 capital* maintained by the *firm* which is not used to meet the *own funds* requirement under Article 92(1)(c) of the *CRR*, expressed as a percentage of the *firm's total risk exposure amount*, is within the second quartile of the *combined buffer*, the factor shall be 0.2;

(c) if the *common equity tier 1 capital* maintained by the *firm* which is not used to meet the *own funds* requirement under Article 92(1)(c) of the *CRR* expressed as a percentage of the *firm's total risk exposure amount* is within the third quartile of the *combined buffer*, the factor shall be 0.4; and

(d) if the *common equity tier 1 capital* maintained by the *firm* which is not used to meet the *own funds* requirement under Article 92(1)(c) of the *CRR* expressed as a percentage of the *firm's total risk exposure amount*, is within the fourth (that is, the highest) quartile of the *combined buffer*, the factor shall be 0.6.

(7) A *firm* must calculate the lower and upper bounds of each quartile of the *combined buffer* as follows:

$$= \frac{\text{Combined buffer}}{4} \times (Q_n - 1)$$

Lower bound of quartile

$$= \frac{\text{Combined buffer}}{4} \times Q_n$$

Upper bound of quartile
"Qn" indicates the ordinal number of the quartile concerned***.***

(8) The restrictions imposed by this rule only apply to payments that result in a reduction of *common equity tier 1 capital* or in a reduction of profits, and where a suspension of payment or failure to pay does not constitute an event of default or a condition for the commencement of proceedings for an order for the appointment of a liquidator or administrator of the *firm*.

(9) If a *firm* does not meet the *combined buffer* and intends to distribute any of its distributable profits or undertake an action referred to in points (a), (b) and (c) of (2) it must give the *PRA* notice of its intention at least one month before the intended date of distribution or action unless there are exceptional circumstances which make it impracticable to give such a period of notice in which event the firm must give as much notice as is practicable in those circumstances. When giving notice a *firm* must provide the following information:

(a) the amount of *own funds* maintained by the *firm*, subdivided as follows:

(i) *common equity tier 1 capital*;

(ii) *additional tier 1 capital*; and

(iii) *tier 2 capital*.

(b) the amount of its interim and year-end profits;

(c) the *MDA* calculated in accordance with (4);

(d) the amount of distributable profits it intends to allocate between the following:

(i) dividend payments;

(ii) share buybacks;

(iii) payments on *additional tier 1 instruments*; and

(iv) the payment of variable remuneration or discretionary pension benefits, whether by creation of a new obligation to pay, or payment pursuant to an obligation to pay created at a time when the *firm* did not meet its *combined buffer*.

[**Note: Art 141(2) to 141(10) of the *CRD***]

Capital conservation plan

4.4 When a *firm* does not meet the *combined buffer*, it must prepare a capital conservation plan and submit it to the *PRA* no later than 5 working days after the *firm* identified that it did not meet the *combined buffer*.

[**Note: Art 142(1) of the *CRD***]

4.5 The capital conservation plan must include the following:

(1) the *MDA*;

(2) estimates of income and expenditure and a forecast balance sheet;

(3) measures to increase the capital ratios of the *firm*; and

(4) a plan and timeframe for the increase of *own funds* with the objective of meeting the *combined buffer*.

[**Note: Art 142(2) of the *CRD***]

5 APPLICATION ON AN INDIVIDUAL AND CONSOLIDATED BASIS

Application on an individual basis

5.1 This Part applies to a *firm* on an individual basis whether or not it also applies to the *firm* on a *consolidated basis* or *sub-consolidated basis*.

Application on a consolidated basis

5.2 A *firm* which is a *parent institution in a Member State* must comply with this Part on the basis of its *consolidated situation*.

5.3 A *UK bank* or *building society* controlled by a *parent financial holding company in a Member State* or a *parent mixed financial holding company in a Member State* must comply with this Part on the basis of the *consolidated situation* of that holding company, if the *PRA* is responsible for supervision of the *UK bank* or *building society* on a *consolidated basis* under [Art. 111 of CRD4][2].

5.4 A *UK designated investment firm* controlled by a *parent financial holding company in a Member State* or a *parent mixed financial holding company in a Member State* must comply with this Part on the basis of the *consolidated situation* of that holding company, if:

(1) there is no *subsidiary* of the holding company which is a *credit institution*; and

(2) the *PRA* is responsible for the supervision of the *UK designated investment firm* on a *consolidated basis* under [Article 111 of CRD4]. [3]

Sub-consolidation in cases of entities in third countries

5.5 A *firm* that is a *subsidiary* must apply this Part on a *sub-consolidated basis* if the *firm*, or the *parent undertaking* where it is a *financial holding company* or *mixed financial holding company,* have an *institution* or *financial institution* as a *subsidiary* in a *third country* or hold a *participation* in such an *institution* or *financial institution*.

Extent and manner of prudential consolidation

5.6 If this Part applies to a *firm* on a *consolidated basis* or on a *sub-consolidated basis*, the *firm* must carry out consolidation to the extent and in the manner prescribed in Articles [18(1), 18(8), 19(1), 19(3), 23 and 24(1) of the *CRR* and [CR firms/Groups/2.1-2.3].

[**Note: Art 129(1) (part) and 130(1) (part) of the *CRD***]

[2] Replace with reference to regulation or rule transposing Art 111 into UK law.
[3] Replace with reference to regulation or rule transposing Art 111 into UK law.

PRA RULEBOOK CRR FIRMS: INTERNAL CAPITAL ADEQUACY ASSESSMENT INSTRUMENT 2013

Powers exercised

A. The Prudential Regulation Authority (the "PRA") makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137G (The PRA's general rules); and
(2) section 137T (General supplementary powers)

B. The rule-making powers listed above are specified for the purpose of section 138G(2) (Rule-making instruments) of the Act.

Pre-conditions to making

C. In accordance with section 138J of the Act (Consultation by the PRA), the PRA consulted the Financial Conduct Authority. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

PRA Rulebook CRR Firms: Internal Capital Adequacy Assessment Instrument 2013

D. The PRA makes the rules in Annex A to this instrument.

Commencement

E. This instrument comes into force on 1 January 2014.

Citation

F. This instrument may be cited as the PRA Rulebook CRR Firms: Internal Capital Adequacy Assessment Instrument 2013.

By order of the Board of the Prudential Regulation Authority
[Date]

Annex A

In this Annex, the text is all new and is not underlined.

Part

INTERNAL CAPITAL ADEQUACY ASSESSMENT

Chapter content

Links

1 APPLICATION AND DEFINITIONS

1.1 This Part applies to every *firm* that is a *CRR firm*.

1.2 In this Part the following definitions shall apply:

Article 12(1) relationship

means a relationship where undertakings are linked by a relationship within the meaning of Article 12(1) Directive 83/349/EEC.

business risk

means any risk to a *firm* arising from:

(1) changes in its business, including:

(a) the acute risk to earnings posed by falling or volatile income; and

(b) the broader risk of a *firm's* business model or strategy proving inappropriate due to macroeconomic, geopolitical, industry, regulatory or other factors; or

(2) its remuneration policy.

consolidation group

means the undertakings included in the scope of consolidation pursuant to Articles 18(1), 18(8), 19(1), 19(3) and 23 of the CRR and [CR firms/Groups /2.1- 2.3]

central counterparty

has the meaning given in point (1) of Article 2 of Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC Derivatives, central counterparties and trade repositories.

financial conglomerate

has the meaning given in point (14) of Article 2 of Directive 2002/87/EC on the supplementary supervision of credit institutions, insurance undertakings and investment firms in a financial conglomerate

group

means in relation to a *person* ("A"), A and any *person*:

(a) who has relationship with A of the kind specified in s. 421 of FSMA 2000;

(b) who is a member of the same *financial conglomerate* as A;

(c) who has a *Article 12(1)* relationship with A;

(d) who has a *Article 12(1)* relationship with any *person* who falls into (a);

(e) who is a *subsidiary* of a person in (c) or (d) ;

(f) who is member of the same *consolidation group* as A; or

(g) whose omission from an assessment of the risks to A of A's connection to any person coming within (a)-(f) or an assessment of the financial resources available to such persons would be misleading.

group risk

means the risk that the financial position of a *firm* may be adversely affected by its relationships (financial or non-financial) with other entities in the same *group* or by risk which may affect the financial position of the whole *group*, including reputational contagion.

ICAAP rules

means the rules in Chapter 3 (Strategies, processes, and systems), Chapter 12 (Stress test and scenario analysis) and Chapter 13 (Documentation of risk assessments).

liquidity risk

means the risk that a *firm* although solvent, either does not have available sufficient financial resources to enable it to meet its obligations as they fall due, or can secure such resources only at excessive cost.

market risk

means the risk that arises from fluctuations in values of or income from assets or in interest or exchange rates.

parent financial holding company in a Member State

means (in accordance with point (26) of Article 1(1) of the *CRD*) a *financial holding company* which is not itself a *subsidiary* of an *institution* authorised in the same *EEA State*, or of a *financial holding company* or *mixed financial holding company* set up in the same *EEA State*.

parent institution in a Member State

means (in accordance with point (24) of Article 1(1) of the *CRD*) an *institution* authorised in an *EEA State* which has an *institution* or *financial institution* as *subsidiary* or which holds a *participation* in such an *institution* or *financial institution*, and which is not itself a *subsidiary* of another *institution* authorised in the same *EEA State* or of a *financial holding company* or *mixed financial holding company* set up in the same *EEA State*.

parent mixed financial holding company in a Member State

means (in accordance with point (28) of Article 1(1) of the *CRD*) a *mixed financial holding company* which is not itself a *subsidiary* of an *institution* authorised in the same *EEA State*, or of a *financial holding company* or *mixed financial holding company* set up in the same *EEA State*.

pension obligation risk

means:

(1) the risk to a *firm* caused by its contractual or other liabilities to or with respect to a pension scheme (whether established for its employees or those of a related company or otherwise); or

(2) the risk that the *firm* will make payments or other contributions to or with respect to a pension scheme because of a moral obligation or because the *firm* considers that it needs to do so for some other reason.

residual risk

means the risk that credit risk mitigation techniques used by the *firm* prove less effective than expected.

risk control rules

means the rules in Chapter 4 to Chapter 11 of this Part.

1.3 Unless otherwise defined, any italicised expression used in this Part and in the *CRR* has the same meaning as in the *CRR*.

2 ADEQUACY OF FINANCIAL RESOURCES

Overall financial adequacy rule

2.1 A *firm* must at all times maintain overall financial resources, including *own funds* and liquidity resources, which are adequate both as to amount and quality, to ensure there is no significant risk that its liabilities cannot be met as they fall due.

3 STRATEGIES, PROCESSES AND SYSTEMS

Overall Pillar 2 rule

3.1 A *firm* must have in place sound, effective and comprehensive strategies, processes and systems:

(1) to assess and maintain on an ongoing basis the amounts, types and distribution of financial resources, *own funds* and internal capital that it considers adequate to cover:

(a) the nature and level of the risks to which it is or might be exposed;

(b) the risk in the overall financial adequacy rule in 2.1; and

(c) the risk that the *firm* might not be able to meet the obligations in Part Three of the *CRR* in the future;

(2) that enable it to identify and manage the major sources of risk referred to in (1) including the major sources of risk in each of the following categories where they are relevant to the *firm* given the nature and scale of its business:

(a) credit and counterparty risk;

(b) *market risk;*

(c) *liquidity risk;*

(d) *liquidity risk;*

(e) concentration risk;

(f) *residual risk;*

(g) *securitisation* risk, including the risk that the *own funds* held by a *firm* in respect of assets which it has securitised are inadequate having regard to the economic substance of the transaction including the degree of risk transfer achieved;

(h) *business risk;*

(i) interest rate risk in the non-trading book;

(j) *risk of excessive leverage;*

(k) *pension obligation risk*; and

(l) *group risk*.

[Note: Art 73 (part) of the *CRD*]

3.2 As part of its obligations under the overall Pillar 2 rule in 3.1, a *firm* must identify separately the amount of *common equity tier one capital*, *additional tier one capital* and *tier two capital* and each category of capital (if any) that is not eligible to form part of its *own funds* which it considers adequate for the purposes described in the overall Pillar 2 rule.

3.3 The processes, strategies and systems required by the overall Pillar 2 rule in 3.1 must be comprehensive and proportionate to the nature, scale and complexity of the *firm's* activities.

3.4 A *firm* must:

(1) carry out regularly the assessments required by the overall Pillar 2 rule in 3.1; and

(2) carry out regularly assessments of the processes, strategies and systems required by the overall Pillar 2 rule in 3.1 to ensure they remain comprehensive and proportionate to the nature, scale and complexity of the *firm's* activities.

[Note: Art 73(part) of the *CRD*]

3.5 As part of its obligations under the overall Pillar 2 rule in 3.1, a *firm* must:

(1) make an assessment of the firm-wide impact of the risks identified in accordance with that rule, to which end a *firm* must aggregate the risks across its various business lines and units, taking appropriate account of any correlation between risks; and

(2) take into account the stress tests that the *firm* is required to carry out under the general stress test and scenario analysis rule in 12.1 and any stress tests that the *firm* is required to carry out under the *CRR*.

4 CREDIT AND COUNTERPARTY RISK

4.1 A *firm* must base credit-granting on sound and well-defined criteria and clearly establish the process for approving, amending, renewing and re-financing credits.

[Note: Art 79(a) of the *CRD*]

4.2 A *firm* must have internal methodologies that:

(1) enable it to assess the credit risk of exposures to individual obligors, securities or *securitisation positions* and credit risk at the portfolio level;

(2) do not rely solely or mechanistically on external credit ratings; and

(3) where its *own funds* requirements under Part Three of the *CRR* are based on a rating by an *ECAI* or based on the fact that an exposure is unrated, enable the *firm* to consider other relevant information for assessing its allocation of financial resources and internal capital.

[Note: Art 79(b) of the *CRD*]

4.3 A *firm* must operate through effective systems the ongoing administration and monitoring of its various credit risk-bearing portfolios and exposures, including for identifying and managing problem credits and for making adequate value adjustments and provisions.

[Note: Art 79(c) of the *CRD*]

4.4 A *firm* must adequately diversify credit portfolios given its target market and overall credit strategy.

[**Note Art 79(d) of the *CRD*]**

5 RESIDUAL RISK

5.1 A *firm* must address and control, by means which include written policies and procedures, the risk that recognised credit risk mitigation techniques used by it prove less effective than expected.

[**Note: Art 80 of the *CRD*]**

6 CONCENTRATION RISK

6.1 A *firm* must address and control, by means which include written policies and procedures, the concentration risk arising from:

(1) exposures to each counterparty including central counterparties, groups of connected counterparties and counterparties in the same economic sector, geographic region or from the same activity or commodity;

(2) the application of credit risk mitigation techniques; and

(3) risks associated with large indirect credit exposures such as a single collateral issuer.

[Note: Art 81 of *CRD*]

7 SECURITISATION RISK

7.1 The risks arising from *securitisation* transactions in relation to which a *firm* is investor, *originator* or *sponsor*, including reputational risks, must be evaluated and addressed through appropriate policies and procedures, to ensure in particular that the economic substance of the transaction is fully reflected in risk assessment and management decisions.

[Note: Art 82(1) of *CRD*]

7.2 A *firm* which is an *originator* of a revolving *securitisation* transaction involving *early amortisation provisions* should have liquidity plans to address the implications of both scheduled and early amortisation.

[Note Art 82(2) of the *CRD]*

8 MARKET RISK

8.1 A *firm* must implement policies and processes for the identification, measurement and management of all material sources and effects of market risks.

[**Note: Art 83(1) of the *CRD]***

8.2 A *firm* must take measures against the risk of a shortage of liquidity if the short position falls due before the long position.

[**Note: Art 83(2) of the *CRD***]

8.3 (1) A *firm's* financial resources and internal capital must be adequate for material market risks that are not subject to an *own funds* requirement.

(2) A *firm* which has, in calculating *own funds* requirements for position risk in accordance with Part Three, Title IV, Chapter 2 of the *CRR,* netted off its positions in one or more of the equities constituting a stock-index against one or more positions in the stock-index future or other stock-index product, must have adequate financial resources and internal capital to cover the basis risk of loss caused by the future's or other product's value not moving fully in line with that of its constituent equities.

(3) A *firm* using the treatment in Article 345 of the *CRR* must ensure that it holds sufficient financial resources and internal capital against the risk of loss which exists between the time of the initial commitment and the following working day.

[Note: Art 83(3) of the *CRD*]

8.4 As part of its obligations under the overall Pillar 2 rule in 3.1, a *firm* must consider whether the value adjustments and provisions taken for positions and portfolios in the *trading book* enable the *firm* to sell or hedge out its positions within a short period without incurring material losses under normal market conditions.

[**Note: Art 98(4) of the *CRD***]

9 INTEREST RISK ARISING FROM NON-TRADING BOOK ACTIVITIES

9.1 A *firm* must implement systems to identify, evaluate and manage the risk arising from potential changes in interest rates that affect a *firm's* non-trading activities.

[**Note: Art 84 of the *CRD***]

9.2 (1) As part of its obligations under the overall Pillar 2 rule in 3.1, a *firm* must carry out an evaluation of its exposure to the interest rate risk arising from its non-trading activities.

(2) The evaluation under (1) must cover the effect of a sudden and unexpected change in interest rates of 200 basis points in both directions.

(3) A *firm* must immediately notify the *PRA* if any evaluation under this *rule* suggests that, as a result of the change in interest rates described in (2), the economic value of the *firm* would decline by more than 20% of its *own funds.*

(4) A *firm* must carry out the evaluation under (1) as frequently as necessary for it to be reasonably satisfied that it has at all times a sufficient understanding of the degree to which it is exposed to the risks referred to in (1) and the nature of that exposure. In any case it must carry out those evaluations no less frequently than once a year.

[**Note: Art 98(5) of the *CRD***]

10 OPERATIONAL RISK

10.1 A *firm* must implement policies and processes to evaluate and manage the exposure to operational risk, including model risk and to cover low-frequency high severity events.

Without prejudice to the definition of *operational risk*, a firm must articulate what constitutes *operational risk* for the purposes of those policies and procedures.

[**Note: Art 85(1) of the *CRD***]

10.2 A *firm* must have in place adequate contingency and business continuity plans aimed at ensuring that in the case of a severe business disruption the *firm* is able to operate on an ongoing basis and that any losses are limited.

11 RISK OF EXCESSIVE LEVERAGE

11.1 (1) A *firm* must have in place policies and procedures for the identification, management and monitoring of the *risk of excessive leverage*.

(2) Those policies and procedures must include, as an indicator for *the risk of excessive leverage*, the leverage ratio determined in accordance with Article 429 of the *CRR* and mismatches between assets and obligations.

[**Note: Art 87(1) of the *CRD***]

11.2 A *firm* must address the *risk of excessive leverage* in a precautionary manner by taking due account of potential increases in that risk caused by reductions of the *firm's own funds* through expected or realised losses, depending on the applicable accounting rules. To that end, a *firm* must be able to withstand a range of different stress events with respect to the *risk of excessive leverage*.

[**Note: Art 87(2) of the *CRD***]

12 STRESS TESTS AND SCENARIO ANALYSIS

General stress test and scenario analysis rule

12.1 (1) As part of its obligation under the overall Pillar 2 rule in 3.1, a *firm* must, for the major sources of risk identified in accordance with that rule, carry out stress tests and scenario analyses that are appropriate to the nature, scale and complexity of those major sources of risk and to the nature, scale and complexity of the *firm's* business.

(2) In carrying out the stress tests and scenario analyses in (1), a *firm* must identify an appropriate range of adverse circumstances of varying nature, severity and duration relevant to its business and risk profile and consider the exposure of the *firm* to those circumstances, including:

(a) circumstances and events occurring over a protracted period of time;

(b) sudden and severe events, such as market shocks or other similar events; and

(c) some combination of the circumstances and events described in (a) and (b), which may include a sudden and severe market event followed by an economic recession.

(3) In carrying out the stress tests and scenario analyses in (1), the *firm* must estimate the financial resources that it would need in order to continue to meet the overall financial adequacy rule in 2.1 and the obligations laid down in Part Three of the *CRR* under the adverse circumstances being considered.

(4) In carrying out the stress tests and scenario analyses in (1), the *firm* must assess how risks aggregate across business lines or units, any material non-linear or contingent risks and how risk correlations may increase in stressed conditions.

13 DOCUMENTATION OF RISK ASSESSMENTS

13.1 (1) A *firm* must make a written record of the assessments required under this Part. These assessments must include assessments carried out on a consolidated basis and on an individual basis. In particular it must make a written record of:

(a) the major sources of risk identified in accordance with the overall Pillar 2 rule in 3.1;

(b) how it intends to deal with those risks; and

(c) details of the stress tests and scenario analyses carried out, including any assumptions made in relation to scenario design, and the resulting financial resources estimated to be required in accordance with the general stress test and scenario analysis rule in 12.1.

(2) A *firm* must maintain the records referred to in (1) for at least three years.

14 APPLICATION OF THIS PART ON AN INDIVIDUAL BASIS, A CONSOLIDATED BASIS AND A SUB-CONSOLIDATED BASIS

The ICAAP rules

14.1 The *ICAAP rules* do not apply on an individual basis to a *firm* to which the *ICAAP rules* apply on a *consolidated basis* or *sub-consolidated basis* under this Chapter.

14.2 The *ICAAP rules* apply on an individual basis to a *firm* to which the *ICAAP rules* do not apply on a *consolidated* or *sub-consolidated* basis under this Chapter.

[**Note: Art 108(1) (part) of the *CRD*]**

14.3 A *firm* which is a *parent institution in a Member State* must comply with the *ICAAP rules* on a *consolidated basis*.

14.4 A *firm* controlled by a *parent financial holding company in a Member State* or a *parent mixed financial holding company in a Member State* must comply with the *ICAAP rules* on the basis of the *consolidated situation* of that holding company, if the *PRA* is responsible for supervision of the *firm* on a *consolidated basis* under [art. 111 of CRD4][1].

[1] Replace with reference to regulation or rule transposing Art 111 into UK law.

[**Note: Art 108(2) and 108(3) of the *CRD***]

14.5 A *firm* that is a *subsidiary* must apply the *ICAAP rules* on a *sub-consolidated basis* if the *firm*, or the *parent undertaking* where it is a *financial holding company* or *mixed financial holding company,* have an *institution* or *financial institution* or an *asset management company* as a *subsidiary* in a *third country* or hold a *participation* in such an undertaking.

[**Note: Art 108(4) of the *CRD***]

14.6 If the *ICAAP rules* apply to a *firm* on a *consolidated basis* or on a *sub-consolidated basis* the *firm* must carry out consolidation to the extent and in the manner prescribed in articles [18(1), 18(8), 19(1), 19(3), 23 and 24(1) of the *CRR* and [CR firms/Groups/2.1-2.3]

14.7 For the purpose of the *ICAAP rules* as they apply on a *consolidated basis* or on *a sub-consolidated basis*:

(1) the *firm* must ensure that the *consolidation group* has the processes, strategies and systems required by the overall Pillar 2 rule in 3.1;

(2) the risks to which the overall Pillar 2 rule in 3.1 and the general stress test and scenario analysis rule refer are those risks as they apply to each member of the *consolidation group*;

(3) the reference in the overall Pillar 2 rule in 3.1 to amounts and types of financial resources, *own funds* and internal capital (referred to in this *rule* as resources) must be read as being to the amounts and types that the *firm* considers should be held by the members of the *consolidation group*;

(4) other references to resources must be read as being to resources of the members of the *consolidation group*;

(5) the reference in the overall Pillar 2 rule in 3.1 to the distribution of resources must be read as including a reference to the distribution between members of the *consolidation group*;

(6) the reference in the overall Pillar 2 rule in 3.1 to the overall financial adequacy rule in 2.1 must be read as being to that *rule* as adjusted under 14.12 – 14.14 (level of application of the overall financial adequacy rule);

(7) a *firm* must be able to explain how it has aggregated the risks referred to in the overall Pillar 2 rule in 3.1 and the financial resources, *own funds* and internal capital required by each member of the *consolidation group*; and

(8) in particular, to the extent that the transferability of resources affects the assessment in (2), a *firm* must be able to explain how it has satisfied itself that resources are transferable between members of the group in question in the stressed cases and the scenarios referred to in the general stress test and scenario analysis rule in 12.1.

14.8 (1) A *firm* must allocate the total amount of financial resources, *own funds* and internal capital identified as necessary under the overall Pillar 2 rule in 3.1 (as applied on a *consolidated basis* or on a *sub-consolidated basis*) between different parts of the *consolidation group*.

(2) The *firm* must carry out the allocation in (1) in a way that adequately reflects the nature, level and distribution of the risks to which the *consolidation group* is subject.

(3) A *firm* must also allocate the total amount of financial resources, *own funds* and internal capital identified as necessary under the overall Pillar 2 rule in 3.1 as applied on a *consolidated basis* or on a *sub-consolidated basis* between each *firm* which is a member of the *consolidated group* on the following basis:

(a) the amount allocated to each *firm* must be decided on the basis of the principles in (2); and

(b) if the process in (a) were carried out for each group member, the total so allocated would equal the total amount of financial resources, *own funds* and internal capital identified as necessary under the overall Pillar 2 rule in 3.1 as applied on a *consolidated basis* or on a *sub-consolidated basis*.

The risk control rules

14.9 The *risk control rules* apply to a *firm* on an individual basis whether or not they also apply to the firm on a *consolidated basis* or *sub-consolidated basis*.

[**Note: Art 109(1) of the *CRD*]**

14.10 Where a *firm* is a member of a *consolidation group*, the *firm* must ensure that the risk management processes and internal control mechanisms at the level of the *consolidation group* of which it is a member comply with the obligations set out in the *risk control rules* on a *consolidated basis* (or a *sub-consolidated basis*).

14.11 Compliance with the obligations referred to in 14.10 must enable the *consolidation group* to have arrangements, processes and mechanisms that are consistent and well integrated and that any data relevant to the purpose of supervision can be produced.

[**Note: Art 109(2) (part) of the *CRD***]

Level of application of the overall financial adequacy rule

14.12 The overall financial adequacy rule in 2.1 applies to a *firm* on an individual basis whether or not it also applies to the *firm* on a *consolidated basis* or *sub-consolidated basis.*

14.13 The overall financial adequacy rule in 2.1 applies to a *firm* on a *consolidated basis* if the *ICAAP rules* apply to it on a *consolidated basis* and applies to a *firm* on a *sub-consolidated basis* if the *ICAAP rules* apply to it on a *sub-consolidated basis*.

14.14 When the overall financial adequacy rule in 2.1 applies on a *consolidated basis* or *sub-consolidated basis*, the *firm* must ensure that at all times its *consolidation group* maintains overall financial resources, including *own funds* and liquidity resources, which are adequate, both as to amount and quality, to ensure that there is no significant risk that the liabilities of any members of its *consolidation group* cannot be met as they fall due.

CAPITAL REQUIREMENTS DIRECTIVE [(GOVERNANCE AND REMUNERATION)] AMENDMENT INSTRUMENT [No. XXX] 2013

Powers exercised

A. The Prudential Regulation Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137G (The PRA's general rules);
(2) section 137H (General rules about remuneration); and
(3) section 137T (General supplementary powers);

B. The rule-making powers referred to above are specified for the purpose of section 138G (Rule-making instrument) of the Act.

Pre-conditions to making

C. In accordance with section 138J of the Act (consultation with the Financial Conduct Authority) ("FCA"), the PRA consulted the FCA. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

Commencement

D. Part 1 of the Annex to this instrument comes into force on 1 January 2014.

E. Part 2 of the Annex to this instrument comes into force on 1 July 2014.

Amendments to the Handbook

F. The Glossary of definitions is amended in accordance with Annex A to this instrument.

G. The Senior Management Arrangements, Systems and Controls manual (SYSC) is amended in accordance with the Annex B to this instrument.

Notes and Guidance

H. In the Annex to this instrument, the "notes" (indicated by "**Note:**") are included for the convenience of readers but do not form part of the legislative text.

I. The Prudential Regulation Authority gives as guidance each provision in the Annex marked with a G.

Citation

J. This instrument may be cited as the Capital Requirements Directive (Governance and Remuneration) Amendment Instrument No XXX 2013.

By order of the Board of the Prudential Regulation Authority
[DATE]

Annex A

Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

Part 1: Comes into force on 1 January 2014.

Insert the following new definitions and amendments in the appropriate alphabetical position. The text is not underlined.

Article 12(1) relationship	means a relationship where *undertakings* are linked by a relationship within the meaning of Article 12(1) of Directive 83/349 EEC.
Article 18(6) relationship	a relationship of one of the following kinds: a) where an *institution* exercises a significant influence over one or more *institutions* or *financial institutions*, but without holding a *participation* or other capital ties in these *institutions*; or b) where two or more *institutions* or *financial institutions* are placed under single management other than pursuant to a contract or clauses of their memoranda or articles of association.

…

Consolidated situation	the situation that results from applying the requirements of the *CRR* in accordance with Part One, Title II, Chapter 2 of the *CRR* to an *institution* as if that *institution* formed, together with one or more other entities, a single *institution*.

…

core UK group eligible capital	the eligible capital of the *core UK group* calculated in accordance with 2.4 of the large exposures chapter of the *PRA* rulebook.

…

CRD credit institution	an undertaking whose business is to receive deposits or other repayable funds from the public and to grant credits for its own account and that has its registered office (or, if it has no registered office, its head office) in an *EEA state*, excluding an institution to which the *CRR* does not apply under article 2 of the *CRR*.

…

CRR	the Regulation of the European Parliament and the Council on prudential requirements for credit institutions and investment firms (Regulation (EU) No 575/2013) and amending Regulation (EU) No 648/2012**.**
CRR firm	for the purposes of *SYSC* means *UK banks, buildings societies*

	and *investment firms* that are subject to the *CRR*.
…	
designated investment firm	a person that has been designated by the *PRA* under article 3 of the *PRA-regulated Activities Order*.
…	
FINREP firm	a *credit institution* or *investment firm* subject to *CRR* that is subject to Article 4 of Regulation (EC) No 1606/2002; or a *credit institution* other than those referred to in Article 4 of Regulation (EC) No 1606/2002 that prepares its consolidated accounts in conformity with the international accounting standards adopted in accordance with the procedure laid down in Article 6(2) of that Regulation
…	
individual consolidation permission	a permission given by the *PRA* under Article 9(1) of the *CRR*
…	
management body	(in accordance with Article 3(8) of the *CRD*) the *governing body* and *senior personnel* of a *CRR firm* who are empowered to set the *firm'* strategy, objectives and overall direction, and which oversee and monitor management decision-making.
…	
PRA-regulated Activities Order	Financial Services and Market Act 2000 (PRA-regulated Activities) Order 2013 (SI 2013/556).
…	
UK designated investment firm	a *designated investment firm* which is a *body corporate* or *partnership* formed under the law of any part of the *United Kingdom*.

Amend the following definitions as shown.

consolidation group	(1)	the following: (a) a *conventional group*; or (b) *undertakings* linked by a *consolidation Article 12(1) relationship* or (for the purposes of *BIPRU*) an *Article 134 relationship*[2] . If a *parent undertaking* or *subsidiary undertaking* in a *conventional group* (the first person) has a *consolidation Article 12(1) relationship* or (for the purposes of *BIPRU*) an *Article 134 relationship*[2] with another *person* (the second person), the second person (and any *subsidiary undertaking* of the second person) is also a member of the same *consolidation group*.

	(2) For the purposes of *SUP 16,* the *group* of *undertakings* which are included in the *consolidated situation* of a *parent institution* in a *Member State*, and *EEA parent institution*, an *EEA parent financial holding company* or an *EEA parent mixed financial holding company* (including any *undertaking* which is included in that consolidation because of an *Article 12(1) relationship*, *Article 18(5) relationship* or *Article 18 relationship*).

…

core UK group	~~(in relation to a *firm*) all *undertakings* which, in relation to the *firm*, satisfy the conditions set out in BIPRU 3.2.25 R (Zero risk-weighting for intra-group exposures: core UK group) and BIPRU 10.8A.2 R (Definition of core UK group).~~ all counterparties which, in relation to a *firm*, satisfy the conditions set out in Article 113(6) of the *CRR* and in respect of which *exposures* are exempted, under Article 400(1)(f) of the *CRR*, from the application of Article 395(1) of the *CRR.*

…

CRD	(1) (in *GENPRU* and *BIPRU* (except in (2)) the *Capital Adequacy Directive* and the *Banking Consolidation Directive*. (2) (in *GENPRU* 3 (Cross sector groups), *BIPRU* 12 (Liquidity standards), *SUP* 13, 13A, 14, 15, 13 Annex 1, 13 Annex 4, 13A Annex 1, 13A Annex 2 (passporting), *SYSC* 4, 7 and 19A, and *IFPRU*) the Directive of the European Parliament and the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms (No 2013/36/EU) and amending Directives 2002/48/EC and 2006/49/EC.

…

eligible ECAIs	an *ECAI*: (a) (for *exposure risk weighting* purposes other than those in (b)) recognised by the *appropriate regulator* under regulation 22 of the *Capital Requirements Regulations 2006* (Recognition for exposure risk-weighting purposes); or (b) (for *securitisation risk weighting* purposes) recognised by the *appropriate regulator* under regulation 23 of the *Capital Requirements Regulations 2006* (Recognition for securitisation risk-weighting purposes)~~.~~; or (c) (in *BIPRU* 12) that is listed in the first row in the table set out in *BIPRU* 12 Annex 1.

…

limited licence firm	has the meaning ~~set out~~ in ~~*BIPRU* 1.1.12R (Types of investment firm: Limited licence firms)~~ article 95(1) of the *CRR*.

…

Non-core large exposures group

~~(in relation to a *firm*) has the meaning in BIPRU 10.9A.3 R (Definition of non-core large exposures group), which is in summary each *non-core concentration risk group counterparty* that is not a member of the *core UK group* but satisfies all the conditions for membership of the firm's *core UK group* except for BIPRU 10.8A.2 R (1) (Core concentration risk group counterparty), BIPRU 10.8A.2 R (5) (Establishment in the United Kingdom) and BIPRU 10.8A.5 R (2) (Capital maintenance arrangements).~~

All counterparties which, in relation to a *firm*, satisfy the conditions set out in 2.1 of the large exposures chapter of the PRA Rulebook and in respect of which exposures as defined in Article 389 of the *CRR*, are exempted under Article 400(2)(c) of the *CRR*, from the application of Article 395(1) of the *CRR*.

…

third country BIPRU firm

(1) (except in *BIPRU* 12 (Liquidity standards)) an *overseas firm* that:

(a) is not an *EEA firm*;

(b) has its head office outside the *EEA*; and

(c) would be a *BIPRU firm* if it had been a *UK domestic firm*, it had carried on all its business in the *United Kingdom* and had obtained whatever authorisations for doing so that are required under the *Act*.

(2) (in *BIPRU* 12 (Liquidity standards)) an *overseas firm* that:

(a) is *bank*;

(b) is not an *EEA firm*; and

(c) has its head office outside the *EEA.*

Annex B

Amendments to the Senior Management Arrangements, Systems and Control manual (SYSC)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

Part 1: Comes into force on 1 January 2014.

4.1 General requirements

4.1.1 R (1) …

(2) ~~A *BIPRU firm* and a *third country BIPRU firm* must comply with the *Remuneration Code*.~~ [deleted]

[**Note**: ~~article 22(1) of the *Banking Consolidation Directive*~~ article 74 (1) of the *CRD*, article 13(5) second paragraph of *MiFID*]and article 12(1)(a) of the *UCITS Directive*]

4.1.2 R For a *common platform firm*, the arrangements, processes and mechanisms referred to in *SYSC* 4.1.1R must be comprehensive and proportionate to the nature, scale and complexity of the risks inherent in the business model and ~~of~~ the *common platform firm's* activities and must take into account the specific technical criteria described in *SYSC* 4.1.7R, *SYSC* 5.1.7R, *SYSC* 7 and (for a *firm* to which *SYSC* 19A applies) ~~(for a *BIPRU firm* and a *third country BIPRU firm*)~~ *SYSC* 19A.

[**Note**: ~~article 22(2) of the *Banking Consolidation Directive*~~ article 74 (2) of the *CRD*]

…

Mechanisms and procedures for a ~~BIPRU~~ firm

4.1.3 R ~~A *BIPRU firm* must ensure that its internal control mechanisms and administrative and accounting procedures permit the verification of its compliance with *rules* adopted in accordance with the *Capital Adequacy Directive* at all times.~~
~~[**Note**: article 35(1) final sentence of the *Capital Adequacy Directive*]~~ [deleted]

…

4.2.2 R A *common platform firm*, a *management company* and the *UK* branch of a *non-EEA bank* must ensure that its management is undertaken by at least two persons meeting the requirements laid down in *SYSC* 4.2.1R.

[**Note**: article 9(4) first paragraph of *MiFID*, article 7(1)(b) of the *UCITS Directive* and ~~11(1) first paragraph of the *Banking Consolidation Directive*~~ article 13(1) of the *CRD*]

(…)

4.3A CRR firms

Management body

4.3A.1 R A *CRR firm* must ensure that the *management body* defines, oversees and is accountable for the implementation of governance arrangements that ensure effective and prudent management of the *firm*, including the segregation of duties in the organisation and the prevention of conflicts of interest. The *firm* must ensure that the *management body*:

(1) has overall responsibility for the firm;

(2) approves and oversees implementation of the *firm*'s strategic objectives, risk strategy and internal governance;

(3) ensures the integrity of the *firm*'s accounting and financial reporting systems, including financial and operational controls and compliance with the *regulatory system*.

(4) oversees the process of disclosure and communications;

(5) has responsibility for providing effective oversight of *senior management*.

(6) monitors and periodically assesses the effectiveness of the *firm*'s governance arrangements and takes appropriate steps to address any deficiencies.

[**Note**: article 88(1) of the *CRD*]

4.3A.2 R A *CRR firm* must ensure that the chairman of the *firm*'s *management body* does not exercise simultaneously the *chief executive function* within the same *firm.*

[**Note**: article 88(1)(e) of the *CRD*]

4.3A.3 R A *CRR firm* must ensure that the members of the *management body* of the *firm*:

(1) are of sufficiently good repute;

(2) possess sufficient knowledge, skills and experience to perform their duties;

(3) possess adequate collective knowledge, skills and experience to understand the *firm*'s activities, including the main risks;

(4) reflect an adequately broad range of experiences;

(5) commit sufficient time to perform their functions in the *firm*; and

(6) act with honesty, integrity and independence of mind to effectively assess and challenge the decisions of *senior management* where necessary and to effectively oversee and monitor management decision-making.

[**Note**: article 91(1)-(2) and (7)-(8) of the *CRD*]

4.3A.4 R A *CRR firm* that is either:

(1) a *financial holding company* or a *mixed financial holding company*; or

(2) a subsidiary of a *financial holding company* or a *mixed financial holding company*;

must ensure that the members of the *management body* of the *financial holding* *company* or *mixed financial holding company* are of sufficiently good repute and possess sufficient knowledge, skills and experience to perform their duties taking into account the specific role of a *financial holding company* or *mixed financial holding company*.]

[**Note**: article 121 of the *CRD*]

4.3A.5 R A *CRR firm* must devote adequate human and financial resources to the induction and training of members of the *management body*.

[**Note**: article 91(9) of the *CRD*]

4.3A.6 R A *CRR firm* must ensure that the members of the *management body* of the *firm* do not hold more directorships than is appropriate taking into account individual circumstances and the nature, scale and complexity of the *firm*'s activities.

[**Note**: article 91(3) of the *CRD*]

…

4.3A.8 R For the purposes of *SYSC* 4.3A.6R and *SYSC* 4.3A.7R:

(1) directorships in organisations which do not pursue predominantly commercial objectives shall not count; and

(2) the following shall count as a single directorship:

(a) executive or non-executive directorships held within the same *group*; or

(b) executive or non-executive directorships held within:

(i) *firms* that are members of the same institutional protection scheme provided that the conditions set out in Article 113(7) of the CRR are fulfilled; or

(ii) *undertakings* (including non-financial entities) in which the *firm* holds a *qualifying holding*.

[**Note**: article 91(4) and (5) of the *CRD*]

Nomination Committee

4.3A.9 R A *CRR firm* that is significant in terms of its size, internal organisation and the nature, the scope and the complexity of its activities must:

(1) establish a nomination committee composed of members of the *management body* who do not perform any executive function in the *firm*;

(2) ensure that the nomination committee is able to use any forms of resources the nomination committee deems appropriate, including external advice; and

(3) ensure that the nomination committee receives appropriate funding.

[**Note**: article 88(2) of the *CRD*]

4.3A.10 R A *CRR firm* that has a nomination committee must ensure that the nomination committee:

(1) has regard to a broad set of qualities and competences when recruiting members to the *management body* and for that purpose puts in place a policy promoting diversity on the *management body*;

(2) identifies and recommends for approval, by the *management body* or by general meeting, candidates to fill *management body* vacancies, having evaluated the balance of knowledge, skills, diversity and experience of the *management body*;

(3) prepares a description of the roles and capabilities for a particular appointment, and assesses the time commitment required;

(4) decides on a target for the representation of the underrepresented gender in the *management body* and prepares a policy on how to increase the number of the underrepresented gender in the *management body* in order to meet that target;

(5) periodically, and at least annually, assesses the structure, size, composition and performance of the *management body* and makes recommendations to the *management body* with regard to any changes;

(6) periodically, and at least annually, assesses the knowledge, skills and experience of individual members of the *management body* and of the *management body* collectively, and reports this to the *management body*;

(7) periodically reviews the policy of the *management body* for selection and appointment of *senior management* and makes recommendations to the *management body*;

(8) in performing its duties, and to the extent possible, on an ongoing basis, takes account of the need to ensure that the *management body*'s decision making is not dominated by any one individual or small group of individuals in a manner that is detrimental to the interest of the *firm* as a whole;

[**Note**: article 88(2) and article 91(10) of the *CRD*]

4.3A.11 R A *CRR firm* that does not have a nomination committee must have regard to a broad set of qualities and competences when recruiting members to the *management body*. For that purpose a *CRR firm* that does not have a nomination committee must put in place a policy promoting diversity on the *management body*.

[**Note**: article 91(10) of the *CRD*]

Website

4.3A.12 R A *CRR firm* that maintains a website must explain there how it complies with the requirements of *SYSC* 4.3A.1R to *SYSC* 4.3A.3R and *SYSC* 4.3A.5R to *SYSC* 4.3A.12R.

[**Note**: article 96 of the *CRD*]

…

7.1 Risk control

…

7.1.4 R The ~~*senior personnel*~~ *management body* of a *common platform firm* must approve and periodically review the strategies and policies for taking up, managing, monitoring and mitigating the risks the *firm* is or might be exposed to, including those posed by the macroeconomic environment in which it operates in relation to the status of the business cycle.

[**Note**: ~~annex V paragraph 2 of the *Banking Consolidation Directive*~~ article 76(1) of the *CRD*]

…

7.1.7B G In setting the method of determining the *remuneration* of *employees* involved in the risk management function, ~~*BIPRU firms*~~ *firms* that *SYSC* 19A applies to will also need to comply with the *Remuneration Code*.

7.1.8 G (1) ~~*SYSC* 4.1.3R requires a *BIPRU firm* to ensure that its internal control mechanisms and administrative and accounting procedures permit the verification of its compliance with *rules* adopted in accordance with the *Capital Adequacy Directive* at all times. In complying with this obligation, a *BIPRU firm* should document the organisation and responsibilities of its risk management function and it should document its risk management framework setting out how the risks in the business are identified, measured, monitored and controlled.~~ [deleted]

…

~~Credit and counterparty risk~~

7.1.9 R ~~A *BIPRU firm* must base credit-granting on sound and well-defined criteria and clearly establish the process for approving, amending, renewing, and re-financing credits.~~
~~[**Note**: annex V paragraph 3 of the *Banking Consolidation Directive*]~~ [deleted]

7.1.10 R ~~A *BIPRU firm* must operate through effective systems the ongoing administration and monitoring of its various credit risk-bearing portfolios and exposures, including for identifying and managing problem credits and for making adequate value adjustments and provisions.~~
~~[**Note**: annex V paragraph 4 of the *Banking Consolidation Directive*]~~ [deleted]

7.1.11 R ~~A *BIPRU firm* must adequately diversify credit portfolios given its target market and overall credit strategy.~~
~~[**Note**: annex V paragraph 5 of the *Banking Consolidation Directive*]~~ [deleted]

7.1.12 G ~~The documentation maintained by a *BIPRU firm* under *SYSC 4.1.3 R* should include its policy for credit risk, including its risk appetite and provisioning policy and should describe how it measures, monitors and controls that risk. This should include descriptions of the systems used to ensure that the policy is correctly implemented.~~ [deleted]

~~Residual risk~~

7.1.13 R ~~A *BIPRU firm* must address and control by means of written policies and procedures the risk that recognised credit risk mitigation techniques used by it prove less effective than expected.~~
~~[**Note**: annex V paragraph 6 of the *Banking Consolidation Directive*]~~ [deleted]

~~Market risk~~

7.1.14 R ~~A *BIPRU firm* must implement policies and processes for the measurement and management of all material sources and effects of market risks.~~
~~[**Note**: annex V paragraph 10 of the *Banking Consolidation Directive*]~~ [deleted]

~~Interest rate risk~~

7.1.15 R ~~A *BIPRU* firm must implement systems to evaluate and manage the risk arising from potential changes in interest rates as they affect a *BIPRU firm's* non-trading activities.~~
~~[**Note**: annex V paragraph 11 of the *Banking Consolidation Directive*]~~ [deleted]

~~Operational risk~~

7.1.16 R ~~A *BIPRU firm* must implement policies and processes to evaluate and manage the exposure to operational risk, including to low-frequency high severity events. Without prejudice to the definition of *operational risk*, *BIPRU firms* must articulate what constitutes operational risk for the purposes of those policies and procedures.~~
~~[**Note**: annex V paragraph 12 of the *Banking Consolidation Directive*]~~ [deleted]

7.1.16A G ~~In meeting the general standard referred to in *SYSC* 7.1.16R, a *BIPRU firm* that undertakes market-related activities should be able to demonstrate to the *appropriate regulator*:~~

~~(1) in the case of a *BIPRU firm* calculating its *ORCR* using the *basic indicator approach* or *standardised approach*, that it has considered; or~~

~~(2) in the case of a *BIPRU firm* with an *AMA permission*, compliance with~~

~~the Committee of European Banking Supervisors Guidelines on the management of operational risk in market-related activities, published in October 2010. These can be found at *http://www.eba.europa.eu/documents/Publications/Standards---Guidelines/2010/Management-of-op-risk/CEBS-2010-216-(Guidelines-on-the-management-of-op-.aspx*~~ [deleted]

7.1.16B G ~~In meeting the general standards referred to in *SYSC* 7.1.16R, a *firm* with AMA approval should be able to demonstrate to the *appropriate regulator* that it has considered and complies with Section III of the European Banking Authority's Guidelines on the Advanced Measurement Approach (AMA) - Extensions and Changes published in January 2012. These can be found at *http://eba.europa.eu/cebs/media/Publications/Standards%20and%20Guidelines/2012/EBA-BS-2011-209-final-(EBA-GL-on-AMA-extensions-and-changes).pdf*~~
[deleted]

Additional rules for CRR firms

7.1.17 R (1) The *management body* of a *CRR firm* has overall responsibility for risk management. It must devote sufficient time to the consideration of risk issues.

(2) The *management body* of a *CRR firm* must be actively involved in and ensure that adequate resources are allocated to the management of all material risks addressed in the *rules* implementing the *CRD* and in the

CRR as well as in the valuation of assets, the use of external ratings and internal models related to those risks.

(3) A *CRR firm* must establish reporting lines to the *management body* that cover all material risks and risk management policies and changes thereof.

[**Note**: article 76(2) of the *CRD]*

7.1.18 R (1) A *CRR firm* that is significant in terms of its size, internal organisation and the nature, the scope and the complexity of its activities must establish a risk committee composed of members of the *management body* who do not perform any executive function in the *firm.* Members of the risk committee must have appropriate knowledge, skills and expertise to fully understand and monitor the risk strategy and the risk appetite of the *firm*.

(2) The risk committee must advise the *management body* on the institution's overall current and future risk appetite and assist the *management body* in overseeing the implementation of that strategy by senior management.

(3) The risk committee must review whether prices of liabilities and assets offered to clients take fully into account the *firm's* business model and risk strategy. Where prices do not properly reflect risks in accordance with the business model and risk strategy, the risk committee must present a remedy plan to the *management body.*

[**Note:** article 76(3) of the *CRD*]

7.1.19 R (1) A *CRR firm* must ensure that the *management body* in its supervisory function and, where a risk committee has been established, the risk committee have adequate access to information on the risk profile of the *firm* and, if necessary and appropriate, to the risk management function and to external expert advice.

(2) The *management body* in its supervisory function and, where one has been established, the risk committee must determine the nature, the amount, the format, and the frequency of the information on risk which it is to receive.

[**Note:** article 76 (4) of the *CRD*]

7.1.20 R In order to assist in the establishment of sound remuneration policies and practices, the risk committee must, without prejudice to the tasks of the remuneration committee, examine whether incentives provided by the remuneration system take into consideration risk, capital, liquidity and the likelihood and timing of earnings.

[**Note**: article 76 (4) of the *CRD*]

7.1.21 R (1) A *CRR firm's* risk management function (SYSC 7.1.6R) must be independent from the operational functions and have sufficient authority, stature, resources and access to the *management body.*

(2) The risk management function must ensure that all material risks are identified, measured and properly reported. It must be actively involved in elaborating the *firm's* risk strategy and in all material risk management decisions and it must be able to deliver a complete view of the whole range

of risks of the *firm.*

(3) A *CRR firm* must ensure that the risk management function is able to report directly to the *management body* in its supervisory function, independent from senior management and that it can raise concerns and warn the *management body*, where appropriate, where specific risk developments affect or may affect the *firm*, without prejudice to the responsibilities of the *management body* in its supervisory and/or managerial functions pursuant to the *CRD* and the *CRR*.

[**Note**: article 76(5) of the *CRD*]

7.1.22 R The head of the risk management function must be an independent senior manager with distinct responsibility for the risk management function. Where the nature, scale and complexity of the activities of the *CRR firm* do not justify a specially appointed person, another senior person within the *firm* may fulfil that function, provided there is no conflict of interest. The head of the risk management function must not be removed without prior approval of the *management body* and must be able to have direct access to the *management body* where necessary.

[**Note**: Article 76(5) of the *CRD*]

12.1 Application

…

~~BIPRU firms and other firms to which BIPRU 8 applies~~ **CRR firms and non-CRR firms that are parent financial holding companies in a Member State**

12.1.13 R If this *rule* applies under *SYSC* 12.1.14R to a *firm*, the *firm* must:

…

(2) ensure that the risk management processes and internal control mechanisms at the level of any ~~*UK*~~ *consolidation group* or non-*EEA sub-group* of which it is a member comply with the obligations set out in the following provisions on a consolidated (or sub-consolidated) basis:

(a) *SYSC* 4.1.1R and *SYSC* 4.1.2R;

(b) *SYSC* 4.1.7R;

(bA) *SYSC* 4.3A;

(c) *SYSC* 5.1.7 R;

(d) *SYSC* 7

(dA) the *Remuneration Code*;

(e) *BIPRU* 12.3.4R, *BIPRU* 12.3.5R, *BIPRU* 12.3.7A R, *BIPRU* 12.3.8R ~~(3)~~, *BIPRU* 12.3.22AR, *BIPRU* 12.3.22BR, *BIPRU* 12.3.27R, *BIPRU* 12.4.-2R, *BIPRU* 12.4.-1R, *BIPRU* 12.4.5AR, *BIPRU* 12.4. 10R, ~~and~~ *BIPRU* 12.4.11R and *BIPRU*

12.4.11A R;

(f) ~~BIPRU 2.3.7 R (1);~~

(g) ~~BIPRU 9.1.6 R and BIPRU 9.13.21 R (Liquidity Plans);~~

(h) ~~BIPRU 10.12.3 R (Concerntration risk policies).~~

[**Note:** ~~article 73(3) of the *Banking Consolidation Directive*~~] article 109(2) of the *CRD*]

(3) ensure that compliance with the obligations in (2) enables the *consolidation gro*up or the non-*EEA sub-group* to have arrangements, processes and mechanisms that are consistent and well integrated and that any data relevant to the purpose of supervision can be produced.

[**Note**: Article 109(2) of the *CRD*]

12.1.14 R *SYSC* 12.1.13R applies to a *firm* that is:

…

(2) ~~a *BIPRU firm*~~ a *CRR firm*; or

(3) a ~~non-*BIPRU firm*~~ non-*CRR firm* that is a *parent financial holding company in a Member State* and is a member of a *consolidation group*.

12.1.15 R In the case of a *firm* that:

(1) is a ~~*BIPRU firm*~~ *CRR firm*; and

…

…

19A.1 General application and purpose

…

19A.1.1 R (1) The *Remuneration Code* applies to: ~~*BIPRU firm* and a *third country BIPRU firm*.~~

(a) a *building society*;

(b) a *bank*;

(c) an *investment firm*;

(d) a *limited activity firm*;

(e) a *limited licence firm*; or

(f) an *overseas firm* that;

(i) is not an *EEA firm*;

(ii) has its head office outside the *EEA*; and

(iii) would be a *firm* referred to in (a), (b), (c), (d) or (e) if it had been a *UK domestic firm*, had carried on all of its business in the United Kingdom and had obtained whatever authorisations for doing so as are required under the Act.

(2) In relation to a ~~third country BIPRU firm~~*firm* that falls under (1)(f), the *Remuneration Code* applies only in relation to activities carried on from an establishment in the *United Kingdom* .

…

…

19A.1.6 G (1) …

(2) The *Remuneration Code* implements the main provisions of the ~~Third Capital Requirements Directive (Directive 2010/76/EU)~~ *CRD* which relate to *remuneration*. The Committee of European Banking Supervisors published Guidelines on Remuneration Policies and Practices on 10 December 2010. ~~Provisions of the Third Capital Requirements Directive relating to Pillar 3 disclosures of information relating to *remuneration* have been implemented through amendments to *BIPRU 11* (specifically the *rules* and *guidance* in *BIPRU* 11.5.18R to *BIPRU* 11.5.21G).~~ Provisions of the Capital Requirements (Amendment) Regulations 2012 (SI 2012/917) together with the European Banking Authority's Guidelines to article 22(3) and (5) of the *Banking Consolidation Directive* relating to the collection of *remuneration* benchmarking information and *high earners* information have been implemented through SUP 16 Annex 33AR and SUP 16 Annex 34AR. The Guidelines can be found at *http://www.eba.europa.eu/cebs/media/Publications/Standards%20and%20Guidelines/2012/EBA-GL-2012-04---GL-4-on-remuneration-benchmarking-exercise-.pdf* and *http://www.eba.europa.eu/cebs/media/Publications/Standards%20and%20Guidelines/2012/EBA-GL-2012-05---GL-5-on-remuneration-data-collection-exercise-.pdf*.

…

19A.2 General requirement

19A.2.1 R …

[**Note:** ~~Article 22(1) of the *Banking Consolidation Directive*~~ article 74(1) of the *CRD*]

…

19A.3.1 R (1) …

(2) …

[**Note:** article 92(1) of the *CRD* ~~Paragraph 23 (final, unnumbered point) of Annex V to the *Banking Consolidation Directive*~~]

19A.3.2 G *SYSC* 12.1.13R(2)(dA*)* requires the *firm* to ensure that the risk management processes and internal control mechanisms at the level of any *UK consolidation group* or *non-EEA sub-group* of which a *firm* is a member comply with the obligations set out in this section on a consolidated (or sub-consolidated) basis. In the *appropriate regulator's* view, the requirement to apply this section at *group*, *parent undertaking* and *subsidiary undertaking* levels (as provided for in *SYSC* 19A.3.1R(1)) is in line with the requirements in ~~73(3) of the *Banking Consolidation Directive*~~ Article 109(2) of the *CRD* article concerning the application of systems and controls requirements to *groups* (as implemented in *SYSC* 12.1.13R).

…

19A.3.3 R (1) …

(2) …

(3) …

[**Note:** ~~Paragraph 23 of Annex V to the *Banking Consolidation Directive*~~ article 92(2) of the *CRD*]

(…)

19A.3.4 R …

[**Note:** ~~paragraph 23 of Annex V to the *Banking Consolidation Directive*~~ article 92(2) of the *CRD*]

…

19A.3.7 R …

[**Note:** ~~Paragraph 23(a) of Annex V to the *Banking Consolidation Directive*~~ article 92(2)(a) of the *CRD*]

19A.3.8 R …

[**Note:** ~~Paragraph 23(b) of Annex V to the *Banking Consolidation Directive*~~ article 92(2)(b) of the *CRD*]

19A.3.9 R …

[**Note:** ~~Paragraph 23(b) of Annex V to the *Banking Consolidation Directive*~~ Article 92(2)(b) of the *CRD*]

19A.3.10 R A *firm* must ensure that its ~~*governing*~~ *management body* in its *supervisory function* adopts and periodically reviews the general principles of the *remuneration* policy and is responsible for overseeing its implementation.

[**Note:** ~~Paragraph 23(c) of Annex V to the *Banking Consolidation Directive*~~ article 92(2)(c) of the *CRD* and Standard 1 of the *FSB Compensation Standards*]

19A.3.11 R A *firm* must ensure that the implementation of the *remuneration* policy is, at least annually, subject to central and independent internal review for compliance with policies and procedures for *remuneration* adopted by the ~~*governing*~~ *management body* in its *supervisory function*.

[**Note:** article 92(2)(d) of the *CRD* ~~Paragraph 23(d) of Annex V to the *Banking Consolidation Directive*~~ and Standard 1 of the *FSB Compensation Standards*]

19A.3.12 R (1) A *CRR firm* that is significant in terms of its size, internal organisation and the nature, the scope and the complexity of its activities must establish a *remuneration* committee.

(2) …

(3) The chairman and the members of the *remuneration* committee must be members of the ~~*governing*~~ *management body* who do not perform any executive function in the *firm*.

(4) The *remuneration* committee must be responsible for the preparation of decisions regarding *remuneration*, including those which have implications for the risk and risk management of the *firm* and which are to be taken by the ~~*governing*~~ *management body* ~~in its *supervisory function*~~.

(5) When preparing such decisions, the *remuneration* committee must take into account the long-term interests of shareholders, investors and other stakeholders in the *firm* and the public interest.

[**Note:** ~~Paragraph 24 of Annex V of the *Banking Consolidation Directive*~~ article 95 of the *CRD* and Standard 1 of the *FSB Compensation Standards*]

…

19A.3.12A R A *firm* that maintains a website must explain on the website how it complies with the *Remuneration Code*.

[**Note:** article 96 of the *CRD*]

…

19A.3.14 R …

[**Note:** ~~Paragraph 23(e) of Annex V to the *Banking Consolidation Directive*~~ article 92(2)(e) of the *CRD* and Standard 2 of the *FSB Compensation Standards*]

…

19A.3.16 R …

[**Note:** ~~Paragraph 23(f) of Annex V to the *Banking Consolidation Directive*~~ article 92(2)(f) of the *CRD*]

…

19A.3.18 R …

[**Note:** ~~Paragraph 23(i) of Annex V to the *Banking Consolidation Directive*~~ article 94(1)(c) of the *CRD* and Standard 3 of the *FSB Compensation Standards*]

…

19A.3.20 R A *firm* that benefits from exceptional government intervention must ensure that:

(1) …

(2) it restructures *remuneration* in a manner aligned with sound risk management and long-term growth, including when appropriate

establishing limits to the remuneration of ~~*senior personnel*~~ members of its *management body*; and

(3) no variable *remuneration* is paid to members of its ~~*senior personnel*~~ *management body* unless this is justified.

[**Note:** ~~Paragraph 23(k) of Annex V to the *Banking Consolidation Directive*~~ article 93 of the *CRD* and Standard 10 of the *FSB Compensation Standards*]

19A.3.21 G The *appropriate regulator* would normally expect it to be appropriate for the ban on paying variable *remuneration* to ~~*senior personnel*~~ members of the *management body* of a *firm* that benefits from exceptional government intervention to apply only in relation to ~~*senior personnel*~~ members of the *management body* who were in office at the time that the intervention was required.

19A.3.22 R (1) …

(2) …

[**Note:** ~~Paragraph 23(n) of Annex V to the *Banking Consolidation Directive*~~ article 94(1)(j), (k) of the *CRD* and Standard 4 of the *FSB Compensation Standards*]

…

19A.3.27 R A *firm* must ensure that its total variable *remuneration* is generally considerably contracted where subdued or negative financial performance of the *firm* occurs, taking into account both current *remuneration* and reductions in payouts of amounts previously earned, including through malus or clawback arrangements.

[**Note:** ~~Paragraph 23(q) of Annex V to the *Banking Consolidation Directive*~~ article 94(1)(n) of the *CRD* and Standard 5 of the *FSB Compensation Standards*]

…

19A.3.29 R A *firm* must ensure that:

(1) …

…

(3) ~~in the case of~~ when an *employee* ~~reaching~~ reaches retirement, *discretionary pension benefits* are paid to the *employee* in the form of instruments referred to in *SYSC* 19A.3.47R(1) and subject to a five-year retention period.

[**Note:** ~~Paragraph 23(r) of Annex V to the *Banking Consolidation Directive*~~ article 94(1)(o) of the *CRD*]

(…)

19A.3.30 R (1) …

(2) …

[**Note:** ~~Paragraph 23(s) of Annex V to the *Banking Consolidation Directive*~~ article 94(1)(p) of the *CRD* and Standard 14 of the *FSB Compensation Standards*]

…

Remuneration Principle 11: ~~Avoidance of~~ Non-compliance with the Remuneration Code

19A.3.32 R A *firm* must ensure that variable *remuneration* is not paid through vehicles or methods that facilitate ~~the avoidance of~~ non-compliance with the *Remuneration Code*.

[**Note:** ~~Paragraph 23(t) of Annex V to the *Banking Consolidation Directive*~~ article 94(1)(q) of the *CRD*]

…

19A.3.35A R A *firm* must ensure that the remuneration policy makes a clear distinction between criteria for setting:

(1) basic fixed remuneration that primarily reflects an employee's professional experience and organisational responsibility as set out in the employee's job description and terms of employment; and

(2) variable remuneration that reflects performance in excess of that required to fulfil the *employee*'s job description and terms of employment and that is subject to performance adjustment in accordance with the *Remuneration Code*.

[**Note:** article 92(2)(g) of the *CRD*]

…

19A.3.36 R A *firm* must ensure that where *remuneration* is performance-related:

(1) …

(2) …

[**Note:** ~~Paragraph 23(g) of Annex V to the *Banking Consolidation Directive*~~ article 94(1)(a) of the *CRD* and Standard 6 of the *FSB Compensation Standards*]

…

19A.3.38 R …

[**Note:** ~~Paragraph 23(h) of Annex V to the *Banking Consolidation Directive*~~ article 94(1)(b) of the *CRD*]

…

19A.3.40 R A *firm* must ensure that guaranteed variable *remuneration* is not part of prospective *remuneration* plans. A *firm* must not award, pay or provide guaranteed variable *remuneration* unless ~~it~~:

(1) it is exceptional;

(2) it occurs in the context of hiring new *Remuneration Code staff*; ~~and~~

(3) the firm has a sound and strong capital base; and

(4~~3~~) it is limited to the first year of service.

[**Note:** ~~Paragraph 23(j) of Annex V to the *Banking Consolidation Directive*~~ article 94(1)(d) and (e) of the *CRD* and Standard 11 of the *FSB Compensation Standards*]

…

19A.3.45 R A *firm* must ensure that payments ~~related~~ relating to the early termination of a contract reflect performance achieved over time and are designed in a way that does not reward failure or misconduct.

[**Note:** ~~Paragraph 23(m) of Annex V to the *Banking Consolidation Directive*~~ article 94(1)(h) of the *CRD* and Standard 12 of the *FSB Compensation Standards*]

…

19A.3.47 R (1) A *firm* must ensure that a substantial portion, which is at least 50%, of any variable *remuneration* consists of an appropriate balance of:

(a) …

(b) where ~~appropriate, *capital instruments* which are eligible for inclusion at stage B1 of the calculation in the *capital resources table*, where applicable~~ possible other instruments which are eligible as Additional Tier 1 instruments or are eligible as Tier 2 instruments or other instruments that can be fully converted to Common Equity Tier 1 instruments or written down, that in each case ~~that~~ adequately reflect~~s~~ the credit quality of the *firm* as a going concern and are appropriate for use as variable remuneration.

(2) …

[**Note:** ~~Paragraph 23(o) of Annex V to the *Banking Consolidation Directive*~~ article 94(1)(l) of the *CRD* and Standard 8 of the *FSB Compensation Standards*]

…

19A.3.49 R (1) …

…

(5) …

[**Note:** ~~Paragraph 23(p) of Annex V to the *Banking Consolidation Directive*~~ article 94(1)(m) of the *CRD* and Standards 6 and 7 of the *FSB Compensation Standards*]

(6) …

…

19A.3.51 R A *firm* must ensure that any variable *remuneration*, including a deferred portion, is paid or vests only if it is sustainable according to the financial situation of the *firm* as a whole, and justified ~~according to~~ on the basis of the performance of the *firm*, the business unit and the individual concerned.

19A.3.51A R A *firm* must:

(1) ensure that any of the total variable *remuneration* is subject to malus or clawback arrangements;

(2) set specific criteria for the application of malus and clawback; and

(3) ensure that the criteria for the application of malus and clawback in particular cover situations where the *employee*:

(a) participated in or was responsible for conduct which resulted in significant losses to the firm;

(b) failed to meet appropriate standards of fitness and propriety.

[**Note:** ~~Paragraph 23(q) of Annex V to the *Banking Consolidation Directive*~~ article 94(1)(n) of the CRD and Standards 6 and 9 of the *FSB Compensation Standards*]

…

Part 2: Comes into force on 1 July 2014.

4.3A.7 R (1) A *CRR firm* that is significant in terms of its size, internal organisation and the nature, the scope and the complexity of its activities must ensure that the members of the *management body* of the *firm* do not hold more than one of the following combinations of directorship in any organisation at the same time:

(a) one executive directorship with two non-executive directorships; and

(b) four non-executive directorships.

(2) (1) does not apply to members of the *management body* that represent the UK.

[**Note**: article 91(3) of the *CRD*]

CAPITAL REQUIREMENTS DIRECTIVE [(PASSPORTING)] AMENDMENT INSTRUMENT [No. XXX] 2013

Powers exercised

A. The Prudential Regulation Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137G (The PRA's general rules);
(2) section 137T (General supplementary powers); and
(3) paragraphs 19(10) and 20(4C) of Schedule 3 (Exercise of passport rights by UK firms).

B. The rule-making powers referred to above are specified for the purpose of section 138G (Rule-making instrument) of the Act.

Pre-conditions to making

C. In accordance with section 138J of the Act (consultation with the Financial Conduct Authority) ("FCA"), the PRA consulted the FCA. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

Commencement

D. Part 1 of the Annex to this instrument comes into force on 1 January 2014.

E. Part 2 of the Annex to this instrument shall come into force on a date specified by a subsequent PRA Board Instrument.

Amendments

F. The Supervisory manual (SUP) is amended in accordance with the Annex to this instrument.

Notes and Guidance

G. In the Annex to this instrument, the "notes" (indicated by "**Note:**") are included for the convenience of readers but do not form part of the legislative text.

H. The Prudential Regulation Authority gives as guidance each provision in the Annex that is marked with a G.

Citation

I. This instrument may be cited as the Capital Requirements Directive (Passporting) Amendment Instrument [No. XXX] 2013.

By order of the Board of the Prudential Regulation Authority
[DATE]

Annex

Amendments to the Supervision manual (SUP)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

Part 1: Comes into force on 1 January 2014.

13.2 Introduction

13.2.1 G This chapter gives *guidance* to *UK firms*. In most cases *UK firms* will be *authorised persons* under the *Act*. However, under the ~~*Banking Consolidation Directive*~~ *CRD*, a subsidiary of a *firm* which is a *credit institution* which meets the criteria set out in that Directive and in Commission Regulation also has an *EEA right*. Such an unauthorised subsidiary is known as a *financial institution*. References in this chapter to a *UK firm* include a *financial institution*.

…

13.3 Establishing a branch in another EEA State

…

13.3.2 G A *UK firm* other than a *UK pure reinsurer* cannot establish a *branch* in another *EEA State* for the first time under an *EEA right* unless the conditions in paragraphs 19(2), (4) and (5) of Part III of Schedule 3 to the *Act* are satisfied. It is an offence for a *UK firm* which is not an *authorised person* to contravene this prohibition (paragraph 21 of Part III of Schedule 3 to the *Act*). These conditions are that:

(1) the *UK firm* has given the *appropriate UK regulator,* in accordance with the *appropriate UK regulator's rules* (see *SUP* 13.5.1R) or the directly applicable regulations made under the CRD (see *SUP* 13.5.1C), notice of its intention to establish a *branch* (known as a *notice of intention*) which:

(a) identifies the activities which it seeks to carry on through the *branch*; and

(b) includes such other information as may be specified by the *appropriate UK regulator* (see *SUP* 13.5.1R) or by the directly applicable regulations made under the CRD (see *SUP* 13.5.1C);

(2) the *appropriate UK regulator* has given a notice (known as a *consent notice*) to the *Host State regulator,*

…

13.3.5 G (1) If the *UK firm's EEA right* derives from the ~~*Banking Consolidation Directive*~~ *CRD* or *MiFID*, the *appropriate UK regulator* will give the *Host State regulator* a *consent notice* within three *months* unless it has reason to doubt the adequacy of a *UK firm's* resources or its administrative structure. The *Host State regulator* then has a further two *months* to notify the *applicable provisions* (if any) and prepare for the supervision, as appropriate, of the *UK firm*, or in the case of a *MiFID investment firm*, to inform the *UK firm* that a *branch* can be established.

…

13.4 Providing cross border services into another EEA State

…

13.4.2F R A *UK firm* that wishes to provide cross-border services under the *CRD* must submit a notice to the *PRA* and comply with the information requirements set out in Commission Regulation (EU) …./…. and [Annex …] Commission Regulation (EU) …/…..[insert full citation and link to EU Regulations made under Article 39 *CRD*.][1]

[Note: article 39(1) to (4) of the CRD**]**

…

13.4.4 G (1) If the *UK firm's EEA right* derives from MiFID, the ~~*Banking Consolidation Directive*~~ *CRD* or the *UCITS Directive*, paragraph 20(3) of Part III of Schedule 3 to the Act requires the *appropriate UK regulator* to send a copy of the *notice of intention* to the Host State Regulator within *one month* of receipt. A *UK firm* passporting under the ~~*Banking Consolidation Directive*~~ *CRD* may start providing *cross border services* as soon as it satisfies the relevant conditions (see *SUP* 13.4.2G).

…

13.5 Notices of intention[2]

13.5.1 R A *UK firm*, other than a *UK pure reinsurer* or *a CRD credit institution*, wishing to establish a *branch* in a particular *EEA State* for the first time under an *EEA right* other than under the *auction regulation* must submit a *notice of intention* in the form set out in *SUP* 13 Annex 1R. [3]

…

13.5.1C R A *UK firm* wishing to establish a *branch* in a particular *EEA state* for the first time under the *CRD* must submit a notice to the *PRA* and comply with the information requirements set out in Commission Regulation (EU) …./…. and [Annex …] Commission Regulation (EU) …/…..[full citation and link to EU Regulations made under Article 35 and 36 *CRD*.]

[Note: article 35(1), (2) to (5) of the CRD**]**

13.5.2 R A *UK firm* wishing to provide *cross border services* into a particular *EEA State* for the first time under an *EEA right* other than under the *auction regulation* must submit a notice in the form set out in:

---

[1] This rule might not be made before 1 January 2014 as it is dependent on the timing of the adoption of the Commission Regulations to be adopted under Articles 39 of the Capital Requirements Directive. EBA has consulted on draft Regulations: see EBA Consultation on draft Passport Notification Regulations.

[2] These rule changes might not be made before 1 January 2014 as they are dependent on the timing of the adoption of the Commission Regulations to be adopted under Articles 35 and 36 of the Capital Requirements Directive.

[3] When the above Commission regulations become applicable, it is intended that the CRD section of the form in *SUP* 13 Annex 1R and the form in *SUP* 13 Annex 4R will be deleted or amended to cross refer to the directly applicable requirements in those Commission Regulations.

… ... …

(2) ~~*Sup*~~ *SUP* 13 Annex 4R[4] if the *UK firm* is passporting under the ~~*Banking Consolidation Directive*~~ *CRD*; or

…

13.5.6 G (1) A *UK firm* passporting under the ~~*Banking Consolidation Directive*~~ *CRD* the *Insurance Directives* or the *Reinsurance Directive* may have to submit the *requisite details* or relevant details in the language of the *Host State* as well as in English. For a *UK firm* passporting under the *Insurance Directives* this translated document will not include the relevant UK details. Further information is available from the *PRA* authorisations team.

…

13.6 Changes to branches

13.6.1 G Where a *UK firm* is exercising an *EEA right*, other than under the *Insurance Mediation Directive* (see *SUP* 13.6.9AG) or the *Reinsurance Directive* (see *SUP* 13.6.9BR) or the *CRD*, and has established a *branch* in another *EEA State*, any changes to the details of the *branch* are governed by the *EEA Passport Rights Regulations*. […]

…

Firms passporting under the ~~Banking Consolidation Directive~~ CRD and the UCITS Directive.

13.6.4 G If a *UK firm* has exercised an *EEA right*, under the ~~*Banking Consolidation Directive*~~ *CRD* or the *UCITS Directive*, and established a *branch* in another *EEA State*, regulation 11(1) states that the *UK firm* must not make a change in the *requisite details* of the *branch* (see *SUP* 13 Annex 1), unless it has satisfied the requirements of regulation 11(2)[5], or, where the change arises from circumstances beyond the *UK firm's* control, regulation 11(3) (see *SUP* 13.6.10G).

…

13.6.13 G If a *UK firm* is passporting under the ~~*Banking Consolidation Directive*~~ *CRD*, then regulation 11(7) provides that the *PRA* may not refuse to consent to a change unless, having regard to the change and to the EEA activities the *UK firm* is seeking to carry on, it doubts the adequacy of the administrative structure or the financial situation of the *UK firm*. In reaching its determination, the *PRA* may have regard to the adequacy of management, systems and the presence of relevant skills needed for the EEA activities to be carried on.

…

[4] See footnote 3.

[5] It is expected that regulation 11 will be amended to cross refer to the Commission regulations under Articles 35, 36 and 39 CRD. If regulation 11 is amended to no longer apply to CRD firms, this will necessitate an amendment here.

13.10 Applicable provisions

13.10.2 G *UK firms* passporting under the ~~*Banking Consolidation Directive*~~ *CRD* should note that, under the Directive, the *Host State* is responsible, together with the *PRA*, for monitoring the liquidity of a *branch* established by a *UK firm* in another *EEA State*.

…

13 Annex 1 Passporting: Notification of intention to establish a branch in another EEA state

R This annex consists of only one or more forms. Forms can be completed online now by visiting: ~~*http://www.fsa.gov.uk/Pages/doing/index.shtml*~~ http://www.bankofengland.co.uk/pra/Pages/authorisations/passporting/notifying.aspx
The forms are also to be found through the following address:
Passporting: Notification of intention to establish a branch in another EEA state - SUP 13 Annex 1

…..

13 Annex 4 Passporting: ~~Banking Consolidation Directive~~ Capital Requirements Directive

R This annex consists of only one or more forms. Forms can be completed online now by visiting: ~~*http://www.fsa.gov.uk/Pages/doing/index.shtml*~~ http://www.bankofengland.co.uk/pra/Pages/authorisations/passporting/notifying.aspx

The forms are also to be found through the following address:

Passporting: ~~Banking Consolidation Directive~~ Capital Requirements Directive - SUP 13 Annex 4

In the *SUP* 13 Annex 1 form, on page 1 substitute 'Capital Requirements Directive' for 'Banking Consolidation Directive'.

Throughout the form in *SUP* 13 Annex 4 substitute 'Capital Requirements Directive' for 'Banking Consolidation Directive' and 'CRD' for 'BCD'.

13A Qualifying for authorisation under the Act

…

13A.1.3 G (1) Under the *Gibraltar Order* made under section 409 of the *Act*, a Gibraltar firm is treated as an *EEA firm* under Schedule 3 to the *Act* if it is:

…

(b) authorised in Gibraltar under the ~~*Banking Consolidation Directive*~~ *CRD*; or

(c) authorised in Gibraltar under the *Insurance Mediation Directive*; or

…

13A.5 EEA firms providing cross border services into the United Kingdom

13A.5.3 G (1) …

…….

(2) For the purposes of paragraph 14(1)(b) of Part II of Schedule 3 to the *Act*, the information to be contained in the regulator's notice has been prescribed under regulation 3 of the *EEA Passport Rights Regulations*~~.~~, and in the case of the *CRD*, the information has been prescribed in Annex […] of Commission Regulation (EU) …/…. [insert full citation and link to Commission Regulation adopted under Article 39 *CRD*.]

The notification procedure

13A.5.4 G (1) Unless the *EEA firm* (other than an *EEA pure reinsurer* or an *EEA firm* that received authorisation under article 18 of the *auction regulation*) is passporting under the *Insurance Mediation Directive*, if the *appropriate UK regulator* receives a regulator's notice or, where no notice is required ~~(in the case of an *EEA firm* passporting under the *Banking Consolidation Directive*)~~, is informed of the *EEA firm's* intention to provide *cross border services* into the *United Kingdom*, the *appropriate UK regulator* will, under paragraphs 14(2) and 14(3) of Part II of Schedule 3 to the *Act*, notify the *EEA firm* of the *applicable provisions* (if any) within two *months* of the *day* on which the *appropriate UK regulator* received the regulator's notice or was informed of the *EEA firm's* intention.

….

13A Annex 1 Application of the Handbook to Incoming EEA Firms

1. ….		
….		
(1) Module of Handbook	**(2) Potential application to an incoming EEA firm with respect to activities carried on from an establishment of the firm (or its appointed representative) in the United Kingdom**	**(3) Potential application to an incoming EEA firm with respect to activities carried on other than from an establishment of the firm (or its appointed representative) in the United Kingdom**
…		
BIPRU	~~*EEA firms* are subject to the prudential standards~~	~~Does not apply if the *firm* has *permission* only for *cross border*~~

	~~of their home state regulator (*BIPRU 1.1.7 R* and *BIPRU 1.1.9 G*).~~ ~~However,~~ *BIPRU 12* applies to an *EEA firm* as respects the activities of its *UK branch*, but in relation to *liquidity risk* only.	~~*services* and does not carry on *regulated activities* in the *United Kingdom*.~~
…		
COMP	Applies, except in relation to the *passported activities* of a *MiFID investment firm*, a ~~*BCD*~~ <u>*CRD*</u> *credit institution* (other than an electronic money institution within the meaning of article 1(3)(a) of the *E-Money Directive* that has the right to benefit from the mutual recognition arrangements under the ~~*Banking Consolidation Directive*~~ <u>*CRD*</u>), an *IMD insurance intermediary* or a *UCITS management company* acting in that capacity other than in relation to a *UCITS scheme* (see the definition of "*participant firm*"). However, a *MiFID investment firm*, ~~*BCD*~~ <u>*CRD*</u> *credit institution*, an *IMD insurance intermediary* or a *UCITS management company* (when carrying on permitted *MiFID business*) may be able to apply for *top-up cover* in relation to its *passported activities* (see *COMP* 14 (Participation by EEA Firms)).	Does not apply in relation to the passported activities of an *MiFID investment firm*, or a ~~*BCD*~~ <u>*CRD*</u> *credit institution*, an *IMD insurance intermediary* or a *UCITS management company* acting in that capacity other than in relation to a *UCITS scheme* (see the definition of "*participant firm*"). Otherwise, *COMP* may apply, but the coverage of the *compensation scheme* is limited for non-*UK* activities (see *COMP* 5).

13A Annex 2 Matters reserved to a Home State regulator

Introduction	
…	
Requirements in the interest of the general good	
2.	The *Single Market Directives*, and the *Treaty* (as interpreted by the European Court of Justice) adopt broadly similar approaches to reserving responsibility to the *Home State regulator*. To summarise, the *FCA* or *PRA*, as *Host State regulator*, is entitled to impose requirements with respect to activities carried on within the *United Kingdom* if these can be justified in the interests of the "general good" and are imposed in a non-discriminatory way. This general proposition is

	subject to the following in relation to activities passported under the *Single Market Directives*:	
	(1)	….
	(2)	….
	(3)	for a ~~*BCD*~~ *CRD credit institution*, the *PRA* or *FCA*, as *Host State regulator*, is jointly responsible with the *Home State regulator* under article ~~41~~ 156 of the ~~*Banking Consolidation Directive*~~*CRD* for supervision of the liquidity of a *branch* in the *United Kingdom*;
	(4)	for a *MiFID investment firm* including a ~~*BCD*~~ *CRD credit institution* (which is a *MiFID investment firm*), the protection of *clients'* money and *clients'* assets is reserved to the *Home State regulator* under *MiFID*; and
	(5)	responsibility for participation in compensation schemes for ~~*BCD*~~ *CRD credit institutions* and *MiFID investment firm* is reserved in most cases to the *Home State regulator* under the *Deposit Guarantee Directive* and the *Investor Compensation Directive*.
…		

14.1 Application and Purpose

…

14.1.3 G (1) Under the *Gibraltar Order* made under section 409 of the *Act*, a Gibraltar firm is treated as an *EEA firm* under Schedule 3 to the *Act* if it is:

(a) authorised in Gibraltar under the *Insurance Directives*; or

(b) authorised in Gibraltar under the ~~*Banking Consolidation Directive*~~ *CRD*;

…

….

Purpose

14.1.4 G This chapter gives *guidance* on the *Act* and the *EEA Passport Rights Regulations* made under the *Act*, for an *incoming EEA firm* which has established a *branch* in, or is providing *cross border services* into, the *United Kingdom* and wishes to change the details of the *branch* or *cross border services*.

Note: An *EEA bank* is required to comply with the requirements set out in Commission Regulation (EU) …/…. and Commission Regulation (EU) …/….[insert full citation and link to Commission Regulation adopted under Articles 35, 36 and 39 CRD.]

…

14.2 Changes to branch details

…

Firms passporting under the ~~Banking Consolidation Directive~~ CRD and the UCITS Directive

14.2.2 G (1) Where an *incoming EEA firm* passporting under the ~~*Banking Consolidation Directive*~~ *CRD* or the *UCITS Directive* has established a *branch* in the *United Kingdom*, regulation 4 states that it must not make a change in the *requisite details* of the *branch* unless it has complied with the relevant requirements.

…

14.2.8 Changes arising from circumstances beyond the control of an incoming EEA firm passporting under the ~~*Banking Consolidation Directive*~~ *CRD,* UCITS Directive or Insurance Directive

…

14.6 Cancelling qualification for authorisation

Incoming EEA firms

14.6.1 G Section 34 of the *Act* states that an *incoming EEA firm* no longer qualifies for *authorisation* under Schedule 3 to the *Act* if it ceases to be an *incoming EEA firm* as a result of:

(1) …

(2) ceasing to have an *EEA right* in circumstances in which *EEA* authorisation is not required; this is relevant to a *financial institution* that is a subsidiary of a *credit institution* (of the kind mentioned in Article ~~19~~ 34 of the ~~*Banking Consolidation Directive*~~ *CRD*) which fulfils the conditions in articles ~~18 and 19~~ 33 and 34 of that *Directive*.

…

Financial institutions giving up right to authorisation

14.6.4 G Where a *financial institution* that is a subsidiary of a *credit institution* is passporting under the ~~*Banking Consolidation Directive*~~ *CRD* (see *SUP* 14.6.1G (2)), regulation 9(1) states that the *incoming EEA firm* may request the *PRA* to direct that its qualification for *authorisation* under Schedule 3 to the *Act* is cancelled from such date as may be specified in the direction.

…

15.1 Application

…

15.1.3 G In some cases, the application of provisions set out in *SUP* 15 Annex 1 depends on whether responsibility is reserved to a *Home State regulator*. ~~*SYSC* App 1 contains *guidance* on this.~~

…

Breaches of rules and other requirements in or under the Act

15.3.11 R (1) A *firm* must notify the *appropriate regulator* of:

(a) …

(da) a breach of a directly applicable provision in *the CRR* or any *directly applicable regulations made under CRD or CRR*; or

(e) …

…

15 Annex 1 Application of SUP 15 to incoming EEA firms and incoming Treaty firms

R

1 .	…
3 .	**For any other** *incoming EEA firm* **or** *incoming Treaty firm*, *SUP* 15 **applies as set out in the following table**.

Applicable sections		Application
SUP 15.1, *SUP* 15.2	**Application, Purpose**	**Apply in full**
SUP 15.3.1R to *SUP* 15.3.6 G	**Matters having a serious regulatory impact**	~~*SUP* 15.3.1R does not apply, otherwise apply in full~~ Apply in so far as responsibility for the matter in question is not reserved by an *EU* instrument to the *firm's Home State regulator*
….		
SUP 15.3.11 R to *SUP* 15.3.14 G	**Breaches of rules and other requirements in or under the Act**	**Apply in full**
SUP 15.3.15 R to *SUP* 15.3.16 G	**Civil, criminal or disciplinary proceedings against a firm**	**Apply in so far as responsibility for the matter in question is not reserved by an** *EU* **instrument to the** *firm's Home State regulator*
SUP 15.3.17 R to *SUP* 15.3.20 G	**Fraud, errors and other irregularities**	**Apply in so far as responsibility for the matter in question is not reserved by an** *EU* **instrument to the** *firm's Home State regulator*

Part 2: Comes into force on date specified by a subsequent PRA Board instrument.[6]

13A Annex 1 Application of the Handbook to Incoming EEA Firms

[6] It is intended that this annex will be commenced when the Commission Regulation introducing the LCR becomes applicable (Article 460 CRR).

….		
(1) Module of Handbook	**(2) Potential application to an incoming EEA firm with respect to activities carried on from an establishment of the firm (or its appointed representative) in the United Kingdom**	**(3) Potential application to an incoming EEA firm with respect to activities carried on other than from an establishment of the firm (or its appointed representative) in the United Kingdom**
PRIN	The *Principles* apply only in so far as responsibility for the matter in question is not reserved by an *EU* instrument to the *firm's Home State regulator* (*PRIN* 3.1.1R(1)). ~~For an *incoming EEA firm* which is a *BCD credit institution* without a *top-up permission*, *Principle* 4 applies only in relation to the liquidity of a branch established in the *United Kingdom* (*PRIN 3.1.1 R (2)*).~~	The *Principles* do not apply if the *firm* has *permission* only for *cross-border services* and does not carry on *regulated activities* in the *United Kingdom* (*PRIN* 3.1.1R(2)). The *Principles* have limited application for activities which are not carried on from a *UK* establishment (see *PRIN* 3.1.1R). Otherwise, see column (2).
….		
~~*BIPRU*~~	~~*BIPRU 12* applies to an *EEA firm* as respects the activities of its *UK branch*, but in relation to *liquidity risk* only.~~	
~~…~~		
SUP	**SUP 16 (Reporting requirements)** Parts of this chapter may apply if the *firm* has a *top-up permission* or if the *firm* is: (a) ~~a *bank*; or~~ [deleted] …..	**SUP 16 (Reporting requirements)** Parts of this chapter may apply if the *firm* has a *top-up permission* or if the *firm* is: (a) a *depositary* of an *ICVC*; or …..
…		

13A Annex 2 Matters reserved to a Home State regulator

Introduction		
…		
Requirements in the interest of the general good		
2.	The *Single Market Directives*, and the *Treaty* (as interpreted by the European Court of Justice) adopt broadly similar approaches to reserving responsibility to the *Home State regulator*. To summarise, the *FCA* or *PRA*, as *Host State regulator*, is entitled to impose requirements with respect to activities carried on within the *United Kingdom* if these can be justified in the interests of the "general good" and are imposed in a non-discriminatory way. This general proposition is subject to the following in relation to activities passported under the *Single Market Directives*:	
	(1)	….
	(2)	….
	(3)	~~for a *BCD credit institution*, the *PRA* or *FCA*, as *Host State regulator*, is jointly responsible with the *Home State regulator* under article 41 of the *Banking Consolidation Directive* for supervision of the liquidity of a *branch* in the *United Kingdom*;~~ [deleted]
…		

PRA RULEBOOK CRR FIRMS: DEFINITION OF CAPITAL INSTRUMENT 2013

Powers exercised

A. The Prudential Regulation Authority ("PRA") makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137G (the PRA's general rules);
(2) section 137T (general supplementary powers); and

B. The rule-making powers referred to above are specified for the purpose of section 138G(2) (Rule-making instrument) of the Act.

Pre-conditions to making

C. In accordance with section 138J of the Act (consultation with the Financial Conduct Authority) ("FCA"), the PRA consulted the FCA. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

PRA Handbook CRR Firms: Definition of Capital Instrument 2013

D. The PRA makes the rules in Annex A to this instrument.

Commencement

E. This instrument comes into force on 1 January 2014.

Citation

F. This instrument may be cited as the PRA Rulebook CRR Firms: Definition of Capital Instrument 2013.

By order of the Board of the Prudential Regulation Authority
[DATE]

Annex A

In this Annex, the text is all new and is not underlined.

Part

DEFINITION OF CAPITAL

Chapter content

Links

1 APPLICATION AND DEFINITIONS

1.1 Unless otherwise stated, this Part applies to every *firm* that is a *CRR firm*.

1.2 Unless otherwise defined, any italicised expression used in this Part and in the *CRR* has the same meaning as in the *CRR*.

2 HOLDINGS OF OWN FUNDS INSTRUMENTS ISSUED BY FINANCIAL SECTOR ENTITIES INCLUDED IN THE SCOPE OF CONSOLIDATED SUPERVISION

2.1 For the purposes of calculating *own funds* on an individual basis and a *sub-consolidated basis*, *firms* subject to supervision on a *consolidated basis* must deduct the relevant percentage of holdings of *own funds instruments* issued by *financial sector entities* included in the scope of consolidated supervision in accordance with Part Two of the *CRR*, except where the exception in 2.3 or 2.6 applies.

2.2 For the purposes of 2.1 the relevant percentage is as follows:

(1) 50% for the period from 1 January 2014 to 31 December 2014;

(2) 60% for the period from 1 January 2015 to 31 December 2015;

(3) 70% for the period from 1 January 2016 to 31 December 2016;

(4) 80% for the period from 1 January 2017 to 31 December 2017;

(5) 90% for the period from 1 January 2018 to 31 December 2018; and

(6) 100% for the period after 31 December 2018.

2.3 A *firm* must not apply the deduction in 2.1 to its holdings of *own funds instruments* issued by a venture capital investor that is included in the scope of consolidated supervision of the *firm*.

2.4 For the purposes of this Chapter, a venture capital investor is a *financial institution*, in relation to which:

(1) the sole purpose is to make venture capital investments and carry out unregulated activities in relation to the administration of venture capital investments; and

(2) none of its venture capital investments is in a *credit institution* or a *financial institution*, the principal activity of which is to perform any activity other than the acquisition of holdings in other undertakings (within the meaning of section of section 1161(1) of the Companies Act 2006).

2.5 For the purposes of this Chapter, a venture capital investment is a designated investment which, at the time the investment is made, is:

(1) in a new or developing company or venture; or

(2) in a management buy-out or buy-in; or

(3) made as a means of financing the investee company or venture and accompanied by a right of consultation, or rights to information, or board representation, or management rights; or

(4) acquired with a view to, or in order to, facilitate a transaction falling within (1) to (3).

2.6 For the purposes of this Chapter, a designated investment is a security or contractually-based investment specified in articles 76 to 85 and 89 of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001.

2.7 A *firm* must not apply the deduction in 2.1 to that percentage of its holdings of *own funds instruments* issued by a venture capital holding company included in the scope of consolidated supervision of the *firm* that represents the value of the venture capital holding company's investment in venture capital investors.

2.8 For the purposes of this Chapter, a venture capital holding company is a *financial institution*, in respect of which:

(1) it is a *financial institution* solely by reason of its principal activity being the acquiring of holdings;

(2) it holds shares (in the meaning of s. 76 of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001) in a venture capital investor;

(3) the proportion of the value of the venture capital holding company attributable to investment in Venture Capital Investors and the proportion of the value of the venture capital holding company attributable to other investments can be identified and valued on a regular basis

[Note: Art 49(2) of the *CRR*]

3 QUALIFYING HOLDINGS OUTSIDE THE FINANCIAL SECTOR

3.1 In respect of the qualifying holdings described in Article 89(1) and (2) of the *CRR*, a *firm* must, in accordance with Article 89(3), comply with the requirement in Article 89(3)(a).

[Note: Art 89(3) of the *CRR*]

4 CONNECTED FUNDING OF A CAPITAL NATURE

4.1 This Chapter applies only to *UK banks*.

4.2 A *UK bank* must not avoid the requirements of the *CRR* by structuring its investments as connected funding of a capital nature.

4.3 A *UK bank* must treat all connected funding of a capital nature as a holding of capital of the connected party and apply to it the treatment under the *CRR* applicable to such a holding, including any reporting or disclosure requirements in respect of such holding.

4.4 If the connected party is *financial sector entity*, the *UK bank* must treat the connected funding of a capital nature as a holding of *Common Equity Tier 1 instruments*, *Additional Tier 1 instruments* or *Tier 2 instruments* of the connected party, as appropriate in light of the funding's characteristics when compared to the characteristics of each type of *own funds instruments*.

4.5 A *UK bank* must report to the *PRA* all connected funding of a capital nature at least 30 days in advance of entry into the relevant funding transaction and identify each relevant transaction with sufficient detail to allow the *PRA* to evaluate it.

4.6 A loan or other funding transaction is connected funding of a capital nature if it is made by the *UK bank* to a connected party and:

(1) based on its terms and other factors of which the UK bank is aware, the connected party would be able to consider it from the point of view of its characteristics as capital as being similar to an *own funds instrument*; or

(2) the position of the *UK bank* from the point of view of maturity and repayment is inferior to that of the senior unsecured and unsubordinated creditors of the connected party.

4.7 A loan or other funding transaction is also connected funding of a capital nature if it:

(1) funds directly or indirectly a loan to a connected party that has the characteristics described in 4.6 or of a capital investment in a connected party; or

(2) has itself the characteristics described in 4.6.

4.8 A guarantee is connected funding of a capital nature if it is a guarantee by the *UK bank* of a loan or other funding transaction from a third party to a connected party of the *UK bank* and:

(1) the loan or other funding transaction has the characteristics described in 4.6 or the characteristics described in 4.7; or

(2) the rights that the *UK bank* would have against the connected party have the characteristics described in 4.6(2).

4.9 For the purposes of this Chapter and in relation to a *UK bank*, a connected party means another person ("P") in respect of whom the *UK bank* has not been permitted to apply the individual consolidation method under Article 8 of the *CRR* and one of the following applies:

(1) P is closely related to the *UK bank*;

(2) P is an associate of the *UK bank*; or

(3) the same persons significantly influence the *management body* of P and the *UK bank*.

4.10 For the purposes of 4.9(1), a *UK bank* and another person are closely related when:

(1) the insolvency of one of them is likely to be associated with the insolvency or default of the others;

(2) it would be prudent when assessing the financial condition or creditworthiness of one to consider that of the other; or

(3) there is, or there is likely to be, a close relationship between the financial performance of the *UK bank* and that person.

4.11 For the purposes of 4.9(2), a person is an associate of a *UK bank* if it is:

(1) in the same group as the *UK bank*;

(2) an appointed representative (in the sense of section 39 of *FSMA 2000*) or tied agent (as described in Article 4(1)(25) of *MiFID*) of the *UK bank* or a member of the *UK bank*'s group; or

(3) any other person whose relationship with the *UK bank* or a member of the *UK bank*'s group might reasonably be expected to give rise to a community of interest between them which may involve a conflict of interest in dealings with third parties.

5 CONNECTED TRANSACTIONS

5.1 In determining whether an item of capital qualifies as a *Common Equity Tier 1 item*, an *Additional Tier 1 item* or a *Tier 2 item* a *firm* must take into account any connected transaction which, when taken together with the item of capital, would cause it not to display the characteristics of a *Common Equity Tier 1 item*, an *Additional Tier 1 item* or a *Tier 2 item*.

5.2 A *firm* must report to the *PRA* all connected transactions described in 5.1 at least 30 days in advance of entry into the relevant transaction and identify each relevant transaction with sufficient detail to allow the *PRA* to evaluate it.

6 OWN FUNDS INSTRUMENTS ISSUED UNDER NON-EEA LAW

6.1 A *firm* must demonstrate to the *PRA* that any *Additional tier 1 instruments* or *Tier 2 instruments* issued by it that are governed by the law of a *third country* are by their terms capable, as part of a resolution of the *firm*, of being written down or converted into *Common Equity Tier 1 instruments* of the *firm* to the same extent as an equivalent *own funds instrument* issued under the law of the United Kingdom.

6.2 A *firm* must include in the materials it provides to the *PRA* under 6.1 a properly reasoned independent legal opinion from an individual appropriately qualified in the relevant *third country*.

7 NOTIFICATION REGIME - ISSUANCE

7.1 A *firm* shall notify the *PRA* in writing of its intention, or the intention of another member of its *group* that is not a *firm* but is included in the supervision on a consolidated basis of the *firm*, to issue a capital instrument that it believes will qualify under the *CRR* as an *own funds instrument* at least thirty days before the intended date of issue. This rule does not apply to the capital instruments described in 7.3 below.

7.2 When giving notice under 7.1, the *firm* shall provide:

(1) details of the amount and type of *own funds* the *firm* is seeking to raise through the intended issue and whether the capital instruments are intended to be issued to external investors or to other members of its *group*;

(2) a copy of the term sheet and details of any features of the capital instrument which are novel, unusual or different from a capital instrument of a similar nature previously issued by the *firm* or widely available in the market;

(3) confirmation from a member of the *firm's senior management* responsible for authorising the intended issue or, in the case of an issue by another *group* member, for the issue's inclusion in the *firm*'s consolidated *own funds*, that the capital instrument meets the conditions for qualification as an own funds instrument; and

(4) a properly reasoned independent legal opinion from an appropriately qualified individual confirming that the capital instrument meets the conditions for qualification as the relevant type of *own funds instrument*.

7.3 The *firm* does not have to give notice under 7.1 if the capital instrument is:

(1) an ordinary share; or

(2) a debt instrument issued under a debt securities programme under which the *firm* or *group* member has previously issued and the *firm* has notified the *PRA* in accordance with this Chapter prior to a previous issuance under the programme.

7.4 A *firm* shall notify the *PRA* in writing no later than the date of issue of its intention, or the intention of another member of its *group* that is not a *firm* but is included in the supervision on a consolidated basis of the *firm*, to issue a capital instrument described in 7.3.

7.5 When giving notice under 7.4, the *firm* shall provide:

(1) confirmation that the terms of the capital instrument have not changed since the previous issue by the *firm* of that type of capital instrument; and

(2) the items described in 7.2(1) and (3).

7.6 The *firm* shall notify the *PRA* in writing of any change to the intended date of issue, amount of issue, type of investors, type of *own funds instrument* or any other feature of the capital instrument to that previously notified to the *PRA* under 7.1 or 7.4.

8 NOTIFICATION REGIME - AMENDMENT

8.1 A *firm* shall notify the *PRA* in writing of its intention, or the intention of another member of its *group* that is not a *firm* but is included in the supervision on a consolidated basis of the *firm*, to amend or otherwise vary the terms of any *own funds instrument* included in its *own funds* or the *own funds* of its consolidated group at least thirty days before the intended date of such amendment or other variation.

9 NOTIFICATION REGIME – REDUCTION OF OWN FUNDS

9.1 A *firm* shall notify the *PRA* of its intention, or the intention of another member of its *group* that is not a *firm* but is included in the supervision on a consolidated basis of the *firm*, to carry out in respect of an *own funds instrument* any of the actions described in Article 77 of the *CRR*.

10 BUILDING SOCIETIES – CREDITOR HIERARCHY

10.1 This Chapter applies only to *building societies*.

10.2 A *building society* must ensure that any *Additional Tier 1 instrument* or *Tier 2 instrument* issued by it is contractually subordinated to its non-deferred shares.

11 TRANSITIONAL PROVISIONS FOR OWN FUNDS

11.1 The *Common Equity Tier 1 capital ratio* which *firm*s must under Article 465(1)(a) of the *CRR* meet or exceed for the period from 1 January 2014 until 31 December 2014 shall be 4.0%.

[**Note: Art 465(1)(a) of the *CRR*]**

11.2 The *Tier 1 capital ratio* which *firm*s must under Article 465(1)(b) of the *CRR* meet or exceed for the period from 1 January 2014 until 31 December 2014 shall be 5.5%.

[Note: Art 465(1)(b) of the *CRR*]

11.3 The applicable percentage for the purposes of Article 467(1) of the *CRR* shall be:

(1) 100% during the period from 1 January 2014 to 31 December 2014;

(2) 100% during the period from 1 January 2015 to 31 December 2015;

(3) 100% during the period from 1 January 2016 to 31 December 2016; and

(4) 100% for the period from 1 January 2017 to 31 December 2017.

[Note: Art 467 of the *CRR*]

11.4 The applicable percentage for the purposes of Article 468(1) of the *CRR* shall be:

(1) 60% during the period from 1 January 2015 to 31 December 2015;

(2) 40% during the period from 1 January 2016 to 31 December 2016; and

(3) 20% for the period from 1 January 2017 to 31 December 2017.

[Note: Art 468(1)-(3) of the *CRR*]

11.5 The applicable percentage for the purposes of Article 468(4) of the *CRR* shall be:

(1) 0% for the period from 1 January 2014 to 31 December 2014;

(2) 0% for the period from 1 January 2015 to 31 December 2015;

(3) 0% for the period from 1 January 2016 to 31 December 2016; and

(4) 0% for the period from 1 January 2017 to 31 December 2017.

[Note: Art 468(4), 478(1) of the *CRR*]

11.6 The applicable percentage for the purposes of Article 469(1)(a) of the CRR as it applies to the items referred to in points (a)-(b) and (d)-(h) of Article 36(1) shall be:

(1) 100% during the period from 1 January 2014 to 31 December 2014;

(2) 100% during the period from 1 January 2015 to 31 December 2015;

(3) 100% during the period from 1 January 2016 to 31 December 2016; and

(4) 100% for the period from 1 January 2017 to 31 December 2017.

[Note: Art 469(1)(a), 478(1) of the *CRR*]

11.7 The applicable percentage for the purposes of Article 469(1)(c) of the *CRR* as it applies to the items referred to in point (c) of Article 36(1) that existed prior to 1 January 2014 shall be:

(1) 100% for the period from 1 January 2014 to 2 January 2015;

(2) 100% for the period from 2 January 2015 to 2 January 2016;

(3) 100% for the period from 2 January 2016 to 2 January 2017;

(4) 100% for the period from 2 January 2017 to 2 January 2018;

(5) 100% for the period from 2 January 2018 to 2 January 2019;

(6) 100% for the period from 2 January 2019 to 2 January 2020;

(7) 100% for the period from 2 January 2020 to 2 January 2021;

(8) 100% for the period from 2 January 2021 to 2 January 2022;

(9) 100% for the period from 2 January 2022 to 2 January 2023; and

(10) 100% for the period from 2 January 2023 to 2 January 2024.

[Note: Art 469(1)(c), 478(2) of the *CRR*]

11.8 The applicable percentage for the purposes of Article 469(1)(c) of the *CRR* as it applies to the items referred to in point (c) of Article 36(1) that did not exist prior to 1 January 2014 and the items referred to in point (i) of Article 36(1) shall be:

(1) 100% during the period from 1 January 2014 to 31 December 2014;

(2) 100% during the period from 1 January 2015 to 31 December 2015;

(3) 100% during the period from 1 January 2016 to 31 December 2016; and

(4) 100% for the period from 1 January 2017 to 31 December 2017.

[Note: Art 469(1)(c), 478(1) of the *CRR*]

11.9 The applicable percentage for the purposes of Article 474(a) of the *CRR* shall be:

(1) 20% during the period from 1 January 2014 to 31 December 2014;

(2) 40% during the period from 1 January 2015 to 31 December 2015;

(3) 60% during the period from 1 January 2016 to 31 December 2016; and

(4) 80% for the period from 1 January 2017 to 31 December 2017.

[Note: Art 474(a), 478(1) of the *CRR*]

11.10 The applicable percentage for the purposes of Article 476(a) of the *CRR* shall be:

(1) 20% during the period from 1 January 2014 to 31 December 2014;

(2) 40% during the period from 1 January 2015 to 31 December 2015;

(3) 60% during the period from 1 January 2016 to 31 December 2016; and

(4) 80% for the period from 1 January 2017 to 31 December 2017.

[Note: Art 476(a), 478(1) of the *CRR*]

11.11 The applicable percentage for the purposes of Article 479(2) of the *CRR* shall be:

(1) 0% for the period from 1 January 2014 to 31 December 2014;

(2) 0% for the period from 1 January 2015 to 31 December 2015;

(3) 0% for the period from 1 January 2016 to 31 December 2016; and

(4) 0% for the period from 1 January 2017 to 31 December 2017.

[Note: Art 479 of the *CRR*]

11.12 The applicable factor for the purposes of Article 480(1) of the *CRR* as it applies to point (b) of Article 84(1) shall be:

(1) 1 in the period from 1 January 2014 to 31 December 2014;

(2) 1 in the period from 1 January 2015 to 31 December 2015;

(3) 1 in the period from 1 January 2016 to 31 December 2016; and

(4) 1 in the period from 1 January 2017 to 31 December 2017.

[**Note: Art 480 of the *CRR*]**

11.13 The applicable factor for the purposes of Article 480(1) of the *CRR* as it applies to point (b) of Article 85(1) and point (b) of Article 87(1) shall be:

(1) 0.2 in the period from 1 January 2014 to 31 December 2014;

(2) 0.4 in the period from 1 January 2015 to 31 December 2015;

(3) 0.6 in the period from 1 January 2016 to 31 December 2016; and

(4) 0.8 in the period from 1 January 2017 to 31 December 2017.

[**Note: Art 480 of the *CRR*]**

11.14 The applicable percentage for the purposes of Article 481(1) of the *CRR* shall be:

(1) 0% for the period from 1 January 2014 to 31 December 2014;

(2) 0% for the period from 1 January 2015 to 31 December 2015;

(3) 0% for the period from 1 January 2016 to 31 December 2016; and

(4) 0% for the period from 1 January 2017 to 31 December 2017.

[Note: Art 481 of the *CRR*]

11.15 The applicable percentage for the purposes of Article 486(2), (3) and (4) of the *CRR* shall be:

(1) 80% for the period from 1 January 2014 to 31 December 2014;

(2) 70% for the period from 1 January 2015 to 31 December 2015;

(3) 60% for the period from 1 January 2016 to 31 December 2016;

(4) 50% for the period from 1 January 2017 to 31 December 2017;

(5) 40% for the period from 1 January 2018 to 31 December 2018;

(6) 30% for the period from 1 January 2019 to 31 December 2019;

(7) 20% for the period from 1 January 2020 to 31 December 2020; and

(8) 10% for the period from 1 January 2021 to 31 December 2021.

[Note: Art 486 of the *CRR*]

PRA RULEBOOK CRR FIRMS: BENCHMARKING OF INTERNAL APPROACHES AND CREDIT RISK INSTRUMENT 2013

Powers exercised

A. The Prudential Regulation Authority (the "PRA") makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137G (The PRA's general rules); and
(2) section 137T (General supplementary powers).

B. The rule-making powers listed above are specified for the purpose of section 138G(2) (Rule-making instruments) of the Act.

Pre-conditions to making

C. In accordance with section 138J of the Act (Consultation by the PRA), the PRA consulted the Financial Conduct Authority. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

PRA Rulebook CRR Firms: Benchmarking of internal Approaches and Credit Risk Instrument 2013

D. The PRA makes the rules in Annexes A and B to this Instrument.

Commencement

E. Subject to F and G, this instrument comes into force on 1 January 2014.

F. Rule 2.2. in Annex A comes into force on the date specified by subsequent PRA Board Instrument.

G. Rule 5 in Annex B comes into force on 31 January 2014.

Citation

H. This instrument may be cited as the PRA Rulebook CRR Firms: Benchmarking of internal Approaches and Credit Risk Instrument 2013.

By order of the Board of the Prudential Regulation Authority
[Date]

Annex A

In this Annex, the text is all new and is not underlined.

Part

BENCHMARKING OF INTERNAL APPROACHES

Chapter content

1. **APPLICATION AND DEFINITIONS**
2. **SUPERVISORY BENCHMARKING OF INTERNAL APPROACHES FOR CALCULATING OWN FUNDS REQUIREMENTS**

Links

1 APPLICATION AND DEFINITIONS

1.1 This Part applies to every firm that is a *CRR firm*.

1.2 Unless otherwise defined, any italicised expression used in this Part and in the *CRD* has the same meaning as in the *CRD*.

2 SUPERVISORY BENCHMARKING OF INTERNAL APPROACHES FOR CALCULATING OWN FUNDS REQUIREMENTS

2.1 Except for *operational risk,* a *firm* that is permitted to use *internal approaches* for the calculation of risk weighted *exposure* amounts or *own funds* requirements must report annually to the *PRA*:

(1) the results of the calculations of their *internal approaches* for their *exposures* or positions that are included in the benchmark portfolios; and

(2) an explanation of the methodologies used to produce those calculations.

2.2 *A firm* shall submit the results of the calculations referred to in 2.1 above to the *PRA* and to *EBA* in accordance with the template set out in the Commission Regulation adopted under Article 78(8) of the *CRD*.

[Note: Art 78(1) and (2) of the *CRD*]

Annex B

In this Annex, the text is all new and is not underlined.

Part

CREDIT RISK

Chapter content

1. **APPLICATION AND DEFINITIONS**
2. **STANDARDISED APPROACH – TREATMENT OF EXPOSURES TO REGIONAL GOVERNMENTS**
3. **INTERNAL RATINGS BASED APPROACH – REQUIREMENTS – RISK QUANTIFICATION**
4. **SECURITISATION – RECOGNITION OF SIGNIFICANT RISK TRANSFER**
5. **CRITERIA FOR CERTAIN EXPOSURES SECURED BY MORTGAGES ON COMMERCIAL IMMOVABLE PROPERTY**
6. **SETTLEMENT RISK**

Links

1 APPLICATION AND DEFINITIONS

1.1 This Part applies to every firm that is a *CRR firm*.

1.2 In this Part, the following definition shall apply:

Exposure an asset or off-balance sheet item as defined for credit risk purposes by Article 5(1) of the *CRR.*

Loss economic loss, including material discount effects, and material direct and indirect costs associated with collecting on the instrument as defined for credit risk purposes by Article 5(2) of the *CRR*

1.3 Unless otherwise defined, any italicised expression used in this Part and in the *CRR* has the same meaning as in the *CRR*.

2 STANDARDISED APPROACH – TREATMENT OF EXPOSURES TO REGIONAL GOVERNMENTS

2.1 For the purposes of Article 115 of the *CRR*, a *firm* may treat *exposures* to the following regional governments as *exposures* to the *UK* central government:

(1) The Scottish Parliament;

(2) The National Assembly for Wales; and

(3) The Northern Ireland Assembly.

[Note: Art 115 of the *CRR*]

3 INTERNAL RATINGS BASED APPROACH – REQUIREMENTS – RISK QUANTIFICATION

3.1 For the purposes of Article 178(2)(d) of the *CRR*, a *firm* must treat a credit obligation as material:

(1) in relation to a retail *exposure*:

(a) where a *firm* applies the definition of default at the level of an individual credit facility, the amount of the credit obligation exceeds £100;

(b) where a *firm* applies the definition of default in relation to the total obligations of a borrower, the amount of the total obligations of the borrower to the *firm* exceed £100; and

(2) in all other cases, where the amount of the credit obligation exceeds £1,000.

[Note: Art 178(2) of the *CRR*]

4 SECURITISATION – RECOGNITION OF SIGNIFICANT RISK TRANSFER

4.1 A *firm* must notify the *PRA* that it is relying on the deemed transfer of significant credit risk under paragraph 2 of Article 243 of the *CRR* or paragraph 2 of Article 244 of the *CRR* no later than one month after the date of the transfer.

4.2 The notification in 4.1 must include sufficient information to allow the *PRA* to assess whether the possible reduction in risk weighted *exposure* amounts which would be achieved by the *securitisation* is justified by a commensurate transfer of credit risk to third parties.

5 CRITERIA FOR CERTAIN EXPOSURES SECURED BY MORTGAGES ON COMMERCIAL IMMOVABLE PROPERTY

5.1 For the purposes of Articles 124(2) and 126(2) of the *CRR* and in addition to the conditions set out therein*,* a *firm* may only treat *exposures* as fully and completely secured by mortgages on commercial immovable property in accordance with Article 126 where annual average *losses* stemming from lending secured by mortgages on commercial property in the *UK* did not exceed 0.5% of risk-weighted exposure amounts over a representative period. A firm shall calculate the *loss* level referred to in this rule on the basis of the aggregate market data for commercial property lending published by the *PRA* in accordance with Article 101.3 of the *CRR*.

5.2 For the purposes of this rule, a representative period shall be a time horizon of sufficient length and which includes a mix of good and bad years.

[Note: Arts. 124(2) and 126(2) of the *CRR*]

6 SETTLEMENT RISK

6.1 In accordance with Article 380 of the *CRR*, where a system wide failure of a settlement system, a clearing system or a *CCP* occurs, the *own funds* requirements calculated as set out in Articles 378 and 379 of the *CRR* are waived until the situation is rectified. In this case, the failure of a counterparty to settle a trade shall not be deemed a default for purposes of credit risk.

[Note: Art. 380 of the *CRR*]

PRA RULEBOOK CRR FIRMS: COUNTERPARTY CREDIT RISK INSTRUMENT 2013

Powers exercised

A. The Prudential Regulation Authority ("PRA") makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137G (the PRA's general rules); and
(2) section 137T (general supplementary powers).

B. The rule-making powers referred to above are specified for the purpose of section 138G (2) (Rule-making instrument) of the Act.

Pre-conditions to making

C. In accordance with section 138J of the Act (consultation with the Financial Conduct Authority) ("FCA"), the PRA consulted the FCA. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

PRA Rulebook CRR Firms: Counterparty Credit Risk Instrument 2013

D. The PRA makes the rules in Annex A to this Instrument.

Commencement

E. This instrument comes into force on 1 January 2014.

Citation

F. This instrument may be cited as the PRA Rulebook CRR Firms: Counterparty Credit Risk Instrument 2013.

By order of the Board of the Prudential Regulation Authority
[DATE]

Annex A

In this Annex, the text is all new and is not underlined.

Part

COUNTERPARTY CREDIT RISK

Chapter content

Links

1 APPLICATION AND DEFINTIONS

1.1 This Part applies to every firm that is a *CRR firm*.

1.2 In this Part the following definitions shall apply:

CCR Mark-to-Market method

means the method set out in in Chapter Six, Section 3 of the *CRR*.

interest-rate contract

means an interest rate contract of a type listed in paragraph 1 of Annex II of the *CRR*.

1.3 Unless otherwise defined, any italicised expression used in this Part and in the *CRR* has the same meaning as in the *CRR*.

2 HEDGING SETS

2.1 For the purpose of Article 282(6) of the CRR, a firm must apply the *CCR Mark-to-Market method* to:

(a) *transactions* with a non-linear risk profile; or

(b) *payment legs* and *transactions* with debt instruments as underlying

for which it cannot determine the delta or modified duration, as the case may be, using an internal model approved by the PRA under Title IV of the CRR for the purposes of determining *own funds* requirements for *market risk*.

2.2 For the purposes of 2.1, a *transaction* means a transaction to which Chapter Six of the CRR applies.

3 RECOGNITION OF NETTING: INTEREST RATE DERIVATIVES

3.1 For the purpose of Article 298(4) of the *CRR*, a *firm* must use the original maturity of the *interest-rate contract*.

PRA RULEBOOK CRR FIRMS: MARKET RISK INSTRUMENT 2013

Powers exercised

A. The Prudential Regulation Authority ("PRA") makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137G (the PRA's general rules); and
(2) section 137T (general supplementary powers).

B. The rule-making powers referred to above are specified for the purpose of section 138G (2) (Rule-making instrument) of the Act.

Pre-conditions to making

C. In accordance with section 138J of the Act (consultation with the Financial Conduct Authority) ("FCA"), the PRA consulted the FCA. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

PRA Rulebook CRR Firms: Market Risk Instrument 2013

D. The PRA makes the rules in Annex A to this Instrument.

Commencement

E. This instrument comes into force on 1 January 2014.

Citation

F. This instrument may be cited as the PRA Rulebook CRR Firms: Market Risk Instrument 2013.

By order of the Board of the Prudential Regulation Authority
[DATE]

Annex A

In this Annex, the text is all new and is not underlined.

Part

MARKET RISK

Chapter content

Links

1 APPLICATION AND DEFINTIONS

1.1 This Part applies to every firm that is a *CRR firm*.

1.2 In this Part the following definitions shall apply:

convertible bond

means a *security* which gives the investor the right to convert the security into a share at an agreed price on an agreed basis*.*

equity

means a *share.*

security

has the meaning specified in Article 3(1) of the *Regulated Activities Order.*

share

means the investment specified in Article 76 of the *Regulated Activities Order.*

1.3 Unless otherwise defined, any italicised expression used in this Part and defined in the *CRR* has the same meaning as in the *CRR*.

2 USE OF INTERNAL MODELS: RISK CAPTURE

2.1 A *firm* which has a permission to use internal models in accordance with Title IV, Chapter 5 of the *CRR:*

(a) must identify any material risks, or risks that when considered in aggregate are material, which are not captured by those models; and

(b) must ensure that it holds own funds to cover those risk(s) in additional to those required to meet its *own funds* requirement calculated in accordance with Title IV, Chapter 5 of the *CRR*.

3 NETTING: CONVERTIBLE BONDS

3.1 For the purposes of Article 327(2) of the *CRR*, the netting of a *convertible bond* and an offsetting position in the instrument underlying is permitted. The *convertible bond* should be:

(a) treated as a position in the *equity* into which it converts; and

(b) the *firm's own funds* requirement for the general and specific risk in its equity instruments should be adjusted by making:

(i) an addition equal to the current value of any loss which the *firm* would make if it did convert to *equity*; or

(ii) a deduction equal to the current value of any profit which the *firm* would make if it did convert to *equity* (subject to a maximum deduction equal to the *own funds requirements* on the notional position underlying the *convertible bond*).

4 INSTRUMENTS FOR WHICH NO TREATMENT SPECIFIED

4.1 (1) Where a *firm* has a position in a *financial instrument* for which no treatment has been specified in the *CRR*, it must calculate its *own funds* requirement for that position by applying the most appropriate *rules* relating to positions that are specified in the *CRR*, if doing so is prudent and appropriate, and if the position is sufficiently similar to those covered by the relevant *rules*.

(2) A *firm* must document its policies and procedures for calculating own funds for such positions in its *trading book policy statement*.

(3) If there are no appropriate treatments the *firm* must calculate an *own funds* requirement of an appropriate percentage of the current value of the position. An appropriate percentage is either 100%, or a percentage that takes into account the characteristics of the position.

(4) For the purposes of this rule, *trading book policy statement* means the statement of policies and procedures relating to the *trading book*.

PRA RULEBOOK CRR FIRMS: GROUPS INSTRUMENT 2013

Powers exercised

A. The Prudential Regulation Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137G (The PRA's general rules); and
(2) section 137T (General supplementary powers).

B. The rule-making powers referred to above are specified for the purpose of section 138G (Rule-making instrument) of the Act.

Pre-conditions to making

C. In accordance with section 138J of the Act (consultation with the Financial Conduct Authority) ("FCA"), the PRA consulted the FCA. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

PRA Rulebook CRR Firms: Groups Instrument 2013

D. The PRA makes the rules in Annex A to this instrument.

Commencement

E. Annex A of this instrument comes into force on 1 January 2014.

Citation

F. This instrument may be cited as the PRA Rulebook CRR Firms: Groups Instrument 2013.

By order of the Board of the Prudential Regulation Authority
[DATE]

Annex A

In this Annex, the text is all new and is not underlined.

Part

GROUPS

Chapter content

Links

1 APPLICATION AND DEFINITIONS

1.1 This Part applies to every firm that is a *CRR firm*.

1.2 In this Part the following definitions shall apply:

Article 12(1) relationship

means a relationship where undertakings are linked by a relationship within the meaning of Article 12(1) of Directive 83/349 EEC.

Article 18(5) relationship

means a relationship where undertaking are linked by participations or capital ties other than those referred to in Article 18of the *CRR*.

Article 18(6) relationship

means a relationship of one of the following kinds:

(a) where an *institution* exercises a significant influence over one or more *institutions* or *financial institutions*, but without holding a *participation* or other capital ties in these *institutions*; or

(b) where two or more *institutions* or *financial institutions* are placed under single management other than pursuant to a contract or clauses of their memoranda or articles of association.

1.3 Unless otherwise defined:

(1) any italicised expression used in this Part and in the *CRR* has the same meaning as in the *CRR*; and

(2) any italicised expression used in this Part and in the *CRD* has the same meaning as in the *CRD.*

2 METHODS OF PRUDENTIAL CONSOLIDATION

2.1 (1) In carrying out the calculations in (Part One, Title II, Chapter 2 of the *CRR*) for the purposes of prudential consolidation, a *firm* must include the relevant proportion of an undertaking with whom it has an:

(a) *Article 12(1) relationship*; or

(b) *Article 18(6) relationship*.

(2) In 2.1 (1), the relevant proportion is such proportion (if any) as stated in a requirement imposed on the *firm* in accordance with section 55M of *FSMA*.

[Note: Art 18(3) and (6) of the *CRR*]

2.2 In carrying out the calculations in Part One, Title II, Chapter 2 of the *CRR* for the purposes of prudential consolidation, a *firm* (for which the *PRA* is the *consolidating supervisor*) must include the proportion of the share of capital held of *participations* in *institutions* and *financial institutions* managed by an undertaking included in the consolidation together with one or more undertakings not included in the consolidation, where those undertakings' liability is limited to the share of capital they hold.

[Note: Art 18(4) of the *CRR*]

2.3 In carrying out the calculations in Part One, Title II, Chapter 2 of the *CRR* for the purposes of prudential consolidation, a *firm* must carry out a full consolidation of any undertaking with whom it has an *Article 18(5) relationship*.

[Note: Art 18(5) of the *CRR*]

PRA RULEBOOK CRR FIRMS: LARGE EXPOSURES INSTRUMENT 2013

Powers exercised

A. The Prudential Regulation Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137G (The PRA's general rules); and
(2) section 137T (General supplementary powers).

B. The rule-making powers referred to above are specified for the purpose of section 138G (Rule-making instrument) of the Act.

Pre-conditions to making

C. In accordance with section 138J of the Act (consultation with the Financial Conduct Authority)("FCA"), the PRA consulted the FCA. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

PRA Rulebook CRR Firms: Large Exposures Instrument 2013

D. The PRA makes the rules in Annex A to this instrument.

Commencement

E. Annex A of this instrument comes into force on 1 January 2014.

Citation

F. This instrument may be cited as the PRA Rulebook CRR Firms: Large Exposures Instrument 2013.

By order of the Board of the Prudential Regulation Authority
[DATE]

Annex A

In this Annex, the text is all new and is not underlined.

Part

LARGE EXPOSURES

Chapter content

Links

1 APPLICATION AND DEFINITIONS

1.1 This Part applies to every firm that is a *CRR firm*.

1.2 In this Part the following definitions shall apply:

core UK group

means all counterparties which, in relation to a *firm*, satisfy the conditions set out in Article 113(6) of the *CRR* and in respect of which *exposures* are exempted, under Article 400(1)(f) of the *CRR*, from the application of Article 395(1) of the *CRR.*

core UK group direction

means a direction given by the *PRA* under Article 113(6) of the *CRR.*

core UK group eligible capital

means the eligible capital of the *core UK group* calculated in accordance with 2.4.

exposure

has the meaning given to it in Article 389 of the *CRR*.

non-core large exposures group

means all counterparties which, in relation to a *firm*, satisfy the conditions set out in 2.1 and in respect of which *exposures* are exempted, under Article 400(2)(c) of the *CRR*, from the application of Article 395(1) of the *CRR.*

non-core large exposures group direction

means a direction given by the PRA under Article 400(2)(c) of the CRR.

non-core large exposures group exemption

means the exemption set out in in 2.1.

sovereign large exposures direction

means a direction given by the *PRA* under Article 400(2)(g)-(h) of the *CRR*.

sovereign large exposures exemption

means the exemption set out in 3.1.

1.3 Unless otherwise defined:

(1) any italicised expression used in this Part and in the *CRR* has the same meaning as in the *CRR*; and

(2) any italicised expression used in this Part and in the *CRD* has the same meaning as in the *CRD.*

2 INTRA-GROUP EXPOSURES: NON-CORE LARGE EXPOSURES GROUP EXEMPTION

2.1 A *firm* with a *non-core large exposures group direction* may (in accordance with that direction) exempt, from the application of Article 395(1) of the *CRR*, *exposures*, including *participations* or other kinds of holdings, incurred by the *firm* to:

(1) its parent undertaking;

(2) other subsidiaries of that parent undertaking; or

(3) its own subsidiaries,

in so far as those undertakings are covered by the supervision on a *consolidated basis* to which the *firm* itself is subject, in accordance with the *CRR*, Directive 2002/87/EC or with equivalent standards in force in a third country; *exposures* that do not meet these criteria, whether or not exempted from Article 395(1), shall be treated as *exposures* to a third party.

[Note: Art 400(2)(c) of the *CRR*]

[Note: supervisory statement on large exposures]

2.2 A firm may only make use of the *non-core large exposures group exemption* where the following conditions are met:

(1) the total amount of non-*trading book exposures* from the *firm* to its *non-core large exposures group* does not exceed 100% of the *firm's eligible capital*; or

(if the firm has a *core UK group direction*) the total amount of non-*trading book exposures* from its *core UK group* (including the *firm*) to its *non-core large exposures group* does not exceed 100% of the *core UK group eligible capital*;

(2) the total amount of *trading book exposures* from the *firm* to its *non-core large exposures group* does not exceed 500% of the *firm's eligible capital*; or

(if the *firm* has a *core UK group direction*) the total amount of *trading book exposures* from its *core UK group* (including the *firm*) to its *non-core large exposures group* does not exceed 500% of the *core UK group eligible capital*;

(3) (if the firm has a *core UK group direction*) it gives the *PRA* prior written notice if it intends to concentrate its intra-group *exposure* to a particular member of its *non-core large exposures group* in excess of 25% of *core UK group eligible capital*.

The written notice must contain the following:

(a) an explanation of how the *firm* will ensure that it will still meet the condition in (1) on a continuing basis;

(b) details of the counterparty, the size of the exposure and the expected duration of the exposure; and

(c) an explanation of the reason for the exposure;

(4) if the firm stops concentrating its intra-group *exposure* to a particular member of its *non-core large exposures group* in excess of 25% of *core UK group*

eligible capital, it gives the *PRA* prior written notice as set out at (3) if it intends to start to do so again; and

(5) the *firm* submits FSA018 in accordance with SUP 16.12.

2.3 A firm may calculate limits in 2.2 after taking into account the effect of credit risk mitigation in accordance with Articles 399 to 403 of the *CRR*.

[Note: Art 400(2)(c) of the *CRR*]

Core UK group eligible capital

2.4 For the purposes of the conditions in 2.2, a firm must calculate *core UK group eligible capital* in accordance with the deduction and aggregation method set out in 2.5.

2.5 (1) *Core UK group eligible capital* is equal to the sum of the following amounts for each member of the *core UK group* and the *firm* (the sub-group):

(a) for the ultimate *parent undertaking* of the sub-group, the amount calculated in accordance with Article 6 of the *CRR* (or other applicable prudential requirements);

(b) for any other member of the sub-group, the amount calculated in accordance with Article 6 of the *CRR* (or other applicable prudential requirements) less the book value of the sub-group's holdings of capital instruments in that member, to the extent not already deducted in calculations done in accordance with Article 6 of the *CRR* (or other applicable prudential requirements) for

(i) the ultimate *parent undertaking* of the sub-group: or

(ii) any other member of the sub-group.

(2) The deduction in (1)(b) must be carried out separately for each type of capital instrument eligible as *own funds*.

3 SOVEREIGN LARGE EXPOSURES EXEMPTION

3.1 (1) A firm that has a sovereign large exposure direction must exempt from Article 395(1) of the CRR the exposures as specified in the sovereign large exposure direction. It must do so to the extent specified in that direction.

(2) For the purposes of the *sovereign large exposure direction*, and in relation to a *firm*, the *exposures* referred to in 3.1(1) are limited to the following:

(a) asset items constituting claims on *central banks* in the form of required minimum reserves held at those *central banks* which are denominated in their national currencies; and

(b) asset items constituting claims on central governments in the form of statutory liquidity requirements held in government securities which are denominated and funded in their national currencies provided that, at the discretion of the *PRA*, the credit assessment of those central governments assigned by a *nominated ECAI* is investment grade.

[Note: Art 400(2)(g)-(h) of the *CRR*]

[Note: supervisory statement on large exposures]

4 CONDITIONS FOR NON-CORE LARGE EXPOSURES GROUP EXEMPTION AND THE SOVEREIGN LARGE EXPOSURES EXEMPTION

4.1 A *firm* may only make use of the *non-core large exposures group exemption* and the *sovereign large exposures exemption* where it can demonstrate to the *PRA* that the following conditions are met:

(1) the specific nature of the *exposure*, the counterparty or the relationship between the *firm* and the counterparty eliminate or reduce the risk of the *exposure*; and

(2) any remaining concentration risk can be addressed by other equally effective means such as the arrangements, processes and mechanisms provided for in Article 81 of *CRD*.

[Note: Art 400(3) of the *CRR*]

PRUDENTIAL SOURCEBOOK FOR BANKS, BUILDING SOCIETIES AND INVESTMENT FIRMS (LIQUIDITY STANDARDS) AMENDMENT INSTRUMENT 2013

Powers exercised

A. The Prudential Regulation Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137G (The PRA's general rules); and
(2) section 137T (General supplementary powers).

B. The rule-making powers referred to above are specified for the purpose of section 138G (Rule-making instrument) of the Act.

Pre-conditions to making

C. In accordance with section 138J of the Act (consultation with the Financial Conduct Authority) ("FCA"), the PRA consulted the FCA. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

Commencement

D. Part 1 of the Annex to this instrument comes into force on 1 January 2014.

E. Part 2 of the Annex to this instrument comes into force on a date specified by subsequent PRA Board Instrument.

Amendments

F. The Prudential sourcebook of Bank, Building Societies and Investment Firms (BIPRU) is amended in accordance with the Annex to this instrument.

Notes

G. In the Annex to this instrument, the "notes" (indicated by "**Note:**") are included for the convenience of readers but do not form part of the legislative text.

Citation

H. This instrument may be cited as the Prudential sourcebook of Bank, Building Societies and Investment Firms (Liquidity Standards) Amendments Instrument 2013.

By order of the Board of the Prudential Regulation Authority
[DATE]

Annex

Amendments to the Prudential sourcebook for Banks, Building Societies and Investment Firms (BIPRU)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

Part 1: Comes into force on 1 January 2014.

Liquidity standards

12.1 Application

12.1.1 R Subject to *BIPRU 12.1.2R*, *BIPRU 12* applies to:

(1) ~~a *BIPRU firm*~~ [deleted];

(1A) a *UK bank*;

(1B) a *building society;*

(1C) a *UK designated investment firm*;

(2) an *incoming EEA firm* which:

(a) is a ~~*full BCD*~~ *CRD* *credit institution*; and

(b) has a *branch* in the *United Kingdom*; and

(3) a *third country BIPRU firm* which:

(a) ~~is bank; and~~ [deleted]

(b) has a *branch* in the *United Kingdom*.

…

12.3 Liquidity risk management

…

12.3.4 R A *firm* must have in place robust strategies, policies, processes and systems that enable it to identify, measure, manage and monitor *liquidity risk* over an appropriate set of time horizons, including intra-day, so as to ensure that it maintains adequate levels of liquidity buffers. These strategies, policies, processes and systems must be tailored to business lines, currencies, *branches* and legal entities and must include adequate allocation mechanisms of liquidity costs, benefits and risks.

[**Note:**~~ annex V paragraph 14 of the *Banking Consolidation Directive*~~ article 86(1) of the *CRD*]

…

12.3.5 R …

[**Note:**~~ annex V paragraph 14a of the *Banking Consolidation Directive*~~ article 86(2) (part) of the *CRD*]

…

12.3.7A R A *firm* must, taking into account the nature, scale and complexity of its activities, have liquidity risk profiles that are consistent with and not in excess of those required for a well-functioning and robust system.

[**Note:** article 86(3) of the *CRD*]

…

12.3.8 R …

[**Note:**~~ annex V paragraph 14a of the *Banking Consolidation Directive*~~ article 86(2) (part) of the *CRD*]

…

12.3.22A R …

[**Note:**~~ annex V paragraph 16 of the *Banking Consolidation Directive*~~ article 86(5) of the *CRD*]

12.3.22B R …

[**Note:**~~ annex V paragraph 17 of the *Banking Consolidation Directive*~~ article 86(6) of the *CRD*]

12.3.27 R …

[**Note:**~~ annex V paragraph 15 of the *Banking Consolidation Directive*~~ article 86(4) of the *CRD*]

12.4 Stress testing and contingency funding

12.4.-2 R …

[**Note:**~~ annex V paragraph 18 of the *Banking Consolidation Directive*~~ article 86(7) of the *CRD*]

…

12.4.-1 R A *firm* must consider alternative scenarios on liquidity positions and on risk mitigants and must review ~~regularly~~ the assumptions underlying decisions concerning the funding position at least annually. For these purposes, alternative scenarios must address, in particular, off-balance sheet items and other contingent liabilities, including those of *securitisation special purpose entities (SSPEs)* or other special purpose entities, as referred to in the *CRR*, in relation to which the *firm* acts as *sponsor* or provides material liquidity support.

[**Note:**~~ annex V paragraph 19 of the *Banking Consolidation Directive*~~ article 86(8) of the *CRD*]

…

12.4.5A R A *firm* must consider the potential impact of institution-specific, market-wide and combined alternative scenarios. Different time ~~horizons~~ periods and varying degrees of stressed conditions must be considered.

[**Note:**~~ annex V paragraph 20 of the *Banking Consolidation Directive*~~ article 86(9) of the *CRD*]

…

12.4.10 R …

[**Note:**~~ annex V paragraph 21 of the *Banking Consolidation Directive*~~ article 86(10) of the *CRD*]

12.4.11 R ~~In order to deal with liquidity crisis, a~~ A *firm* must have in place ~~contingency~~ liquidity recovery plans setting out adequate strategies and proper implementation measures in order to address possible liquidity shortfalls~~.~~, including in relation to *branches* established in another *EEA State*. Those plans must be ~~regularly~~ tested~~,~~ at least annually, updated on the basis of the outcome of the alternative scenarios set out in *BIPRU* 12.4.-1R, and be reported to and approved by the *firm's governing body*, so that internal policies and processes can be adjusted accordingly. A *firm* must take the necessary operational steps in advance to ensure that liquidity recovery plans can be implemented immediately.

[**Note:**~~ annex V paragraph 22 of the *Banking Consolidation Directive*~~ article 86(11) (part) of the *CRD*]

12.4.11A R For a *firm* that is a *CRD credit institution* the operational steps referred to in *BIPRU* 12.4.11R must include holding collateral immediately available for central bank funding. This includes holding collateral where necessary in the currency of another *EEA State*, or currency of a *non-EEA state* to which the *firm* has exposures, and where operationally necessary within the territory of a *Host State* or *non-EEA state* to whose currency it is exposed.

[**Note:** article 86(11) (part) of the *CRD*]

…

12.7 Liquid assets buffer

…

12.7.4 R …

(1) the central government or central bank in question has been assessed by at least two *eligible ECAIs* as having a credit rating associated with ~~*credit quality step*~~ credit quality step 1 in the table set out in *BIPRU* 12 Annex 1 (Mapping of credit assessments of *ECAIs* to credit quality steps) ~~in the *credit quality assessment scale* published by the *appropriate regulator* for the purpose of *BIPRU* 3 (The Standardised Approach: mapping of the ECAIs credit assessments to credit quality~~

~~steps (Long term mapping))~~; and

…

…

12.7.6 R …

(1) the central bank in question has been assessed by at least two *eligible ECAIs* as having a credit rating associated with ~~*credit quality step*~~ credit quality step 1 in the table set out in *BIPRU* 12 Annex 1 (Mapping of credit assessments of *ECAIs* to credit quality steps) ~~in the *credit quality assessment scale* published by the *appropriate regulator* for the purpose of *BIPRU* 3 (The Standardised Approach: mapping of the ECAIs credit assessments to credit quality steps (Long term mapping))~~; and

…

12.7.6A R …

(1) the *designated multilateral development bank* in question has been assessed by at least two *eligible ECAIs* as having a credit rating associated with ~~*credit quality step*~~ credit quality step 1 in the table set out in *BIPRU* 12 Annex 1 (Mapping of credit assessments of *ECAIs* to credit quality steps) ~~in the *credit quality assessment scale* published by the *appropriate regulator* for the purpose of *BIPRU 3* (The Standardised Approach: mapping of the ECAIs' credit assessments to credit quality steps (Long term mapping))~~; and

…

After BIPRU 12, insert the following new annex.

12 Annex 1 R Mapping of credit assessments of *ECAIs* to credit quality steps

Credit Quality Step	**Fitch's assessment**	**Moody's assessments**	**S&P's assessments**	**DBRS' assessments**
1	AAA to AA-	Aaa to Aa3	AAA to AA-	AAA to AAL
2	A+ to A-	A1 to A3	A+ to A-	AH to AL
3	BBB+ to BBB-	Baa1 to Baa3	BBB+ to BBB-	BBBH to BBBL
4	BB+ to BB-	Ba1 to Ba3	BB+ to BB-	BBH to BBL

5	B+ to B-	B1 to B3	B+ to B-	BH to BL
6	CCC+ and below	Caa1 and below	CCC+ and below	CCCH and below

Part 2: Comes into force on a date specified by a subsequent PRA Board Instrument.

12.1 Application

12.1.1 R Subject to *BIPRU* 12.1.2R, *BIPRU* 12 applies to:

…

(2) ~~an *incoming EEA firm* which:~~

~~(a)~~ ~~is a *CRD credit institution*; and~~

~~(b)~~ ~~has a *branch* in the *United Kingdom*~~ [deleted]; and

…

CAPITAL REQUIREMENTS REGULATION [(REPORTING)] AMENDMENT INSTRUMENT [No. XXX] 2013

Powers exercised

A. The Prudential Regulation Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137G (The PRA's general rules); and
(2) section 137T (General supplementary powers);

B. The rule-making powers referred to above are specified for the purpose of section 138G (Rule-making instrument) of the Act.

Pre-conditions to making

C. In accordance with section 138J of the Act (consultation with the Financial Conduct Authority) ("FCA"), the PRA consulted the FCA. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

Commencement

D. Part 1 - 4 of the Annex to this instrument comes into force on 1 January 2014.

E. Part 5 of the Annex to this instrument comes into force on 1 July 2014.

F. Part 6 of the Annex to this instrument shall come into force on the date specified by a subsequent PRA Board Instrument.

Amendments to the Handbook

G. The Supervisory manual (SUP) is amended in accordance with the Annex to this instrument.

Guidance

H. The Prudential Regulation Authority gives as guidance each provision in this Annex that is marked with a G.

Citation

I. This instrument may be cited as the Capital Requirements Regulation (Reporting) Amendment Instrument [No. XXX] 2013.

By order of the Board of the Prudential Regulation Authority
[DATE]

Annex

Amendments to the Supervision manual (SUP)

Part 1: Comes into force on 1 January 2014.

In this Part, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

16.12 Integrated Regulatory Reporting

…

Purpose

16.12.2 G (1) *Principle* 4 requires *firms* to maintain adequate financial resources. ~~The Interim Prudential sourcebooks, *BIPRU* and *GENPRU* set out the *appropriate regulator's* detailed capital adequacy requirements.~~ By submitting regular data, *firms* enable the *appropriate regulator* to monitor their compliance with *Principle* 4 and their prudential requirements. ~~in the *Handbook*.~~

…

…

16.12.3A G The following is designed to assist *firms* to understand how the reporting requirements set out in this chapter operate when the circumstances set out in *SUP* 16.12.3 R (1)(a)(ii) apply.

(1) Example 1
A ~~*BIPRU 730K firm*~~ *UK designated investment firm* that undertakes activities in both *RAG* 3 and *RAG* 7
Overlaying the requirements of *RAG* 3 (*data items*) with the requirements of *RAG* 7 shows the following:

RAG 3 (*SUP* 16.12.11R) data items	RAG 7 (*SUP* 16.12.22AR) data items
…	…
~~Capital adequacy~~	Capital adequacy
~~Credit risk~~	~~Credit risk~~
~~Operational risk~~	~~Operational risk~~
~~Large exposures~~	~~Large exposures~~
~~UK integrated group large exposures~~ Exposures between *core UK group* and *non-core*	~~UK integrated group large exposures~~ Exposures between *core UK group* and *non-core*

large exposures group	*large exposures group*
…	…
~~Non-EEA sub-group~~	~~Non-EEA sub-group~~
…	…
~~Securitisation : non-trading book~~	~~Securitisation : non-trading book~~
…	…
~~Securitisation: trading book~~	~~Securitisation: trading book~~

…

…

The reporting frequency and submission times for items (b), (d) and (e) above are then derived from the rules applicable to ~~*BIPRU*~~ *firms* in *SUP* 16.12.23R and *SUP* 16.12.24R. Threshold conditions and fees and levies reports do not need to be submitted as they are not required under the lowest numbered of the two *RAGs* in this example, see *SUP* 16.12.3R(1)(a)(iii).

(2) Example 2
A *UK bank* that is not a *FINREP firm* in *RAG* 1 that also carries on activities in *RAG* 5
Again, overlaying the *RAG* 1 reporting requirements with the requirements for a *RAG* 5 *firm* gives the following :

RAG 1 requirements (*SUP* 16.12.5R)	*RAG* 5 requirements (*SUP* 16.12.18AR)
…	…
~~Capital adequacy~~	~~Capital Adequacy~~
~~Credit risk~~	
…	
~~Operational risk~~	
~~Large exposures~~	
~~UK integrated group large exposures~~ Exposures between *core UK group* and *non-core large exposures group*	
…	
~~Non-EEA sub-group~~	

…	
~~Securitisation: non-trading book~~	
…	
~~Securitisation: trading book~~	
	…

…

(…)

16.12.4 R Table of applicable rules containing *data items*, frequency and submission periods

(1)		**(2)**	**(3)**	**(4)**
RAG **number**	*Regulated Activities*	**Provisions containing:**		
…	…	…		
RAG 3	• dealing in investment as principal • dealing in investments as agent • advising on investments (excluding retail investment activities) • arranging (bringing about) deals in investments (excluding retail investment activities)	*SUP* 16.12.10R *SUP* ~~16.12.11R~~ 16.12.11B R	*SUP 16.12.10R* *SUP* ~~*16.12.12R*~~ 16.12.12A R	*SUP 16.12.10R* *SUP 16.12.13R*
RAG 4	• managing investments • establishing, operating or winding up a regulated collective investment scheme • establishing, operating or winding up an unregulated collective	*SUP* 16.12.14R ~~*SUP 16.12.15 R*~~ *SUP* 16.12.15B R	*SUP 16.12.14R* *SUP* ~~*16.12.16R*~~ 16.12.16A R	*SUP 16.12.14R* *SUP 16.12.17R*

	investment scheme • establishing, operating or winding up a stakeholder pension scheme • establishing, operating or winding up a personal pension scheme			
…	…	…		
RAG 7	• retail investment activities • advising on pensions transfers & opt-outs • arranging (bringing about deals) in retail investments	~~*SUP* 16.12.22AR~~ <u>*SUP* 16.12.22CR</u>	*SUP 16.12.23R*	*SUP 16.12.24R*
RAG 8	• making arrangements with a view to transactions in investments • operating a multilateral trading facility	~~*SUP* 16.12.25AR~~ <u>*SUP* 16.12.25CR</u>	*SUP 16.12.26R*	*SUP 16.12.27R*
…				

…

Regulated Activity Group 1

16.12.5 R The applicable *data items* and forms or reports referred to in *SUP* 16.12.4R are set out according to *firm* type in the table below:

Description of *data item*	Prudential category of *firm*, applicable *data items* and reporting format (Note 1)

	UK bank	*Building society*	*Non-EEA bank*	*EEA bank* that has *permission* to accept deposits, other than one with permission for cross border services only	*EEA bank* that does not have permission to accept deposits, other than one with permission for cross border services only	[deleted]	*Credit union*	*Dormant account fund operator* (note 15)
…								
Capital adequacy	~~FSA 003 (note 2)~~ [deleted]	~~FSA003 (note 2)~~ [deleted]					CQ; CY	
Credit risk	~~FSA 004 (note 2)~~ [deleted]	~~FSA004 (note 2)~~ [deleted]						
…								
Operational risk	~~FSA 007 (notes 2, 6)~~ [deleted]	~~FSA007 (notes 2, 6)~~ [deleted]						
Large exposures	~~FSA 008 (note 2)~~ [deleted]	~~FSA008 (note 2)~~ [deleted]					CQ; CY	
~~UK integrated group large exposures~~ Exposures between *core UK group* and *non-core*	FSA 018 (note 12)	FSA018 (note 12)						

large exposures group									
…									
Non-EEA sub-group	~~FSA 028 (note 8)~~ [deleted]								
…									
Securitisation: non-trading book	~~FSA 046 (Notes 2 and 14)~~ [deleted]	~~FSA046 (Notes 2 and 14)~~ [deleted]							
Securitisation: trading book	~~FSA 058 (Notes 2 and 23)~~ ~~[deleted]~~								
…									
Note 4	~~This applies to a *firm* that is required to submit *data item* FSA003 and, at any time within the 12 *months* up to its latest *accounting reference date* ("the relevant period"), was reporting *data item* FSA005 ("Firm A") or not reporting this item ("Firm B"). In the case of Firm A it must report this *data item* if one or both of its last two submissions in the relevant period show that the threshold was exceeded. In the case of Firm B it must report this item if both the last two submissions in the relevant period show that the threshold has been exceeded. The threshold is exceeded where *data element* 93A in *data item* FSA003 is greater than £50 million, or its currency equivalent, at the relevant reporting date for the *firm*.~~ This applies to a *firm* that applies add-ons to their market risk capital calculation under the RNIV framework.								
…									
Note 6	~~This is only applicable to a *firm* that has adopted, in whole or in part, either the *standardised approach*, *alternative standardised approach*, or *advanced measurement approach* under *BIPRU* 6.~~ [deleted]								
…									
Note 12	~~Members of a *UK integrated group* should only submit this *data item* at the *UK integrated group* level.~~ Only applicable to a *firm* that has both a *core UK group* and a *non-core large exposures group*.								

…	
Note 14	~~Only applicable to *firms* that hold *securitisation positions*, or are the *originator* or *sponsor* of *securitisations* of *non-trading book exposures*.~~ [deleted]
…	

16.12.6 R The applicable reporting frequencies for submission of *data items* and periods referred to in *SUP* 16.12.5R are set out in the table below according to *firm* type. Reporting frequencies are calculated from a *firm's accounting reference date*, unless indicated otherwise.

Data item	Unconsolidated *UK banks* and *building societies*	Solo consolidated *UK banks* and *building societies*	Report on a ~~*UK*~~ *consolidation group* or, as applicable, *defined liquidity group*basis by *UK banks* and *building societies*	Other members of *RAG* 1
…				
FSA003	~~Quarterly or monthly (note 1)~~ [deleted]		~~Half yearly~~ [deleted]	
FSA004	~~Quarterly~~ [deleted		~~Half yearly~~ [deleted]	
…				
FSA007	~~Annually~~ [deleted]			
FSA008	~~Quarterly~~ [deleted]			
…				
FSA028	~~Half yearly~~ [deleted]			
…	Quarterly		Half yearly	
FSA046	~~Quarterly~~ [deleted]		~~Quarterly~~ [deleted]	
FSA058	~~Quarterly~~ [deleted]		~~Quarterly~~ [deleted]	
Note 1	~~Monthly submission only applicable if the *firm* has been notified in writing that it is required to report (when, on an annual review, it has two consecutive quarterly submissions of FSA003 showing *data element* 93A being greater than £50 million, or its currency equivalent, and also greater than 50% of *data element* 70A.~~ [deleted]			
…				

16.12.7 R The applicable due dates for submission referred to in *SUP* 16.12.4R are set out in the table below. The due dates are the last day of the periods given in the table below following the relevant reporting frequency period set out in *SUP* 16.12.6R, unless indicated otherwise.

Data item	Daily	Weekly	Monthly	Quarterly	Half yearly	Annual
…						
~~FSA003~~ [deleted]			~~15 *business days*~~ [deleted]	~~20 *business days*~~ [deleted]	~~45 *business days*~~ [deleted]	
~~FSA004~~ [deleted]				~~20 *business days*~~ [deleted]	~~45 *business days*~~ [deleted]	
…						
~~FSA007~~ [deleted]						~~6 months~~ [deleted]
~~FSA008~~ [deleted]				~~20 *business days* (note 3) 45 *business days* (note 4)~~ [deleted]		
…						
~~FSA028~~ [deleted]					~~30 *business days*~~ [deleted]	
…						
~~FSA046~~ [deleted]				~~20 *business days* (Note 3), 45 *business days* (Note 4)~~ [deleted]		
…						
~~FSA058~~ [deleted]				~~20 *business days* (Note 3), 45 *business days* (Note 4)~~ [deleted]		

…	

...

16.12.11 ~~R~~ ~~The applicable *data items* referred to in *SUP 16.12.4 R* are set out according to *firm* type in the table below:~~ [deleted]

~~Description of *data item*~~	~~*Firms'* **prudential category and applicable** data items **(note 1)**~~							
	~~*BIPRU firms* **(note 17)**~~			~~*Firms* **other than** *BIPRU firms*~~				
	~~**730K**~~	~~**125K and** *UCITS investment firms*~~	~~**50K**~~	~~*IPRU(INV)* **Chapter 3**~~	~~*IPRU(INV)* **Chapter 5**~~	~~*IPRU(INV)* **Chapter 9**~~	~~*IPRU(INV)* **Chapter 13**~~	~~*UPRU*~~
~~*Annual report and accounts*~~	~~No standard format~~			~~No standard format (note 19)~~	~~No standard format~~		~~No standard format~~	~~No standard format~~
~~*Annual report and accounts* of the *mixed-activity holding company* (note 10)~~	~~No standard format~~							
~~Solvency statement~~	~~No standard format (note 11)~~			~~No standard format (note 20)~~	~~No standard format (note 11)~~			~~No standard format (note 11)~~
~~Balance sheet~~	~~FSA001 (note 2)~~	~~FSA001 (note 2)~~	~~FSA001 (note 2)~~	~~FSA029 (note 18)~~	~~FSA029~~	~~FSA029~~	~~FSA029 (note 15) or Section A RMAR (note 15)~~	~~FSA029~~
~~Income statement~~	~~FSA002 (note 2)~~	~~FSA002 (note 2)~~	~~FSA002 (note 2)~~	~~FSA030 (note 18)~~	~~FSA030~~	~~FSA030~~	~~FSA030 (note 15) or Section~~	~~FSA030~~

							~~B RMAR (note 15)~~	
~~Capital adequacy~~	~~FSA003 (note 2)~~	~~FSA003 (note 2)~~	~~FSA003 (note 2)~~	~~FSA033 (note 18)~~	~~FSA034 or FSA035 (note 14)~~	~~FSA031~~	~~FSA032 (note 15) or Section D6 RMAR (note 15)~~	~~FSA036~~
~~Credit risk~~	~~FSA004 (notes 2, 3)~~	~~FSA004 (notes 2, 3)~~	~~FSA004 (notes 2, 3)~~					
~~Market risk~~	~~FSA005 (notes 2, 4)~~	~~FSA005 (notes 2, 4)~~	~~FSA005 (notes 2, 4)~~					
~~Market risk - supplementary~~	~~FSA006 (note 5)~~	~~FSA006 (note 5)~~	~~FSA006 (note 5)~~					
~~Operational risk~~	~~FSA007 (notes 2, 6, 7)~~	~~FSA007 (notes 2, 6, 7)~~	~~FSA007 (notes 2, 6, 7)~~					
~~Large exposures~~	~~FSA008 (Notes 2, 6)~~	~~FSA008 (Notes 2, 6)~~	~~FSA008 (Notes 2, 6)~~					
~~UK integrated group large exposures~~	~~FSA018 (note 12)~~	~~FSA018 (note 12)~~	~~FSA018 (note 12)~~					
~~Solo consolidation data~~	~~FSA016 (note 25)~~	~~FSA016 (note 25)~~	~~FSA016 (note 25)~~					
~~Pillar 2 questionnaire~~	~~FSA019 (note 8)~~	~~FSA019 (note 8)~~	~~FSA019 (note 8)~~					
~~Non-EEA sub-~~	~~FSA028 (note 9)~~	~~FSA028 (note 9)~~	~~FSA028 (note 9)~~					

~~group~~								
~~Threshold conditions~~							~~Section F RMAR (Note 15)~~	
~~Client money and client assets~~	~~FSA039~~	~~FSA039~~	~~FSA039~~	~~FSA039 (note 18)~~	~~FSA039~~	~~FSA039~~	~~Section C RMAR (Note 15) or FSA039~~	~~FSA039~~
~~CFTC~~	~~FSA040 (note 24)~~	~~FSA040 (note 24)~~	~~FSA040 (note 24)~~	~~FSA040 (note 24)~~	~~FSA040 (note 24)~~	~~FSA040 (note 24)~~	~~FSA040 (note 24)~~	~~FSA040 (note 24)~~
~~IRB portfolio risk~~	~~FSA045 (note 22)~~	~~FSA045 (note 22)~~	~~FSA045 (note 22)~~					
~~Securitisation : non-trading book~~	~~FSA046 (note 23)~~	~~FSA046 (note 23)~~	~~FSA046 (note 23)~~					
~~Daily Flows~~	~~FSA047 (Notes 26, 29 , 31 and 33)~~							
~~Enhanced Mismatch Report~~	~~FSA048 (Notes 26, 29, 31 and 33)~~							
~~Liquidity Buffer Qualifying Securities~~	~~FSA050 (Notes 27, 30, 31 and 33)~~							
~~Funding Concentration~~	~~FSA051 (Notes 27, 30, 31 and 33)~~							
~~Pricing data~~	~~FSA052 (Notes 27, 31, 33 and 34)~~							
~~Retail and corporate funding~~	~~FSA053 (Notes 27, 30, 31 and 33)~~							

~~Currency Analysis~~	~~FSA054 (Notes 27, 30, 31 and 33)~~							
~~Systems and Controls Questionnaire~~	~~FSA055 (Notes 28 and 33)~~							
~~Securitisation: trading book~~	~~FSA058 (Note 32)~~	~~FSA058 (Note 32)~~	~~FSA058 (Note 32)~~					
~~Note 1~~	~~When submitting the completed *data item* required, a *firm* must use the format of the *data item* set out in *SUP 16 Annex 24 R*. Guidance notes for completion of the data items are contained in *SUP 16 Annex 25 G*.~~							
~~Note 2~~	~~*Firms* that are members of a *UK consolidation group* are also required to submit this report on a *UK consolidation group* basis.~~							
~~Note 3~~	~~This applies to a *firm* that is required to submit *data item* FSA003 and, at any time within the 12 *months* up to its latest *accounting reference date* ("the relevant period"), was reporting *data item* FSA004 ("Firm A") or not reporting this item ("Firm B").~~ ~~In the case of Firm A it must report this *data item* if one or both of its last two submissions in the relevant period show that the threshold was exceeded.~~ ~~In the case of Firm B it must report this item if both the last two submissions in the relevant period show that the threshold has been exceeded.~~ ~~The threshold is exceeded where *data element* 77A in *data item* FSA003 is greater than £10 million, or its currency equivalent, at the relevant reporting date for the *firm*.~~							
~~Note 4~~	~~This applies to a *firm* that is required to submit *data item* FSA003 and, at anytime within the 12 *months* up to its latest *accounting reference date* ("the relevant period"), was reporting *data item* FSA005 ("Firm A") or not reporting this item ("Firm B").~~ ~~In the case of Firm A it must report this *data item* if one or both of its last two submissions in the relevant period show that the threshold was exceeded.~~ ~~In the case of Firm B it must report this item if both the last two submissions in the relevant period show that the threshold has been exceeded.~~ ~~The threshold is exceeded where *data element* 93A in *data item* FSA003 is greater than £50 million, or its currency equivalent, at the relevant reporting date for the *firm* .~~							
~~Note 5~~	~~Only applicable to *firms* with a *VaR model permission*.~~							
~~Note 6~~	~~This will not be applicable to *BIPRU limited activity firms* or *BIPRU limited licence firms* unless they have a waiver under *BIPRU 6.1.2 G*.~~							

~~Note 7~~	~~This is only applicable to a *firm* that has adopted, in whole or in part, either the *standardised approach*, *alternative standardised approach*, or *advanced measurement approach* under *BIPRU 6*~~
~~Note 8~~	~~Only applicable to *BIPRU investment firms* that:~~ ~~(a) are subject to consolidated supervision under *BIPRU 8*, except those that are either included within the consolidated supervision of a group that includes a UK *credit institution*, or that have been granted an *investment firm consolidation waiver*; or~~ ~~(b) have been granted an *investment firm consolidation waiver*; or~~ ~~(c) are not subject to consolidated supervision under *BIPRU 8*.~~ ~~A *BIPRU investment firm* under (a) must complete the report on the basis of its *UK consolidation group*. A *BIPRU investment firm* under (b) or (c) must complete the report on the basis of its solo position.~~
~~Note 9~~	~~This will be applicable to firms that are members of a *UK consolidation group* on the reporting date.~~
~~Note 10~~	~~Only applicable to a *firm* whose ultimate parent is a *mixed activity holding company*.~~
~~Note 11~~	~~Only applicable to a firm that is a *sole trader* or a *partnership*, when the report must be submitted by each *partner*.~~
~~Note 12~~	~~Members of a *UK integrated group* should only submit this *data item* at the *UK integrated group* level.~~
~~Note 13~~	~~This does not apply to a *firm* subject to *IPRU(INV)* Chapter 13 which is an *exempt CAD firm*.~~
~~Note 14~~	~~FSA034 must be completed by a *firm* not subject to the exemption in *IPRU(INV)* 5.2.3(2)R.~~ ~~FSA035 must be completed by a firm subject to the exemption in *IPRU(INV)* 5.2.3(2)R.~~
~~Note 15~~	~~FSA029, FSA030, FSA032 and FSA039 only apply to a *firm* subject to *IPRU(INV)* Chapter 13 which is an *exempt CAD firm*. Sections A, B, C, D1, D6 and F RMAR only apply to a *firm* subject to *IPRU(INV)* Chapter 13 which is not an *exempt CAD firm*. Where a *firm* submits data items for both *RAG* 3 and *RAG* 9, the *firm* must complete both Sections D1 and D6 RMAR.~~
~~Note 16~~	~~[deleted]~~
~~Note 17~~	~~An *exempt BIPRU commodity firm* will, by virtue of the definition of *BIPRU TP 15*, be exempt from completing FSA003 (and thus FSA004, FSA005, FSA006 and FSA007) for the duration of the transitional provision. It is however required to submit all other *data items* applicable according to the firm's *BIPRU* classification including, for the avoidance of doubt, *BIPRU TP 16*.~~ [deleted]
~~Note 18~~	~~Except if the *firm* is an *adviser*, *local* or traded options market maker (as referred to in *IPRU(INV)* 3-60(4)R.~~
~~Note 19~~	~~In the case of an *adviser*, *local* or traded options market maker (as referred to in *IPRU(INV)* 3-60(4)R), it is only required from *partnerships* and *bodies corporate*, and then only if the report was audited as a result of a statutory provision other than under the *Act*.~~

~~Note 20~~	~~Only required in the case of an *adviser*, *local* or traded options market maker (as referred to in *IPRU(INV)* 3-60(4)R) that is a *sole trader*.~~
~~Note 21~~	~~[deleted]~~
~~Note 22~~	~~Only applicable to *firms* that have an *IRB permission*.~~
~~Note 23~~	~~Only applicable to *firms* that hold *securitisation positions*, or are the *originator* or *sponsor* of *securitisations*. of *non-trading book exposures*.~~
~~Note 24~~	~~Only applicable to *firms* granted a *Part 30 exemption order* and operating an arrangement to cover forward profits on the London Metals Exchange.~~
~~Note 25~~	~~Only applicable to a *firm* that has a *solo consolidation waiver*.~~
~~Note 26~~	~~A *firm* must complete this item separately on each of the following bases (if applicable).~~ ~~(1) It must complete it on a solo basis. Therefore even if it has a *solo consolidation waiver* it must complete the item on an unconsolidated basis by reference to the *firm* alone.~~ ~~(2) If it is a *group liquidity reporting firm* in a *DLG by default* and is a *UK lead regulated firm*, it must complete the item on the basis of that group.~~ ~~(3) If it is a *group liquidity reporting firm* in a *UK DLG by modification*, it must complete the item on the basis of that group.~~ ~~(4) If it is a *group liquidity reporting firm* in a *non-UK DLG by modification*, it must complete the item on the basis of that group.~~
~~Note 27~~	~~A *firm* must complete this item separately on each of the following bases that are applicable.~~ ~~(1) It must complete it on a solo basis unless it is a *group liquidity reporting firm* in a *UK DLG by modification*. Therefore even if it has a *solo consolidation waiver* it must complete the item on an unconsolidated basis by reference to the *firm* alone.~~ ~~(2) If it is a *group liquidity reporting firm* in a *UK DLG by modification*, it must complete the item on the basis of that group.~~
~~Note 28~~	~~If it is a *non-ILAS BIPRU firm*, it must complete it on a solo basis. Therefore even if it has a *solo consolidation waiver* it must complete the item on an unconsolidated basis by reference to the *firm* alone.~~
~~Note 29~~	~~(1) This item must be reported in the reporting currency.~~ ~~(2) If any *data element* is in a currency or currencies other than the reporting currency, all currencies (including the reporting currency) must be combined into a figure in the reporting currency.~~ ~~(3) In addition, all *material currencies* (which may include the reporting currency) must each be recorded separately (translated into the reporting currency). However if:~~ ~~(a) the reporting frequency is (whether under a *rule* or under a *waiver*) quarterly or less than quarterly; or~~ ~~(b) the only *material currency* is the reporting currency;~~ ~~(3) does not apply.~~ ~~(4) If there are more than three *material currencies* for this *data item*, (3) only applies to the three largest in amount. A *firm* must identify the largest in amount in accordance with the following procedure.~~ ~~(a) For each currency, take the largest of the asset or liability figure as referred to in the definition of *material currency*.~~ ~~(b) Take the three largest figures from the resulting list of amounts.~~ ~~(5) The date as at which the calculations for the purposes of the definition of *material currency* are carried out is the last day of the reporting period in question.~~ ~~(6) The reporting currency for this *data item* is whichever of the following currencies~~

	~~the *firm* chooses, namely USD (the United States Dollar), EUR (the euro), GBP (sterling), JPY (the Japanese Yen), CHF (the Swiss Franc), CAD (the Canadian Dollar) or SEK (the Swedish Krona).~~
~~Note 30~~	~~Note 29 applies, except that paragraphs (3), (4) and (5) do not apply, meaning that *material currencies* must not be recorded separately.~~
~~Note 31~~	~~Any changes to reporting requirements caused by a *firm* receiving an *intra-group liquidity modification* (or a variation to one) do not take effect until the first day of the next reporting period applicable under the changed reporting requirements for the *data item* in question if the *firm* receives that *intra-group liquidity modification* or variation part of the way through such a period. If the change is that the *firm* does not have to report a particular *data item* or does not have to report it at a particular *reporting level*, the *firm* must nevertheless report that item or at that *reporting level* for any reporting period that has already begun. This paragraph is subject to anything that the *intra-group liquidity modification* says to the contrary.~~
~~Note 32~~	~~Only applicable to *firms* that hold *securitisation positions* in the trading book and/ or are the *originator* or *sponsor* of *securitisations* held in the *trading book*.~~
~~Note 33~~	~~FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054 must be completed by an *ILAS BIPRU firm*. An *ILAS BIPRU firm* does not need to complete FSA055. A *non-ILAS BIPRU firm* must complete FSA055 and does not need to complete FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054.~~
~~Note 34~~	~~This *data item* must be reported only in the currencies named in FSA052, so that liabilities in GBP are reported in GBP in rows 1 to 4, those in USD are reported in USD in rows 5 to 8, and those in Euro are reported in Euro in rows 9 to 12. Liabilities in other currencies are not to be reported.~~

16.12.11A G ~~The columns in the table in *SUP* 16.12.11R that deal with *BIPRU 50K firms* and *BIPRU 125K firms* cover some liquidity items that only have to be reported by an *ILAS BIPRU firm*. In fact a *BIPRU 50K firm* and a *BIPRU 125K firm* cannot be an *ILAS BIPRU firm*. One reason for drafting the table in this way is that the classification of *firms* into *ILAS BIPRU firms* and *non-ILAS BIPRU firms* is not based on the classification into *BIPRU 50K firms*, *BIPRU 125K firms* and *BIPRU 730K firms* and the drafting of the table emphasises that. Also, the table covers consolidated reports and the conditions about what sort of group has to supply what type of liquidity report do not always depend on how the individual *firm* is classified.~~ [deleted]

16.12.11B R The applicable *data items* referred to in *SUP* 16.12.4R for *UK designated investment firms* are set out below:

Description of *data item*	**Applicable *data item***
Annual report and accounts	No standard format
Annual report and accounts of the *mixed-activity holding company* (note 5)	No standard format
Solvency statement	No standard format (Note 6)
Balance sheet	FSA001 (Note 2)
Income statement	FSA002 (Note2)

Market risk	FSA005 (notes 2, 19)
Market risk –supplementary	FSA006 (Note 3)
Exposures between *core UK group* and *non-core large exposures group*	FSA018 (Note 7)
Solo consolidation data	FSA016 (Note 9)
Pillar 2 questionnaire	FSA019 (Note 4)
Client money and client assets	FSA039
CFTC	FSA040 (Note 8)
IRB portfolio risk	FSA045 (Note 18)
Daily flows	FSA047 (Notes 10, 13, 15 and 16)
Enhanced Mismatch Report	FSA048 (Notes 10, 13, 15 and 16)
Liquidity Buffer Qualifying Securities	FSA050 (Notes 11, 14, 15 and 16)
Funding Concentration	FSA051 (Notes 11, 14, 15 and 16)
Pricing data	FSA052 (Notes 11, 15, 16 and 17)
Retail and corporate funding	FSA 053 (Notes 11, 14, 15 and 16)
Currency Analysis	FSA054 (Notes 11, 14, 15 and 16)
Systems and Controls Questionnaire	FSA055 (Notes 12 and 16)

Note 1	When submitting the completed *data item* required, a *firm* must use the format of the *data item* set out in *SUP* 16 Annex 24R. Guidance notes for completion of the data items are contained in *SUP* 16 Annex 25 G.
Note 2	*Firms* that are members of a *consolidation group* are also required to submit this report on a *consolidation group* basis.
Note 3	*Only applicable to firms with a VaR model permission.*
Note 4	Only applicable to *firms* that: (a) are subject to consolidated supervision under *CRR*, except those that are either included within the consolidated supervision of a group that includes a UK *credit institution*, or (b) are not subject to consolidated supervision under *CRR*.

	A *UK designated investment firm* under (a) must complete the report on the basis of its *consolidation group*. A *UK designated investment firm* under (b) must complete the report on the basis of its solo position.
Note 5	Only applicable to a *firm* whose ultimate parent is a *mixed activity holding company*.
Note 6	Only applicable to a firm that is a *sole trader* or a *partnership*, when the report must be submitted by each *partner*.
Note 7	Only applicable to a *firm* that has both a *core UK group* and a *non-core large exposures group.*
Note 8	Only applicable to *firms* granted a *Part 30 exemption order* and operating an arrangement to cover forward profits on the London Metals Exchange.
Note 9	Only applicable to a *firm* with an *individual consolidation permission*.
Note 10	A *firm* must complete this item separately on each of the following bases (if applicable). (1) It must complete it on a solo basis. Therefore even if it has an *individual consolidation permission* it must complete the item on an unconsolidated basis by reference to the *firm* alone. (2) If it is a *group liquidity reporting firm* in a *DLG by default* and is a *UK lead regulated firm*, it must complete the item on the basis of that group. (3) If it is a *group liquidity reporting firm* in a *UK DLG by modification*, it must complete the item on the basis of that group. (4) If it is a *group liquidity reporting firm* in a *non-UK DLG by modification*, it must complete the item on the basis of that group.
Note 11	A *firm* must complete this item separately on each of the following bases that are applicable. (1) It must complete it on a solo basis unless it is a *group liquidity reporting firm* in a *UK DLG by modification*. Therefore even if it has an *individual consolidation permission* it must complete the item on an unconsolidated basis by reference to the *firm* alone. (2) If it is a *group liquidity reporting firm* in a *UK DLG by modification*, it must complete the item on the basis of that group.
Note 12	If it is a *non-ILAS BIPRU firm*, it must complete it on a solo basis. Therefore even if it has an *individual consolidation permission* it must complete the item on an unconsolidated basis by reference to the *firm* alone.
Note 13	(1) This item must be reported in the reporting currency. (2) If any *data element* is in a currency or currencies other than the reporting currency, all currencies (including the reporting currency) must be combined into a figure in the reporting currency.

	(3) In addition, all *material currencies* (which may include the reporting currency) must each be recorded separately (translated into the reporting currency). However if: (a) the reporting frequency is (whether under a *rule* or under a *waiver*) quarterly or less than quarterly; or (b) the only *material currency* is the reporting currency; (3) does not apply. (4) If there are more than three *material currencies* for this *data item*, (3) only applies to the three largest in amount. A *firm* must identify the largest in amount in accordance with the following procedure. (a) For each currency, take the largest of the asset or liability figure as referred to in the definition of *material currency*. (b) Take the three largest figures from the resulting list of amounts. (5) The date as at which the calculations for the purposes of the definition of *material currency* are carried out is the last day of the reporting period in question. (6) The reporting currency for this *data item* is whichever of the following currencies the *firm* chooses, namely USD (the United States Dollar), EUR (the euro), GBP (sterling), JPY (the Japanese Yen), CHF (the Swiss Franc), CAD (the Canadian Dollar) or SEK (the Swedish Krona).
Note 14	Note 13 applies, except that paragraphs (3), (4) and (5) do not apply, meaning that *material currencies* must not be recorded separately.
Note 15	Any changes to reporting requirements caused by a *firm* receiving an *intra-group liquidity modification* (or a variation to one) do not take effect until the first day of the next reporting period applicable under the changed reporting requirements for the *data item* in question if the *firm* receives that *intra-group liquidity modification* or variation part of the way through such a period. If the change is that the *firm* does not have to report a particular *data item* or does not have to report it at a particular *reporting level*, the *firm* must nevertheless report that item or at that *reporting level* for any reporting period that has already begun. This paragraph is subject to anything that the *intra-group liquidity modification* says to the contrary.
Note 16	FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054 must be completed by an *ILAS BIPRU firm*. An *ILAS BIPRU firm* does not need to complete FSA055. A *non-ILAS BIPRU firm* must complete FSA055 and does not need to complete FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054.
Note 17	This *data item* must be reported only in the currencies named in FSA052, so that liabilities in GBP are reported in GBP in rows 1 to 4, those in USD are reported in USD in rows 5 to 8, and those in Euro are reported in Euro in rows 9 to 12. Liabilities in other currencies are not to be reported.
Note 18	Only applicable to *firms* that have an *IRB permission*.

Note 19	This applies to a *firm* that applies add-ons to their market risk capital calculation under the RNIV framework.

16.12.12 ~~R~~ ~~The applicable reporting frequencies for *data items* referred to in *SUP* 16.12.4R are set out in the table below according to *firm* type. Reporting frequencies are calculated from a *firm's accounting reference date*, unless indicated otherwise.~~ [deleted]

~~*Data Item*~~	~~*BIPRU 730K firm*~~	~~*BIPRU 125K firm* **and** *UCITS investment firm*~~	~~*BIPRU 50K firm*~~	~~*UK consolidation group* or *defined liquidity group*~~	~~*Firm* **other than** *BIPRU firms*~~
~~*Annual report and accounts*~~	~~Annually~~	~~Annually~~	~~Annually~~		~~Annually~~
~~*Annual report and accounts* of the *mixed-activity holding company*~~	~~Annually~~	~~Annually~~	~~Annually~~		
~~Solvency statement~~	~~Annually~~	~~Annually~~	~~Annually~~		~~Annually~~
~~FSA001~~	~~Quarterly~~	~~Quarterly~~	~~Half yearly~~	~~Half yearly~~	
~~FSA002~~	~~Quarterly~~	~~Quarterly~~	~~Half yearly~~	~~Half yearly~~	
~~FSA003~~	~~Monthly~~	~~Quarterly~~	~~Half yearly~~	~~Half yearly~~	
~~FSA004~~	~~Quarterly~~	~~Quarterly~~	~~Half yearly~~	~~Half yearly~~	
~~FSA005~~	~~Quarterly~~	~~Quarterly~~	~~Half yearly~~	~~Half yearly~~	
~~FSA006~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	
~~FSA007~~	~~Annual (note 4)~~	~~Annual (note 4)~~	~~Annual (note 4)~~	~~Annual (note 4)~~	
~~FSA008~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	
~~FSA016~~	~~Half yearly~~	~~Half yearly~~	~~Half yearly~~		
~~FSA018~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~		
~~FSA019~~	~~Annually~~	~~Annually~~	~~Annually~~	~~Annually~~	
~~FSA028~~	~~Half yearly~~	~~Half yearly~~	~~Half yearly~~		
~~FSA029~~					~~Quarterly~~

~~FSA030~~					~~Quarterly~~
~~FSA031~~					~~Quarterly~~
~~FSA032~~					~~Quarterly~~
~~FSA033~~					~~Quarterly~~
~~FSA034~~					~~Quarterly~~
~~FSA035~~					~~Quarterly~~
~~FSA036~~					~~Quarterly~~
~~FSA039~~	~~Half yearly~~	~~Half yearly~~	~~Half yearly~~		~~Half yearly~~
~~FSA040~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~		~~Quarterly~~
~~FSA045~~	~~Quarterly~~	~~Quarterly~~	~~Half yearly~~	~~Half yearly~~	
~~FSA046~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	
~~FSA047~~	~~Daily, weekly, monthly or quarterly (Notes 5, 6 and 8)~~			~~Daily, weekly, monthly or quarterly (Notes 5, 7 and 8)~~	
~~FSA048~~	~~Daily, weekly, monthly or quarterly (Notes 5, 6 and 8)~~			~~Daily, weekly, monthly or quarterly (Notes 5, 7 and 8)~~	
~~FSA050~~	~~Monthly (Note 5)~~			~~Monthly (Note 5)~~	
~~FSA051~~	~~Monthly (Note 5)~~			~~Monthly (Note 5)~~	
~~FSA052~~	~~Weekly or monthly (Notes 5 and 9)~~			~~Weekly or monthly (Notes 5 and 10)~~	
~~FSA053~~	~~Quarterly (Note 5)~~			~~Quarterly (Note 5)~~	
~~FSA054~~	~~Quarterly (Note 5)~~			~~Quarterly (Note 5)~~	
~~FSA055~~	~~Annually (Note 5)~~			~~Annually (Note 5)~~	
~~FSA058~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	

~~Section A RMAR~~					~~Half yearly (note 2) Quarterly (note 3)~~
~~Section B RMAR~~					~~Half yearly (note 2) Quarterly (note 3)~~
~~Section C RMAR~~					~~Half yearly (note 2) Quarterly (note 3)~~
~~Section D6 RMAR~~					~~Half yearly (note 2) Quarterly (note 3)~~
~~Section F RMAR~~					~~Half yearly~~
~~Note 1~~	~~[deleted]~~				
~~Note 2~~	~~Annual regulated business revenue up to and including £5 million.~~				
~~Note 3~~	~~Annual regulated business revenue over £5 million.~~				
~~Note 4~~	~~The reporting date for this *data item* is six months after a *firm's* most recent *accounting reference date*.~~				
~~Note 5~~	~~Reporting frequencies and reporting periods for this *data item* are calculated on a calendar year basis and not from a *firm's accounting reference date*. In particular:~~ ~~(1) A week means the period beginning on Saturday and ending on Friday.~~ ~~(2) A month begins on the first day of the calendar month and ends on the last day of that month.~~ ~~(3) Quarters end on 31 March, 30 June, 30 September and 31 December.~~ ~~(4) Daily means each *business day*.~~ ~~All periods are calculated by reference to London time.~~ ~~Any changes to reporting requirements caused by a *firm* receiving an *intra-group liquidity modification* (or a variation to one) do not take effect until the first day of the next reporting period applicable under the changed reporting requirements if the *firm* receives that *intra-group liquidity modification* or variation part of the way through such a period, unless the *intra-group liquidity modification* says otherwise.~~				
~~Note 6~~	~~If the report is on a solo basis the reporting frequency is as follows:~~ ~~(1) if the *firm* does not have an *intra-group liquidity modification* the frequency is:~~				

	~~(a) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and~~ ~~(b) monthly if the *firm* is a *low frequency liquidity reporting firm*;~~ ~~(2) if the *firm* is a *group liquidity reporting firm* in a *non-UK DLG by modification (firm level)* the frequency is:~~ ~~(a) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and~~ ~~(b) monthly if the *firm* is a *low frequency liquidity reporting firm*;~~ ~~(3) the frequency is quarterly if the *firm* is a *group liquidity reporting firm* in a *UK DLG by modification*.~~
~~Note 7~~	~~(1) If the report is by reference to the *firm's DLG by default* the reporting frequency is:~~ ~~(a) weekly if the *group liquidity standard frequency reporting conditions* are met;~~ ~~(b) monthly if the *group liquidity low frequency reporting conditions* are met.~~ ~~(2) If the report is by reference to the *firm's UK DLG by modification* the reporting frequency is:~~ ~~(a) weekly if the *group liquidity standard frequency reporting conditions* are met;~~ ~~(b) monthly if the *group liquidity low frequency reporting conditions* are met.~~ ~~(3) If the report is by reference to the *firm's non-UK DLG by modification* the reporting frequency is quarterly.~~
~~Note 8~~	~~(1) If the reporting frequency is otherwise weekly, the item is to be reported on every *business day* if (and for as long as) there is a *firm-specific liquidity stress* or *market liquidity stress* in relation to the *firm* or group in question.~~ ~~(2) If the reporting frequency is otherwise monthly, the item is to be reported weekly if (and for as long as) there is a *firm-specific liquidity stress* or *market liquidity stress* in relation to the *firm* or group in question.~~ ~~(3) A *firm* must ensure that it would be able at all times to meet the requirements for daily or weekly reporting under paragraph (1) or (2) even if there is no *firm-specific liquidity stress* or *market liquidity stress* and none is expected.~~
~~Note 9~~	~~If the report is on a solo basis the reporting frequency is as follows:~~ ~~(1) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and~~ ~~(2) monthly if the *firm* is a *low frequency liquidity reporting firm*.~~
~~Note 10~~	~~If the report is by reference to the *firm's UK DLG by modification* the reporting frequency is:~~ ~~(1) weekly if the *group liquidity standard frequency reporting conditions* are met;~~ ~~(2) monthly if the *group liquidity low frequency reporting conditions* are met.~~

16.12.12A R The applicable reporting frequencies for *data items* referred to in *SUP*

16.12.4R are set out in the table below. Reporting frequencies are calculated from a *firm's accounting reference date,* unless indicated otherwise.

Data item	**Reporting frequency**
Annual report and accounts	Annually
Annual report and accounts of the *mixed-activity holding company*	Annually
Solvency statement	Annually
FSA001	Quarterly
FSA002	Quarterly
FSA005	Quarterly
FSA006	Quarterly
FSA016	Quarterly
FSA018	Quarterly
FSA019	Annually
FSA039	Half yearly
FSA040	Quarterly
FSA045	Quarterly
FSA047	Daily, weekly, monthly or quarterly (Notes 1, 2 and 3)
FSA048	Daily, weekly, monthly or quarterly (Notes 1, 2 and 3)
FSA050	Monthly (Note 1)
FSA051	Monthly (Note 1)
FSA052	Weekly or monthly (Notes 1 and 4)
FSA053	Quarterly (Note 1)
FSA054	Quarterly (Note 1)
FSA055	Annually (Note 1)

Note 1	Reporting frequencies and reporting periods for this *data item* are calculated on a calendar year basis and not from a *firm's accounting reference date*. In particular:

	(1) A week means the period beginning on Saturday and ending on Friday. (2) A month begins on the first day of the calendar month and ends on the last day of that month. (3) Quarters end on 31 March, 30 June, 30 September and 31 December. (4) Daily means each *business day*. All periods are calculated by reference to London time. Any changes to reporting requirements caused by a *firm* receiving an *intra-group liquidity modification* (or a variation to one) do not take effect until the first day of the next reporting period applicable under the changed reporting requirements if the *firm* receives that *intra-group liquidity modification* or variation part of the way through such a period, unless the *intra-group liquidity modification* says otherwise.
Note 2	If the report is on a solo basis the reporting frequency is as follows: (1) if the *firm* does not have an *intra-group liquidity modification* the frequency is: (a) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and (b) monthly if the *firm* is a *low frequency liquidity reporting firm*; (2) if the *firm* is a *group liquidity reporting firm* in a *non-UK DLG by modification (firm level)* the frequency is: (a) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and (b) monthly if the *firm* is a *low frequency liquidity reporting firm*; (3) the frequency is quarterly if the *firm* is a *group liquidity reporting firm* in a *UK DLG by modification*.
Note 3	(1) If the reporting frequency is otherwise weekly, the item is to be reported on every *business day* if (and for as long as) there is a *firm-specific liquidity stress* or *market liquidity stress* in relation to the *firm* or group in question. (2) If the reporting frequency is otherwise monthly, the item is to be reported weekly if (and for as long as) there is a *firm-specific liquidity stress* or *market liquidity stress* in relation to the *firm* or group in question. (3) A *firm* must ensure that it would be able at all times to meet the requirements for daily or weekly reporting under paragraph (1) or (2) even if there is no *firm-specific liquidity*

	*stress* or _*market liquidity stress*_ and none is expected.

16.12.13 R The applicable due dates for submission referred to in *SUP* 16.12.4R are set out in the table below. The due dates are the last day of the periods given in the table below following the relevant reporting frequency period set out in ~~*SUP* 16.12.12R,~~ _*SUP* 16.12.12AR and *SUP* 16.12.12BR_ unless indicated otherwise.

Data item	**Daily**	**Weekly**	**Monthly**	**Quarterly**	**Half yearly**	**Annual**
…						
~~FSA003~~ _[deleted]_			~~15 *business days*~~	~~20 *business days*~~	~~30 *business days* (note 1)~~ ~~45 *business days* (note 2)~~	
~~FSA004~~ _[deleted]_				~~20 *business days*~~	~~30 *business days* (note 1)~~ ~~45 *business days* (note 2)~~	
…						
~~FSA007~~ _[deleted]_						~~2 months~~
~~FSA008~~ _[deleted]_				~~20 *business days* (note 1);~~ ~~45 *business days* (note 2)~~		
…						
~~FSA028~~ _[deleted]_					~~30 *business days*~~	
…						
~~FSA046~~ _[deleted]_				~~20 business days (Note 1), 45 business~~		

				~~days (Note 2)~~		
…						
~~FSA058~~ [deleted]				~~20 business days (Note 1), 45 business days (Note 2)~~ [deleted]		
…						

…

Regulated Activity Group 4

16.12.15 R ~~The applicable *data items* referred to in *SUP* 16.12.4R according to type of *firm* are set out in the table below:~~ [deleted]

~~**Description of** *data item*~~	~~*Firms'* **prudential category and applicable data items (note 1)**~~							
	~~*BIPRU firms*~~			~~*Firms* **other than** *BIPRU firms*~~				
	~~**730K**~~	~~**125K and** *UCITS investment firms*~~	~~**730K**~~	~~**125K and** *UCITS investment firms*~~	~~**730K**~~	~~**125K and** *UCITS investment firms*~~	~~**730K**~~	~~**125K and** *UCITS investment firms*~~
~~*Annual report and accounts*~~	~~No standard format (note 13)~~							
~~*Annual report and accounts* of the *mixed-activity holding company* (note 10)~~	~~No standard format~~							
~~Solvency statement (note 11~~	~~No standard format~~				~~No standard format~~			~~No standard format~~

~~Balance sheet~~	~~FSA001 (note 2)~~	~~FSA001 (note 2)~~	~~FSA001 (note 2)~~	~~FSA029~~	~~FSA029~~	~~FSA029~~	~~FSA029 (note 15) or Section A RMAR (note 15)~~	~~FSA029~~
~~Income statement~~	~~FSA002 (note 2)~~	~~FSA002 (note 2)~~	~~FSA002 (note 2)~~	~~FSA030~~	~~FSA030~~	~~FSA030~~	~~FSA030 (note 15) or Section B RMAR (note 15)~~	~~FSA030~~
~~Capital adequacy~~	~~FSA003 (note 2)~~	~~FSA003 (note 2)~~	~~FSA003 (note 2)~~	~~FSA033~~	~~FSA034 or FSA035 (note 14)~~	~~FSA031~~	~~Section D6 RMAR or FSA032 (note 15)~~	~~FSA036~~
~~Credit risk~~	~~FSA004 (notes 2, 3)~~	~~FSA004 (notes 2, 3)~~	~~FSA004 (notes 2, 3)~~					
~~Market risk~~	~~FSA005 (notes 2, 4)~~	~~FSA005 (notes 2, 4)~~	~~FSA005 (notes 2, 4)~~					
~~Market risk – supplementary~~	~~FSA006 (note 5)~~	~~FSA006 (note 5)~~	~~FSA006 (note 5)~~					
~~Operational risk~~	~~FSA007 (notes 2, 6, 7)~~	~~FSA007 (notes 2, 6, 7)~~	~~FSA007 (notes 2, 6, 7)~~					
~~Large exposure~~	~~FSA008 (Notes 2, 6)~~	~~FSA008 (Notes 2, 6)~~	~~FSA008 (Notes 2, 6)~~					
~~UK integrated group large exposure~~	~~FSA018 (note 12)~~	~~FSA018 (note 12)~~	~~FSA018 (note 12)~~					

~~Solo consolidation data~~	~~FSA016 (note 20)~~	~~FSA016 (note 20)~~	~~FSA016 (note 20)~~					
~~Pillar 2 questionnaire~~	~~FSA019 (note 8)~~	~~FSA019 (note 8)~~	~~FSA019 (note 8)~~					
~~Non-EEA sub-group~~	~~FSA028 (note 9)~~	~~FSA028 (note 9)~~	~~FSA028 (note 9)~~					
~~Threshold conditions~~							~~Section F RMAR (note 15)~~	
~~Volumes and type of business (note 21)~~	~~FSA038~~	~~FSA038~~	~~FSA038~~	~~FSA038~~	~~FSA038~~	~~FSA038~~	~~FSA038~~	~~FSA038~~
~~Client money and client assets~~	~~FSA039~~	~~FSA039~~	~~FSA039~~	~~FSA039~~	~~FSA039~~	~~FSA039~~	~~Section C RMAR (note 15) or FSA039~~	~~FSA039~~
~~Asset managers that use hedge fund techniques (note 21)~~	~~FSA041~~	~~FSA041~~	~~FSA041~~	~~FSA041~~	~~FSA041~~	~~FSA041~~	~~FSA041~~	~~FSA041~~
~~UCITS (note 22)~~	~~FSA042~~	~~FSA042~~	~~FSA042~~	~~FSA042~~	~~FSA042~~	~~FSA042~~	~~FSA042~~	~~FSA042~~
~~IRB portfolio risk~~	~~FSA045 (note 18)~~	~~FSA045 (note 18)~~	~~FSA045 (note 18)~~					
~~Securitisation: non-trading book~~	~~FSA046 (note 19)~~	~~FSA046 (note 19)~~	~~FSA046 (note 19)~~					

~~Daily Flows~~	~~FSA047 (Notes 23, 26, 28 and 30)~~							
~~Enhanced Mismatch Report~~	~~FSA048 (Notes 23, 26, 28 and 30)~~							
~~Liquidity Buffer Qualifying Securities~~	~~FSA050 (Notes 24, 27, 28 and 30)~~							
~~Funding Concentration~~	~~FSA051 (Notes 24, 27, 28 and 30)~~							
~~Pricing data~~	~~FSA052 (Notes 24, 28, 30 and 31)~~							
~~Retail and corporate funding~~	~~FSA053 (Notes 24, 27, 28 and 30)~~							
~~Currency Analysis~~	~~FSA054 (Notes 24, 27, 28 and 30)~~							
~~Systems and Controls Questionnaire~~	~~FSA055 (Notes 25 and 30)~~							
~~Securitisation: trading book~~	~~FSA058 (Note 29)~~	~~FSA058 (Note 29)~~	~~FSA058 (Note 29)~~					
~~Note 1~~	~~When submitting the completed *data item* required, a *firm* must use the format of the *data item* set out in *SUP 16 Annex 24 R*. Guidance notes for completion of the *data items* are contained in *SUP 16 Annex 25 G*.~~							
~~Note 2~~	~~*Firms* that are members of a *UK consolidation group* are also required to submit this report on a *UK consolidation group* basis.~~							
~~Note 3~~	~~This applies to a *firm* that is required to submit *data item* FSA003 and at anytime within the 12 *months* up to its latest *accounting reference date* ("the relevant period"), was reporting *data item* FSA004 ("Firm A") or not reporting this item ("Firm B").~~ ~~In the case of Firm A it must report this *data item* if one or both of its last two~~							

	~~submissions in the relevant period show that the threshold was exceeded.~~ ~~In the case of Firm B it must report this item if both the last two submissions in the relevant period show that the threshold has been exceeded.~~ ~~The threshold is exceeded where *data element* 77A in *data item* FSA003 is greater than £10 million, or its currency equivalent, at the relevant reporting date for the *firm*.~~
~~Note 4~~	~~This applies to a *firm* that is required to submit *data item* FSA003 and at any time within the 12 *months* up to its latest *accounting reference date* ("the relevant period"), was reporting *data item* FSA005 ("Firm A") or not reporting this item ("Firm B").~~ ~~In the case of Firm A it must report this *data item* if one or both of its last two submissions in the relevant period show that the threshold was exceeded.~~ ~~In the case of Firm B it must report this item if both the last two submissions in the relevant period show that the threshold has been exceeded.~~ ~~The threshold is exceeded where *data element* 93A in *data item* FSA003 is greater than £50 million, or its currency equivalent, at the relevant reporting date for the *firm*.~~
~~Note 5~~	~~Only applicable to *firms* with a *VaR model permission*.~~
~~Note 6~~	~~This will not be applicable to *BIPRU limited activity firms* or *BIPRU limited licence firms* unless they have a waiver under *BIPRU 6.1.2 G*.~~
~~Note 7~~	~~This is only applicable to a *firm* that has adopted, in whole or in part, either the *standardised approach*, *alternative standardised approach*, or *advanced measurement approach* under *BIPRU 6*.~~
~~Note 8~~	~~Only applicable to *BIPRU investment firms* that :~~ ~~(a) are subject to consolidated supervision under *BIPRU 8*,~~ except ~~those that are either included within the consolidated supervision of a group that includes a UK *credit institution*, or that have been granted an *investment firm consolidation waiver*; or~~ ~~(b) have been granted an *investment firm consolidation waiver*; or~~ ~~(c) are not subject to consolidated supervision under *BIPRU 8*.~~ ~~A *BIPRU investment firm* under (a) must complete the report on the basis of its *UK consolidation group*. A *BIPRU investment firm* under (b) or (c) must complete the report on the basis of its solo position.~~
~~Note 9~~	~~This will be applicable to firms that are members of a *UK consolidation group* on the reporting date.~~
~~Note 10~~	~~Only applicable to a *firm* whose ultimate parent is a *mixed-activity holding company*.~~
~~Note 11~~	~~Only applicable to a *firm* that is a *sole trader* or a *partnership*, when the report must be submitted by each *partner*.~~
~~Note 12~~	~~Members of a *UK integrated group* should only submit this *data item* at the *UK integrated group* level.~~
~~Note 13~~	~~This *data item* is applicable to all *firms* in this table except a *firm* subject to *IPRU(INV)* Chapter 13 which is not an *exempt CAD firm*.~~

~~Note 14~~	~~FSA034 must be completed by a *firm* not subject to the exemption in *IPRU(INV)* 5.2.3(2)R.~~ ~~FSA035 must be completed by a *firm* subject to the exemption in *IPRU(INV)* 5.2.3(2)R.~~
~~Note 15~~	~~FSA029, FSA030, FSA032 and FSA039 only apply to a *firm* subject to *IPRU(INV)* Chapter 13 which is an *exempt CAD firm*.~~ ~~Sections A, B, C, D1, D6 and F RMAR only apply to a *firm* subject to *IPRU(INV)* Chapter 13 which is not an *exempt CAD firm*.~~
~~Note 16~~	~~[deleted]~~
~~Note 17~~	~~[deleted]~~
~~Note 18~~	~~Only applicable to *firms* that have an *IRB permission*.~~
~~Note 19~~	~~Only applicable to *firms* that hold *securitisation positions*, or are the *originator* or *sponsor* of *securitisations* of *non-trading book exposures*.~~
~~Note 20~~	~~Only applicable to a *firm* that has a *solo consolidation waiver*.~~
~~Note 21~~	~~Only applicable to *firms* that have a *managing investments permission*.~~
~~Note 22~~	~~Only applicable to *firms* that have *permission* for *establishing, operating or winding up a regulated collective investment scheme*.~~
~~Note 23~~	~~A *firm* must complete this item separately on each of the following bases (if applicable).~~ ~~(1) It must complete it on a solo basis. Therefore even if it has a *solo consolidation waiver* it must complete the item on an unconsolidated basis by reference to the *firm* alone.~~ ~~(2) If it is a *group liquidity reporting firm* in a *DLG by default* and is a *UK lead regulated firm*, it must complete the item on the basis of that group.~~ ~~(3) If it is a *group liquidity reporting firm* in a *UK DLG by modification*, it must complete the item on the basis of that group.~~ ~~(4) If it is a *group liquidity reporting firm* in a *non-UK DLG by modification*, it must complete the item on the basis of that group.~~
~~Note 24~~	~~A *firm* must complete this item separately on each of the following bases that are applicable.~~ ~~(1) It must complete it on a solo basis unless it is a *group liquidity reporting firm* in a *UK DLG by modification*. Therefore even if it has a *solo consolidation waiver* it must complete the item on an unconsolidated basis by reference to the *firm* alone.~~ ~~(2) If it is a *group liquidity reporting firm* in a *UK DLG by modification*, it must complete the item on the basis of that group.~~
~~Note 25~~	~~If it is a *non-ILAS BIPRU firm*, it must complete it on a solo basis. Therefore even if it has a *solo consolidation waiver* it must complete the item on an unconsolidated basis by reference to the *firm* alone.~~
~~Note 26~~	~~(1) This item must be reported in the reporting currency.~~ ~~(2) If any *data element* is in a currency or currencies other than the reporting~~

	~~currency, all currencies (including the reporting currency) must be combined into a figure in the reporting currency.~~ ~~(3) In addition, all *material currencies* (which may include the reporting currency) must each be recorded separately (translated into the reporting currency). However if:~~ ~~(a) the reporting frequency is (whether under a *rule* or under a *waiver*) quarterly or less than quarterly; or~~ ~~(b) the only *material currency* is the reporting currency;~~ ~~(3) does not apply.~~ ~~(4) If there are more than three *material currencies* for this *data item*, (3) only applies to the three largest in amount. A *firm* must identify the largest in amount in accordance with the following procedure.~~ ~~(a) For each currency, take the largest of the asset or liability figure as referred to in the definition of *material currency*.~~ ~~(b) Take the three largest figures from the resulting list of amounts.~~ ~~(5) The date as at which the calculations for the purposes of the definition of *material currency* are carried out is the last day of the reporting period in question.~~ ~~(6) The reporting currency for this *data item* is whichever of the following currencies the *firm* chooses, namely USD (the United States Dollar), EUR (the euro), GBP (sterling), JPY (the Japanese Yen), CHF (the Swiss Franc), CAD (the Canadian Dollar) or SEK (the Swedish Krona).~~
~~Note 27~~	~~Note 26 applies, except that paragraphs (3), (4), and (5) do not apply, meaning that *material currencies* must not be recorded separately.~~
~~Note 28~~	~~Any changes to reporting requirements caused by a *firm* receiving an *intra-group liquidity modification* (or a variation to one) do not take effect until the first day of the next reporting period applicable under the changed reporting requirements for the *data item* in question if the firm receives that *intra-group liquidity modification* or variation part of the way through such a period. If the change is that the *firm* does not have to report a particular *data item* or does not have to report it at a particular *reporting level*, the *firm* must nevertheless report that item or at that *reporting level* for any reporting period that has already begun. This paragraph is subject to anything that the *intra-group liquidity modification* says to the contrary.~~
~~Note 29~~	~~Only applicable to *firms* that hold *securitisation positions* in the *trading book* and/ or are the *originator* or *sponsor* of *securitisations* held in the *trading book*.~~
~~Note 30~~	~~FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054 must be completed by an *ILAS BIPRU firm*. An *ILAS BIPRU firm* does not need to complete FSA055. A *non-ILAS BIPRU firm* must complete FSA055 and does not need to complete FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054.~~
~~Note 31~~	~~This *data item* must be reported only in the currencies named in FSA052, so that liabilities in GBP are reported in GBP in rows 1 to 4, those in USD are reported in USD in rows 5 to 8, and those in Euro are reported in Euro in rows 9 to 12. Liabilities in other currencies are not to be reported.~~

16.12.15A G ~~The columns in the table in *SUP* 16.12.15R that deal with *BIPRU 50K firms* and *BIPRU 125K firms* cover some liquidity items that only have to be reported by an *ILAS BIPRU firm*. In fact a *BIPRU 50K firm* and a *BIPRU 125K firm* cannot be an *ILAS BIPRU firm*. One reason for drafting the table in this way is that the classification of firms into *ILAS BIPRU firms* and *non-ILAS BIPRU firms* is not based on the classification into *BIPRU 50K firms*,~~

~~*BIPRU 125K firms* and *BIPRU 730K firms* and the drafting of the table emphasises that. Also, the table covers consolidated reports and the conditions about what sort of group has to supply what type of liquidity report do not always depend on how the individual *firm* is classified.~~ [deleted]

16.12.15B R The applicable *data items* referred to in *SUP* 16.12.4R for *UK designated investment firms* are set out below:

Description of *data item*	**Applicable data items (Note 1)**
Annual report and accounts	No standard format
Annual report and accounts of the *mixed-activity holding company* *(Note 19)*	No standard format
Solvency statement (Note 11)	No standard format
Balance sheet	FSA001 (Note 2)
Income statement	FSA002 (Note 2)
Market risk	FSA005 (notes 2, 18)
Market risk – supplementary	FSA006 (Note 3)
Exposures between *core UK group* and *non-core large exposures group*	FSA018 (Note 5)
Solo consolidation data	FSA016 (Note 6)
Pillar 2 questionnaire	FSA019 (Note 4)
Volumes and type of business (Note 15)	FSA038
Client money and client assets	FSA039
Asset managers that use hedge fund techniques (Note 15)	FSA041
UCITS (Note 16)	FSA042
IRB portfolio risk	FSA045 (note 17)
Daily Flows	FSA047 (Notes 7,10, 12 and 13)
Enhanced Mismatch Report	FSA048 (Notes 7, 10, 12 and 13)
Liquidity Buffer Qualifying Securities	FSA050 (Notes 8, 11, 12 and 13)
Funding Concentration	FSA051 (Notes 8, 11, 12 and 13)
Pricing data	FSA052 (Notes 8, 12, 13 and 14)

Retail and corporate funding	FSA053 (Notes 8, 11, 12 and 13)
Currency Analysis	FSA054 (Notes 8, 11, 12 and 13)
Systems and Control Questionnaire	FSA055 (Notes 9 and 13)

Note 1	When submitting the completed *data item* required, a *firm* must use the format of the *data item* set out in *SUP 16 Annex 24 R*. Guidance notes for completion of the *data items* are contained in *SUP 16 Annex 25 G*.
Note 2	*Firms* that are members of a *consolidation group* are also required to submit this report on a *consolidation group* basis.
Note 3	Only applicable to *firms* with a *VaR model permission.*
Note 4	Only applicable to *UK designated investment firms* that : (a) are subject to consolidated supervision under *CRR*, except those that are either included within the consolidated supervision of a group that includes a UK *credit institution*, or (b) are not subject to consolidated supervision under *CRR*. A *UK designated investment firm* under (a) must complete the report on the basis of its *consolidation group*. A *UK designated investment firm* under (b) must complete the report on the basis of its solo position.
Note 5	Only applicable to a *firm* that has both a *core UK group* and a *non-core large exposures group.*
Note 6	Only applicable to a *firm* that has an *individual consolidation permission*.
Note 7	A *firm* must complete this item separately on each of the following bases (if applicable). (1) It must complete it on a solo basis. Therefore even if it has an *individual consolidation permission* it must complete the item on an unconsolidated basis by reference to the *firm* alone. (2) If it is a *group liquidity reporting firm* in a *DLG by default* and is a *UK lead regulated firm*, it must complete the item on the basis of that group. (3) If it is a *group liquidity reporting firm* in a *UK DLG by modification*, it must complete the item on the basis of that group. (4) If it is a *group liquidity reporting firm* in a *non-UK DLG by modification*, it must complete the item on the basis of that group.

Note 8	A *firm* must complete this item separately on each of the following bases that are applicable. (1) It must complete it on a solo basis unless it is a *group liquidity reporting firm* in a *UK DLG by modification*. Therefore even if it has an *individual consolidation permission* it must complete the item on an unconsolidated basis by reference to the *firm* alone. (2) If it is a *group liquidity reporting firm* in a *UK DLG by modification*, it must complete the item on the basis of that group.
Note 9	If it is a *non-ILAS BIPRU firm*, it must complete it on a solo basis. Therefore even if it has an *individual consolidation permission* it must complete the item on an unconsolidated basis by reference to the *firm* alone.
Note 10	(1) This item must be reported in the reporting currency. (2) If any *data element* is in a currency or currencies other than the reporting currency, all currencies (including the reporting currency) must be combined into a figure in the reporting currency. (3) In addition, all *material currencies* (which may include the reporting currency) must each be recorded separately (translated into the reporting currency). However if: (a) the reporting frequency is (whether under a *rule* or under a *waiver*) quarterly or less than quarterly; or (b) the only *material currency* is the reporting currency; (3) does not apply. (4) If there are more than three *material currencies* for this *data item*, (3) only applies to the three largest in amount. A *firm* must identify the largest in amount in accordance with the following procedure. (a) For each currency, take the largest of the asset or liability figure as referred to in the definition of *material currency*. (b) Take the three largest figures from the resulting list of amounts. (5) The date as at which the calculations for the purposes of the definition of *material currency* are carried out is the last day of the reporting period in question. (6) The reporting currency for this *data item* is whichever of the following currencies the *firm* chooses, namely USD (the United States Dollar), EUR (the euro), GBP (sterling), JPY (the Japanese Yen), CHF (the Swiss Franc), CAD (the Canadian Dollar) or SEK (the Swedish Krona).
Note 11	Note 10 applies, except that paragraphs (3), (4), and (5) do not apply, meaning that *material currencies* must not be recorded separately.
Note 12	Any changes to reporting requirements caused by a *firm* receiving an *intra-group liquidity modification* (or a variation to one) do not take effect until the first day of the next

	reporting period applicable under the changed reporting requirements for the *data item* in question if the firm receives that *intra-group liquidity modification* or variation part of the way through such a period. If the change is that the *firm* does not have to report a particular *data item* or does not have to report it at a particular *reporting level*, the *firm* must nevertheless report that item or at that *reporting level* for any reporting period that has already begun. This paragraph is subject to anything that the *intra-group liquidity modification* says to the contrary.
Note 13	FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054 must be completed by an *ILAS BIPRU firm*. An *ILAS BIPRU firm* does not need to complete FSA055. A *non-ILAS BIPRU firm* must complete FSA055 and does not need to complete FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054.
Note 14	This *data item* must be reported only in the currencies named in FSA052, so that liabilities in GBP are reported in GBP in rows 1 to 4, those in USD are reported in USD in rows 5 to 8, and those in Euro are reported in Euro in rows 9 to 12. Liabilities in other currencies are not to be reported.
Note 15	Only applicable to *firms* that have a *managing investments permission*.
Note 16	Only applicable to *firms* that have *permission* for *establishing, operating or winding up a regulated collective investment scheme*.
Note 17	Only applicable to *firms* that have an *IRB permission*.
Note 18	This applies to a *firm* that applies add-ons to their market risk capital calculation under the RNIV framework.
Note 19	Only applicable to a *firm* whose ultimate parent is a *mixed activity holding company*.

16.12.16 R ~~The applicable reporting frequencies for *data items* referred to in *SUP* 16.12.15R are set out in the table below according to *firm* type. Reporting frequencies are calculated from a *firm's accounting reference date*, unless indicated otherwise.~~

~~*Data item*~~	~~*Firms'* prudential category~~				
	~~*BIPRU 730K firm*~~	~~*BIPRU 125K firm* and *UCITS investment firm*~~	~~*BIPRU 50K firm*~~	~~*UK consolidation group* or *defined liquidity group*~~	~~*Firm* **other than** *BIPRU firms*~~
~~*Annual report and accounts*~~	~~Annually~~	~~Annually~~	~~Annually~~		~~Annually~~

~~*Annual report and accounts* of the *mixed-activity holding company*~~	~~Annually~~	~~Annually~~	~~Annually~~		
~~Solvency statement~~	~~Annually~~	~~Annually~~	~~Annually~~		~~Annually~~
~~FSA001~~	~~Quarterly~~	~~Quarterly~~	~~Half yearly~~	~~Half yearly~~	
~~FSA002~~	~~Quarterly~~	~~Quarterly~~	~~Half yearly~~	~~Half yearly~~	
~~FSA003~~	~~Monthly~~	~~Quarterly~~	~~Half yearly~~	~~Half yearly~~	
~~FSA004~~	~~Quarterly~~	~~Quarterly~~	~~Half yearly~~	~~Half yearly~~	
~~FSA005~~	~~Quarterly~~	~~Quarterly~~	~~Half yearly~~	~~Half yearly~~	
~~FSA006~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	
~~FSA007~~	~~Annual(note 4)~~	~~Annual (note 4)~~	~~Annual (note 4)~~	~~Annual (note 4)~~	
~~FSA008~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	
~~FSA016~~	~~Half yearly~~	~~Half yearly~~	~~Half yearly~~		
~~FSA018~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~		
~~FSA019~~	~~Annually~~	~~Annually~~	~~Annually~~	~~Annually~~	
~~FSA028~~	~~Half yearly~~	~~Half yearly~~	~~Half yearly~~		
~~FSA029~~					~~Quarterly~~
~~FSA030~~					~~Quarterly~~
~~FSA031~~					~~Quarterly~~
~~FSA032~~					~~Quarterly~~
~~FSA033~~					~~Quarterly~~
~~FSA034~~					~~Quarterly~~
~~FSA035~~					~~Quarterly~~
~~FSA036~~					~~Quarterly~~
~~FSA038~~	~~Half yearly~~	~~Half yearly~~	~~Half yearly~~		~~Half yearly~~
~~FSA039~~	~~Half yearly~~	~~Half yearly~~	~~Half yearly~~		~~Half yearly~~

~~FSA041~~	~~Annually~~	~~Annually~~	~~Annually~~		~~Annually~~
~~FSA042~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~		~~Quarterly~~
~~FSA045~~	~~Quarterly~~	~~Quarterly~~	~~Half yearly~~	~~Half yearly~~	
~~FSA046~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	
~~FSA047~~	~~Daily, weekly, monthly or quarterly (Notes 5, 6 and 8)~~			~~Daily, weekly, monthly or quarterly (Notes 5, 7 and 8)~~	
~~FSA048~~	~~Daily, weekly, monthly or quarterly (Notes 5, 6 and 8)~~			~~Daily, weekly, monthly or quarterly (Notes 5, 7 and 8)~~	
~~FSA050~~	~~Monthly (Note 5)~~			~~Monthly (Note 5)~~	
~~FSA051~~	~~Monthly (Note 5)~~			~~Monthly (Note 5)~~	
~~FSA052~~	~~Weekly or monthly (Notes 5 and 9)~~			~~Weekly or monthly (Notes 5 and 10)~~	
~~FSA053~~	~~Quarterly (Note 5)~~			~~Quarterly (Note 5)~~	
~~FSA054~~	~~Quarterly (Note 5)~~			~~Quarterly (Note 5)~~	
~~FSA055~~	~~Annually (Note 5)~~			~~Annually (Note 5)~~	
~~FSA058~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	
~~Section A RMAR~~					~~Half yearly (note 2) Quarterly (note 3)~~
~~Section B RMAR~~					~~Half yearly (note 2) Quarterly (note 3)~~
~~Section C RMAR~~					~~Half yearly (note 2) Quarterly (note 3)~~

~~Section D6 RMAR~~					~~Half yearly (note 2)~~ ~~Quarterly (note 3)~~
~~Section F RMAR~~					~~Half yearly~~
~~Note 1~~	~~[deleted]~~				
~~Note 2~~	~~Annual regulated business revenue up to and including £5 million.~~				
~~Note 3~~	~~Annual regulated business revenue over £5 million.~~				
~~Note 4~~	~~The reporting date for this *data item* is six months after a *firm's* most recent *accounting reference date*.~~				
~~Note 5~~	~~Reporting frequencies and reporting periods for this *data item* are calculated on a calendar year basis and not from a *firm's accounting reference date*. In particular:~~ ~~(1) A week means the period beginning on Saturday and ending on Friday.~~ ~~(2) A month begins on the first day of the calendar month and ends on the last day of that month.~~ ~~(3) Quarters end on 31 March, 30 June, 30 September and 31 December.~~ ~~(4) Daily means each *business day*.~~ ~~All periods are calculated by reference to London time.~~ ~~Any changes to reporting requirements caused by a *firm* receiving an *intra-group liquidity modification* (or a variation to one) do not take effect until the first day of the next reporting period applicable under the changed reporting requirements if the *firm* receives that *intra-group liquidity modification* or variation part of the way through such a period, unless the *intra-group liquidity modification* says otherwise.~~				
~~Note 6~~	~~If the report is on a solo basis the reporting frequency is as follows:~~ ~~(1) if the *firm* does not have an *intra-group liquidity modification* the frequency is:~~ ~~(a) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and~~ ~~(b) monthly if the *firm* is a *low frequency liquidity reporting firm*;~~ ~~(2) if the *firm* is a *group liquidity reporting firm* in a *non-UK DLG by modification (firm level)* the frequency is:~~ ~~(a) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and~~ ~~(b) monthly if the *firm* is a *low frequency liquidity reporting firm*;~~ ~~(3) the frequency is quarterly if the *firm* is a *group liquidity reporting firm* in a *UK DLG by modification*.~~				

~~Note 7~~	~~(1) If the report is by reference to the *firm's DLG by default* the reporting frequency is:~~ ~~(a) weekly if the *group liquidity standard frequency reporting conditions* are met;~~ ~~(b) monthly if the *group liquidity low frequency reporting conditions* are met.~~ ~~(2) If the report is by reference to the *firm's UK DLG by modification* the reporting frequency is:~~ ~~(a) weekly if the *group liquidity standard frequency reporting conditions* are met;~~ ~~(b) monthly if the *group liquidity low frequency reporting conditions* are met.~~ ~~(3) If the report is by reference to the *firm's non-UK DLG by modification* the reporting frequency is quarterly.~~
~~Note 8~~	~~(1) If the reporting frequency is otherwise weekly, the item is to be reported on every *business day* if (and for as long as) there is a *firm-specific liquidity stress* or *market liquidity stress* in relation to the *firm* or group in question.~~ ~~(2) If the reporting frequency is otherwise monthly, the item is to be reported weekly if (and for as long as) there is a *firm-specific liquidity stress* or *market liquidity stress* in relation to the *firm* or group in question.~~ ~~(3) A *firm* must ensure that it would be able at all times to meet the requirements for daily or weekly reporting under paragraph (1) or (2) even if there is no *firm-specific liquidity stress* or *market liquidity stress* and none is expected.~~
~~Note 9~~	~~If the report is on a solo basis the reporting frequency is as follows:~~ ~~(1) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and~~ ~~(2) monthly if the *firm* is a *low frequency liquidity reporting firm*.~~
~~Note 10~~	~~If the report is by reference to the *firm's UK DLG by modification* the reporting frequency is:~~ ~~(1) weekly if the *group liquidity standard frequency reporting conditions* are met;~~ ~~(2) monthly if the *group liquidity low frequency reporting conditions* are met.~~

16.12.16A R The applicable reporting frequencies for *data items* referred to in *SUP* 16.12.15B are set out in the table below. Reporting frequencies are calculated from a *firm's accounting reference date*, unless indicated otherwise.

Data item	**Reporting frequency**
Annual report and accounts	Annually

Annual report and accounts of the *mixed-activity holding company*	Annually
Solvency statement	Annually
FSA001	Quarterly
FSA002	Quarterly
FSA005	Quarterly
FSA006	Quarterly
FSA016	Half yearly
FSA018	Quarterly
FSA019	Annually
FSA038	Half yearly
FSA039	Half yearly
FSA041	Annually
FSA042	Quarterly
FSA045	Quarterly
FSA047	Daily, weekly, monthly or quarterly (Notes 1, 2 and 3)
FSA048	Daily, weekly, monthly or quarterly (Notes 1, 2 and 3)
FSA050	Monthly (Note 1)
FSA051	Monthly (Note 1)
FSA052	Weekly or monthly (Notes 1 and 4)
FSA053	Quarterly (Note 1)
FSA054	Quarterly (Note 1)
FSA055	Annually (Note 1)

Note 1	Reporting frequencies and reporting periods for this *data item* are calculated on a calendar year basis and not from a *firm's accounting reference date*. In particular: (1) A week means the period beginning on Saturday and ending on Friday. (2) A month begins on the first day of the calendar month and ends on the last day of that month.

	(3) Quarters end on 31 March, 30 June, 30 September and 31 December. (4) Daily means each *business day*. All periods are calculated by reference to London time. Any changes to reporting requirements caused by a *firm* receiving an *intra-group liquidity modification* (or a variation to one) do not take effect until the first day of the next reporting period applicable under the changed reporting requirements if the *firm* receives that *intra-group liquidity modification* or variation part of the way through such a period, unless the *intra-group liquidity modification* says otherwise.
Note 2	If the report is on a solo basis the reporting frequency is as follows: (1) if the *firm* does not have an *intra-group liquidity modification* the frequency is: (a) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and (b) monthly if the *firm* is a *low frequency liquidity reporting firm*; (2) if the *firm* is a *group liquidity reporting firm* in a *non-UK DLG by modification (firm level)* the frequency is: (a) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and (b) monthly if the *firm* is a *low frequency liquidity reporting firm*; (3) the frequency is quarterly if the *firm* is a *group liquidity reporting firm* in a *UK DLG by modification*.
Note 3	(1) If the reporting frequency is otherwise weekly, the item is to be reported on every *business day* if (and for as long as) there is a *firm-specific liquidity stress* or *market liquidity stress* in relation to the *firm* or group in question. (2) If the reporting frequency is otherwise monthly, the item is to be reported weekly if (and for as long as) there is a *firm-specific liquidity stress* or *market liquidity stress* in relation to the *firm* or group in question. (3) A *firm* must ensure that it would be able at all times to meet the requirements for daily or weekly reporting under paragraph (1) or (2) even if there is no *firm-specific liquidity stress* or *market liquidity stress* and none is expected.
Note 4	If the report is on a solo basis the reporting frequency is as follows:

	(1) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and (2) monthly if the *firm* is a *low frequency liquidity reporting firm*.

16.12.17 R The applicable due dates for submission referred to in *SUP* 16.12.4R are set out in the table below. The due dates are the last day of the periods given in the table below following the relevant reporting frequency period set out in ~~*SUP* 16.12.16R~~ *SUP* 16.12.16AR , unless indicated otherwise.

Data item	Daily	Weekly	Monthly	Quarterly	Half yearly	Annual
…						
~~FSA003~~			~~15 *business days*~~	~~20 *business days*~~	~~30 *business days* (note 2); 45 *business days* (note 3)~~	
~~FSA004~~				~~20 *business days*~~	~~30 *business days* (note 2); 45 *business days* (note 3)~~	
…						
~~FSA007~~						~~2 months~~
~~FSA008~~				~~20 *business days* (note 2); 45 *business days* (note 3)~~		
…						
~~FSA028~~					~~30 *business days*~~	
…						
~~FSA046~~				~~20 business days (Note 2), 45 business days (Note 3)~~		

…						
~~FSA058~~				~~20 business days (Note 2), 45 business days (Note 3)~~		
…						

Regulated Activity Group 7

…

16.12.22A ~~R~~ ~~The applicable *data items* referred to in *SUP* 16.12.4R are set out according to type of *firm* in the table below:~~ [deleted]

~~**Description of** *Data item*~~	~~*Firms'* prudential category and applicable *data item* (note 1)~~					
	~~*BIPRU 730K firm*~~	~~*BIPRU 125K firm* **and** *UCITS investment firm*~~	~~*BIPRU 50K firm*~~	~~*Exempt CAD firms* **subject to** *IPRU(INV)* **Chapter 13**~~	~~*Firms* **(other than** *exempt CAD firms*) **subject to** *IPRU(INV)* **Chapter 13**~~	~~*Firms* **that are also in one or more of** *RAGs* **1 to 6 and not subject to** *IPRU(INV)* **Chapter 13**~~
~~*Annual report and accounts*~~	~~No standard format~~			~~No standard format~~		
~~*Annual report and accounts* of the *mixed-activity holding company* (note 10)~~	~~No standard format~~					
~~Solvency statement~~	~~No standard format (note 11)~~					
~~Balance Sheet~~	~~FSA001 (note 2)~~	~~FSA001 (note 2)~~	~~FSA001 (note 2)~~	~~FSA029~~	~~Section A RMAR~~	

~~Income Statement~~	~~FSA002 (note 2)~~	~~FSA002 (note 2)~~	~~FSA002 (note 2)~~	~~FSA030~~	~~Section B RMAR~~	
~~Capital Adequacy~~	~~FSA003 (note 2)~~	~~FSA003 (note 2)~~	~~FSA003 (note 2)~~	~~FSA032~~	~~Section D6 RMAR (Note 23)~~	
~~Credit risk~~	~~FSA004 (notes 2, 3)~~	~~FSA004 (notes 2, 3)~~	~~FSA004 (notes 2, 3)~~			
~~Market risk~~	~~FSA005 (notes 2, 4)~~	~~FSA005 (notes 2, 4)~~	~~FSA005 (notes 2, 4)~~			
~~Market risk – supplementary~~	~~FSA006 (note 5)~~	~~FSA006 (note 5)~~	~~FSA006 (note 5)~~			
~~Operational risk~~	~~FSA007 (notes 2, 6, 7)~~	~~FSA007 (notes 2, 6, 7)~~	~~FSA007 (notes 2, 6, 7)~~			
~~Large exposures~~	~~FSA008 (Notes 2, 6)~~	~~FSA008 (Notes 2, 6)~~	~~FSA008 (Notes 2, 6)~~			
~~UK integrated group large exposures~~	~~FSA018 (note 12)~~	~~FSA018 (note 12)~~	~~FSA018 (note 12)~~			
~~Solo consolidation data~~	~~FSA016~~	~~FSA016~~	~~FSA016~~			
~~Pillar 2 questionnaire~~	~~FSA019 (note 8)~~	~~FSA019 (note 8)~~	~~FSA019 (note 8)~~			
~~Non-EEA sub-group~~	~~FSA028 (note 9)~~	~~FSA028 (note 9)~~	~~FSA028 (note 9)~~			
~~Professional indemnity insurance (note 15)~~	~~Section E RMAR~~	~~Section E RMAR~~	~~Section E RMAR~~		~~Section E RMAR~~	~~Section E RMAR~~
~~Threshold Conditions~~				~~Section F RMAR~~	~~Section F RMAR~~	
~~Training and Competence~~	~~Section G RMAR~~	~~Section G RMAR~~	~~Section G RMAR~~	~~Section G RMAR~~	~~Section G RMAR~~	~~Section G RMAR~~

~~COBS data~~	~~Section H RMAR~~	~~Section H RMAR~~	~~Section H RMAR~~	~~Section H RMAR~~	~~Section H RMAR~~	~~Section H RMAR~~
~~Client money and client assets~~	~~Section C RMAR~~	~~Section C RMAR~~	~~Section C RMAR~~	~~Section C RMAR~~	~~Section C RMAR~~	
~~Fees and levies~~	~~Section J RMAR~~	~~Section J RMAR~~	~~Section J RMAR~~	~~Section J RMAR~~	~~Section J RMAR~~	
~~*Adviser charges*~~	~~Section K RMAR (Note 26)~~	~~Section K RMAR (Note 26)~~	~~Section K RMAR (Note 26)~~	~~Section K RMAR (Note 26)~~	~~Section K RMAR (Note 26)~~	~~Section K RMAR (Note 26)~~
~~*Consultancy charges*~~	~~Section L RMAR (Note 27)~~	~~Section L RMAR (Note 27)~~	~~Section L RMAR (Note 27)~~	~~Section L RMAR (Note 27)~~	~~Section L RMAR (Note 27)~~	~~Section L RMAR (Note 27)~~
~~IRB portfolio risk~~	~~FSA045 (note 13)~~	~~FSA045 (note 13)~~	~~FSA045 (note 13)~~			
~~Securitisation: non-trading book~~	~~FSA046 (note 14)~~	~~FSA046 (note 14)~~	~~FSA046 (note 14)~~			
~~Daily Flows~~	~~FSA047 (Notes 16, 19, 21 and 24)~~					
~~Enhanced Mismatch Report~~	~~FSA048 (Notes 16, 19, 21 and 24)~~					
~~Liquidity Buffer Qualifying Securities~~	~~FSA050 (Notes 17, 20, 21 and 24)~~					
~~Funding Concentration~~	~~FSA051 (Notes 17, 20, 21 and 24)~~					
~~Pricing data~~	~~FSA052 (Notes 17, 20, 24 and 25)~~					
~~Retail and corporate funding~~	~~FSA053 (Notes 17, 20, 21 and 24)~~					
~~Currency Analysis~~	~~FSA054 (Notes 17, 20, 21 and 24)~~					
~~Systems and Controls Questionn~~	~~FSA055 (Notes 18 and 24)~~					

~~aire~~						
~~Securitisation: trading book~~	~~FSA058 (Note 22)~~	~~FSA058 (Note 22)~~	~~FSA058 (Note 22)~~			
~~Note 1~~	~~When submitting the completed *data item* required, a *firm* must use the format of the *data item* set out in *SUP 16 Annex 24 R*, or *SUP 16 Annex 18A R* in the case of the RMAR. Guidance notes for completion of the data items are contained in *SUP 16 Annex 25 G*, or *SUP 16 Annex 18B G* in the case of the RMAR.~~					
~~Note 2~~	~~*Firms* that are members of a *UK consolidation group* are also required to submit this report on a *UK consolidation group* basis.~~					
~~Note 3~~	~~This applies to a *firm* that is required to submit *data item* FSA003 and, at any time within the 12 *months* up to its latest *accounting reference date* ("the relevant period"), was reporting *data item* FSA004 ("Firm A") or not reporting this item ("Firm B").~~ ~~In the case of Firm A it must report this *data item* if one or both of its last two submissions in the relevant period show that the threshold was exceeded.~~ ~~In the case of Firm B it must report this item if both the last two submissions in the relevant period show that the threshold has been exceeded.~~ ~~The threshold is exceeded where *data element* 77A in data item FSA003 is greater than £10 million, or its currency equivalent, at the relevant reporting date for the *firm*.~~					
~~Note 4~~	~~This applies to a *firm* that is required to submit *data item* FSA003 and, at any time within the 12 *months* up to its latest *accounting reference date* ("the relevant period"), was reporting *data item* FSA005 ("Firm A") or not reporting this item ("Firm B").~~ ~~In the case of Firm A it must report this *data item* if one or both of its last two submissions in the relevant period show that the threshold was exceeded.~~ ~~In the case of Firm B it must report this item if both the last two submissions in the relevant period show that the threshold has been exceeded.~~ ~~The threshold is exceeded where *data element* 93A in *data item* FSA003 is greater than £50 million, or its currency equivalent, at the relevant reporting date for the *firm*.~~					
~~Note 5~~	~~Only applicable to *firms* with a *VaR model permission*.~~					
~~Note 6~~	~~This will not be applicable to *BIPRU limited activity firms* or *BIPRU limited licence firms* unless they have a waiver under *BIPRU 6.1.2 G*.~~					
~~Note 7~~	~~This is only applicable to a *firm* that has adopted, in whole or in part, either the *standardised approach*, *alternative standardised approach*, or *advanced measurement approach* under *BIPRU 6*.~~					
~~Note 8~~	~~Only applicable to *BIPRU investment firms* that:~~ ~~(a) are subject to consolidated supervision under *BIPRU 8*, except those that are either included within the consolidated supervision of a group that includes a UK *credit institution*, or that have been granted an *investment firm consolidation waiver*; or~~					

	~~(b) have been granted an *investment firm consolidation waiver*; or~~ ~~(c) are not subject to consolidated supervision under *BIPRU 8* .~~ ~~A *BIPRU investment firm* under (a) must complete the report on the basis of its *UK consolidation group*. A *BIPRU investment firm* under (b) or (c) must complete the report on the basis of its solo position.~~	
~~Note 9~~	~~This will be applicable to *firms* that are members of a *UK consolidation group* on the reporting date.~~	
~~Note 10~~	~~Only applicable to a *firm* whose ultimate parent is a *mixed-activity holding company*.~~	
~~Note 11~~	~~Only applicable to a firm that is a *sole trader* or a *partnership*, when the report must be submitted by each *partner*.~~	
~~Note 12~~	~~Members of a *UK integrated group* should only submit this *data item* at the *UK integrated group* level.~~	
~~Note 13~~	~~Only applicable to *firms* that have an *IRB permission*.~~	
~~Note 14~~	~~Only applicable to *firms* that hold *securitisation positions*, or are the *originator* or *sponsor* of *securitisations* of *non-trading book exposures*.~~	
~~Note 15~~	~~This item only applies to *firms* that are subject to an *FSA* requirement to hold professional indemnity insurance and are not *exempt CAD firms*.~~	
~~Note 16~~	~~A *firm* must complete this item separately on each of the following bases (if applicable).~~ ~~(1) It must complete it on a solo basis. Therefore even if it has a *solo consolidation waiver* it must complete the item on an unconsolidated basis by reference to the *firm* alone.~~ ~~(2) If it is a *group liquidity reporting firm* in a *DLG by default* and is a *UK lead regulated firm*, it must complete the item on the basis of that group.~~ ~~(3) If it is a *group liquidity reporting firm* in a *UK DLG by modification*, it must complete the item on the basis of that group.~~ ~~(4) If it is a *group liquidity reporting firm* in a *non-UK DLG by modification*, it must complete the item on the basis of that group.~~	
~~Note 17~~	~~A *firm* must complete this item separately on each of the following bases that are applicable.~~ ~~(1) It must complete it on a solo basis unless it is a *group liquidity reporting firm* in a *UK DLG by modification*. Therefore even if it has a *solo consolidation waiver* it must complete the item on an unconsolidated basis by reference to the *firm* alone.~~ ~~(2) If it is a *group liquidity reporting firm* in a *UK DLG by modification*, it must complete the item on the basis of that group.~~	
~~Note 18~~	~~If it is a *non-ILAS BIPRU firm*, it must complete it on a solo basis. Therefore even if it has a *solo consolidation waiver* it must complete the item on an unconsolidated basis by reference to the~~	

	~~*firm* alone.~~	
~~Note 19~~	~~(1) This item must be reported in the reporting currency.~~ ~~(2) If any *data element* is in a currency or currencies other than the reporting currency, all currencies (including the reporting currency) must be combined into a figure in the reporting currency.~~ ~~(3) In addition, all *material currencies* (which may include the reporting currency) must each be recorded separately (translated into the reporting currency). However if:~~ ~~(a) the reporting frequency is (whether under a *rule* or under a *waiver*) quarterly or less than quarterly; or~~ ~~(b) the only *material currency* is the reporting currency;~~ ~~(3) does not apply.~~ ~~(4) If there are more than three *material currencies* for this *data item*, (3) only applies to the three largest in amount. A *firm* must identify the largest in amount in accordance with the following procedure.~~ ~~(a) For each currency, take the largest of the asset or liability figure as referred to in the definition of *material currency*.~~ ~~(b) Take the three largest figures from the resulting list of amounts.~~ ~~(5) The date as at which the calculations for the purposes of the definition of *material currency* are carried out is the last day of the reporting period in question.~~ ~~(6) The reporting currency for this *data item* is whichever of the following currencies the *firm* chooses, namely USD (the United States Dollar), EUR (the euro), GBP (sterling), JPY (the Japanese Yen), CHF (the Swiss Franc), CAD (the Canadian Dollar) or SEK (the Swedish Krona).~~	
~~Note 20~~	~~Note 19 applies, except that paragraphs (3), (4) and (5) do not apply, meaning that *material currencies* must not be recorded separately.~~	
~~Note 21~~	~~Any changes to reporting requirements caused by a *firm* receiving an *intra-group liquidity modification* (or a variation to one) do not take effect until the first day of the next reporting period applicable under the changed reporting requirements for the *data item* in question if the *firm* receives that *intra-group liquidity modification* or variation part of the way through such a period. If the change is that the *firm* does not have to report a particular *data item* or does not have to report it at a particular *reporting level*, the *firm* must nevertheless report that item or at that *reporting level* for any reporting period that has already begun. This paragraph is subject to anything that the *intra-group liquidity modification* says to the contrary.~~	
~~Note 22~~	~~Only applicable to *firms* that hold *securitisation positions* in the *trading book* and/ or are the *originator* or *sponsor* of *securitisations* held in the *trading book*.~~	

~~Note 23~~	~~Where a *firm* submits data items for both *RAG 7* and *RAG 9*, the *firm* must complete both Sections D1 and D6 RMAR.~~
~~Note 24~~	~~FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054 must be completed by an *ILAS BIPRU firm*. An *ILAS BIPRU firm* does not need to complete FSA055. A *non-ILAS BIPRU firm* must complete FSA055 and does not need to complete FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054.~~
~~Note 25~~	~~This *data item* must be reported only in the currencies named in FSA052, so that liabilities in GBP are reported in GBP in rows 1 to 4, those in USD are reported in USD in rows 5 to 8, and those in Euro are reported in Euro in rows 9 to 12. Liabilities in other currencies are not to be reported.~~
~~Note 26~~	~~This item only applies to *firms* that provide advice on *retail investment products*.~~
~~Note 27~~	~~This item applies only to firms that provide advice and related services to employers on *group personal pension schemes* and/or *group stakeholder pension schemes*.~~

16.12.22B G ~~The columns in the table in *SUP* 16.12.22AR that deal with *BIPRU 50K firms* and *BIPRU 125K firms* cover some liquidity items that only have to be reported by an *ILAS BIPRU firm*. In fact a *BIPRU 50K firm* and a *BIPRU 125K firm* cannot be an *ILAS BIPRU firm*. One reason for drafting the table in this way is that the classification of *firms* into *ILAS BIPRU firms* and *non-ILAS BIPRU firms* is not based on the classification into *BIPRU 50K firms*, *BIPRU 125K firms* and *BIPRU 730K firms* and the drafting of the table emphasises that. Also, the table covers consolidated reports and the conditions about what sort of group has to supply what type of liquidity report do not always depend on how the individual *firm* is classified.~~ [deleted]

16.12.22C R The applicable *data items* referred to in *SUP* 16.12.4R for *UK designated investment firms* are set out in the table below:

Description of *data item*	Applicable *data item* (Note 1)
Annual report and accounts	No standard format
Annual report and accounts of the *mixed-activity holding company* (note 16)	No standard format
Solvency statement	No standard format (Note 17)
Balance sheet	FSA001 (Note 2)
Income statement	FSA 002 (note 2)
Market risk	FSA005 (notes 2, 20)
Market risk – supplementary	FSA006 (note 3)
Exposures between *core UK group* and *non-core large*	FSA018 (note 18)

exposures group	
Solo consolidation data	FSA016
Pillar 2 questionnaire	FSA019 (note 4)
IRB portfolio risk	FSA045 (note 19)
Daily Flows	FSA047 (Notes 6, 9, 11 and 12)
Enhanced Mismatch Report	FSA048 (Notes 6, 9, 11 and 12)
Liquidity Buffer Qualifying Securities	FSA050 (Notes 7, 10, 11 and 12)
Funding Concentration	FSA051 (Notes 7, 10, 11 and 12)
Pricing Data	FSA052 (Note 7, 10, 12 and 13)
Retail and corporate funding	FSA053 (Notes 7, 10, 11 and 12)
Currency Analysis	FSA054 (Notes 7, 10, 11 and 12)
Systems and Controls Questionnaire	FSA055 (Notes 8 and 12)

Note 1	When submitting the completed *data item* required, a *firm* must use the format of the *data item* set out in *SUP 16 Annex 24 R*, or *SUP 16 Annex 18A R* in the case of the RMAR. Guidance notes for completion of the data items are contained in *SUP 16 Annex 25 G*, or *SUP 16 Annex 18B G* in the case of the RMAR.
Note 2	*Firms* that are members of a *consolidation group* are also required to submit this report on a *consolidation group* basis.
Note 3	Only applicable to *firms* with a *VaR model permission*.
Note 4	Only applicable to *UK designated investment firms* that: (a) are subject to consolidated supervision under *CRR*, except those that are either included within the consolidated supervision of a group that includes a UK *credit institution* or (b) are not subject to consolidated supervision under *CRR*. A *UK designated investment firm* under (a) must complete the report on the basis of its *consolidation group*. A *UK designated investment firm* under (b) or must complete the report on the basis of its solo position.
Note 5	This item only applies to *firms* that are subject to a requirement to hold professional indemnity insurance and

	are not *exempt CAD firms*.
Note 6	A *firm* must complete this item separately on each of the following bases (if applicable). (1) It must complete it on a solo basis. Therefore even if it has an *individual consolidation permission* it must complete the item on an unconsolidated basis by reference to the *firm* alone. (2) If it is a *group liquidity reporting firm* in a *DLG by default* and is a *UK lead regulated firm*, it must complete the item on the basis of that group. (3) If it is a *group liquidity reporting firm* in a *UK DLG by modification*, it must complete the item on the basis of that group. (4) If it is a *group liquidity reporting firm* in a *non-UK DLG by modification*, it must complete the item on the basis of that group.
Note 7	A *firm* must complete this item separately on each of the following bases that are applicable. (1) It must complete it on a solo basis unless it is a *group liquidity reporting firm* in a *UK DLG by modification*. Therefore even if it has an *individual consolidation permission* it must complete the item on an unconsolidated basis by reference to the *firm* alone. (2) If it is a *group liquidity reporting firm* in a *UK DLG by modification*, it must complete the item on the basis of that group.
Note 8	If it is a *non-ILAS BIPRU firm*, it must complete it on a solo basis. Therefore even if it has an *individual consolidation permission* it must complete the item on an unconsolidated basis by reference to the *firm* alone.
Note 9	(1) This item must be reported in the reporting currency. (2) If any *data element* is in a currency or currencies other than the reporting currency, all currencies (including the reporting currency) must be combined into a figure in the reporting currency. (3) In addition, all *material currencies* (which may include the reporting currency) must each be recorded separately (translated into the reporting currency). However if: (a) the reporting frequency is (whether under a *rule* or under a *waiver*) quarterly or less than quarterly; or (b) the only *material currency* is the reporting currency; (3) does not apply. (4) If there are more than three *material currencies* for this *data item*, (3) only applies to the three largest in amount. A

	firm must identify the largest in amount in accordance with the following procedure. (a) For each currency, take the largest of the asset or liability figure as referred to in the definition of *material currency*. (b) Take the three largest figures from the resulting list of amounts. (5) The date as at which the calculations for the purposes of the definition of *material currency* are carried out is the last day of the reporting period in question. (6) The reporting currency for this *data item* is whichever of the following currencies the *firm* chooses, namely USD (the United States Dollar), EUR (the euro), GBP (sterling), JPY (the Japanese Yen), CHF (the Swiss Franc), CAD (the Canadian Dollar) or SEK (the Swedish Krona).
Note 10	Note 9 applies, except that paragraphs (3), (4) and (5) do not apply, meaning that *material currencies* must not be recorded separately.
Note 11	Any changes to reporting requirements caused by a *firm* receiving an *intra-group liquidity modification* (or a variation to one) do not take effect until the first day of the next reporting period applicable under the changed reporting requirements for the *data item* in question if the *firm* receives that *intra-group liquidity modification* or variation part of the way through such a period. If the change is that the *firm* does not have to report a particular *data item* or does not have to report it at a particular *reporting level*, the *firm* must nevertheless report that item or at that *reporting level* for any reporting period that has already begun. This paragraph is subject to anything that the *intra-group liquidity modification* says to the contrary.
Note 12	FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054 must be completed by an *ILAS BIPRU firm*. An *ILAS BIPRU firm* does not need to complete FSA055. A *non-ILAS BIPRU firm* must complete FSA055 and does not need to complete FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054.
Note 13	This *data item* must be reported only in the currencies named in FSA052, so that liabilities in GBP are reported in GBP in rows 1 to 4, those in USD are reported in USD in rows 5 to 8, and those in Euro are reported in Euro in rows 9 to 12. Liabilities in other currencies are not to be reported.
Note 14	This item only applies to *firms* that provide advice on *retail investment products*.
Note 15	This item applies only to firms that provide advice and related services to employers on *group personal pension schemes* and/or *group stakeholder pension schemes*.

<u>Note 16</u>	<u>Only applicable to a *firm* whose ultimate parent is a *mixed-activity holding company*.</u>
<u>Note 17</u>	<u>Only applicable to a firm that is a *sole trader* or a *partnership*, when the report must be submitted by each *partner*.</u>
<u>Note 18</u>	<u>Only applicable to a *firm* that has both a *core UK group* and a *non-core large exposures group*.</u>
<u>Note 19</u>	<u>Only applicable to *firms* that have an *IRB permission*.</u>
<u>Note 20</u>	<u>This applies to a *firm* that applies add-ons to their market risk capital calculation under the RNIV framework.</u>

16.12.23 R The applicable reporting frequencies for *data items* referred to in *SUP* 16.12.22AR are set out in the table below. Reporting frequencies are calculated from a *firm's accounting reference date*, unless indicated otherwise.

Data item	**Frequency**				
	Unconsolidated ~~*BIPRU investment firm*~~ *UK* <u>*designated investment firm*</u>	~~**Solo consolidated**~~ ~~*BIPRU investment firm*~~ *UK* <u>*designated investment firm* with an individual consolidation permission</u>	~~*UK*~~ *Consolidation Group* or *defined liquidity group*	**Annual regulated business revenue up to and including £5 million**	**Annual regulated business revenue over £5 million**
…					
~~FSA003~~	~~Monthly, quarterly or half yearly (note 2)~~	~~Monthly, quarterly or half yearly (note 2)~~	~~Half yearly~~		
~~FSA004~~	~~Quarterly or half yearly (note 1)~~	~~Quarterly or half yearly (note 1)~~	~~Half yearly~~		
…					
~~FSA007~~	~~Annually (note 3)~~	~~Annually (note 3)~~	~~Annually (note 3)~~		
~~FSA008~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~		
…					
~~FSA028~~	~~Half yearly~~	~~Half yearly~~			
…					

~~FSA046~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~		
…					
~~FSA058~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~		
…					
Note 1:	*UK designated investment firms* – quarterly; ~~*BIPRU 730K firms* and *BIPRU 125K firms* - quarterly;~~ ~~*BIPRU 50K firms* - half yearly.~~				
Note 2	~~*BIPRU 730K firms* - monthly;~~ ~~*BIPRU 125K firms* - quarterly;~~ ~~*BIPRU 50K firms* - half yearly.~~ [deleted]				
Note 3	~~The reporting date for this *data item* is six months after a *firm's* most recent *accounting reference date*.~~ [deleted]				
…					

16.12.24 R The applicable due dates for submission referred to in *SUP* 16.12.4R are set out in the table below. The due dates are the last day of the periods given in the table below following the relevant reporting frequency period set out in *SUP* 16.12.23R, unless indicated otherwise.

Data Item	Daily	Weekly	Monthly	Quarterly	Half yearly	Annual
…						
~~FSA003~~	~~15 *business days*~~			~~20 *business days*~~	~~30 *business days* (note 1); 45 *business days* (note 2)~~	
~~FSA004~~				~~20 *business days*~~	~~30 *business days* (note 1); 45 *business days* (note 2)~~	
…						
~~FSA007~~						~~2 months~~
~~FSA008~~				~~20 *business days* (note 1); 45 *business days* (note 2)~~		

…						
~~FSA028~~					~~30 *business days*~~	
…						
~~FSA046~~				~~20 business days (Note 1), 45 business days (Note 2)~~		
…						
~~FSA058~~				~~20 business days (Note 1), 45 business days (Note 2)~~		
…						

Regulated Activity Group 8

16.12.25A ~~R~~ ~~The applicable *data items* referred to in *SUP* 16.12.4R are set out according to type of *firm* in the table below:~~ [deleted]

~~**Description of** *data item*~~	~~*Firms'* **prudential category and applicable** *data item* **(note 1)**~~							
	~~*BIPRU*~~			~~*Firms* **other than** *BIPRU firms*~~				
	~~**730K**~~	~~**125K**~~	~~**50K**~~	~~*IPRU(INV)* **Chapter 3**~~	~~*IPRU(INV)* **Chapter 5**~~	~~*IPRU(INV)* **Chapter 9**~~	~~*IPRU(INV)* **Chapter 13**~~	~~*UPRU*~~
~~*Annual report and accounts*~~	~~No standard format~~							
~~*Annual report and accounts* of the *mixed-*~~	~~No standard format~~							

~~*activity holding company* (note 10)~~								
~~Solvency statement (note 11)~~	~~No standard format~~							~~No standard format~~
~~Balance sheet~~	~~FSA001 (note 2)~~	~~FSA001 (note 2)~~	~~FSA001 (note 2)~~	~~FSA029~~	~~FSA029~~	~~FSA029~~	~~Section A RMAR (note 17) or FSA029~~	
~~Income statement~~	~~FSA002 (note 2)~~	~~FSA002 (note 2)~~	~~FSA002 (note 2)~~	~~FSA030~~	~~FSA030~~	~~FSA030~~	~~Section B RMAR (note 17) or FSA030~~	~~FSA030~~
~~Capital adequacy~~	~~FSA003 (note 2)~~	~~FSA003 (note 2)~~	~~FSA003 (note 2)~~	~~FSA033~~	~~FSA034 or FSA035 (note 14)~~	~~FSA031~~	~~Section D6 RMAR (note 17) or FSA 032 (note 15)~~	~~FSA036~~
~~Credit risk~~	~~FSA004 (note 2, 3)~~	~~FSA004 (note 2, 3)~~	~~FSA004 (note 2, 3)~~					
~~Market risk~~	~~FSA005 (notes 2, 4)~~	~~FSA005 (notes 2, 4)~~	~~FSA005 (notes 2, 4)~~					
~~Market risk – supplementary~~	~~FSA006 (note 5)~~	~~FSA006 (note 5)~~	~~FSA006 (note 5)~~					
~~Operational risk~~	~~FSA007 (notes 2, 6, 7)~~	~~FSA007 (notes 2, 6, 7)~~	~~FSA007 (notes 2, 6, 7)~~					
~~Large exposures~~	~~FSA008 (Notes 2, 6)~~	~~FSA008 (Notes 2, 6)~~	~~FSA008 (Notes 2, 6)~~					

~~UK Integrated group large exposures~~	~~FSA018 (note 12)~~	~~FSA018 (note 12)~~	~~FSA018 (note 12)~~						
~~Solo consolidation data~~	~~FSA016 (note 20)~~	~~FSA016 (note 20)~~	~~FSA016 (note 20)~~						
~~Pillar 2 questionnaire~~	~~FSA019 (note 8)~~	~~FSA019 (note 8)~~	~~FSA019 (note 8)~~						
~~Non-EEA sub-group~~	~~FSA028 (note 9)~~	~~FSA028 (note 9)~~	~~FSA028 (note 9)~~						
~~Threshold conditions~~							~~Section F RMAR (note 17)~~		
~~Client money and client assets~~	~~FSA039~~	~~FSA039~~	~~FSA039~~	~~FSA039~~	~~FSA039~~	~~FSA039~~	~~Section C RMAR (Note 13) or FSA039~~	~~FSA039~~	
~~IRB portfolio risk~~	~~FSA045 (note 18)~~	~~FSA045 (note 18)~~	~~FSA045 (note 18)~~						
~~Securitisation: non-trading book~~	~~FSA046 (note 19)~~	~~FSA046 (note 19)~~	~~FSA046 (note 19)~~						
~~Daily Flows~~	~~FSA047 (Notes 21, 24, 26 and 28)~~								
~~Enhanced Mismatch Report~~	~~FSA048 (Notes 21, 24, 26 and 28)~~								
~~Liquidity Buffer Qualifying Securiti~~	~~FSA050 (Notes 22, 25, 26 and 28)~~								

~~es~~								
~~Funding Concentration~~	~~FSA051 (Notes 22, 25, 26 and 28)~~							
~~Pricing data~~	~~FSA052 (Notes 22, 26, 28 and 29)~~							
~~Retail and corporate funding~~	~~FSA053 (Notes 22, 25, 26 and 28)~~							
~~Currency Analysis~~	~~FSA054 (Notes 22, 25, 26 and 28)~~							
~~Systems and Controls Questionnaire~~	~~FSA055 (Notes 23 and 28)~~							
~~Securitisation: trading book~~	~~FSA058 (Note 27)~~	~~FSA058 (Note 27)~~	~~FSA058 (Note 27)~~					
~~Note 1:~~	~~When submitting the completed *data item* required, a *firm* must use the format of the *data item* set out in *SUP 16 Annex 24 R*. Guidance notes for completion of the data items are contained in *SUP 16 Annex 25 G*.~~							
~~Note 2~~	~~*Firms* that are members of a *UK consolidation group* are also required to submit this report on a *UK consolidation group* basis.~~							
~~Note 3~~	~~This applies to a *firm* that is required to submit *data item* FSA003 and, at any time within the 12 *months* up to its latest *accounting reference date* ("the relevant period"), was reporting *data item* FSA004 ("Firm A") or not reporting this item ("Firm B").~~ ~~In the case of Firm A it must report this *data item* if one or both of its last two submissions in the relevant period show that the threshold was exceeded.~~ ~~In the case of Firm B it must report this item if both the last two submissions in the relevant period show that the threshold has been exceeded.~~ ~~The threshold is exceeded where *data element* 77A in *data item* FSA003 is greater than £10 million, or its currency equivalent, at the relevant reporting date for the *firm*.~~							
~~Note 4~~	~~This applies to a *firm* that is required to submit *data item* FSA003 and, at any time within the 12 *months* up to its latest *accounting reference date* ("the relevant period"), was reporting *data item* FSA005 ("Firm A") or not reporting this item ("Firm B").~~							

	~~In the case of Firm A it must report this *data item* if one or both of its last two submissions in the relevant period show that the threshold was exceeded.~~ ~~In the case of Firm B it must report this item if both the last two submissions in the relevant period show that the threshold has been exceeded.~~ ~~The threshold is exceeded where *data element* 93A in *data item* FSA003 is greater than £50 million, or its currency equivalent, at the relevant reporting date for the *firm*.~~
~~Note 5~~	~~Only applicable to *firms* with a *VaR model permission*.~~
~~Note 6~~	~~This will not be applicable to *BIPRU limited activity firms* or *BIPRU limited licence firms* unless they have a waiver under *BIPRU 6.1.2 G*.~~
~~Note 7~~	~~This is only applicable to a *firm* that has adopted, in whole or in part, either the *standardised approach*, *alternative standardised approach*, or *advanced measurement approach* under *BIPRU 6*.~~
~~Note 8~~	~~Only applicable to *BIPRU investment firms* that :~~ ~~(a) are subject to consolidated supervision under *BIPRU 8*, except those that are either included within the consolidated supervision of a group that includes a UK *credit institution*, or that have been granted an *investment firm consolidation waiver*; or~~ ~~(b) have been granted an *investment firm consolidation waiver*; or~~ ~~(c) are not subject to consolidated supervision under *BIPRU 8*.~~ ~~A *BIPRU investment firm* under (a) must complete the report on the basis of its *UK consolidation group*. A *BIPRU investment firm* under (b) or (c) must complete the report on the basis of its solo position.~~
~~Note 9~~	~~This will be applicable to firms that are members of a *UK consolidation group* on the reporting date.~~
~~Note 10~~	~~Only applicable to a *firm* whose ultimate parent is a *mixed-activity holding company*.~~
~~Note 11~~	~~Only applicable to a firm that is a *sole trader* or a *partnership*, when the report must be submitted by each *partner*.~~
~~Note 12~~	~~Members of a *UK integrated group* should only submit this data item at the *UK integrated group* level.~~
~~Note 13~~	~~FSA039 must only be completed by a *firm* subject to *IPRU(INV)* Chapter 13 which is an *exempt CAD firm*. Section C RMAR must only be completed by a *firm* subject to *IPRU(INV)* Chapter 13 which is not an *exempt CAD firm*.~~
~~Note 14~~	~~FSA034 must be completed by a *firm* not subject to the exemption in *IPRU(INV)* 5.2.3(2)R.~~ ~~FSA035 must be completed by a *firm* subject to the exemption in *IPRU(INV)* 5.2.3(2) R.~~
~~Note 15~~	~~FSA032 must be completed by a *firm* subject to *IPRU(INV)* Chapter 13 which is an *exempt CAD firm*.~~
~~Note 16~~	~~[deleted]~~

~~Note 17~~	~~This is only applicable to a *firm* subject to *IPRU(INV)* Chapter 13 that is not an *exempt CAD firm*.~~
~~Note 18~~	~~Only applicable to *firms* that have an *IRB permission*.~~
~~Note 19~~	~~Only applicable to *firms* that hold *securitisation positions*, or are the *originator* or *sponsor* of *securitisations* of *non-trading book exposures*.~~
~~Note 20~~	~~Only applicable to a *firm* that has a *solo consolidation waiver*.~~
~~Note 21~~	~~A *firm* must complete this item separately on each of the following bases (if applicable).~~ ~~(1) It must complete it on a solo basis. Therefore even if it has a *solo consolidation waiver* it must complete the item on an unconsolidated basis by reference to the *firm* alone.~~ ~~(2) If it a *group liquidity reporting firm* in a *DLG by default* and is a *UK lead regulated firm*, it must complete the item on the basis of that group.~~ ~~(3) If it is a *group liquidity reporting firm* in a *UK DLG by modification*, it must complete the item on the basis of that group.~~ ~~(4) If it is a *group liquidity reporting firm* in a *non-UK DLG by modification*, it must complete the item on the basis of that group.~~
~~Note 22~~	~~A *firm* must complete this item separately on each of the following bases that are applicable.~~ ~~(1) It must complete it on a solo basis unless it is a *group liquidity reporting firm* in a *UK DLG by modification*. Therefore even if it has a *solo consolidation waiver* it must complete the item on an unconsolidated basis by reference to the *firm* alone.~~ ~~(2) If it is a *group liquidity reporting firm* in a *UK DLG by modification*, it must complete the item on the basis of that group.~~
~~Note 23~~	~~If it is a *non-ILAS BIPRU firm*, it must complete it on a solo basis. Therefore even if it has a *solo consolidation waiver* it must complete the item on an unconsolidated basis by reference to the *firm* alone.~~
~~Note 24~~	~~(1) This item must be reported in the reporting currency.~~ ~~(2) If any *data element* is in a currency or currencies other than the reporting currency, all currencies (including the reporting currency) must be combined into a figure in the reporting currency.~~ ~~(3) In addition, all *material currencies* (which may include the reporting currency) must each be recorded separately (translated into the reporting currency). However if:~~ ~~(a) the reporting frequency is (whether under a *rule* or under a *waiver*) quarterly or less than quarterly; or~~ ~~(b) the only *material currency* is the reporting currency;~~ ~~(3) does not apply.~~ ~~(4) If there are more than three *material currencies* for this *data item*, (3) only applies to the three largest in amount. A *firm* must identify the largest in amount in accordance with the following procedure.~~ ~~(a) For each currency, take the largest of the asset or liability figure as referred to in the definition of *material currency*.~~ ~~(b) Take the three largest figures from the resulting list of amounts.~~ ~~(5) The date as at which the calculations for the purposes of the definition of *material currency* are carried out is the last day of the reporting period in question.~~ ~~(6) The reporting currency for this *data item* is whichever of the following currencies the *firm* chooses, namely USD (the United States Dollar), EUR (the euro), GBP (sterling), JPY (the Japanese Yen), CHF (the Swiss Franc), CAD (the Canadian Dollar) or SEK (the Swedish Krona).~~

~~Note 25~~	~~Note 24 applies, except that paragraphs (3), (4) and (5) do not apply, meaning that *material currencies* must not be recorded separately.~~
~~Note 26~~	~~Any changes to reporting requirements caused by a *firm* receiving an *intra-group liquidity modification* (or a variation to one) do not take effect until the first day of the next reporting period applicable under the changed reporting requirements for the *data item* in question if the *firm* receives that *intra-group liquidity modification* or variation part of the way through such a period. If the change is that the *firm* does not have to report a particular *data item* or does not have to report it at a particular *reporting level*, the *firm* must nevertheless report that item or at that *reporting level* for any reporting period that has already begun. This paragraph is subject to anything that the *intra-group liquidity modification* says to the contrary.~~
~~Note 27~~	~~Only applicable to *firms* that hold *securitisation positions* in the *trading book* and/ or are the *originator* or *sponsor* of *securitisations* held in the *trading book*.~~
~~Note 28~~	~~FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054 must be completed by an *ILAS BIPRU firm*. An *ILAS BIPRU firm* does not need to complete FSA055. A *non-ILAS BIPRU firm* must complete FSA055 and does not need to complete FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054.~~
~~Note 29~~	~~This *data item* must be reported only in the currencies named in FSA052, so that liabilities in GBP are reported in GBP in rows 1 to 4, those in USD are reported in USD in rows 5 to 8, and those in Euro are reported in Euro in rows 9 to 12. Liabilities in other currencies are not to be reported.~~

…

16.12.25B G ~~The columns in the table in *SUP* 16.12.25AR that deal with *BIPRU 50K firms* and *BIPRU 125K firms* cover some liquidity items that only have to be reported by an *ILAS BIPRU firm*. In fact a *BIPRU 50K firm* and a *BIPRU 125K firm* cannot be an *ILAS BIPRU firm*. One reason for drafting the table in this way is that the classification of *firms* into *ILAS BIPRU firms* and *non-ILAS BIPRU firms* is not based on the classification into *BIPRU 50K firms*, *BIPRU 125K firms* and *BIPRU 730K firms* and the drafting of the table emphasises that. Also, the table covers consolidated reports and the conditions about what sort of group has to supply what type of liquidity report do not always depend on how the individual *firm* is classified.~~ [deleted]

16.12.25C R The applicable *data items* referred to in *SUP* 16.12.4R are set out in the table below:

Description of *data item*	**Applicable *data item* (Note 1)**
Annual report and accounts	No standard format
Annual report and accounts of the *mixed-activity holding company* (Note 5)	No standard format
Solvency statement (Note 6)	No standard format
Balance sheet	FSA001 (note 2)
Income statement	FSA002 (note 2)

Market risk	FSA005 (notes 2, 18)
Market risk – supplementary	FSA006 (Note 3)
Exposures between *core UK group* and *non-core large exposures group*	FSA018 (note 7)
Solo consolidation data	FSA016 (note 8)
Pillar 2 questionnaire	FSA019 (note 4)
Client money and client assets	FSA039
IRB portfolio risk	FSA045 (note 17)
Daily flows	FSA047 (Notes 9, 12, 14 and 15)
Enhanced Mismatch Report	FSA048 (Notes 9, 12, 14 and 15)
Liquidity Buffer Qualifying Securities	FSA050 (Notes 10, 13, 14 and 15)
Funding Concentration	FSA051 (Notes 10, 13, 14 and 15)
Pricing data	FSA052 (Notes 10, 14, 15 and 16)
Retail and corporate funding	FSA053 (Notes 10, 13, 14 and 15)
Currency Analysis	FSA054 (Notes 10, 13, 14 and 15)
Systems and Controls Questionnaire	FSA055 (Notes 11 and 15)

Note1	When submitting the completed *data item* required, a *firm* must use the format of the *data item* set out in *SUP 16 Annex 24 R*. Guidance notes for completion of the data items are contained in *SUP 16 Annex 25 G*.
Note 2	*Firms* that are members of a *consolidation group* are also required to submit this report on a *consolidation group* basis.
Note 3	Only applicable to *firms* with a *VaR model permission*.
Note 4	Only applicable to *UK designated investment firms* that : (a) are subject to consolidated supervision under *CRR*, except those that are either included within the consolidated supervision of a group that includes a UK *credit institution*; or (c) are not subject to consolidated supervision under *CRR*. A *UK designated investment firm* under (a) must complete the report on the basis of its *consolidation group*. A *UK designated investment firm* under (b) must complete the

	report on the basis of its solo position.
Note 5	Only applicable to a *firm* whose ultimate parent is a *mixed-activity holding company*.
Note 6	Only applicable to a firm that is a *sole trader* or a *partnership*, when the report must be submitted by each *partner*.
Note 7	Only applicable to a *firm* that has both a *core UK group* and a *non-core large exposures group.*
Note 8	Only applicable to a *firm* that has an *individual consolidation permission*.
Note 9	A *firm* must complete this item separately on each of the following bases (if applicable). (1) It must complete it on a solo basis. Therefore even if it has an *individual consolidation permission* it must complete the item on an unconsolidated basis by reference to the *firm* alone. (2) If it a *group liquidity reporting firm* in a *DLG by default* and is a *UK lead regulated firm*, it must complete the item on the basis of that group. (3) If it is a *group liquidity reporting firm* in a *UK DLG by modification*, it must complete the item on the basis of that group. (4) If it is a *group liquidity reporting firm* in a *non-UK DLG by modification*, it must complete the item on the basis of that group.
Note 10	A *firm* must complete this item separately on each of the following bases that are applicable. (1) It must complete it on a solo basis unless it is a *group liquidity reporting firm* in a *UK DLG by modification*. Therefore even if it has an *individual consolidation permission* it must complete the item on an unconsolidated basis by reference to the *firm* alone. (2) If it is a *group liquidity reporting firm* in a *UK DLG by modification*, it must complete the item on the basis of that group.
Note 11	If it is a *non-ILAS BIPRU firm*, it must complete it on a solo basis. Therefore even if it has an *individual consolidation permission* it must complete the item on an unconsolidated basis by reference to the *firm* alone.
Note 12	(1) This item must be reported in the reporting currency. (2) If any *data element* is in a currency or currencies other than the reporting currency, all currencies (including the reporting currency) must be combined into a figure in the reporting currency. (3) In addition, all *material currencies* (which may include the reporting currency) must each be recorded separately (translated into the reporting currency). However if: (a) the reporting frequency is (whether under a *rule* or under a *waiver*) quarterly or less than quarterly; or (b) the only *material currency* is the reporting currency; (3) does not apply.

	(4) If there are more than three *material currencies* for this *data item*, (3) only applies to the three largest in amount. A *firm* must identify the largest in amount in accordance with the following procedure. (a) For each currency, take the largest of the asset or liability figure as referred to in the definition of *material currency*. (b) Take the three largest figures from the resulting list of amounts. (5) The date as at which the calculations for the purposes of the definition of *material currency* are carried out is the last day of the reporting period in question. (6) The reporting currency for this *data item* is whichever of the following currencies the *firm* chooses, namely USD (the United States Dollar), EUR (the euro), GBP (sterling), JPY (the Japanese Yen), CHF (the Swiss Franc), CAD (the Canadian Dollar) or SEK (the Swedish Krona).
Note 13	Note 24 applies, except that paragraphs (3), (4) and (5) do not apply, meaning that *material currencies* must not be recorded separately.
Note 14	Any changes to reporting requirements caused by a *firm* receiving an *intra-group liquidity modification* (or a variation to one) do not take effect until the first day of the next reporting period applicable under the changed reporting requirements for the *data item* in question if the *firm* receives that *intra-group liquidity modification* or variation part of the way through such a period. If the change is that the *firm* does not have to report a particular *data item* or does not have to report it at a particular *reporting level*, the *firm* must nevertheless report that item or at that *reporting level* for any reporting period that has already begun. This paragraph is subject to anything that the *intra-group liquidity modification* says to the contrary.
Note 15	FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054 must be completed by an *ILAS BIPRU firm*. An *ILAS BIPRU firm* does not need to complete FSA055. A *non-ILAS BIPRU firm* must complete FSA055 and does not need to complete FSA047, FSA048, FSA050, FSA051, FSA052, FSA053 and FSA054.
Note 16	This *data item* must be reported only in the currencies named in FSA052, so that liabilities in GBP are reported in GBP in rows 1 to 4, those in USD are reported in USD in rows 5 to 8, and those in Euro are reported in Euro in rows 9 to 12. Liabilities in other currencies are not to be reported.
Note 17	Only applicable to *firms* that have an *IRB permission*.
Note 18	This applies to a *firm* that applies add-ons to their market risk capital calculation under the RNIV framework.

16.12.26 R ~~The applicable reporting frequencies for *data items* referred to in *SUP* 16.12.25AR are set out according to the type of *firm* in the table below. Reporting frequencies are calculated from a *firm's accounting reference date*, unless indicated otherwise.~~ [deleted]

~~*Data item*~~	~~*BIPRU 730K*~~	~~*BIPRU 125K*~~	~~*BIPRU 50K*~~	~~*UK*~~	~~*Firms* other~~

	~~*firm*~~	~~*firm*~~	~~*firm*~~	~~*consolidation group* or *defined liquidity group*~~	~~than *BIPRU firms*~~
~~*Annual reports and accounts*~~	~~Annually~~	~~Annually~~	~~Annually~~		~~Annually~~
~~*Annual report and accounts* of the *mixed-activity holding company*~~	~~Annually~~	~~Annually~~	~~Annually~~	~~Annually~~	
~~Solvency statement~~	~~Annually~~	~~Annually~~	~~Annually~~		~~Annually~~
~~FSA001~~	~~Quarterly~~	~~Quarterly~~	~~Half yearly~~	~~Half yearly~~	
~~FSA002~~	~~Quarterly~~	~~Quarterly~~	~~Half yearly~~	~~Half yearly~~	
~~FSA003~~	~~Monthly~~	~~Quarterly~~	~~Half yearly~~	~~Half yearly~~	
~~FSA004~~	~~Quarterly~~	~~Quarterly~~	~~Half yearly~~	~~Half yearly~~	
~~FSA005~~	~~Quarterly~~	~~Quarterly~~	~~Half yearly~~	~~Half yearly~~	
~~FSA006~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~		
~~FSA007~~	~~Annually(note 4)~~	~~Annually(note 4)~~	~~Annually(note 4)~~	~~Annually (note 4)~~	
~~FSA008~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	
~~FSA016~~	~~Half yearly~~	~~Half yearly~~	~~Half yearly~~		
~~FSA018~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~		
~~FSA019~~	~~Annually~~	~~Annually~~	~~Annually~~	~~Annually~~	
~~FSA028~~	~~Half yearly~~	~~Half yearly~~	~~Half yearly~~		
~~FSA029~~					~~Quarterly~~
~~FSA030~~					~~Quarterly~~
~~FSA031~~					~~Quarterly~~
~~FSA032~~					~~Quarterly~~
~~FSA033~~					~~Quarterly~~
~~FSA034~~					~~Quarterly~~

~~FSA035~~					~~Quarterly~~
~~FSA036~~					~~Quarterly~~
~~FSA039~~	~~Half yearly~~	~~Half yearly~~	~~Half yearly~~		~~Half yearly~~
~~FSA045~~	~~Quarterly~~	~~Quarterly~~	~~Half yearly~~	~~Half yearly~~	
~~FSA046~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	
~~FSA047~~	~~Daily, weekly, monthly or quarterly (Notes 5, 6 and 8)~~			~~Daily, weekly, monthly or quarterly (Notes 5, 7 and 8)~~	
~~FSA048~~	~~Daily, weekly, monthly or quarterly (Notes 5, 6 and 8)~~			~~Daily, weekly, monthly or quarterly (Notes 5, 7 and 8)~~	
~~FSA050~~	~~Monthly (Note 5)~~			~~Monthly (Note 5)~~	
~~FSA051~~	~~Monthly (Note 5)~~			~~Monthly (Note 5)~~	
~~FSA052~~	~~Weekly or monthly (Notes 5 and 9)~~			~~Weekly or monthly (Notes 5 and 10)~~	
~~FSA053~~	~~Quarterly (Note 5)~~			~~Quarterly (Note 5)~~	
~~FSA054~~	~~Quarterly (Note 5)~~			~~Quarterly (Note 5)~~	
~~FSA055~~	~~Annually (Note 5)~~			~~Annually (Note 5)~~	
~~FSA058~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	~~Quarterly~~	
~~Section A RMAR~~					~~Half yearly (note 2)~~ ~~Quarterly (note 3)~~
~~Section B RMAR~~					~~Half yearly (note 2)~~ ~~Quarterly (note 3)~~
~~Section C RMAR~~					~~Half yearly (note 2)~~ ~~Quarterly (note 3)~~

~~Section D6 RMAR~~					~~Half yearly (note 2)~~ ~~Quarterly (note 3)~~
~~Section F RMAR~~					~~Half yearly~~
~~Note 1~~	~~[deleted]~~				
~~Note 2~~	~~Annual regulated business revenue up to and including £5 million.~~				
~~Note 3~~	~~Annual regulated business revenue over £5 million.~~				
~~Note 4~~	~~The reporting date for this *data item* is six months after a *firm's* most recent *accounting reference date*.~~				
~~Note 5~~	~~Reporting frequencies and reporting periods for this *data item* are calculated on a calendar year basis and not from a *firm's accounting reference date*. In particular:~~ ~~(1) A week means the period beginning on Saturday and ending on Friday.~~ ~~(2) A month begins on the first day of the calendar month and ends on the last day of that month.~~ ~~(3) Quarters end on 31 March, 30 June, 30 September and 31 December.~~ ~~(4) Daily means each *business day*.~~ ~~All periods are calculated by reference to London time.~~ ~~Any changes to reporting requirements caused by a *firm* receiving an *intra-group liquidity modification* (or a variation to one) do not take effect until the first day of the next reporting period applicable under the changed reporting requirements if the *firm* receives that *intra-group liquidity modification* or variation part of the way through such a period, unless the *intra-group liquidity modification* says otherwise.~~				
~~Note 6~~	~~If the report is on a solo basis the reporting frequency is as follows:~~ ~~(1) if the *firm* does not have an *intra-group liquidity modification* the frequency is:~~ ~~(a) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and~~ ~~(b) monthly if the *firm* is a *low frequency liquidity reporting firm*;~~ ~~(2) if the *firm* is a *group liquidity reporting firm* in a *non-UK DLG by modification (firm level)* the frequency is:~~ ~~(a) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and~~ ~~(b) monthly if the *firm* is a *low frequency liquidity reporting firm*;~~ ~~(3) the frequency is quarterly if the *firm* is a *group liquidity reporting firm* in a *UK DLG by modification*.~~				
~~Note 7~~	~~(1) If the report is by reference to the *firm's DLG by default* the reporting frequency is:~~ ~~(a) weekly if the *group liquidity standard frequency reporting conditions* are met;~~ ~~(b) monthly if the *group liquidity low frequency reporting conditions* are met.~~ ~~(2) If the report is by reference to the *firm's UK DLG by modification* the reporting frequency is:~~ ~~(a) weekly if the *group liquidity standard frequency reporting conditions* are met;~~ ~~(b) monthly if the *group liquidity low frequency reporting conditions* are met.~~ ~~(3) If the report is by reference to the *firm's non-UK DLG by modification* the reporting frequency is quarterly.~~				

~~Note 8~~	~~(1) If the reporting frequency is otherwise weekly, the item is to be reported on every *business day* if (and for as long as) there is a *firm-specific liquidity stress* or *market liquidity stress* in relation to the *firm* or group in question.~~ ~~(2) If the reporting frequency is otherwise monthly, the item is to be reported weekly if (and for as long as) there is a *firm-specific liquidity stress* or *market liquidity stress* in relation to the firm or group in question.~~ ~~(3) A *firm* must ensure that it would be able at all times to meet the requirements for daily or weekly reporting under paragraph (1) or (2) even if there is no *firm-specific liquidity stress* or *market liquidity stress* and none is expected.~~
~~Note 9~~	~~If the report is on a solo basis the reporting frequency is as follows:~~ ~~(1) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and~~ ~~(2) monthly if the *firm* is a *low frequency liquidity reporting firm*.~~
~~Note 10~~	~~If the report is by reference to the *firm's UK DLG by modification* the reporting frequency is:~~ ~~(1) weekly if the *group liquidity standard frequency reporting conditions* are met;~~ ~~(2) monthly if the *group liquidity low frequency reporting conditions* are met.~~

16.12.26A R The applicable reporting frequencies for *data items* referred to in *SUP* 16.12.25C R are set out in the table below. Reporting frequencies are calculated from a *firm's accounting reference date*, unless indicated otherwise.

Data item	*UK designated investment firm*	*consolidation group* or *defined liquidity group*
Annual reports and accounts	Annually	Annually
Annual report and accounts of the *mixed-activity holding company*	Annually	Annually
Solvency statement	Annually	
FSA001	Quarterly	Half yearly
FSA002	Quarterly	Half yearly
FSA005	Monthly	Monthly
FSA006	Quarterly	
FSA016	Half yearly	
FSA018	Quarterly	
FSA019	Annually	Annually
FSA039	Half yearly	

FSA045	Quarterly	Half yearly
FSA047	Daily, weekly, monthly or quarterly (Notes 1, 2 and 4)	Daily, weekly, monthly or quarterly (Notes 1, 3 and 4)
FSA048	Daily, weekly, monthly or quarterly (Notes 1, 2 and 4)	Daily, weekly, monthly or quarterly (Notes 1, 3 and 4)
FSA050	Monthly (Note 1)	Monthly (Note 1)
FSA051	Monthly (Note 1)	Monthly (note 1)
FSA052	Weekly or monthly (Notes 1 and 5)	Weekly or monthly (notes 1 and 6)
FSA053	Quarterly (Note 1)	Quarterly (Note 1)
FSA054	Quarterly (Note 1)	Quarterly (Note 1)
FSA055	Annually (Note 1)	Annually (Note 1)

Note 1	Reporting frequencies and reporting periods for this *data item* are calculated on a calendar year basis and not from a *firm's accounting reference date*. In particular: (1) A week means the period beginning on Saturday and ending on Friday. (2) A month begins on the first day of the calendar month and ends on the last day of that month. (3) Quarters end on 31 March, 30 June, 30 September and 31 December. (4) Daily means each *business day*. All periods are calculated by reference to London time. Any changes to reporting requirements caused by a *firm* receiving an *intra-group liquidity modification* (or a variation to one) do not take effect until the first day of the next reporting period applicable under the changed reporting requirements if the *firm* receives that *intra-group liquidity modification* or variation part of the way through such a period, unless the *intra-group liquidity modification* says otherwise.
Note 2	If the report is on a solo basis the reporting frequency is as follows: (1) if the *firm* does not have an *intra-group liquidity modification* the frequency is: (a) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and (b) monthly if the *firm* is a *low frequency liquidity reporting firm*; (2) if the *firm* is a *group liquidity reporting firm* in a *non-UK DLG by modification (firm level)* the frequency is: (a) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and (b) monthly if the *firm* is a *low frequency liquidity reporting firm*;

	(3) the frequency is quarterly if the *firm* is a *group liquidity reporting firm* in a *UK DLG by modification*.
Note 3	(1) If the report is by reference to the *firm's DLG by default* the reporting frequency is: (a) weekly if the *group liquidity standard frequency reporting conditions* are met; (b) monthly if the *group liquidity low frequency reporting conditions* are met. (2) If the report is by reference to the *firm's UK DLG by modification* the reporting frequency is: (a) weekly if the *group liquidity standard frequency reporting conditions* are met; (b) monthly if the *group liquidity low frequency reporting conditions* are met. (3) If the report is by reference to the *firm's non-UK DLG by modification* the reporting frequency is quarterly.
Note 4	(1) If the reporting frequency is otherwise weekly, the item is to be reported on every *business day* if (and for as long as) there is a *firm-specific liquidity stress* or *market liquidity stress* in relation to the *firm* or group in question. (2) If the reporting frequency is otherwise monthly, the item is to be reported weekly if (and for as long as) there is a *firm-specific liquidity stress* or *market liquidity stress* in relation to the firm or group in question. (3) A *firm* must ensure that it would be able at all times to meet the requirements for daily or weekly reporting under paragraph (1) or (2) even if there is no *firm-specific liquidity stress* or *market liquidity stress* and none is expected.
Note 5	If the report is on a solo basis the reporting frequency is as follows: (1) weekly if the *firm* is a *standard frequency liquidity reporting firm*; and (2) monthly if the *firm* is a *low frequency liquidity reporting firm*.
Note 6	If the report is by reference to the *firm's UK DLG by modification* the reporting frequency is: (1) weekly if the *group liquidity standard frequency reporting conditions* are met; (2) monthly if the *group liquidity low frequency reporting conditions* are met.

16.12.27 R The applicable due dates for submission referred to in SUP 16.12.4R are set out in the table below. The due dates are the last day of the periods given in the table below following the relevant reporting frequency period set out in SUP 16.12.26R, unless indicated otherwise.

Data item	Daily	Weekly	Monthly	Quarterly	Half yearly	Annual
…						
~~FSA003~~				~~20 *business days*~~	~~30 *business days* (note 1);45 *business*~~	

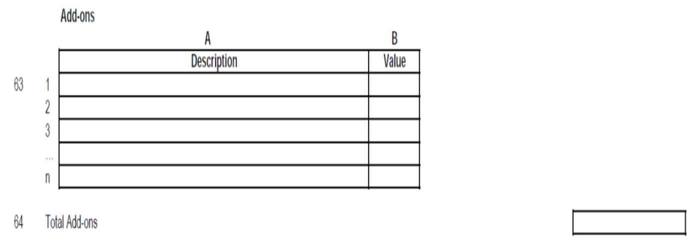
					~~*days* (note 2)~~	
~~FSA004~~				~~20 *business days*~~	~~30 *business days* note 1);45 *business days* (note 2)~~	
…						
~~FSA007~~						~~2 months~~
~~FSA008~~				~~20 *business days* (note 1);45 *business days* (note 2)~~		
…						
~~FSA028~~					~~30 *business days*~~	
…						
~~FSA046~~				~~20 business days (Note 1), 45 business days (Note 2)~~		
…						
~~FSA058~~				~~20 business days (Note 1), 45 business days (Note 2)~~		
…						

…

Part 2

16 Annex 24R Data items for SUP 16.12

In this Part, the text in the data item, the title of which is set out in column (1), is deleted, except as indicated in column (2), unless the context otherwise requires.

(1)	(2)
FSA003 Capital Adequacy	
FSA004 Credit Risk	
FSA005 Market Risk	Delete and substitute with the following: 
FSA007 Operational risk	
FSA008 Large exposures	
FSA028 Non-EEA sub-group	
FSA046 Securitisation: Non-Trading Book	
FSA058 Securitisation: Trading Book	

Part 3

16 Annex 25G Guidance notes for data items in SUP 16 Annex 24R

In this Part, the text in the data item, the title of which is set out in column (1), is deleted, except as indicated in column (2), unless the context otherwise requires.

(1)	(2)
FSA003 Capital Adequacy	
FSA004 – Credit Risk	
FSA005 – Market Risk	Delete text and replace with the following: **FSA005 – Market risk** This data item provides the appropriate regulator with information on individual requirements placed on firms regarding market risk capital requirements. **Add-ons** **63 Add-ons** This comprises the add-ons under the RNIV framework. **64 Total Add-ons**

	The total of items 1 to n in 63 **FSA005 – Market risk validations** **Internal validations** Data elements are referenced by row then column. 53 | 64G | = | SUM (63B)
FSA007 – Operational Risk	
FSA008 – Large Exposures	
FSA009 – Key data validations	
FSA018 – UK integrated group large exposures	Delete text and substitute with the following: **FSA018 – Exposures from the core UK group to the non-core large exposures group** This data item is only applicable to *firms* that have both a *core UK group* and a *non-core large exposures group* and captures information on *exposures* from the *core UK group (*including the *firm)* to the *non-core large exposures group.* A single report is required in respect of exposures from all members of the *core UK group* (including the *firm)*, reflecting the exposures at the reporting date*.* FSA018 was originally constructed to capture information on the level of exposures from the UK integrated group to the diverse blocks and residual blocks. However, *firms* should interpret this form on the basis of the *core UK group* and *non-core large exposures group* respectively, and follow the specific instructions provided for the individual data cells. Unless indicated otherwise, the valuation of items should follow CRR Article 390. **Valuation** Unless indicated otherwise, the valuation of data elements should follow CRR Article 390. **Currency** You should report in the currency of your annual audited accounts (i.e. in either Sterling, Euro, US dollars, Canadian dollars, Swedish Kroner, Swiss Francs or Yen). Figures should be reported in 000s. **Data elements** These are referred to by row first, then by column, so data element 2B will be the element numbered 2 in column B. Individual rows within an element are identified as 2B.1, 2B.2 etc. **General** **1** [deleted] **2 Firm Reference Numbers** List the Firm Reference Numbers for all the authorised firms in the *core UK group* only. As this report is a joint requirement across all firms that are members of that group, this notifies us which firms' requirements are being met by this data item. Firms should be listed sequentially in 2A, with the Firm Reference

	Numbers being entered in 2B. Complete cell for CNCOM charge. **3A Core UK group eligible capital** This is c*ore UK group eligible capital* **4A Exposure number** Please number each exposure consecutively. **4B Non-core large exposures group** Complete one line only in respect of aggregate exposure of the *core UK group* (including the *firm*) to all members of the *non-core large exposures group*. Ignore line marked 'Total'. **4C Gross exposure** Report here the gross exposure of the *core UK group* (including the *firm*) to all members of the *non-core large exposures group*. **4D % of core UK group eligible capital** This is column C as a percentage of data element 3A (*core UK group eligible capital*). It should be entered to two decimal places, omitting the % sign. **4E Exposure after credit risk mitigation** This is the figure reported in column D after credit risk mitigation. This figure is subsequently broken down in columns F to M. **4F Amount of the exposure that is exempt** That part of the amount reported in column E that is an exempt under CRR Article 400. **4G % of core UK group eligible capital** This is column F as a percentage of data element 3A (*core UK group eligible capital*. It should be entered to two decimal places, omitting the % sign. **4H Amount of the exposure that is not exempt and is in the non-trading book** That part of the exposure reported in column E that is not exempt and is in the non-*trading book*. **4J % of core UK group eligible capital** This is column H as a percentage of *core UK group eligible capital*. It should be entered to two decimal places, omitting the % sign. **4K Amount of the exposure that is not exempt and is in the trading book** That part of the exposure reported in column E that is not exempt and is in the *trading book*. **4L % of core UK group eligible capital** This is column K as a percentage of *core UK group eligible capital*. It should be entered to two decimal places, omitting the % sign. **4M Aggregate % of *core UK group eligible capital*** This is the sum of columns J and L. The total of the column should be monitored against the limit set out in [2.2 of the large exposures chapter of PRA rulebook]. It should be entered to two decimal places, omitting the % sign. **4N CNCOM** This is the amount of CNCOM calculated as set out in CRR Article 397 before being allocated to individual members of the core UK group in accordance with CRR Article 395(c)&(d). *Firms* will be expected to have sufficient capital resources at the reporting dates to meet this requirement.
FSA028 – Non EEA-sub group	
FSA046 – Securitisation: Non-Trading Book	
FSA058 –	

Securitisation: Trading Book	

Part 4

16 Annex 25G Guidance notes for data items in SUP 16 Annex 24R

In this Part, underlining indicates new text and striking through indicates deleted text.

FSA001 – Balance sheet

…

Valuation

Firms should follow their normal accounting practice wherever possible. ~~As there is no direct linkage with FSA003, there is no need for the data to follow the valuation rules applicable for capital adequacy purposes eg in relation to adjustments to the accounting values set out in *GENPRU* 1.3.36R.~~

Consolidation

When reporting the balance sheet on a ~~*UK*~~ *consolidation group* basis, firms should where possible treat the consolidation group as a single entity (ie line-by-line) rather than on an aggregation basis. However, for the liabilities, ~~in the same way as for the *capital resources* calculation figure in FSA003,~~ the consolidation should only treat the group as a single entity (ie line-by-line).

…

Assets

These are broken down between trading book assets, and those that are not trading book assets. Hence the items reported in column B will exclude the items reported in column A. If a firm cannot easily identify trading book assets, all assets should be reported in the non-trading book column.

Firms can determine whether they have trading book or not. However, it is expected that a firm that identifies trading book profits in FSA002~~, or reports trading book profits in FSA003 (in data element 61A),~~ should be able to identify trading book assets.

~~However, even if a firm does not identify trading book assets, it does not preclude that firm from having foreign exchange and commodities risk in the *market risk capital requirement* (data element 93A) in FSA003.~~

…

16 Other intangible assets

Include here intangible assets, other than goodwill. ~~The value here may differ from that reported in FSA003 - see *GENPRU* 2.2.155R and *GENPRU* 2.2.156G.~~

…

42A Called up share capital, including partnership, LLP and sole trader capital

Exclude holdings by the firm of its own shares ~~(although these holdings should be reported in FSA003)~~ and also excess of drawings over profits for partnerships, LLPs or sole traders ~~(which are also reported in FSA003)~~. *Building societies* should exclude *PIBS*, which should be reported in 38A.

43A Reserves

~~As firms may use figures compiled on the same basis as audited accounts, the figures presented here may differ from those reported in FSA003. This is because of the different valuation basis used for capital adequacy, as set out in *GENPRU* 1.3.~~ <u>Firms may use figures compiled on the same basis as audited accounts.</u>

44A Minority interests

~~As firms may use figures compiled on the same basis as audited accounts, the figures presented here may differ from those reported in FSA003 as a memorandum item. This is because of the different valuation basis used for capital adequacy, as set out in *GENPRU* 1.3.~~ Firms may use figures compiled on the same basis as audited accounts.

…

FSA002 – Income statement

…

Valuation

Firms should follow their normal accounting practice wherever possible. ~~In this regard, the figure for profits reported here may differ from the figures reported at the same date in FSA003, primarily because of valuation differences that arise from the application of *GENPRU* 1.3.~~

…

Consolidation

Firms reporting on a ~~*UK*~~ *consolidation group* basis can use the same accounting basis for consolidation as in their accounts, as long as the group on which it is based accords with the ~~*UK*~~ *consolidation group*. ~~(On FSA003, such firms will, however, have to report their capital resources on a line-by-line basis under *BIPRU* 8, and firms may prefer to do so here too.)~~

…

Trading book

Data elements in column A relate only the trading book. Firms should identify their trading book profits separately from the non-trading book profits wherever possible. ~~Firms that intend to include 'net interim trading book profit and loss' in data element 61A in FSA003 should complete this column. It is optional for other firms. See *BIPRU* 1.2 for the definition of the trading book..~~

…

46B Net profit (loss)

This is the total profit (loss) after tax, before accounting for any minority interests. ~~(which only get reported on FSA003).~~

…

FSA045 – IRB portfolio risk

~~This data enables the appropriate regulator to understand the relationship between cyclicality and capital requirements under the CRD, help mitigate the risk of financial instability or economic recession, and be in a position to influence/contribute to international discussions on this. The information provided should be used to calculate that *firm's* capital requirements. *Firms* should submit the data in their own PD bands.~~

…

Credit risk

…

Exposure at default estimate

Calculate in accordance with ~~*BIPRU* 4~~ Article 166 *CRR*. This should be the downturn EAD.

Maturity

This is the exposure weighted average maturity in days. It should take into account the maturity floor and ceiling.

…

Risk weighted exposure amount

Calculate in accordance with ~~*BIPRU* 4~~ Articles 153 and 154 *CRR*. The SME-supporting factor according to Article 501 *CRR* should be excluded.

…

Part 5: **Comes into force on 1 July 2014.**

In this Part, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

16.12.4 R Table of applicable rules containing *data items*, frequency and submission periods

(1)		**(2)**	**(3)**	**(4)**
RAG **number**	*Regulated Activities*	**Provisions containing:**		
		applicable *data items*	**reporting frequency/ period**	**due date**
RAG 1	• accepting deposits • *meeting of repayment claims* • *managing dormant account funds (including the investment of such funds)*	*SUP* 16.12.5R, except FSA001 and FSA002 for *FINREP firms*	*SUP* 16.12.6 R	*SUP* 16.12.7R
…				
RAG 3	• dealing in investment as principal • dealing in investments as agent • advising on investments (excluding retail investment activities) • arranging (bringing about) deals in investments (excluding retail investment activities)	*SUP* 16.12.10R *SUP* 16.12.11B R, except FSA001 and FSA002 for *FINREP firms*	*SUP* 16.12.10R *SUP* 16.12.12R	*SUP* 16.12.10 R *SUP* 16.12.13R
RAG 4	• managing investments • establishing, operating or winding up a regulated collective investment scheme • establishing, operating or winding up an unregulated collective investment scheme • establishing, operating or winding up a stakeholder pension scheme • establishing, operating or winding up a personal pension scheme	*SUP* 16.12.14R *SUP* 16.12.15B R, except FSA001 and FSA002 for *FINREP firms*	*SUP* 16.12.14R *SUP* 16.12.16R	*SUP* 16.12.14 R *SUP* 16.12.17 R
…				
RAG 7	• retail investment	*SUP* 16.12.22CR,	*SUP*	*SUP*

	activities • advising on pensions transfers & opt-outs • arranging (bringing about deals) in retail investments	except FSA001 and FSA002 for *FINREP firms*	16.12.23R	16.12.24R
RAG 8	• making arrangements with a view to transactions in investments • operating a multilateral trading facility	*SUP* 16.12.25CR, except FSA001 and FSA002 for *FINREP firms*	*SUP* 16.12.26R	*SUP* 16.12.27 R
…				

Part 6: **Comes into force on a date specified by a subsequent PRA Board Instrument.**

16.12 Integrated Regulatory Reporting

Application

16.12.1 G The effect of SUP 16.1.1R is that this section applies to every *firm* carrying on business set out in column (1) of *SUP* 16.12.4R except:

(1)

(1B) an *EEA bank*;

…

(…)

Reporting requirement

16.12.3 R (1) Any *firm* permitted to carry on any of the activities within each of the *RAG*s set out in column (1) of the table in *SUP* 16.12.4R must:

(a) …

…

(iv) in the case of a *non-EEA bank*~~, or an *EEA bank* (whether or not it has *permission* for *accepting deposits*) other than one with *permission* for *cross border services* only,~~ any *data items* submitted should, unless indicated otherwise, only cover the activities of the branch operation in the *United Kingdom*;

in the format specified as applicable to the *firm* in the provision referred to in column (2);

…)

…

16.12.4A ~~G~~ ~~*RAG* 1 includes an *incoming EEA firm* exercising a *BCD* right through a *UK* branch.~~ [deleted]

…

Regulated Activity Group 1

16.12.5 R The applicable *data items* and forms or reports referred to in *SUP* 16.12.4R are set out according to *firm* type in the table below:

Description of *data item*	Prudential category of *firm*, applicable *data items* and reporting format (Note 1)							
	UK bank	*Building society*	*Non-EEA*	~~*EEA bank* that has~~	~~*EEA bank* that~~	[deleted]	*Credit union*	*Dormant account*

			bank	~~*permission* to accept deposits, other than one with permission for cross border services only~~ [deleted]	~~does not have permission to accept deposits, other than one with permission for cross border services only~~ [deleted]			*fund operator* (note 15)
…								
Daily Flows	FSA 047 (Notes 16, 20 and 22)	FSA047 (Notes 16, 20 and 22)	FSA047 (Notes 16, 18, 20 and 22)	~~FSA047 (Notes 16, 18, 20 and 22)~~ [deleted]	~~FSA047 (Notes 16, 18, 20 and 22)~~ [deleted]			
Enhanced Mismatch Report	FSA 048 (Notes 16, 20 and 22)	FSA048 (Notes 16, 20 and 22)	FSA048 (Notes 16, 18, 20 and 22)	~~FSA048 (Notes 16, 18, 20 and 22)~~ [deleted]	~~FSA048 (Notes 16, 18, 20 and 22)~~ [deleted]			
Liquidity Buffer Qualifying Securities	FSA 050 (Notes 17, 21 and 22)	FSA050 (Notes 17, 21 and 22)	FSA050 (Notes 17, 19, 21 and 22)	~~FSA050 (Notes 17, 19, 21 and 22)~~ [deleted]	~~FSA050 (Notes 17, 19, 21 and 22)~~ [deleted]			
Funding Concentration	FSA 051 (Notes 17, 21 and 22)	FSA051 (Notes 17, 21 and 22)	FSA051 (Notes 17, 19, 21 and 22)	~~FSA051 (Notes 17, 19, 21 and 22)~~ [deleted]	~~FSA051 (Notes 17, 19, 21 and 22)~~ [deleted]			
Pricing	FSA 052	FSA052 (Notes	FSA052 (Notes	~~FSA052 (Notes~~	~~FSA052 (Notes~~			

data	(Notes 17, 22 and 24)	17, 22 and 24)	17, 19, 22 and 24)	~~17, 19, 22 and 24)~~ [deleted]	~~17, 19, 22 and 24)~~ [deleted]			
Retail and corporate funding	FSA 053 (Notes 17, 21 and 22)	FSA053 (Notes 17, 21 and 22)	FSA053 (Notes 17, 19, 21 and 22)	~~FSA053 (Notes 17, 19, 21 and 22)~~ [deleted]	~~FSA053 (Notes 17, 19, 21 and 22)~~ [deleted]			
Currency Analysis	FSA 054 (Notes 17, 21 and 22)	FSA054 (Notes 17, 21 and 22)	FSA054 (Notes 17, 19, 21 and 22)	~~FSA054 (Notes 17, 19, 21 and 22)~~ [deleted]	~~FSA054 (Notes 17, 19, 21 and 22)~~ [deleted]			
…								

…

PRA RULEBOOK CRR FIRMS: PUBLIC DISCLOSURE INSTRUMENT 2013

Powers exercised

A. The Prudential Regulation Authority ("PRA") makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137G (the PRA's general rules); and
(2) section 137T (general supplementary powers).

B. The rule-making powers referred to above are specified for the purpose of section 138G (2) (Rule-making instrument) of the Act.

Pre-conditions to making

C. In accordance with section 138J of the Act (consultation with the Financial Conduct Authority) ("FCA"), the PRA consulted the FCA. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

PRA Rulebook CRR Firms: Public Disclosure Instrument 2013

D. The PRA makes the rules in the Annex to this Instrument.

Commencement

E. This instrument comes into force on 1 January 2014.

Citation

F. This instrument may be cited as the PRA Rulebook CRR Firms: Public Disclosure Instrument 2013.

By order of the Board of the Prudential Regulation Authority
[DATE]

Annex

In this Annex, the text is all new and is not underlined.

Part

PUBLIC DISCLOSURE

Chapter content

Links

1 APPLICATION AND DEFINITIONS

1.1 This Part applies to every firm that is a *CRR firm*.

1.2 In this Part the following definitions shall apply:

annual report and accounts

(1) (in relation to a company incorporated in the United Kingdom) an annual report and annual accounts as those terms are defined in:

(a) (section 262(1) of the Companies Act 1985, together with an auditor's report prepared in relation to those accounts under section 235 of the same Act where these provisions are applicable; or

(b) section 471 of the Companies Act 2006 together with an auditor's report prepared in relation to those accounts under sections 495 to 497 of the same Act;

(2) (in relation to any other body) any similar or analogous documents which it is required to prepare whether by its constitution or by the law under which it is established.

2 PUBLIC DISCLOSURE OF RETURN ON ASSETS

2.1 A *firm* must disclose in its *annual report and accounts* among the key indicators their return on assets, calculated as their net profit divided by their total balance sheet.

[Note: Art 90 of the *CRD*]

PRA 2013/XX

PRA RULEBOOK CRR FIRMS: WAIVERS TRANSITIONAL PROVISIONS INSTRUMENT 2013

Powers exercised

A. The Prudential Regulation Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):

(1) section 137G (the PRA’s general rules); and
(2) section 137T (general supplementary powers).

B. The rule-making powers referred to above are specified for the purpose of section 138G (Rule-making instrument) of the Act.

Pre-conditions to making

C. In accordance with section 138J of the Act (consultation with the Financial Conduct Authority) (“FCA”), the PRA consulted the FCA. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

PRA Rulebook CRR Firms: Waivers Transitional Provisions Instrument 2013

D. The PRA makes the rules in Annex A to this instrument.

Commencement

E. Annex A of this instrument comes into force on 1 January 2014.

Citation

F. This instrument may be cited as the PRA Rulebook CRR Firms: Waivers Transitional Provisions Instrument 2013.

By order of the Board of the Prudential Regulation Authority
[DATE]

Annex A

In this Annex, the text is all new and is not underlined.

Part

WAIVERS TRANSITIONAL PROVISIONS

Chapter content

Links

1 APPLICATION AND DEFINITIONS

1.1 This Part applies to every *firm* that is a *CRR firm*.

1.2 In this Part the following definitions shall apply:

CRR permission

means a direction given to a *firm* by the *PRA* under any *CRR* Article listed in column B of the Tables in Schedules 1 and 2 in the exercise of the discretion afforded to it as a *competent authority.*

Requirement

means a requirement imposed by the *PRA* on a *firm* under section 55M of *FSMA.*

Waiver

means a direction waiving or modifying a rule given by the *PRA* under section 138A (waiver or modification of rules) *FSMA.*

1.3 Unless otherwise defined, any italicised expression used in this Part and in the *CRR* has the same meaning as in the *CRR*.

2 WAIVERS TRANSITIONAL PROVISIONS

2.1 (1) This rule applies where, immediately before 1 January 2014, a *waiver* given or a *requirement* imposed in relation to a rule listed in column A of the Tables in Schedules 1 and 2 has effect.

(2) Subject to paragraphs (5) to (7), each *waiver* or *requirement* given in relation to a *PRA* rule listed in column A of the Tables in Schedules 1 and 2 is to be treated as a *CRR permission* given by the PRA to the *firm* under the *CRR* Article listed in the same row in column B of the Table.

(3) Each *CRR permission* given in accordance with paragraph (2) shall continue to have effect until the expiry date specified in the *waiver* or in the Written Notice of the *requirement*.

(4) Where a *waiver* listed in Schedules 1 and 2 specifies that it applies to a *firm* on a consolidated basis in accordance with a relevant provision in *BIPRU* 8, the *permission* shall apply to the *firm* on the basis of its *consolidated situation* in accordance with Article 11 of the *CRR*.

(5) Paragraphs (1) to (4) only have effect in relation to a *waiver* listed in Schedule 1 where the *firm* has confirmed to the *PRA* that it materially complies with the requirements relevant to the *rules* listed in Column A of the Table, as waived or modified by the *waiver*, and any conditions relevant to the application of the *waiver.*

(6) Paragraphs (1) to (4) do not have effect in relation to a *waiver* listed in Schedule 2 if the *firm* ceases to comply at any time with the *rules* listed in Column A of the Table, as waived or modified by the *waiver*, or any conditions relevant to the application of the *waiver,*.

(7) A *waiver* listed in row 1 of the Table in Schedule 2 (individual consolidation method) only includes a deemed *solo consolidation waiver* under *BIPRU* TP 22.3R where a *firm* has confirmed to the *PRA* that the solo consolidation minimum standards are met with respect to the relevant *subsidiary undertaking*.

2.2 (1) This rule applies where, immediately before 1 January 2014, a *waiver* given in relation to a *SUP rule* listed in column A of the Table in Schedule 3 has effect.

(2) Each *waiver* given in relation to a *SUP rule* listed in column A of the Table in Schedule 3 is to be treated as a *waiver* given by the PRA to the *firm* under the *SUP rule* listed in the same row in column B of the Table.

Schedule 1

Internal model waivers

	CRR Permission	Column A PRA/FCA Rule (rule waiver or modification)	Column B CRR Reference
1	Internal Ratings Based (IRB) permission for credit risk	- *BIPRU* 4 applies to a *firm* with an *IRB permission* - *Rules* waived or modified: (a) *GENPRU* 2.1.51R (b) *BIPRU* 3.1.1R	- Part Three, Title II, Chapter 3 - Art. 143 - Art. 178.1(b) (where a *firm* is authorised by its *IRB waiver* to use a 180 days definition of default for exposures secured by residential real estate in the retail exposure class, as well as for exposures to public sector entities)
2	Eligibility of physical collateral under the IRB Approach	- *BIPRU* 4.10.16R (Where authorised by the *firm's IRB permission*)	Art. 199.6
3	Master netting agreement internal models approach	- *BIPRU* 5.6.1R in accordance with *BIPRU* 5.6.12R	Art. 221
4	Supervisory formula method for securitisation transactions	- *BIPRU* 9.12.3R - *BIPRU* 9.12.5R - *BIPRU* 9.12.21R (Where authorised by the *firm's IRB permission*)	Art. 259.1(b) Art. 262
5	ABCP internal assessment approach	- *BIPRU* 9.12.20R (Where authorised by the *firm's IRB permission*)	Art. 259.3
6	Exceptional treatment for liquidity facilities where pre-securitisation RWEA cannot be calculated	- *BIPRU* 9.11.10R as modified in accordance with *BIPRU* 9.12.28G (Where authorised by the *firm's IRB permission*)	Art. 263.2
7	Advanced Measurement Approach (AMA) permission	- *BIPRU* 6.5 applies to a firm with an *AMA permission*	- Art. 312.2 - Part Three, Title III,

		- *Rule* waived or modified: *BIPRU* 6.2.1R	Chapter 4
8	Combined use of different approaches for operational risk – AMA and standardised approach or basic indicator approach	- *BIPRU* 6.2.9R (in accordance with *BIPRU* 6.2.10G and the *firm's AMA permission*)	Art. 314, par. 2 and 3
9	Permission to use internal models to calculate own funds requirements for market risk (Value at Risk)	- *BIPRU* 7.10 applies to a firm with a *VaR model permission* - *Standard market risk PRR rules* as specified and waived or modified by the *firm's VaR model permission waiver* - *GENPRU* 2.1.52R	- Art. 363 - Part Three; Title IV; Chapter 5; Sections 2, 3 and 4
10	Permission to use internal models to calculate own fund requirements for the correlation trading portfolio	- *BIPRU* 7.10.55T R to *BIPRU* 7.10 55ZA R (Where the *firm* is authorised to use the *all price risk measure* in its *VaR model permission waiver*)	Art. 377

Schedule 2

Other Waivers and Requirements

	CRR Permission	**Column A** **PRA/FCA Rule** **(rule waiver or modification)**	**Column B** **CRR Reference**
1	Individual consolidation method	- *BIPRU* 2.1.7R (*Solo consolidation waivers*)	Art. 9
2	Application of requirements of Part Five (exposures to transferred credit risk) on a consolidated basis	- *BIPRU* 9.15.16A R	Art. 14.3
3	Methods of prudential consolidation – Art. 12(1) relationship	- *BIPRU* 8.5.6(2)R (As required by the Part 4A permission of the *firm*)	- Art. 18.3 as implemented by rule 2.1 of the PRA Rulebook CRR Firms: Groups Instrument 2013
4	Methods of prudential consolidation- Significant influence or single management relationship	- *BIPRU* 8.5.6(2)R - "*Art. 134 relationship*" (as required by the Part 4A permission of the *firm*)	- Art. 18.6 as implemented by rule 2.1 of the PRA Rulebook CRR Firms: Groups Instrument 2013
5	Entities excluded from the scope of prudential consolidation	- *BIPRU* 8.5.9R - *BIPRU* 8.5.10R	Art. 19.2
6	Permission to revert to the use of a less sophisticated approach for credit risk	- *BIPRU* 4.2.23R (as modified in accordance with *BIPRU* 4.2.25G) - *BIPRU* 4.2.24R (as modified in accordance with *BIPRU* 4.2.25G)	Art. 149
7	Traditional securitisation – recognition of significant risk transfer	- *BIPRU* 9.4.11R - *BIPRU* 9.4.12R (subject to conditions in *BIPRU* 9.4.15D)	Art. 243 par. 2, 3, 4 and 5
8	Synthetic securitisation – recognition of significant risk transfer	- *BIPRU* 9.5.1R (6) and(7) (subject to conditions in *BIPRU* 9.5.1B D)	Art. 244, par. 2, 3, 4 and 5

9	Securitisations of revolving exposures with early amortisation provisions – similar transactions	- *BIPRU* 9.13.11R - *BIPRU* 9.13.13R - *BIPRU* 9.13.14R - *BIPRU* 9.13.15R - *BIPRU* 9.13.16R - *BIPRU* 9.13.17R (subject to conditions in *BIPRU* 9.13.18G)	Art. 256.7
10	Permission to revert to the use of a less sophisticated approach for operational risk	- *BIPRU* 6.2.5R (as modified in accordance with *BIPRU* 6.2.6G) - *BIPRU* 6.2.7R (as modified in accordance with *BIPRU* 6.2.8G)	Art. 313
11	Combined use of different approaches for operational risk – standardised approach and basic indicator approach	- *BIPRU* 6.2.12R (as modified in accordance with *BIPRU* 6.2.13G)	Art. 314.4
12	Waiver of the 3 year average for calculating the own funds requirement under the basic indicator approach for operational risk	- *BIPRU* 6.3.2R (as modified in accordance with *BIPRU* 6.3.9G)	Art. 315
13	Waiver of the 3 year average for calculating the own funds requirement under the standardised approach for operational risk	- *BIPRU* 6.4.5R (as modified in accordance with *BIPRU* 6.4.8G)	Art. 317.4
14	Own funds requirements for position risk for options and warrants on: (a) interest rates; (b) debt instruments; (c) equities; (d) equity indices; (e) financial futures; (f) swaps; and (g) foreign currencies	- *BIPRU* 7.9 applies to a *firm* with a *CAD1 model waiver*. - *Rules* waived or modified: (a) *GENPRU* 2.1.52R (b) *BIPRU* 7.6.1R	Art. 329
15	Own funds requirements for commodities risk for options and warrants on: (a) commodities; and (b) commodities derivatives	- *BIPRU* 7.9 applies to a *firm* with a *CAD1 model waiver*. - *Rules* waived or modified: (a) *GENPRU* 2.1.52R (b) *BIPRU* 7.4.1R	Art. 358.3
16	Interest rate risk on derivative instruments	- *CAD1 model waiver* for the use of an interest rate pre-processing model in accordance with BIPRU 7.9.44G - *Rule* waived: *GENPRU* 2.1.52R	Art. 331 Art. 340

17	Waiver of 100% large exposure limit where the €150 million limit applies	- *BIPRU* 10.6.32R – As waived in accordance with *BIPRU* 10.6.33G - *SUP* 15.3.11R	- Art. 396 in relation to the 100% large exposure limit set out in Art. 395(1)
18	Waiver of large exposure limits in relation to intra-group exposures: core group waivers	- *BIPRU* 3.2.25R(2) - *BIPRU* 10.8A	Art. 113.6 Art. 400.1(f)
19	Waiver of large exposure limits in relation to intra-group exposures: non-core group waivers	- *BIPRU* 10.9A	- Art. 400.2(c) as implemented by rule 2 of the PRA Rulebook CRR Firms: Large Exposures Instrument 2013
20	Waiver of large exposure limits in relation to sovereign exposures	- BIPRU 10.6.34R as waived in accordance with BIPRU 10.6.37G	- Art. 400.2(g) and (h) as implemented by rule 3 of the PRA Rulebook CRR Firms: Large Exposures Instrument 2013

Schedule 3

Waivers in Supervision Manual (SUP) 16

Column A SUP 16 rule as in force until 31 December 2013	Column B SUP 16 rule as in force from 1 January 2014
SUP 16.12.11R	SUP 16.12.11B R
SUP 16.12.12. R	SUP 16.12.12A R
SUP 16.12.15 R	SUP 16.12.15B R
SUP 16.12.16 R	SUP 16.12.16A R
SUP 16.12.22A R	SUP 16.12.22C R
SUP 16.12.25A R	SUP 16.12.25C R
SUP 16.12.26 R	SUP 16.12.26A R

PRA RULEBOOK – GLOSSARY INSTRUMENT 2013

Powers exercised

A. The Prudential Regulation Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137G (the PRA's general rules), and
(2) section 137T (general supplementary powers).

B. The rule-making powers referred to above are specified for the purpose of section 138G (Rule-making instrument) of the Act.

Pre-conditions to making

C. In accordance with section 138J of the Act (consultation with the Financial Conduct Authority) ("FCA"), the PRA consulted the FCA. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

Making the PRA Rulebook – Glossary Instrument 2013

D. The PRA makes the rules in Annex A to this instrument.

Commencement

E. This instrument comes into force on 1 January 2014.

Citation

F. This instrument may be cited as the PRA Rulebook – Glossary Instrument 2013.

By order of the Board of the Prudential Regulation Authority
[DATE]

Annex A

PRA RULEBOOK – GLOSSARY

In this Annex, the text is all new and is not underlined.

After […] insert the following new Part.

building society

means a building society within the meaning of section 119 of the Building Societies Act 1986.

CRD

means Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC.

credit union

means a credit union within the meaning of section 31 of the Credit Unions Act 1979.

CRR

Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012.

CRR firm

means a *UK bank*, a *building society* or a *UK designated investment firm.*

EBA

means the European Banking Authority.

firm

means a *PRA-authorised person* within the meaning of section 2B(5) *FSMA.*

FSMA

means Financial Services and Markets Act 2000.

market risk

means the risk that arises from fluctuations in values of, or income from assets, or in interest or exchange rates.

PRA

means the Prudential Regulation Authority.

third country

means a territory or country that is not an *EEA State.*

UK bank

means a *UK undertaking* that has permission under Part 4A of FSMA to carry on the *regulated activity* of accepting deposits and is a *credit institution*, but is not a *credit union* or a *building society.*

UK designated investment firm

means a *UK undertaking* that is an investment firm that has been designated by the PRA under Article 3 of Financial Services and Markets Act 2000 (PRA-regulated Activities) Order (S.I. 2013/556).

UK undertaking

means an undertaking within the meaning of section 1161(1) of the Companies Act 2006 (meaning of "undertaking" and related expressions) that is established in any part of the UK.

unregulated activity

means an activity that is not a *regulated activity*.

PRA RULEBOOK CRR FIRMS: INTERPETATION INSTRUMENT 2013

Powers exercised

A. The Prudential Regulation Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):

(1) section 137G (the PRA’s general rules).

B. The rule-making powers referred to above are specified for the purpose of section 138G (rule-making instrument) of the Act.

Pre-conditions to making

C. In accordance with section 138J of the Act (consultation with the Financial Conduct Authority) (“FCA”), the PRA consulted the FCA. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

PRA Rulebook CRR Firms: Interpretation Instrument 2013

D. The PRA makes the rules in Annex A to this instrument.

Commencement

E. Annex A of this instrument comes into force on 1 January 2014.

Citation

F. This instrument may be cited as the PRA Rulebook CRR Firms: Interpretation Instrument 2013.

By order of the Board of the Prudential Regulation Authority
[DATE]

Annex A

Part

INTERPRETATION

Chapter content

Links

1 APPLICATION

1.1 This Part applies to a f*irm.*

2 INTERPRETATIVE PROVISIONS

Purposive interpretation

2.1 Every provision in the *PRA* Rulebook must be interpreted in the light of its purpose.

Use of defined expressions

2.2 In the PRA Rulebook, save as otherwise indicated in a Part of the *PRA* Rulebook, an expression in italics defined in:

(1) the *PRA* Rulebook Glossary has the meaning given in that glossary;

(2) *FSMA* has the meaning given in that Act;

(3) the Interpretation Act 1978 has the meaning given in that Act.

Application of the Interpretation Act 1978

2.3 Save as otherwise indicated, the Interpretation Act 1978 applies to the *PRA* Rulebook.

Cross-references in the PRA Rulebook

2.4 A reference in the *PRA* Rulebook to another provision in the *PRA* Rulebook is a reference to that provision as amended from time to time.

Activities covered by rules

2.5 In the *PRA* Rulebook, a rule made by the *PRA* under section 137G of *FSMA* applies to a *firm* with respect to the carrying on of any activities, except to the extent that a contrary intention appears.

Continuity of authorised partnerships and unincorporated associations

2.6 If a *firm* is dissolved, but its authorisation continues to have effect under section 32 (Partnerships and unincorporated associations) of *FSMA* in relation to any partnership or unincorporated association that succeeds to the business of the dissolved *firm*, the successor partnership or unincorporated association is to be regarded as the same *firm* for the purposes of the *PRA* Rulebook unless the context otherwise requires.

CAPITAL REQUIREMENTS DIRECTIVE (DISAPPLICATION) INSTRUMENT 2013

Powers exercised

A. The Prudential Regulation Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137G (the PRA's general rules); and
(2) section 137T (general supplementary powers).

B. The Prudential Regulation Authority gives as guidance each provision in the Annex marked with a G.

C. The rule-making powers referred to above are specified for the purpose of section 138G (Rule-making instrument) of the Act.

Pre-conditions to making

D. In accordance with section 138J of the Act (consultation with the Financial Conduct Authority) ("FCA"), the PRA consulted the FCA. After consulting, the PRA published a draft of proposed amended rules and had regard to representations made.

Commencement

E. This instrument comes into force on 1 January 2014.

Amendments

F. The General Prudential sourcebook (GENPRU) is amended in accordance with Annex A to this instrument.

G. The Prudential sourcebook for Banks, Building Societies and Investment Firms (BIPRU) is amended in accordance with Annex B to this instrument.

Citation

H. This instrument may be cited as the Capital Requirements Directive (Disapplication) Instrument 2013.

By order of the Board of the Prudential Regulation Authority
[DATE]

Annex A

Amendments to the General Prudential sourcebook (GENPRU)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

Application

1.1 Application

…

1.1.2 G ~~Broadly speaking however, *GENPRU* applies to:~~

~~(1) an *insurer*;~~

~~(2) a *bank*;~~

~~(3) a *building society*;~~

~~(4) a *BIPRU investment firm*; and~~

~~(5) groups containing such *firms*.~~ [deleted]

1.1.-2 G Further, *GENPRU* also broadly applies to:

(1) an *insurer*;

(2) groups containing an *insurer*.

…

1.2 Adequacy of financial resources

Application

1.2.1 R ~~This section applies to:~~

~~(1) a *BIPRU firm*; and~~

~~(2) an *insurer*, unless it is:~~

~~(a) a *non-directive friendly society*; or~~

~~(b) a *Swiss general insurer*; or~~

~~(c) an *EEA-deposit insurer*; or~~

~~(d) an *incoming EEA firm*; or~~

~~(e) an *incoming Treaty firm*.~~

~~(3) [deleted]~~ [deleted]

1.2.1A R This section also applies to an *insurer*, unless it is:

(1) a *non-directive friendly society*; or

(2) a *Swiss general insurer*; or

(3) an *EEA-deposit insurer*; or

(4) an *incoming EEA firm*; or

(5) an *incoming Treaty firm*.

1.2.2A R ~~In relation to any provision in this section which applies to a *BIPRU firm*, a reference in that provision to "financial resources" does not constitute a reference to "liquidity resources".~~ [deleted]

1.2.3A G ~~In relation to:~~

~~(1) a *BIPRU firm*;~~

~~(2) an *incoming EEA firm* which:~~

~~(a) is a *full BCD credit institution*; and~~

~~(b) has a *branch* in the *United Kingdom*; and~~

~~(3) a *third country BIPRU firm* which:~~

~~(a) is a *bank*; and~~

~~(b) has a *branch* in the *United Kingdom*;~~

~~*BIPRU* 12 contains *rules* and *guidance* in relation to the adequacy of that *firm's* liquidity resources.~~ [deleted]

…

1.2.11 G The adequacy of a *firm's* financial resources needs to be assessed in relation to all the activities of the *firm* and the risks to which they give rise and so this section applies to a *firm* in relation to the whole of its business. ~~In the case of a *UCITS investment firm* this means that this section is not limited to *designated investment business* excluding *scheme management activity*. It also applies to *scheme management activity* and to activities that are not *designated investment business*.~~

Purpose

…

1.2.13 G This section amplifies *Principle* 4, under which a *firm* must maintain adequate financial resources. It is concerned with the adequacy of the financial resources that a *firm* needs to hold in order to be able to meet its liabilities as they fall due. These resources include both capital and liquidity resources. ~~As noted in *GENPRU 1.2.3AG*, however, the *appropriate regulator's rules* and *guidance* in relation to the adequacy of the liquidity resources of a *BIPRU firm* are set out in *BIPRU 12*.~~

1.2.14 G ~~In the case of a *bank* or *building society* this section implements Article 123 and (in part) Annex XI of the *Banking Consolidation Directive*. In the case of a *BIPRU investment firm* this section implements Article 34 of the *Capital Adequacy Directive* so far as that Article applies Article 123 of the *Banking*~~

~~*Consolidation Directive*.~~ [deleted]

…

Outline of other related provisions

…

1.2.21 G (1) *SYSC* 11 sets out material on systems and controls that apply specifically to *liquidity risk* as that concept relates to an *insurer*.

(2) [deleted]

(2A) ~~*BIPRU* 12 sets out material on systems and controls that apply specifically to *liquidity risk* in relation to a *BIPRU firm*, a *branch* of an *incoming EEA firm* that is a *full BCD credit institution* and a *branch* of a *third country BIPRU firm* that is a *bank*.~~ [deleted]

(3) [deleted]

…

1.2.22 G ~~*BIPRU* 2.3 contains *rules* and *guidance* on interest rate risk in the *non-trading book*. That material elaborates on the general obligation in the *overall Pillar 2 rule*.~~ [deleted]

1.2.23 G ~~For a *BIPRU firm* using a *VaR model BIPRU 7.10.72R* (Risk management standards: Stress testing) sets out certain stress tests that the *firm* should carry out.~~ [deleted]

1.2.24 G ~~*BIPRU 10.2.22R* (Stress testing of credit risk concentrations) sets out further stress tests that a *firm* should carry out if it uses certain approaches to collateral for the purposes of the *rules* about *large exposures*.~~ [deleted]

1.2.25 G ~~For a *BIPRU firm* using the *IRB approach BIPRU 4.3.39R* to *BIPRU 4.3.40R* set out a recession credit rating migration stress test that the *firm* should carry out. Further *rules* and *guidance* on such stress tests are set out in *BIPRU 2.2* (Internal capital adequacy standards).~~ [deleted]

Requirement to have adequate financial resources

…

1.2.26A G ~~*BIPRU 12* contains *rules* and *guidance* in relation to the adequacy of a *BIPRU firm's* liquidity resources. Consistent with *GENPRU 1.2.2AR*, in assessing the adequacy of its liquidity resources, a *BIPRU firm* should do so by reference to the *overall liquidity adequacy rule*, rather than the *overall financial adequacy rule*.~~ [deleted]

…

Systems, strategies, processes and reviews

…

1.2.33 R …

(2) ~~In the case of a *BIPRU firm* the processes, strategies and systems relating to concentration risk must include those necessary to ensure~~

~~compliance with *BIPRU 10* (*Large exposures* requirements).~~ [deleted]

…

…

Application of this section on a solo and consolidated basis: Processes and tests

…

1.2.46 R ~~The *ICAAP rules* do not apply on a solo basis to a *BIPRU firm* to which the *ICAAP rules*:~~

~~(1) apply on a consolidated basis under *BIPRU 8.2.1R* (Basic consolidation *rule* for a *UK consolidation group*); or~~

~~(2) apply on a sub-consolidated basis under *BIPRU 8.3.1R* (Basic consolidation *rule* for a non-*EEA sub-group*).~~ [deleted]

1.2.47 R ~~The *ICAAP rules* apply on a solo basis:~~

~~(1) to an *insurer* to which those *rules* do not apply on a consolidated basis under *GENPRU 1.2.45R*;~~

~~(2) to a *BIPRU firm* to which those *rules* do not apply on a consolidated or sub-consolidated basis as referred to in *GENPRU 1.2.46R* (including a *BIPRU investment firm* with an *investment firm consolidation waiver*); and~~

~~(3) a *firm* referred to in *GENPRU 1.2.2R* (Application of this section to certain non-*EEA firms*).~~ [deleted]

1.2.47A R The *ICAAP rules* apply on a solo basis to an *insurer* to which those *rules* do not apply on a consolidated basis under *GENPRU 1.2.45R*.

…

Capital planning

…

1.2.78 G Additional *guidance* in relation to stress tests and scenario analysis for *liquidity risk* as that concept relates to an *insurer* is available in *SYSC 11* (Liquidity risk systems and controls). ~~*BIPRU 12* sets out the main *Handbook* provisions in relation to *liquidity risk* for a *BIPRU firm*.~~

…

1.3 Valuation

Application

1.3.1 R ~~(1) This section of the *Handbook* applies to an *insurer*, unless it is:~~

~~(a) *non-directive friendly society*;~~

~~(b) an *incoming EEA firm*; or~~

~~(c)~~ ~~an *incoming Treaty firm*.~~

~~(2)~~ ~~This section of the *Handbook* applies to a *BIPRU firm*.~~

~~(3)~~ ~~This section of the *Handbook* applies to a *UK ISPV*.~~ [deleted]

1.3.1A R (1) This section of the *Handbook* also applies to an *insurer*, unless it is:

(a) a *non-directive friendly society*;

(b) an *incoming EEA firm*; or

(c) an *incoming Treaty firm*.

(2) This section of the *Handbook* also applies to a *UK ISPV*.

Purpose

…

1.3.3 G (1) In the case of a *BIPRU firm*, this section implements ~~Article 74 of the *Banking Consolidation Directive*,~~ Articles 64(4) and 64(5) of the *Banking Consolidation Directive* (Own funds) and Article 33 and Part B of Annex VII of the *Capital Adequacy Directive*.

…

General requirements: Accounting principles to be applied

1.3.4 R Subject to *GENPRU 1.3.9R* to *GENPRU 1.3.10R* and *GENPRU 1.3.36R*, except where a *rule* in *GENPRU*, *BIPRU* or *INSPRU* provides for a different method of recognition or valuation, whenever a *rule* in *GENPRU*, *BIPRU* or *INSPRU* refers to an asset, liability, *exposure*, equity or income statement item, a *firm* must, for the purpose of that *rule*, recognise the asset, liability, *exposure*, equity or income statement item and measure its value in accordance with whichever of the following are applicable:

…

(4) ~~the Building Societies (Accounts and Related Provisions) Regulation 1998;~~ [deleted]

…

General requirements: Valuation adjustments or, in the case of an insurer or a UK ISPV, valuation adjustments or reserves

…

1.3.35 G Reconciliation differences under *GENPRU 1.3.34R* should not be reflected in the valuations under *GENPRU 1.3* but should be disclosed to the *appropriate regulator* in prudential returns. *Firms* which are subject to the reporting requirement under *SUP 16.16* should disclose those reconciliation differences in the Present Valuation Return which they are required to submit to the appropriate regulator under *SUP 16.16.4R*.

1.3.35A G ~~*UK banks* and *BIPRU 730k firms* are reminded that they may, in respect of their prudent valuation assessments under *GENPRU 1.3.4R* and *GENPRU 1.3.14R* to *GENPRU 1.3.34R*, be subject to the requirement under *SUP*~~

~~*16.16.4R* to submit a Prudent Valuation Return to the *appropriate regulator*.~~ [deleted]

Specific requirements: BIPRU firms

1.3.36 R ~~Adjustments to accounting values~~

~~(1)~~ ~~For the purposes of *GENPRU* and *BIPRU*, the adjustments in (2) and (3) apply to values calculated pursuant to *GENPRU 1.3.4R* in addition to those required by *GENPRU 1.3.9R* to *GENPRU 1.3.10R*.~~

~~(2)~~ ~~A *BIPRU firm* must not recognise either:~~

~~(a)~~ ~~the fair value reserves related to gains or losses on cash flow hedges of financial instruments measured at amortised cost; or~~

~~(b)~~ ~~any unrealised gains or losses on debt instruments held, or formerly held, in the available-for-sale category.~~

~~(3)~~ ~~A *BIPRU investment firm* must deduct any asset in respect of deferred acquisition costs and add back in any liability in respect of deferred income (but exclude from the deduction or addition any asset or liability which will give rise to future cash flows), together with any associated deferred tax.~~

~~(4)~~ ~~The items referred to in (2) and (3) must be excluded from *capital resources*.~~ [deleted]

1.3.37 G ~~Provisions for equity instruments held in the available-for-sale category can be found in *GENPRU 2.2.185R*.~~ [deleted]

Trading book and other fair-valued positions, and revaluations

1.3.38 R ~~*GENPRU 1.3.39R* to *GENPRU 1.3.40R* apply only to a *BIPRU firm*.~~ [deleted]

1.3.39 R ~~Both *trading book* positions and other fair-valued positionsare subject to prudent valuation rules as specified in *GENPRU 1.3.14 R* to *GENPRU 1.3.34R* (Marking to market, Marking to model, Independent price verification, Valuation adjustments or, in the case of an insurer or a UK ISPV, valuation adjustments or reserves). In accordance with those *rules*, a *firm* must ensure that the value applied to each of its *trading book* positions and other fair-valued positions appropriately reflects the current market value. This value must contain an appropriate degree of certainty having regard to the dynamic nature of *trading book* positions, the demands of prudential soundness and the mode of operation and purpose of capital requirements in respect of *trading book* positions and other fair-valued positions.~~ [deleted]

1.3.40 R ~~*Trading book* positions must be re-valued at least daily.~~ [deleted]

…

Capital

2.1 Calculation of capital resources requirements

Application

2.1.1 R ~~This section applies to:~~

~~(1) a *BIPRU firm*; and~~

~~(2) an *insurer*, unless it is:~~

~~(a) a *non-directive friendly society*; or~~

~~(b) a *Swiss general insurer*; or~~

~~(c) an *EEA-deposit insurer*; or~~

~~(d) an *incoming EEA firm*; or~~

~~(e) an *incoming Treaty firm*.~~ [deleted]

2.1.1A R Except as indicated in *SUP* 2.1.60R, this section applies to an *insurer*, unless it is:

(1) a *non-directive friendly society*; or

(2) a *Swiss general insurer*; or

(3) an *EEA-deposit insurer*; or

(4) an *incoming EEA firm*; or

(5) an *incoming Treaty firm*.

Purpose

…

2.1.8 G ~~(1) This section implements minimum EC standards for the *capital resources* required to be held by an *insurer* undertaking business that falls within the scope of the *Consolidated Life Directive* (2002/83/EC), the *Reinsurance Directive* (2005/68/EC) or the *First Non-Life Directive* (1973/239/EEC) as amended.~~

~~(2) This section also implements provisions of the *Capital Adequacy Directive* and *Banking Consolidation Directive* concerning the level of *capital resources* which a *BIPRU firm* is required to hold. In particular it implements (in part) Articles 9, 10 and 75 of the *Banking Consolidation Directive* and Articles 5, 9, 10 and 18 of the *Capital Adequacy Directive*.~~

~~(3) In the case of a *UCITS investment firm* this section implements (in part) Article 7 of the *UCITS Directive*.~~ [deleted]

2.1.8A G This section implements minimum EC standards for the *capital resources* required to be held by an *insurer* undertaking business that falls within the scope of the *Consolidated Life Directive* (2002/83/EC), the *Reinsurance Directive* (2005/68/EC) or the *First Non-Life Directive* (1973/239/EEC) as amended.

…

Main requirement: BIPRU firms

2.1.40 R ~~A *BIPRU firm* must maintain at all times *capital resources* equal to or in excess of the amount specified in the table in *GENPRU 2.1.45R* (Calculation of the variable capital requirement for a BIPRU firm).~~ [deleted]

2.1.41 R ~~A *BIPRU firm* must maintain at all times *capital resources* equal to or in excess of the *base capital resources requirement* (see the table in *GENPRU 2.1.48R*).~~ [deleted]

2.1.42 R ~~At the time that it first becomes a *bank*, *building society* or *BIPRU investment firm*, a *firm* must hold *initial capital* of not less than the *base capital resources requirement* applicable to that *firm*.~~ [deleted]

2.1.43 G ~~The purpose of the *base capital resources requirement* for a *BIPRU firm* is to act as a minimum capital requirement or floor. It has been written as a separate requirement as there are restrictions in *GENPRU 2.2* (Capital resources) on the types of capital that a *BIPRU firm* may use to meet the *base capital resources requirement* which do not apply to some other parts of the capital requirement calculation. In order to preserve the *base capital resources requirement's* role as a floor rather than an additional requirement, *GENPRU 2.2.60R* allows a *BIPRU firm* to meet the *base capital resources requirement* with capital that is also used to meet the variable capital requirements in *GENPRU 2.1.40 R*.~~ [deleted]

2.1.44 G ~~The *base capital resources requirement* and the variable capital requirement in *GENPRU 2.1.40R* are together called the *capital resources requirement* (*CRR*) in the case of a *BIPRU firm*.~~ [deleted]

Calculation of the variable capital requirement for a BIPRU firm

2.1.45 ~~R~~ ~~Table: Calculation of the variable capital requirement for a BIPRU firm This table belongs to *GENPRU 2.1.40R*~~

~~*Firm* category~~	~~Capital requirement~~	
~~*Bank*, *building society* or *full scope BIPRU investment firm*~~	~~the sum of the following:~~	
	~~(1)~~	~~the *credit risk capital requirement*;~~
	~~(2)~~	~~the *market risk capital requirement*; and~~
	~~(3)~~	~~the *operational risk capital requirement*.~~
~~*BIPRU limited activity firm*~~	~~the sum of the following:~~	
	~~(1)~~	~~the *credit risk capital requirement*;~~
	~~(2)~~	~~the *market risk capital requirement*; and~~
	~~(3)~~	~~the *fixed overheads requirement*.~~

~~*BIPRU limited licence firm* (including *UCITS investment firm*)~~	~~the higher of (1) and (2):~~		
	~~(1)~~	~~the sum of:~~	
	-	~~(a)~~	~~the *credit risk capital requirement*; and~~
	-	~~(b)~~	~~the *market risk capital requirement*; and~~
	~~(2)~~	~~the *fixed overheads requirement*.~~	

[deleted]

…

Calculation of the base capital resources requirement for a BIPRU firm

2.1.47 R ~~The amount of a *BIPRU firm's base capital resources requirement* is set out in the table in *GENPRU 2.1.48R*.~~ [deleted]

Table: Base capital resources requirement for a BIPRU firm

2.1.48 R

~~This table belongs to *GENPRU 2.1.47R*~~

~~*Firm* category~~	~~Amount: Currency equivalent of~~
~~*Bank*~~	~~€5 million~~
~~*Building society*~~	~~The higher of €1 million and £1 million~~
~~*BIPRU 730K firm*~~	~~€730,000~~
~~*BIPRU 125K firm*~~	~~€125,000~~
~~*BIPRU 50K firm*~~	~~€50,000~~
~~*UCITS investment firm*~~	~~€125,000 plus, if the *funds under management* exceed €250,000,000, 0.02% of the excess, subject to a maximum of €10,000,000.~~

[deleted]

Definition of BIPRU 730K firm, BIPRU 125K firm and BIPRU 50K firm

2.1.49 G ~~The terms *BIPRU 730K firm*, *BIPRU 125K firm* and *BIPRU 50K firm* are defined in *BIPRU 1.1* (Application and purpose). However for convenience the table in *GENPRU 2.1.50G* briefly summarises them.~~ [deleted]

Table: Definition of BIPRU 730K firm, BIPRU 125K firm and BIPRU 50K firm

2.1.50 G ~~This table belongs to *GENPRU 2.1.49G*~~

~~Category of BIPRU investment firm~~			~~Definition~~
~~*BIPRU 50K firm*~~	~~(1)~~		~~it does not deal in any *financial instruments* for its own account or underwrite issues of *financial instruments* on a firm commitment basis;~~
	~~(2)~~		~~it offers one or more of the following services:~~
	-	~~(a)~~	~~reception and transmission of investors' orders for *financial instruments*; or~~
	-	~~(b)~~	~~the execution of investors' orders for *financial instruments*; or~~
	-	~~(c)~~	~~the management of individual portfolios of investments in *financial instruments*; and~~
	~~(3)~~		~~it does not hold clients' money and/or securities and it is not authorised to do so (it should have a *limitation* or *requirement* prohibiting the holding of client money and its *permission* should not include *safeguarding and administering investments*).~~
~~*BIPRU 125K firm*~~	~~(1)~~		~~it does not deal in any *financial instruments* for its own account or underwrite issues of *financial instruments* on a firm commitment basis;~~
	~~(2)~~		~~it offers one or more of the following services:~~
	-	~~(a)~~	~~reception and transmission of investors' orders for *financial instruments*; or~~
	-	~~(b)~~	~~the execution of investors' orders for *financial instruments*; or~~
	-	~~(c)~~	~~the management of individual portfolios of investments in *financial instruments*; and~~
	~~(3)~~		~~it holds clients' money and/or securities or it is authorised to do so.~~
~~*BIPRU 730K firm*~~	~~is subject to the *Capital Adequacy Directive* and is neither a *BIPRU 50K firm* nor a *BIPRU 125K firm*.~~		

[deleted]

Calculation of the credit risk capital requirement (BIPRU firm only)

2.1.51 R ~~A *BIPRU firm* must calculate its *credit risk capital requirement* as the sum of:~~

~~(1) the *credit risk capital component*;~~

~~(2)~~ ~~the *counterparty risk capital component*; and~~

~~(3)~~ ~~the *concentration risk capital component*.~~ [deleted]

Calculation of the market risk capital requirement (BIPRU firm only)

2.1.52 R ~~(1)~~ ~~A *BIPRU firm* must calculate its *market risk capital requirement* as the sum of:~~

~~(a)~~ ~~the *interest rate PRR* (including the basic *interest rate PRR* for equity derivatives set out in *BIPRU 7.3* (Equity PRR and basic interest rate PRR for equity derivatives));~~

~~(b)~~ ~~the *equity PRR*;~~

~~(c)~~ ~~the *commodity PRR*;~~

~~(d)~~ ~~the *foreign currency PRR*;~~

~~(e)~~ ~~the *option PRR*; and~~

~~(f)~~ ~~the *collective investment undertaking PRR*.~~

~~(2)~~ ~~Any amount calculated under *BIPRU 7.1.9R - BIPRU 7.1.13R* (Instruments for which no PRR treatment has been specified) must be allocated between the *PRR* charges in (1) in the most appropriate manner.~~ [deleted]

…

Calculation of base capital resources requirement for banks authorised before 1993

2.1.60 R ~~(1)~~ ~~This *rule* applies to a *bank* that meets the following conditions:~~

~~(a)~~ ~~on 31 December 2006 it had the benefit of IPRU(BANK) rule 3.3.12 (Reduced minimum capital requirement for a *bank* that is a *credit institution* which immediately before 1 January 1993 was authorised under the Banking Act 1987);~~

~~(b)~~ ~~the relevant amount (as referred to in IPRU(BANK) rule 3.3.12) applicable to it was below €5 million as at 31 December 2006; and~~

~~(c)~~ ~~on 1 January 2007 it did not comply with the *base capital resources requirement* as set out in the table in *GENPRU 2.1.48 R* (€5 million requirement).~~

~~(2)~~ ~~Subject to (3), the applicable *base capital resources requirement* as at any time (the "relevant time") is the higher of:~~

~~(a)~~ ~~the relevant amount applicable to it under IPRU(BANK) rule 3.3.12 as at 31 December 2006 as adjusted under *GENPRU 2.1.62 R (2)*; and~~

~~(b)~~ ~~the highest amount of eligible *capital resources* which that *bank* has held between 1 January 2007 and the relevant time.~~

~~(3)~~ ~~This *rule* ceases to apply when:~~

~~(a)~~ ~~that *bank's* eligible *capital resources* at any time since 1 January 2007 equal or exceed €5 million; or~~

~~(b)~~ ~~a *person* (other than an existing controller) becomes the *parent undertaking* of that *bank*.~~

~~(4)~~ ~~If this *rule* ceases to apply under (3)(a) it continues not to apply if the *bank's* eligible *capital resources* later fall below €5 million.~~ [deleted]

2.1.61 G ~~Where two or more *banks* merge, all of which individually have the benefit of *GENPRU 2.1.60 R*, the *PRA* may agree in certain circumstances that the *base capital resources requirement* for the *bank* resulting from the merger may be the sum of the aggregate *capital resources* of the merged *banks*, calculated at the time of the merger, provided this figure is less than €5 million.~~ [deleted]

2.1.62 R ~~For the purpose of *GENPRU 2.1.60 R*:~~

~~(1)~~ ~~an existing controller of a *bank* means:~~

~~(a)~~ ~~a *person* who has been a *parent undertaking* of that *bank* since 31 December 2006 or earlier; or~~

~~(b)~~ ~~a *person* who became a *parent undertaking* of that *bank* after 31 December 2006 but who, when he became a *parent undertaking* of that *bank*, was a *subsidiary undertaking* of an existing controller of that *bank*;~~

~~(2)~~ ~~the relevant amount of capital as referred to in *GENPRU 2.1.60 R (2)(a)* is adjusted by identifying the time as of which the amount of capital it was obliged to hold under IPRU(BANK) rule 3.3.12 as referred to in *GENPRU 2.1.60 R (2)(a)* was fixed and then recalculating the capital resources it held at that time in accordance with the definition of eligible *capital resources* (as defined in (3)); and~~

~~(3)~~ ~~eligible *capital resources* mean *capital resources* eligible under *GENPRU 2.2* (Capital resources) to be used to meet the *base capital resources requirement*.~~ [deleted]

…

2.2 Capital resources

Application

2.2.1 R ~~This section applies to:~~

~~(1)~~ ~~a *BIPRU firm*; and~~

~~(2)~~ ~~an *insurer* unless it is:~~

~~(a)~~ ~~a *non-directive friendly society*; or~~

~~(b)~~ ~~a *Swiss general insurer*; or~~

~~(c)~~ ~~an *EEA-deposit insurer*; or~~

~~(d)~~ ~~an *incoming EEA firm*; or~~

~~(e) an *incoming Treaty firm*.~~ [deleted]

2.2.1A R This section applies to an *insurer* unless it is:

(1) a *non-directive friendly society*; or

(2) a *Swiss general insurer*; or

(3) an *EEA-deposit insurer*; or

(4) an *incoming EEA firm*; or

(5) an *incoming Treaty firm*.

Purpose

…

2.2.4 G ~~This section also implements minimum EC standards for the composition of *capital resources* required to be held by a *BIPRU firm*. In particular it implements Articles 56 - 61, Articles 63 - 64, Article 66 and Articles 120 - 122 of the *Banking Consolidation Directive* (2006/48/EC) and Articles 12 - 16, Article 17 (in part), Article 22(1)(c) (in part) and paragraphs 13 - 15 of Part B of Annex VII of the *Capital Adequacy Directive* (2006/49/EC).~~ [deleted]

Contents guide

2.2.5 G ~~The table in *GENPRU 2.2.6G* sets out where the main topics in this section can be found.~~ [deleted]

Table: Arrangement of GENPRU 2.2

2.2.6 G ~~This table belongs to *GENPRU 2.2.5G*~~

~~Topic~~	~~Location of text~~
~~Application and purpose of the *rules* in this section~~	~~*GENPRU 2.2.1R* to *GENPRU 2.2.4 G*~~
~~*BIPRU firms* that only have simple types of *capital resources* (*simple capital issuers*)~~	~~*GENPRU 2.2.7G*~~
~~Principles underlying the definition of *capital resources*~~	~~*GENPRU 2.2.8G*~~
~~Which method of calculating *capital resources* applies to which type of *firm*~~	~~*GENPRU 2.2.17R* to *GENPRU 2.2.19R*~~
~~Purpose of the limits on the use of different forms of capital~~	~~*GENPRU 2.2.24G*~~
~~Use of higher tier capital in lower tiers~~	~~*GENPRU 2.2.25R* to *GENPRU 2.2.28R*~~
~~Calculation of *capital resources* for~~	~~*GENPRU 2.2.22G* to *GENPRU 2.2.23G*;~~

~~*insurers*~~	~~*GENPRU 2 Annex 1R*~~
~~Limits on the use of different forms of capital for *insurer* (*capital resources gearing rules* for *insurer*)~~	~~*GENPRU 2.2.29R* to *GENPRU 2.2.41R*~~
~~Calculation of *capital resources* for *banks*~~	~~*GENPRU 2 Annex 2R*~~
~~Calculation of *capital resources* for *building societies*~~	~~*GENPRU 2 Annex 3R*~~
~~Limits on the use of different forms of capital for *banks* and *building societies* (certain types of *capital resources* cannot be used for certain purposes)~~	~~*GENPRU 2.2.44R* to *GENPRU 2.2.45R*; *GENPRU 2.2.47R* to *GENPRU 2.2.48R*~~
~~Limits on the use of different forms of capital for *banks* and *building societies* (*capital resources gearing rules*)~~	~~*GENPRU 2.2.29R* to *GENPRU 2.2.31G*; *GENPRU 2.2.46R*; *GENPRU 2.2.49R*~~
~~Calculation of *capital resources* for *BIPRU investment firms*~~	~~*GENPRU 2.2.20G* to *GENPRU 2.2.21G*; *GENPRU 2 Annex 4R* to *GENPRU 2 Annex 6R*~~
~~Limits on the use of different forms of capital for *BIPRU investment firms* (certain types of *capital resources* cannot be used for certain purposes)~~	~~*GENPRU 2.2.44R* to *GENPRU 2.2.45R*; *GENPRU 2.2.47R* to *GENPRU 2.2.48R*~~
~~Limits on the use of different forms of capital for *BIPRU investment firms* (*capital resources gearing rules*)~~	~~*GENPRU 2.2.29R* to *GENPRU 2.2.31G*; *GENPRU 2.2.46R*; *GENPRU 2.2.50R*~~
~~Example of how the *capital resources* calculation for *BIPRU firms* works~~	~~*GENPRU 2.2.51G* to *GENPRU 2.2.59G*~~
~~Capital used to meet the *base capital resources requirement* for *BIPRU firms*~~	~~*GENPRU 2.2.60R* to *GENPRU 2.2.6 G*~~
~~Notification of issuance of *capital instruments*.~~	~~*GENPRU 2.2.61AR* to *GENPRU 2.2.61HG*~~
~~*Tier one capital* instruments: general~~	~~*GENPRU 2.2.9G* to *GENPRU 2.2.10G*; *GENPRU 2.2.62R* to *GENPRU 2.2.69G*; *GENPRU 2.2.80R* to *GENPRU 2.2.82G*~~
~~*Tier one capital*: payment of *coupons* (*BIPRU firm* only)~~	~~*GENPRU 2.2.69AR* to *GENPRU 2.2.69FG*~~
~~*Core tier one capital*: permanent~~	~~*GENPRU 2.2.83R* to *GENPRU*~~

~~*share capital*~~	~~*2.2.84AG*~~
~~General conditions for eligibility of *capital instruments* as *core tier one capital* (*BIPRU firm* only)~~	~~*GENPRU 2.2.83AR* to *GENPRU 2.2.83DG*; *GENPRU 2.2.84AG*~~
~~*Core tier one capital*: exception to eligibility criteria (*building societies* only)~~	~~*GENPRU 2.2.83ER* to *GENPRU 2.2.83HG*~~
~~*Core tier one capital*: profit and loss account and other reserves: material applicable to all *firms*~~	~~*GENPRU 2.2.85R*; *GENPRU 2.2.87 R* to *GENPRU 2.2.89G*; *GENPRU 2.2.91G*~~
~~*Core tier one capital*: profit and loss account and other reserves: material specific to *BIPRU firms*~~	~~*GENPRU 2.2.86R*; *GENPRU 2.2.90 R*; *GENPRU 2.2.92G*~~
~~*Core tier one capital*: provisions relating to partnerships and *limited liability partnerships*~~	~~*GENPRU 2.2.93R* to *GENPRU 2.2.100R*~~
~~*Core tier one capital*: *share* premium account~~	~~*GENPRU 2.2.101R*~~
~~*Core tier one capital*: externally verified interim net profits~~	~~*GENPRU 2.2.102R* to *GENPRU 2.2.103G*~~
~~*Core tier one capital*: valuation differences and fund for future appropriations for *insurer*~~	~~*GENPRU 2.2.104R* to *GENPRU 2.2.108R*~~
~~*Core tier one capital*: *deferred shares* (*building society* only)~~	~~*GENPRU 2.2.108AR* to *GENPRU 2.2.108BG*~~
~~*Tier one capital*: perpetual non-cumulative *preference shares* (*insurer* only)~~	~~*GENPRU* 2.2.109R to *GENPRU* 2.2.110G~~
~~*Innovative tier one capital* (excluding issues through *SPVs*) (*insurer* only)~~	~~*GENPRU* 2.2.76R; *GENPRU 2.2.113R* to *GENPRU 2.2.122G*~~
~~*Hybrid capital* (excluding issues through *SPVs*) (*BIPRU firm* only)~~	~~*GENPRU 2.2.115AR* to *GENPRU* 2.2.119G~~
~~*Hybrid capital* (issues through *SPVs*) (*BIPRU firm* only)~~	~~*GENPRU* 2.2.123R to *GENPRU* 2.2.137R~~
~~*Tier one capital*: conversion ratio~~	~~*GENPRU* 2.2.138R to *GENPRU* 2.2.144G~~
~~*Tier one capital*: requirement to have sufficient unissued stock~~	~~*GENPRU* 2.2.145R~~
~~Deductions from *tier one capital resources*~~	~~*GENPRU* 2.2.155R to *GENPRU 2.2.156G*~~

~~*Tier two capital*~~	~~*GENPRU* 2.2.11G; *GENPRU* 2.2.157G to *GENPRU* 2.2.197G~~
~~Deductions from *tier one capital resources* and *tier two capital resources*~~	~~*GENPRU 2.2.202R* to *GENPRU 2.2.240G*~~
~~*Tier three capital*~~	~~*GENPRU* 2.2.12G; *GENPRU 2.2.241R* to *GENPRU 2.2.249R*~~
~~Deductions from total *capital resources*~~	~~*GENPRU 2.2.14G* to *GENPRU 2.2.16G*; *GENPRU 2.2.250R* to *GENPRU 2.2.265R*~~
~~The effect of swaps~~	~~*GENPRU 2.2.198R* to *GENPRU 2.2.201R*~~
~~*Step-ups* (*Tier one capital* and *tier two capital*)~~	~~*GENPRU 2.2.76R*; *GENPRU 2.2.146R* to *GENPRU 2.2.154G*~~
~~Redemption of *tier one instruments*~~	~~*GENPRU 2.2.64R(3)*; *GENPRU 2.2.70R* to *GENPRU 2.2.79G*~~
~~Purchases of *tier one instruments*: *BIPRU firm* only~~	~~*GENPRU 2.2.79AR* to *GENPRU 2.2.79HG*; *GENPRU 2.2.79LG*~~
~~Redemption of *tier two instruments*~~	~~*GENPRU 2.2.172R* to *GENPRU 2.2.174R*; *GENPRU 2.2.177R* to *GENPRU 2.2.178R* (*upper tier two instruments*); *GENPRU 2.2.194R* to *GENPRU 2.2.197G* (*lower tier two instruments*)~~
~~Non-standard capital instruments~~	~~*GENPRU 2.2.13G*~~
~~Standard form documentation for subordinated debt~~	~~*GENPRU 2.2.164G*~~
~~Public sector guarantees~~	~~*GENPRU 2.2.276R*~~
~~Other capital resources for insurers: unpaid *share* capital or *unpaid initial funds* and calls for supplementary contributions~~	~~*GENPRU 2.2.266G* to *GENPRU 2.2.269G*~~
~~Additional requirements for *insurer* carrying on *with-profits insurance business*~~	~~*GENPRU 2.2.270R* to *GENPRU 2.2.275G*~~

[deleted]

Simple capital issuers

2.2.7 G ~~Parts of this section are irrelevant to a *BIPRU firm* whose *capital resources* consist of straightforward *capital instruments*.~~ [deleted]

…

Deductions from capital

2.2.14 G Deductions should be made at the relevant stage of the calculation of *capital resources* to reflect capital that may not be available to the *firm* or assets of uncertain value (for example, holdings of intangible assets and assets that are inadmissible for an *insurer*)~~)~~.~~, or, in the case of a *bank* or *building society*, where that *firm* has made investments in a *subsidiary undertaking* or in another *financial institution* or in respect of *participations* that it holds).~~

2.2.15 G ~~Deductions should also be made, in the case of certain *BIPRU investment firms* for *illiquid assets* (see *GENPRU 2.2.19R*).~~ [deleted]

…

Which method of calculating capital resources applies to which type of firm

2.2.17 R ~~A *firm* must calculate its *capital resources* in accordance with the version of the *capital resources table* applicable to the *firm*, subject to the *capital resources gearing rules*. The version of the *capital resources table* that applies to a *firm* is specified in the table in *GENPRU 2.2.19R*.~~ [deleted]

2.2.18 ~~R~~ ~~In the case of a *BIPRU firm* the *capital resources table* also sets out how the *capital resources requirement* is deducted from *capital resources* in order to decide whether its *capital resources* equal or exceed its *capital resources requirement*.~~ [deleted]

Table: Applicable capital resources calculation

2.2.19 R ~~This table belongs to *GENPRU 2.2.17R*~~

~~Type of *firm*~~	~~Location of *rules*~~	~~Remarks~~
~~*Insurer*~~	~~*GENPRU 2 Annex 1R*~~	~~-~~
~~*Bank*~~	~~*GENPRU 2 Annex 2R*~~	~~-~~
~~*Building society*~~	~~*GENPRU 2 Annex 3R*~~	~~-~~
~~*BIPRU investment firm* without an *investment firm consolidation waiver*~~	~~*GENPRU 2 Annex 4 R* (Deducts *material holdings*)~~	~~Applies to a *BIPRU investment firm* not using *GENPRU 2 Annex 5 R* or *GENPRU 2 Annex 6 R*~~
~~*BIPRU investment firm* without an *investment firm consolidation waiver*~~	~~*GENPRU 2 Annex 5 R* (Deducts *illiquid assets*)~~	~~A *BIPRU investment firm* must give one *Month's* prior notice to the *appropriate regulator* before starting to use or stopping using this method~~
~~*BIPRU investment firm* with an *investment firm consolidation*~~	~~*GENPRU 2 Annex 6 R* (Deducts *illiquid assets* and~~	~~A *firm* with an *investment firm consolidation waiver* must use this method. No other *BIPRU*~~

~~*waiver*~~	~~*material holdings*)~~	~~*investment firm* may use it.~~

Calculation of capital resources: Which rules apply to BIPRU investment firms

2.2.20 G ~~*GENPRU 2.2.19R* sets out three different methods of calculating *capital resources* for *BIPRU investment firms*. The differences between the three methods relate to whether and how *material holdings* and *illiquid assets* are deducted when calculating *capital resources*. The method depends on whether a *firm* has an *investment firm consolidation waiver*. If a *firm* does have such a *waiver*, it should deduct *illiquid assets*, own *group material holdings* and certain contingent liabilities. If a *firm* does not have such a *waiver*, it should choose to deduct either *material holdings* or, subject to notifying the *appropriate regulator*, *illiquid assets*.~~ [deleted]

2.2.21 G ~~A consequence of a *firm* deducting all of its *illiquid assets* under *GENPRU 2 Annex 5 R* is that it is allowed a higher limit on short term subordinated debt under *GENPRU 2.2.49R*.~~ [deleted]

Calculation of capital resources: Insurers

2.2.22 G *Capital resources* for an *insurer* can be calculated either as the total of eligible assets less foreseeable liabilities (which is the approach taken in the *Insurance Directives*) or by identifying the components of capital. Both calculations give the same result for the total amount of *capital resources*. The approach taken in this section has been to specify the components of capital and the relevant deductions. This is set out in the *capital resources table*. ~~This approach is the same as that used for the calculation of *capital resources* for *banks*, *building societies* and *BIPRU investment firms*.~~ A simple example, showing the reconciliation of the two methods, is given in the table in *GENPRU 2.2.23G*.

…

2.2.28 R ~~In the case of a *BIPRU firm*, the requirement to obtain a legal opinion in *GENPRU 2.2.159R(12)* does not apply to *hybrid capital* treated under *GENPRU 2.2.25R* but the requirements to obtain a legal opinion in *GENPRU 2.2.118R* continue to apply.~~ [deleted]

…

Limits on the use of different forms of capital: Limits relating to tier one capital applicable to BIPRU firms

2.2.30A R ~~In relation to the *tier one capital resources* of a *BIPRU firm*, calculated at stage F of the calculation in the *capital resources table* (Total tier one capital after deductions):~~

~~(1)~~ ~~no more than 50% may be accounted for by *hybrid capital*;~~

~~(2)~~ ~~no more than 35% may be accounted for by *hybrid capital* included at stages B2 and C of the calculation in the *capital resources table*; and~~

~~(3)~~ ~~no more than 15% may be accounted for by *hybrid capital* included at stage C of the calculation in the *capital resources table*.~~ [deleted]

…

Limits on the use of different kinds of capital: Purposes for which tier three capital may not be used (BIPRU firm only)

2.2.44 R ~~*Tier one capital* and *tier two capital* are the only type of *capital resources* that a *BIPRU firm* may use for the purpose of meeting:~~

~~(1)~~ ~~the *credit risk capital component*;~~

~~(2)~~ ~~the *operational risk capital requirement*;~~

~~(3)~~ ~~the *counterparty risk capital component*; and~~

~~(4)~~ ~~the *base capital resources requirement*.~~ [deleted]

2.2.45 R ~~*GENPRU 2.2.44R* (and the *capital resources gearing rules* that relate to it) also applies for the purposes of any other requirement in the *Handbook* for which it is necessary to calculate the *capital resources* of a *BIPRU firm*, except for the purposes described in *GENPRU 2.2.47R* and except as may otherwise be stated in the relevant part of the *Handbook*.~~ [deleted]

Limits on the use of different kinds of capital: Tier two limits (BIPRU firm only)

2.2.46 R ~~For the purpose of *GENPRU 2.2.44R*:~~

~~(1)~~ ~~the amount of the items which may be included in a *BIPRU firm's tier two capital resources* must not exceed the amount calculated at stage F of the calculation in the *capital resources table* (Total tier one capital after deductions); and~~

~~(2)~~ ~~the amount of the items which may be included in a *BIPRU firm's lower tier two capital resources* must not exceed 50% of the amount calculated at stage F of the calculation in the *capital resources table*.~~ [deleted]

Limits on the use of different kinds of capital: Purposes for which tier three capital may be used (BIPRU firm only)

2.2.47 R ~~For the purposes of meeting:~~

~~(1)~~ ~~the *market risk capital requirement*;~~

~~(2)~~ ~~the *concentration risk capital component*; and~~

~~(3)~~ ~~the *fixed overheads requirement* (where applicable);~~

~~a *BIPRU firm* may only use the following parts of its *capital resources*:~~

~~(4)~~ ~~*tier one capital* to the extent that it is not required to meet the requirements in *GENPRU 2.2.44R* (*GENPRU 2.2.48R* explains how to calculate how much *tier one capital* is required to meet the requirements in *GENPRU 2.2.44R*);~~

~~(5)~~ ~~*tier two capital* to the extent that it:~~

~~(a)~~ ~~comes within the limits in *GENPRU 2.2.46R* (100% limit for *tier two capital resources* and 50% limit for *lower tier two capital resources*); and~~

~~(b)~~ ~~it is not required to meet the requirements in *GENPRU 2.2.44R*;(*GENPRU 2.2.48R* explains how to calculate how much *tier two capital* is required to meet the requirements in *GENPRU 2.2.44R*);~~

~~(6) *tier two capital* that cannot be used for the purposes in *GENPRU 2.2.44R* because it falls outside the limits in *GENPRU 2.2.46R*; and~~

~~(7) *tier three capital*.~~ [deleted]

2.2.48 R ~~The amount of *tier one capital* and *tier two capital* that is not used to meet the requirements in *GENPRU 2.2.44R* as referred to in *GENPRU 2.2.47R (4)* and *(5)*(5) is equal to the amount calculated at stage N of the calculation in the *capital resources table* (Total tier one capital plus tier two capital after deductions) less the parts of the *capital resources requirement* deducted immediately after stage N of the *capital resources table* (the parts of the *capital resources requirements* listed in *GENPRU 2.2.44 R*).~~ [deleted]

Limits on the use of different kinds of capital: Combined tier two and tier three limits (BIPRU firm only)

2.2.49 R ~~For the purpose of meeting the requirements in *GENPRU 2.2.47R(1)* to *GENPRU 2.2.47R(3)* and subject to *GENPRU 2.2.50R*, a *BIPRU firm* must not include any item in either:~~

~~(1) its *tier two capital resources* falling within *GENPRU 2.2.47R (6)* (excess *tier two capital*); or~~

~~(2) its *upper tier three capital resources*;~~

~~to the extent that the sum of (1) and (2) would exceed 250% of the amount resulting from the following calculation:~~

~~(3) calculate the amount at stage F of the calculation in the *capital resources table* (Total tier one capital after deductions); and~~

~~(4) deduct from (3) those parts of the *firm's tier one capital* used to meet the requirements in *GENPRU 2.2.44R(1)* and *(2)* as established by *GENPRU 2.2.48R*.~~ [deleted]

2.2.50 R ~~In relation to a *BIPRU investment firm* which calculates its *capital resources* under *GENPRU 2 Annex 4 R* (Capital resources table for a BIPRU investment firm deducting material holdings), the figure of 200% replaces that of 250% in *GENPRU 2.2.49R*.~~ [deleted]

Example of how the capital resources calculation for BIPRU firms works

2.2.51 G ~~*GENPRU 2.2.52G* to *GENPRU 2.2.59G* illustrate how to calculate a *BIPRU firm's capital resources* and how the *capital resources gearing rules* work. In this example the *BIPRU firm* has a combined credit, operational and counterparty risk requirement of £100 (of which £10 is due to counterparty risk) and a market risk requirement of £90, making a total capital requirement of £190. Its *capital resources* are as set out in the table in *GENPRU 2.2.52G*.~~ [deleted]

Table: Example of the calculation of the capital resources of a BIPRU firm

2.2.52 G ~~This table belongs to *GENPRU 2.2.51G*~~

~~Description of the stage of the capital resources calculation~~	~~Stage in the *capital resources table*~~	~~Amount (£)~~

~~Total *tier one capital* after deductions~~	~~Stage F~~	~~80~~
~~Total *tier two capital*~~	~~Stage K~~	~~80~~
~~Deductions~~	~~Stage M~~	~~(20)~~
~~Total *tier one capital* and *tier two capital* after deductions~~	~~Stage N~~	~~140~~
~~*Upper tier three capital* (this example assumes the *firm* has no *lower tier three capital* (*trading book* profits))~~	~~Stage Q~~	~~50~~
~~Total *capital resources*~~	~~Stage T~~	~~190~~

[deleted]

…

2.2.54 G ~~In the example in the table in *GENPRU 2.2.52G* the *firm* has total *tier one capital* after deductions of £80. Its *tier two capital* of £80 is therefore the maximum permitted under *GENPRU 2.2.46R* (Tier two limits), that is 100% of *tier one capital*.~~ [deleted]

2.2.55 G ~~The combined credit, operational and counterparty risk capital requirement is deducted after stage N of the *capital resources table* and the market risk requirement following stage T of the *capital resources table*. These calculations are shown in the table in *GENPRU 2.2.56G*.~~ [deleted]

Table: Example of how capital resources of a BIPRU firm are measured against its capital resources requirement

2.2.56 G ~~This table belongs to *GENPRU 2.2.55G*~~

~~Description of the stage of the capital resources calculation~~	~~Stage in the *capital resources table*~~	~~Amount (£)~~
~~Total *tier one capital* and *tier two capital* after deductions~~	~~Stage N~~	~~140~~
~~Credit, operational and counterparty risk requirement~~	~~-~~	~~(100)~~
~~*Tier one capital* and *tier two capital* available to meet market risk requirement~~	~~-~~	~~40~~
~~*Tier three capital*~~	~~Stage Q~~	~~50~~
~~Total capital available to meet market risk requirement~~	~~-~~	~~90~~
~~Market risk requirement~~	~~-~~	~~(90)~~
~~Market risk requirement met subject to meeting gearing limit set out in *GENPRU 2.2.49 R* - see~~	~~-~~	~~-~~

~~*GENPRU 2.2.57 G*~~		

[deleted]

2.2.57 G ~~The gearing limit in *GENPRU 2.2.49R* (Combined tier two and tier three limits) requires that the *upper tier three capital* used to meet the market risk requirement does not exceed 250% of the relevant *tier one capital*.~~ [deleted]

2.2.58 G ~~In this example it is assumed that the maximum possible amount of *tier one capital* is carried forward to meet the market risk requirement. There are other options as to the allocation of *tier one capital* and *tier two capital* to the credit, operational and counterparty risk requirement.~~
~~In order to calculate the relevant *tier one capital* for the *upper tier three* gearing limit in accordance with *GENPRU 2.2.49 R* it is first necessary to allocate *tier one capital* and *tier two capital* to the individual credit, operational and counterparty risk requirements. This allocation process underlies the calculation of the overall amount referred to in *GENPRU 2.2.48 R*. The calculation in *GENPRU 2.2.49 R (3)* and *GENPRU 2.2.49 R (4)* then focuses on the *tier one* element of this earlier calculation.~~
~~In this worked example, if it is assumed that the counterparty risk requirement has been met by *tier one capital*, the relevant *tier one capital* for gearing is £50. This is because the deductions of £20 and the credit and operational risk requirements of £90 have been met by *tier two capital* in the first instance. However, the total sum of deductions and credit and operational risk requirements exceed the *tier two capital* amount of £80 by £30. Hence the £80 of *tier one capital* has been reduced by £30 to leave £50.~~
~~In practical terms, the same result is achieved for the relevant *tier one capital* for gearing by taking the amount carried forward to meet market risk of £40 and adding back the £10 in respect of the counterparty risk requirement. Again, there are other options as to the allocation to credit, operational and counterparty risk of the constituent elements of Stage N of the *capital resources table*.~~
~~The outcome of these calculations can be summarised as follows:~~

~~(1) the relevant *tier one capital* for the gearing calculation is £50;~~

~~(2) 250% of the relevant *tier one capital* is £125; and~~

~~(3) the *upper tier three capital* used to meet market risk is £50.~~ [deleted]

2.2.59 G ~~The 250% gearing limit is met as the limit of £125 is greater than the *upper tier three capital* of £50 used in this example.~~ [deleted]

Capital used to meet the base capital resources requirement (BIPRU firm only)

2.2.60 R ~~A *BIPRU firm* may use the *capital resources* used to meet the *base capital resources requirement* to meet any other part of the *capital resources requirement*.~~ [deleted]

2.2.61 G ~~The explanation for *GENPRU 2.2.60R* can be found in *GENPRU 2.1.43G* (Base capital resources requirement). In brief the reason is that the *base capital resources requirement* is not in practice meant to act as an additional capital resources requirement. It is meant to act as a floor to the *capital resources requirement*.~~ [deleted]

…

Guidance on certain of the general conditions for eligibility as tier one capital

…

2.2.68A R ~~A *BIPRU firm* must not include a *capital instrument* in its *tier one capital resources* if:~~

~~(1)~~ ~~the *capital instrument* is affected by a dividend stopper; and~~

~~(2)~~ ~~the dividend stopper operates in a way that hinders recapitalisation.~~ [deleted]

2.2.68B G ~~A dividend stopper prevents the *firm* from paying any *coupon* on more junior or pari passu instruments in a period in which the *firm* omits payments to the holder of the *capital instrument* containing the dividend stopper, and so may hinder the recapitalisation of the *firm* contrary to *GENPRU 2.2.64 R (6)*.~~ [deleted]

…

Tier one capital: payment of coupons (BIPRU firm only)

2.2.69A R ~~A *BIPRU firm* must not make a payment of a *coupon* on an item of *hybrid capital* if the *firm* has no distributable reserves.~~ [deleted]

2.2.69B R ~~A *BIPRU firm* must cancel the payment of a *coupon* on an item of *hybrid capital* if the *BIPRU firm* does not meet its *capital resources requirement* or if the payment of that *coupon* would cause it to breach its *capital resources requirement*.~~ [deleted]

2.2.69C R ~~A *BIPRU firm* must not pay a *coupon* on an item of *hybrid capital* in the form of *core tier one capital* in accordance with *GENPRU*~~ *2.2.64R (4)(b)* ~~unless:~~

~~(1)~~ ~~the *firm* meets its *capital resources requirement*; and~~

~~(2)~~ ~~such a substituted payment preserves the *firm's* financial resources.~~ [deleted]

2.2.69D G ~~The *appropriate regulator* considers that a *BIPRU firm's* financial resources are not preserved under *GENPRU 2.2.69CR(2)* unless, among other things, the conditions of the substituted payment are that:~~

~~(1)~~ ~~there is no decrease in the amount of the *firm's core tier one capital*;~~

~~(2)~~ ~~the deferred *coupon* is satisfied without delay using newly issued *core tier one capital* that has an aggregate fair value no more than the amount of the *coupon*;~~

~~(3)~~ ~~the *firm* is not obliged to find new investors for the newly issued instruments; and~~

~~(4)~~ ~~if the holder of the newly issued instruments subsequently sells the instruments and the sale proceeds are less than the value of the *coupon*, the *firm* is not obliged to issue further new instruments to cover the loss incurred by the holder of the instruments.~~ [deleted]

2.2.69E R ~~A *BIPRU firm* must cancel the payment of a *coupon* if circumstances arise whereby the payment of the *coupon* by newly issued instruments, in accordance with *GENPRU 2.2.64R(4)(b)*, does not comply with the requirements of *GENPRU 2.2.69CR*.~~ [deleted]

2.2.69F G ~~(1)~~ ~~In relation to the cancellation or deferral of the payment of a *coupon* in accordance with *GENPRU 2.2.64R(4)* and *GENPRU 2.2.64R(5)*, *GENPRU 2.2.68A R*, or *GENPRU 2.2.69B R*, the *appropriate regulator* expects that situations where a *coupon* may need to be cancelled or deferred will be resolved through analysis and discussion between the *firm* and the *appropriate regulator*. If the *appropriate regulator* and the *firm* do not agree on the cancellation or deferral of the payment of a *coupon*, then the *appropriate regulator* may consider using its powers under 55J of the *Act* to, on its own initiative, vary a *firm's Part 4A permission* to require it to cancel or defer a *coupon* in accordance with the *appropriate regulator's* view of the financial and solvency situation of the *firm*.~~

~~(2)~~ ~~In considering a *firm's* financial and solvency situation, the *appropriate regulator* will normally take into account, among other things, the following:~~

~~(a)~~ ~~the *firm's* financial and solvency position before and after the payment of the *coupon*, in particular whether that payment, or other foreseeable internal and external events or circumstances, may increase the risk of the *firm* breaching its *capital resources requirement* or the *overall financial adequacy rule*;~~

~~(b)~~ ~~an appropriately stressed capital plan, covering 3-5 years, which includes the effect of the proposed payment of the *coupon*; and~~

~~(c)~~ ~~an evaluation of the risks to which the *firm* is or might be exposed and whether the level of *tier one capital* ensures the coverage of those risks, including stress tests on the main risks showing potential loss under different scenarios.~~

~~(3)~~ ~~If the *BIPRU firm* is required to cancel or defer the payment of a *coupon* by the *appropriate regulator*, it may still be able to pay the *coupon* by way of newly issued *core tier one capital* in accordance with *GENPRU 2.2.64 R (4)(b)* and *GENPRU 2.2.69C R*. The *appropriate regulator* may consider using its powers under 55J of the *Act* to, on its own initiative, vary a *firm's Part 4A permission* to impose conditions on the use of such a mechanism or to require its cancellation, based on the factors outlined in this *guidance*.~~ [deleted]

Redemption of tier one instruments

…

2.2.70A G ~~In the case of a *BIPRU firm*, an incentive to redeem is a feature of a *capital instrument* that would lead a reasonable market participant to have an expectation that the *firm* will redeem the instrument. The *appropriate regulator* considers that interest rate step-ups and principal stock settlements, in conjunction with a call option, are incentives to redeem. Only instruments with moderate incentives to redeem are permitted as *tier one capital*, in accordance with the limited conversion ratio in *GENPRU 2.2.138R* and the *rule* on step-ups in *GENPRU 2.2.147R*.~~ [deleted]

…

2.2.74B R ~~If a *BIPRU firm* does not comply with its *capital resources requirement* or if the redemption of any dated *tier one instrument* would cause it to breach its *capital resources requirement*, it must suspend the redemption of its dated *tier one instruments*.~~ [deleted]

…

Purchases of tier one instruments: BIPRU firm only

2.2.79A R ~~A *BIPRU firm* must not purchase a *tier one instrument* that it has included in its *tier one capital resources* unless:~~

~~(1)~~ ~~the *firm* initiates the purchase;~~

~~(2)~~ ~~[deleted]~~

~~(3)~~ ~~the *firm* has given notice to the *appropriate regulator* in accordance with *GENPRU 2.2.79GR*; and~~

~~(4)~~ ~~(in the case of *hybrid capital*) it is on or after the fifth anniversary of the date of issue of the instrument.~~ [deleted]

2.2.79B G ~~In exceptional circumstances a *BIPRU firm* may apply for a *waiver* of *GENPRU 2.2.79AR(4)* under section 138A (Modification or waiver of rules) of the *Act*.~~ [deleted]

2.2.79C R ~~*GENPRU 2.2.79AR(4)* does not apply if:~~

~~(1)~~ ~~the *firm* replaces the *capital instrument* it intends to purchase with a *capital instrument* that is included in a *higher stage of capital* or the *same stage of capital*; and~~

~~(2)~~ ~~the replacement *capital instrument* has already been issued.~~ [deleted]

2.2.79D R ~~*GENPRU 2.2.79AR(4)* does not apply if:~~

~~(1)~~ ~~the *firm* intends to hold the purchased instrument for a temporary period as *market maker*; and~~

~~(2)~~ ~~the purchased instruments held by the *firm* do not exceed the lower of:~~

~~(a)~~ ~~10% of the relevant issuance; or~~

~~(b)~~ ~~3% of the *firm's* total issued *hybrid capital*.~~ [deleted]

2.2.79E G ~~In the circumstances provided for in *GENPRU 2.2.79DR*, a *firm* would purchase the instrument and, instead of cancelling it, the *firm* would hold the instrument for a temporary period. In that case a *firm* should have in place adequate policies to take into account any relevant regulations and *rules*, which include those relating to market abuse.~~ [deleted]

2.2.79F R ~~For the purposes of calculating its *tier one capital resources*, a *firm* must deduct the amount of any item of *hybrid capital* which it then holds.~~ [deleted]

2.2.79G R ~~A *BIPRU firm* must not purchase a *tier one instrument* in accordance with *GENPRU 2.2.79AR* unless it has notified the *appropriate regulator* of its intention at least one month before it becomes committed to doing so. When giving notice, the *firm* must provide details of its position after the purchase in order to show how, over an appropriate timescale, adequately stressed, and without planned recourse to the capital markets, it will:~~

~~(1)~~ ~~meet its *capital resources requirement*; and~~

(2) ~~have sufficient financial resources to meet the *overall financial adequacy rule*.~~ [deleted]

2.2.79H G ~~The *appropriate regulator* considers that:~~

(1) ~~in order to comply with *GENPRU 2.2.79GR*, the *firm* should, at a minimum, provide the *appropriate regulator* with the following information:~~

(a) ~~a comprehensive explanation of the rationale for the purchase;~~

(b) ~~the *firm's* financial and solvency position before and after the purchase, in particular whether the purchase, or other foreseeable internal and external events or circumstances, may increase the risk of the *firm* breaching its *capital resources requirement* or the *overall financial adequacy rule*;~~

(c) ~~an appropriately stressed capital plan covering 3-5 years, which includes the effect of the proposed purchase; and~~

(d) ~~an evaluation of the risks to which the *firm* is or might be exposed and whether the level of *tier one capital* ensures the coverage of such risks including stress tests on the main risks showing potential loss under different scenarios; and~~

(2) ~~the proposed purchase should not be on the basis that the *firm* reduces capital on the date of the purchase and then plans to raise new external capital during the following 3-5 years to replace the purchased capital.~~ [deleted]

2.2.79I R ~~A *BIPRU firm* must not announce to the holders of a *tier one instrument* its intention to purchase that instrument unless it has notified that intention to the *appropriate regulator* in accordance with *GENPRU 2.2.79GR* and it has not, during the period of one month from the date of giving notice, received an objection from the *appropriate regulator*.~~ [deleted]

2.2.79J R ~~If a *BIPRU firm* announces the purchase of any *tier one instrument*, the *firm* must no longer include that instrument in its *tier one capital resources*.~~ [deleted]

2.2.79K R ~~If a *BIPRU firm* does not comply with its *capital resources requirement*, or if the purchase of any *tier one instrument* would cause it to breach its *capital resources requirement*, it must suspend the purchase of *tier one instruments*.~~ [deleted]

2.2.79L G ~~A *firm* should continue to exclude from its *tier one capital resources* all *tier one instruments* that are the subject of a purchase notification under *GENPRU 2.2.79GR* and for which the offer to purchase has been declined by the instrument holders unless the purchase offer period has expired.~~ [deleted]

Loss absorption

2.2.80 R A *firm* may not include a *share* in its *tier one capital resources* unless (in addition to complying with the other relevant *rules* in *GENPRU 2.2*):

(1) (in the case of a *firm* that is a company as defined in the Companies Act 2006 it is "called-up *share* capital" within the meaning given to that term in that Act; or

(2) ~~(in the case of a *building society*) it is a *deferred share*; or~~ [deleted]

(3) (in the case of any other *firm*) it is:

(a) in economic terms; and

(b) in its characteristics as capital (including loss absorbency, permanency, ranking for repayment and fixed costs);substantially the same as called-up *share* capital falling into (1).

…

Core tier one capital: permanent share capital

2.2.83 R *Permanent share capital* means an item of capital which (in addition to satisfying *GENPRU 2.2.64R*) meets the following conditions:

(1) it is:

(a) an ordinary *share*; or

(b) a *members' contribution*; or

(c) part of the *initial fund* of a *mutual*; or

(d) ~~a *deferred share*;~~ [deleted]

…

General conditions for eligibility of capital instruments as core tier one capital (BIPRU firm only)

2.2.83A R ~~The conditions that a *BIPRU firm's permanent share capital* must comply with under *GENPRU 2.2.83AR(4)* or that a *BIPRU firm's eligible partnership capital* or *eligible LLP members' capital* must comply with under *GENPRU 2.2.95R* are as follows:~~

(1) ~~it is undated;~~

(2) ~~the terms upon which it is issued do not give the holder a preferential right to the payment of a *coupon*;~~

(3) ~~the terms upon which it is issued do not indicate the amount of any *coupon* that may be payable nor impose an upper limit on the amount of any *coupon* that may be payable;~~

(4) ~~the *firm's* obligations under the instrument do not constitute a liability (actual, contingent or prospective) under section 123(2) of the Insolvency Act 1986 and the holder has no right to petition for the winding up or administration of the *firm* or for any similar procedure in relation to the *firm* arising from the non-payment of a *coupon* or any other sums payable under the instrument;~~

(5) ~~there is no contractual or other obligation arising out of the terms upon which it is issued that requires the *firm* to repay capital to the holders other than on a liquidation of the *firm*;~~

(6) ~~the terms upon which it is issued do not include a dividend pusher or a~~

~~dividend stopper;~~

(7) ~~the *firm* is under no obligation to issue *core tier one capital* or to make a payment in kind in lieu of making a *coupon* payment and non-payment of a *coupon* is not an event of default on the part of the *firm*;~~

(8) ~~it is simple and the terms upon which it is issued are clearly defined;~~

(9) ~~it is able to fully and unconditionally absorb losses on a non-discretionary basis as soon as they arise to allow the *firm* to continue trading, and it absorbs losses before all *capital instruments* that are not eligible for inclusion in stage A of the *capital resources table* and equally and proportionately with all *capital instruments* that are eligible for inclusion in stage A of the *capital resources table*;~~

(10) ~~it ranks for repayment on winding up, administration or any other similar process lower than all other items of capital, and on a liquidation of the *firm* the holders have a claim on the residual assets remaining after satisfaction of all prior claims that is proportional to their holding and do not have a priority claim or a fixed claim for the nominal amount of their holding;~~

(11) ~~the *firm* has not provided the holder with a direct or indirect financial contribution specifically to pay for the whole or a part of its subscription or purchase;~~

(12) ~~a reasonable person would not think that the *firm* is likely to redeem or purchase it because of the description of its characteristics used in its marketing and in its contractual terms of issue; and~~

(13) ~~its issue is not connected with one or more other transactions which, when taken together with its issue, could result in it no longer displaying all of the characteristics set out in *GENPRU 2.2.83R (2)*, *GENPRU 2.2.83AR (1)* to *(12)* and (in the case of *permanent share capital*) *GENPRU 2.2.83R (3)*.~~ [deleted]

2.2.83B R ~~A *BIPRU firm* must not include in stage A of the *capital resources table* different classes of the same *share* type (for example "A ordinary shares" and "B ordinary shares") that meet the conditions in *GENPRU 2.2.83R* and *GENPRU 2.2.83AR* but have differences in voting rights, unless it has notified the *appropriate regulator* of its intention at least one month before the *shares* are issued or (in the case of existing issued *shares*) the differences in voting rights take effect.~~ [deleted]

2.2.83C R ~~A *BIPRU firm* must not pay a *coupon* on a *tier one instrument* included in stage A of the *capital resources table* if it has no distributable reserves.~~ [deleted]

2.2.83D G ~~A *BIPRU firm* may disclose its dividend policy, provided that the policy only reflects the current intention of the *firm* and does not undermine the *firm's* right to choose the amount of any *coupon* that it pays.~~ [deleted]

Core tier one capital: exception to eligibility criteria (building societies only)

2.2.83E R ~~A *building society* may include in stage A of the *capital resources table* a *capital instrument* that includes in its terms of issue an upper limit on the amount of any *coupon* that may be payable and the prohibition on a *coupon* limit under *GENPRU 2.2.83AR (3)* does not apply to that *capital instrument*, provided that:~~

(1) ~~the *capital instrument* satisfies all other conditions for eligibility as *core tier one capital* set out in *GENPRU 2.2.83 R* to *GENPRU 2.2.83A R*;~~

(2) ~~the *coupon* limit has been imposed by law or the constitutional documents of the *firm*;~~

(3) ~~the objective of the limit is to protect the capital reserves of the *firm*;~~

(4) ~~the *firm* continues to have the effective right to choose the amount of any *coupon* that it pays;~~

(5) ~~all other *capital instruments* issued by the *firm* and included in stage A of the *capital resources table*:~~

~~(a)~~ ~~meet the conditions set out in *GENPRU 2.2.83 R (2)*, *GENPRU 2.2.83 R (3)* and *GENPRU 2.2.83A R* (General conditions for eligibility of capital instruments as core tier one capital (BIPRU firm only)); and~~

~~(b)~~ ~~if subject to a *coupon* limit, are subject to the same *coupon* limit; and~~

(6) ~~any preferential *coupon* on a *capital instrument* included in stage A of the *capital resources table*, arising as a result of the inclusion of a *coupon* limit on another *capital instrument*, must be restricted to a fixed multiple of the *coupon* payment on the *capital instrument* that is subject to the *coupon* limit. *GENPRU 2.2.83A R (2)* to *(3)* do not prevent a *capital instrument* from being included in stage A of the *capital resources table* if the only reason for those prohibitions not being met is that a preferential *coupon* arises, and is restricted, in the manner referred to in this paragraph (6).~~ [deleted]

2.2.83F R ~~A *building society* must not issue a *capital instrument* that includes a *coupon* limit in its terms of issue in accordance with *GENPRU 2.2.83E R* unless it has notified the *PRA* of its intention to do so at least one month before the intended date of issue.~~ [deleted]

2.2.83G G ~~Under *GENPRU 2.2.83E R (4)*, an effective right means that in practice the *firm* has, and exercises, full discretion to choose the amount of *coupon* that it pays (for example, it has not fettered that discretion by indicating to instrument holders that the *coupon* limit is the standard level of *coupon* they will receive).~~ [deleted]

2.2.83H G ~~The purpose of *GENPRU 2.2.83E R (6)* is to limit the potential preferential rights that may arise on *capital instruments* that are not subject to a *coupon* limit. The *PRA* considers that "preferential" refers to both priority of *coupon* payment and level of *coupon* payment. Therefore the *PRA* considers that:~~

(1) ~~a *coupon* arising on a *capital instrument* which is not subject to an explicit *coupon* limit within its terms of issue is likely to be preferential to a coupon on a *capital instrument* included in the *same stage of capital* which is subject to a *coupon* limit; and~~

(2) ~~the preference so arising should be restricted so that it is not an unlimited preference.~~ [deleted]

Core tier one capital: additional information

2.2.84 G In the case of an *insurer*, *GENPRU 2.2.83R(2)* and *GENPRU 2.2.83R (3)* have the effect that the *firm* should be under no obligation to make any payment in respect of a *tier one instrument* if it is to form part of its *permanent share capital* unless and until the *firm* is wound up. A *tier one instrument* that forms part of *permanent share capital* should not therefore count as a liability before the *firm* is wound up. The fact that relevant company law permits the *firm* to make earlier repayment does not mean that the *tier one instruments* are not eligible. However, the *firm* should not be required by any contractual or other obligation arising out of the terms of that capital to repay *permanent share capital*. Similarly a *tier one instrument* may still qualify if company law allows dividends to be paid on this capital, provided the *firm* is not contractually or otherwise obliged to pay them. There should therefore be no fixed costs. *GENPRU 2.2.83AR* to ~~*GENPRU 2.2.83F R*~~ <u>*GENPRU 2.2.83DG*</u> impose more specific conditions on *coupon* payment and winding up which are applicable to *BIPRU firms*.

…

Core tier one capital: profit and loss account and other reserves: Losses

2.2.85 R ~~(1)~~ ~~Negative amounts, including any interim net losses (but in the case of a *BIPRU investment firm*, only material interim net losses), must be deducted from profit and loss account and other reserves.~~

~~(2)~~ ~~For these purposes material interim net losses mean unaudited interim losses arising from a *firm's trading book* and *non-trading book* business which exceed 10% of the sum of its *capital resources* calculated at stage A (Core tier one capital) in the *capital resources table*.~~

~~(3)~~ ~~If interim losses as referred to in (2) exceed the 10% figure in (2) then a *BIPRU investment firm* must deduct the whole amount of those losses and not just the excess.~~ <u>[deleted]</u>

<u>2.2.85A</u> <u>R</u> <u>(1)</u> <u>Negative amounts, including any interim net losses, must be deducted from profit and loss account and other reserves.</u>

<u>(2)</u> <u>For these purposes material interim net losses mean unaudited interim losses arising from a *firm's trading book* and *non-trading book* business which exceed 10% of the sum of its *capital resources* calculated at stage A (Core tier one capital) in the *capital resources table*.</u>

Core tier one capital: profit and loss account and other reserves: Losses arising from valuation adjustments (BIPRU firm only)

2.2.86 R ~~(1)~~ ~~This *rule* applies to *trading book* valuation adjustments or reserves referred to in *GENPRU 1.3.29R* to *GENPRU 1.3.35AG* (Valuation adjustments and reserves). It applies to a *BIPRU firm*.~~

~~(2)~~ ~~When valuation adjustments or reserves give rise to losses of the current financial year, a *firm* must treat them in accordance with *GENPRU 2.2.85R*.~~

~~(3)~~ ~~Valuation adjustments or reserves which exceed those made under the accounting framework to which a *firm* is subject must be treated in accordance with (2) if they give rise to losses and under *GENPRU 2.2.248R* (Net interim *trading book* profits) otherwise.~~ <u>[deleted]</u>

…

Core tier one capital: profit and loss account and other reserves: Securitisation

(BIPRU firm only)

2.2.90 R ~~In the case of a *BIPRU firm* which is the *originator* of a *securitisation*, net gains arising from the capitalisation of future income from the *securitised* assets and providing *credit enhancement* to *positions* in the *securitisation* must be excluded from profit and loss account and other reserves.~~ [deleted]

…

Core tier one capital: profit and loss account and other reserves: Revaluation reserves (BIPRU firm only)

2.2.92 G ~~A revaluation reserve is not included as part of a *BIPRU firm's* profit and loss account and other reserves. It is dealt with separately and forms part of a *BIPRU firm's upper tier two capital*.~~ [deleted]

Core tier one capital: partnership capital account (BIPRU firm only)

2.2.93 R ~~*Eligible partnership capital* means a partners' account:~~

~~(1)~~ ~~into which capital contributed by the partners is paid; and~~

~~(2)~~ ~~from which under the terms of the partnership agreement an amount representing capital may be withdrawn by a partner only if:~~

~~(a)~~ ~~he ceases to be a partner and an equal amount is transferred to another such account by his former partners or any *person* replacing him as their partner;~~

~~(b)~~ ~~the partnership is wound up or otherwise dissolved; or~~

~~(c)~~ ~~the *BIPRU firm* has ceased to be *authorised* or no longer has a *Part 4A permission*.~~ [deleted]

Core tier one capital: Eligible LLP members' capital (BIPRU firm only)

2.2.94 R ~~*Eligible LLP members' capital* means a members' account:~~

~~(1)~~ ~~into which capital contributed by the members is paid; and~~

~~(2)~~ ~~from which under the terms of the *limited liability partnership* agreement an amount representing capital may be withdrawn by a member only if:~~

~~(a)~~ ~~he ceases to be a member and an equal amount is transferred to another such account by his former fellow members or any *person* replacing him as a member;~~

~~(b)~~ ~~the *limited liability partnership* is wound up or otherwise dissolved; or~~

~~(c)~~ ~~the *BIPRU firm* has ceased to be *authorised* or no longer has a *Part 4A permission*.~~ [deleted]

Core tier one capital: Eligible LLP members' and partnership capital accounts (BIPRU firm only)

2.2.95 R ~~A *BIPRU firm* that is a partnership or a *limited liability partnership* may not include *eligible partnership capital* or *eligible LLP members' capital* in its *tier one capital resources* unless (in addition to *GENPRU 2.2.62 R* (General~~

~~conditions relating to *tier one capital*)) it complies with *GENPRU 2.2.83 R (2)* (Coupons should not be cumulative or mandatory) and *GENPRU 2.2.83A R* to *GENPRU 2.2.83C R* (General conditions for eligibility of capital instruments as core tier one capital (BIPRU firm only). However, *GENPRU 2.2.64 R (3)* (Redemption), *GENPRU 2.2.83A R (5)* (Capital repayment) and *GENPRU 2.2.83A R (12)* (Characteristics in contract) are replaced by *GENPRU 2.2.93 R* or *GENPRU 2.2.94 R*.~~ [deleted]

2.2.96 G ~~If a *firm* has surplus *eligible partnership capital* or *eligible LLP members' capital* that it wishes to repay in circumstances other than those set out in *GENPRU 2.2.93 R* or *GENPRU 2.2.94 R* it may apply to the *appropriate regulator* for a *waiver* to allow it to do so. If a *firm* applies for such a *waiver* the information that the *firm* supplies with the application might include:~~

~~(1) a demonstration that the *firm* would have sufficient *capital resources* to meet its *capital resources requirement* immediately after the repayment;~~

~~(2) a demonstration that the *firm* would have sufficient financial resources to meet any *individual capital guidance* and the *firm's* latest assessment under the *overall Pillar 2 rule* immediately after the repayment; and~~

~~(3) a two to three year capital plan demonstrating that the *firm* would be able to meet the requirements in (1) and (2) at all times without needing further capital injections.~~ [deleted]

Core tier one capital: Other capital items for limited liability partnerships and partnerships (BIPRU firm only)

2.2.97 R ~~The items *permanent share capital* and *share* premium account (which form part of *core tier one capital*) do not apply to a *BIPRU firm* that is a partnership or a *limited liability partnership*.~~ [deleted]

2.2.98 R ~~Without prejudice to *GENPRU 2.2.62 R* (Tier one capital: General), the item other reserves (which forms part of the item profit and loss and other reserves) applies to a *BIPRU firm* that is a partnership or a *limited liability partnership* to the extent the reserves correspond to reserves that are eligible for inclusion as other reserves in the case of a *BIPRU firm* that is incorporated under the Companies Act 2006.~~ [deleted]

2.2.99 G ~~A *BIPRU firm* that is a partnership or a *limited liability partnership* should include profit and loss (taking into account interim losses or material interim net losses) in its *core tier one capital*.~~ [deleted]

Core tier one capital: partnership and limited liability partnership excess drawings (BIPRU firm only)

2.2.100 R ~~A *BIPRU firm* which is a partnership or *limited liability partnership* must deduct at stage E of the calculation in the *capital resources table* (Deductions from tier one capital) the amount by which the aggregate of the amounts withdrawn by its partners or members exceeds the profits of that *firm*. Amounts of *eligible partnership capital* or *eligible LLP members' capital* repaid in accordance with *GENPRU 2.2.93 R* or *GENPRU 2.2.94 R* are not included in this calculation.~~ [deleted]

…

Core tier one capital: deferred shares (building society only)

2.2.108A R ~~A *building society* may include a *deferred share* at stage A of the calculation in the *capital resources table* if (in addition to satisfying all the other requirements~~

~~in relation to *tier one capital*) it is *permanent share capital* and is otherwise equivalent to an ordinary *share* in terms of its capital qualities, taking into account the specific constitution of *building societies* under the Building Societies Act 1986.~~ [deleted]

2.2.108B G ~~The other main provisions relevant to inclusion of a *deferred share* in *tier one capital* are *GENPRU 2.2.62 R* (Tier one capital: General), *GENPRU 2.2.64 R* (General conditions for eligibility as tier one capital), *GENPRU 2.2.65 R* (Connected transactions) and *GENPRU 2.2.80 R* (Loss absorption).~~ [deleted]

…

Other tier one capital: conditions for eligibility for hybrid capital to be included at the different stages B1, B2 and C of the calculation in the capital resources table (BIPRU firm only)

2.2.115A R ~~A *BIPRU firm* must not include a *capital instrument* at stage B1 of the calculation in the *capital resources table* unless (in addition to satisfying all the other requirements in relation to *tier one capital* and *hybrid capital*) its contractual terms are such that:~~

~~(1) it cannot be redeemed in cash but can only be converted into *core tier one capital*;~~

~~(2) it must be converted into *core tier one capital* by the *firm* during emergency situations;~~

~~(3) the emergency situations referred to in (2):~~

~~(a) are clearly defined within the terms of the *capital instrument*, legally certain and transparent; and~~

~~(b) occur at the latest, and include, when the *BIPRU firm* does not meet its *capital resources requirement*;~~

~~(4) the *appropriate regulator* may require its conversion into *core tier one capital* when the appropriate regulator considers it necessary;~~

~~(5) it may be converted into *core tier one capital* by the *firm* or the holder of the instrument at any time; and~~

~~(6) the maximum number of *capital instruments* which are *core tier one capital* into which it may be converted must:~~

~~(a) be determined at the date of its issue;~~

~~(b) be determined on the basis of the market value of those other instruments at the date of its issue;~~

~~(c) have an aggregate value equal to its par value; and~~

~~(d) not increase if the price of those other instruments decreases.~~ [deleted]

2.2.115B G ~~The intention of *GENPRU 2.2.115A R* is to ensure that *capital instruments* included in stage B1 of the calculation in the *capital resources table* have the same permanence as *core tier one capital*; the presence of a call option for these instruments may reduce their permanence.~~ [deleted]

2.2.115C G ~~(1)~~ ~~In respect of *GENPRU 2.2.115A R (4)*, the *appropriate regulator* may require the *firm* to convert the instrument into *core tier one capital* based on its financial and solvency situation. The *appropriate regulator* will take into account, among other things, the factors identified at *GENPRU 2.2.69F G (2)*, adjusted to take into account the effects of a conversion rather than payment of a *coupon*.~~

~~(2)~~ ~~Even if a *firm* meets its *capital resources requirement*, the *appropriate regulator* may consider the amount or composition of the *firm's tier one capital* as inadequate to cover the financial and solvency risks of the *firm* in which event the *appropriate regulator* may require the *firm* to convert the instrument into *core tier one capital*.~~ [deleted]

2.2.115D R ~~A *BIPRU firm* may include a *capital instrument* at stage B2 of the calculation in the *capital resources table* if (while satisfying all the other requirements in relation to *tier one capital* and *hybrid capital*)it cannot be included at stage B1 of that calculation as it does not satisfy the requirements of *GENPRU 2.2.115A R*.~~ [deleted]

2.2.115E G ~~(1)~~ ~~The other main provisions relevant to the eligibility of a *capital instrument* to be included at stages B1 and B2 of the calculation in the *capital resources table* are *GENPRU 2.2.62 R* (Tier one capital: General), *GENPRU 2.2.64 R* (General conditions for eligibility as tier one capital), *GENPRU 2.2.65 R* (Connected transactions), *GENPRU 2.2.68A R* (Dividend stoppers), *GENPRU 2.2.70 R* to *GENPRU 2.2.75 R* (Redemption of tier one instruments), *GENPRU 2.2.80 R* (Loss absorption) and *GENPRU 2.2.116 R* to *GENPRU 2.2.118 R* (Other tier one capital: loss absorption).~~

~~(2)~~ ~~The *rule* about *hybrid capital* included at stage C of the calculation in the *capital resources table* in *GENPRU 2.2.115F R* is also relevant. *Capital instruments* that would otherwise qualify for inclusion at stages B1 or B2 of the calculation in the *capital resources table* may only be eligible for inclusion at stage C of that calculation.~~ [deleted]

2.2.115F R ~~A *BIPRU firm* may include a *capital instrument* at stage C of the calculation in the *capital resources table*, and must not include it in stage B1 or B2 of that calculation, if (in addition to satisfying all the other requirements in relation to *tier one capital* and *hybrid capital*) it either:~~

~~(1)~~ ~~is dated; or~~

~~(2)~~ ~~provides an incentive for the *firm* to redeem it, as assessed at the date of its issue.~~ [deleted]

2.2.115G G ~~An incentive to redeem is a feature of a *capital instrument* that would lead a reasonable market participant to have an expectation that the *firm* will redeem the instrument. The effect of *GENPRU 2.2.115F R (2)* is that the classification of an instrument that provides an incentive to redeem is always assessed at the date of its issue, and it cannot be reclassified.~~ [deleted]

Other tier one capital: loss absorption

…

2.2.116A R ~~A *BIPRU firm* must not include a *capital instrument* that is not a *share* at stage B1, B2 or C of the calculation in the *capital resources table* unless (in addition to satisfying all the other requirements in relation to *tier one capital* and *hybrid capital*) the *firm's* obligations under the instrument either:~~

~~(1) do not constitute a liability (actual, contingent or prospective) under section 123(2) of the Insolvency Act 1986; or~~

~~(2) do constitute such a liability but the terms of the instrument are such that:~~

~~(a) any such liability is not relevant for the purposes of deciding whether:~~

~~(i) the *firm* is, or is likely to become, unable to pay its debts; or~~

~~(ii) its liabilities exceed its assets;~~

~~(b) a *person* (including, but not limited to, a holder of the instrument) is not able to petition for the winding up or administration of the *firm* or for any similar procedure in relation to the *firm* on the grounds that the *firm* is or may become unable to pay any such liability; and~~

~~(c) the *firm* is not obliged to take into account such a liability for the purposes of deciding whether or not the *firm* is, or may become, insolvent for the purposes of section 214 of the Insolvency Act 1986 (Wrongful trading).~~ [deleted]

…

2.2.117A R ~~A *BIPRU firm* must not include a *capital instrument* at stage B1, B2 or C of the calculation in the *capital resources table* unless (in addition to satisfying all the other requirements in relation to *tier one capital* and *hybrid capital*) its contractual terms provide for a mechanism within the instrument which:~~

~~(1) is clearly defined and legally certain;~~

~~(2) is disclosed and transparent to the market;~~

~~(3) makes the recapitalisation of the *firm* more likely by adequately reducing the potential future outflows to a holder of the *capital instrument* at certain trigger points;~~

~~(4) enables the *firm*, at and after the trigger points, to operate the mechanism; and~~

~~(5) when initiated, operates in one of the following ways:~~

~~(a) the principal of the instrument is written down permanently; or~~

~~(b) the principal of the instrument is written down temporarily. During the write-down period any *coupon* payable on the instrument must be cancelled and any related dividend stoppers and pushers must operate in a way that does not hinder recapitalisation; or~~

~~(c) the instrument is converted into *core tier one capital*. The maximum number of *capital instruments* which are *core tier one capital* into which it must be converted must;~~

~~(i) be determined at the date of its issue;~~

~~(ii) be determined on the basis of the market value of those other instruments at the date of its issue;~~

(iii) ~~have an aggregate value no more than 150% of its par value; and~~

(iv) ~~not increase if the share price decreases; or~~

(d) ~~an alternative process applies which has the same or greater effect on the likelihood of recapitalisation as (a), (b), and (c).~~ [deleted]

2.2.117B R ~~The trigger points required by *GENPRU 2.2.117A R (3)* must:~~

(1) ~~be clearly defined within the instrument and legally certain;~~

(2) ~~be disclosed and transparent to the market; and~~

(3) ~~be prudent and timely, and include trigger points which occur:~~

(a) ~~before a breach of the *firm's capital resources requirement* and both:~~

(i) ~~when the *firm's* losses lead to a significant reduction of the *firm's* retained earnings or other reserves which causes a significant deterioration of the *firm's* financial and solvency conditions; and~~

(ii) ~~when it is reasonably foreseeable that the events described in (i) will occur; and~~

(b) ~~when the *firm* is in breach of its *capital resources requirement*.~~ [deleted]

2.2.117C G (1) ~~The effects of the mechanisms described in *GENPRU 2.2.117A R* will be more meaningful if they happen immediately after losses cause a significant deterioration of the financial as well as the solvency situation and even before the reserves are exhausted.~~

(2) ~~If a *firm* does not operate the loss absorption mechanism in a prudent and timely way, then the *appropriate regulator* may consider using its powers under 55J of the *Act* to, on its own initiative, vary the *firm's Part 4A permission* to require it to operate the mechanism.~~ [deleted]

…

2.2.118A G ~~For the purposes of *GENPRU 2.2.118R (2)*, the focus of the legal opinion in considering *GENPRU 2.2.64R (6)(b)* should be on whether appropriate mechanisms exist and are designed to operate to ensure that the value of the *hybrid capital* instrument and the position of the *hybrid capital* holder are not enhanced by recapitalisation.~~ [deleted]

…

Other tier one capital: hybrid capital: indirectly issued tier one capital (BIPRU firm only)

2.2.123 R ~~*GENPRU 2.2.123 R* to *GENPRU 2.2.137 R* apply to a *BIPRU firm*.~~ [deleted]

2.2.124 R (1) ~~*GENPRU 2.2.123 R - GENPRU 2.2.137 R* apply to capital of a *firm* if:~~

(a) ~~either or both of the conditions in (2) are satisfied; and~~

~~(b) any of the *SPVs* referred to in (2) is a *subsidiary undertaking* of the *firm*.~~

~~(2) The conditions referred to in (1) are:~~

~~(a) that capital is issued to an *SPV*; or~~

~~(b) the subscription for the capital issued by the *firm* is funded directly or indirectly by an *SPV*.~~

~~(3) A *BIPRU firm* may not include capital coming within this *rule* in its *capital resources* unless the requirements in the following *rules* are satisfied:~~

~~(a) (if (2)(a) applies and (2)(b) does not) *GENPRU 2.2.127 R*, *GENPRU 2.2.129 R* and *GENPRU 2.2.132 R*; or~~

~~(b) (in any other case) *GENPRU 2.2.133 R*.~~ [deleted]

2.2.125 R ~~A *BIPRU firm* may only count capital to which *GENPRU 2.2.124 R* applies at stage C of the calculation in the *capital resources table*.~~ [deleted]

2.2.126 R ~~For the purpose of *GENPRU 2.2*, an *SPV* is, in relation to a *BIPRU firm*, any *undertaking* whose main activity is to raise funds for that *firm* or for a *group* to which that *BIPRU firm* belongs.~~ [deleted]

2.2.127 R ~~The *SPV* referred to in *GENPRU 2.2.124 R (2)(a)* must satisfy the following conditions:~~

~~(1) it is controlled by the *firm* and may not operate independently of the *firm*;~~

~~(2) the rights of investors in the *SPV* who do not belong to the *group* of the *BIPRU firm* in question are not such as to affect the ability of the *firm* to control the *SPV*;~~

~~(3) all or virtually all of its *exposures* (calculated by reference to the amount) consist of *exposures* to the *firm* or to that *firm's group*; and~~

~~(4) it is incorporated under, and governed by, the laws and jurisdiction of England and Wales, Scotland or Northern Ireland.~~ [deleted]

2.2.128 G ~~An *SPV* could take the form of a limited partnership. In such an arrangement, holders of a *capital instrument* issued by the *SPV* which do not belong to the *group* of the *BIPRU firm* in question should have no right to participate in the management of the partnership, whether under the partnership's constitutional documents or the transaction documents. In general, this means that they should be treated as limited partners. It is expected that the general partner, having control of the *SPV*, would be the *firm*.~~ [deleted]

2.2.128A R ~~*GENPRU 2.2.127 R (4)* does not apply if the *firm* has conducted a properly reasoned analysis confirming that any potential risks, including legal and operational risks, associated with cross-border issues, which undermine the quality of the capital for the issuer, that arise from an *SPV* not being incorporated under or governed by the laws and jurisdiction of England and Wales, Scotland or Northern Ireland, are adequately mitigated.~~ [deleted]

2.2.128B R ~~The analysis must be set out in writing and dated before the date of issue of the *capital instrument* and the *firm* must be able to show that the analysis has been fully considered as part of its decision to proceed with the issue. The analysis must be conducted by a person or persons appropriately qualified to~~

~~assess the relevant risks and that person may be an independent adviser or an employee of the *firm* who is not part of the business unit responsible for the transaction (including the drafting of the issue documentation).~~ [deleted]

2.2.129 R ~~The *SPV* referred to in *GENPRU 2.2.124 R (2)(a)* must fund its subscription for the capital issued by the *firm* by the issue of capital that satisfies the following conditions:~~

~~(1)~~ ~~it must comply with the conditions for qualification as *tier one capital*, as amended by *GENPRU 2.2.130 R*, as if the *SPV* was itself a *firm* seeking to include that capital in its *tier one capital resources*;~~

~~(2)~~ ~~(a)~~ ~~its terms must include an obligation on the *firm* that, in the event of a collapse of the *SPV* structure, and if the mechanism contained within the instrument under *GENPRU 2.2.117A R* is a conversion, the *firm* must substitute the *capital instrument* issued by the *SPV* with *core tier one capital* issued by the *firm*; and~~

~~(b)~~ ~~there must be no obstacle to the *firm's* issue of new securities;~~

~~(3)~~ ~~the conversion ratio in respect of the substitution described in (2) must be fixed when the *SPV* issues the *capital instrument*;~~

~~(4)~~ ~~to the extent that investors have the benefit of an obligation by a *person* other than the *SPV*:~~

~~(a)~~ ~~that obligation must be one owed by a member of the *firm's group*; and~~

~~(b)~~ ~~the extent of that obligation must be no greater than would be permitted by *GENPRU* if that obligation formed part of the terms of a *capital instrument* issued by that member which complied with the *rules* in *GENPRU* relating to *tier one capital* included at stage C of the calculation in the *capital resources table*; and~~

~~(5)~~ ~~if the *SPV* structure collapses, the holder of it has no better a claim against the *firm* than a holder of the same type of instrument directly issued by the *firm*.~~ [deleted]

2.2.130 R ~~For the purpose of *GENPRU 2.2.129 R* and *GENPRU 2.2.132 R*, *GENPRU 2.2.118 R* (Requirement to obtain a legal opinion) does not apply.~~ [deleted]

2.2.131 R ~~In relation to the obligation to substitute described in *GENPRU 2.2.129 R (2)*, a *firm* must take all reasonable steps to ensure that it has at all times authorised and unissued *capital instruments* which are *core tier one capital* (and the authority to issue them) sufficient to discharge its obligation to substitute.~~ [deleted]

2.2.131A G ~~*GENPRU 2.2.129 R (2)* and *GENPRU 2.2.131 R* allow a *firm* to replace the capital issued by the *SPV* with *capital instrument* which are *core tier one capital*.~~ [deleted]

2.2.132 R ~~The capital which the *firm* seeks to include in its *capital resources* under *GENPRU 2.2.124 R (3)(a)* must satisfy the following conditions:~~

~~(1)~~ ~~it meets the conditions for inclusion in *tier one capital* (subject to *GENPRU 2.2.130 R*);~~

~~(2)~~ ~~its first call date (if any) must not arise before that on the instrument~~

~~issued by the *SPV*; and~~

~~(3)~~ ~~its terms relating to repayment must be the same as those of the instrument issued by the *SPV*.~~ [deleted]

2.2.133 R ~~(1)~~ ~~This rule deals with any transaction:~~

~~(a)~~ ~~under which an *SPV* directly or indirectly funds the subscription for capital issued by the *firm* as described in *GENPRU 2.2.124 R*; or~~

~~(b)~~ ~~that is directly or indirectly funded by a transaction in (1)(a).~~

~~(2)~~ ~~Each *undertaking* that is a party to a transaction to which this *rule* applies (other than the *firm*) must be a *subsidiary undertaking* of the *firm*.~~

~~(3)~~ ~~Each *SPV* that is a party to a transaction to which this *rule* applies must comply with *GENPRU 2.2.127 R*.~~

~~(4)~~ ~~Any capital to which (1) applies (other than the capital that is to be included in the *firm's capital resources*) must be in the form of capital that complies with *GENPRU 2.2.129 R (1)* and *GENPRU 2.2.129 R (4)*, whether or not issued by an *SPV*.~~

~~(5)~~ ~~The obligations in *GENPRU 2.2.129 R (2)* and *GENPRU 2.2.129 R (3)* only apply to capital issued by an *SPV* at the end of the chain of transactions beginning with the issue of capital by the *firm* referred to in *GENPRU 2.2.124 R*.~~

~~(6)~~ ~~*GENPRU 2.2.132 R* applies to the capital issued by the *firm* as referred to in *GENPRU 2.2.124 R*. For these purposes references in *GENPRU 2.2.132 R* to the instrument issued by the *SPV* are to the instrument referred to in (5).~~ [deleted]

2.2.134 G ~~The purpose of *GENPRU 2.2.133 R* is to deal with a capital-raising under which the capital raised by a special purpose vehicle is passed through a number of *undertakings* before it is invested in the *firm*. If the *capital resources* of the *firm* fall below, or are likely to fall below, its *capital resources requirement* the *firm* should replace the capital issued by that first special purpose vehicle with a *tier one instrument* directly issued by the *firm* which complies with *GENPRU 2.2.129 R (2)*.~~ [deleted]

2.2.135 R ~~A *firm* which satisfies the conditions for the inclusion of capital set out in *GENPRU 2.2.124 R*, must, in addition, if that transaction is in any respect unusual, notify the *appropriate regulator* at least one *Month* in advance of the date on which the *firm* intends to include that capital in its *capital resources*.~~ [deleted]

2.2.136 G ~~The *appropriate regulator* is likely to consider as unusual a transaction which involves the raising by the *firm* of *tier one capital* through a *subsidiary undertaking* of that *firm* that is not an *SPV*. The *appropriate regulator* would expect a *firm* to request individual *guidance* in such circumstances.~~ [deleted]

2.2.137 R ~~A *firm* must ensure that, in relation to a transaction falling within *GENPRU 2.2.124 R*:~~

~~(1)~~ ~~the marketing document for the transaction contains all the information which a reasonable third party would require to understand the transaction fully and its effect on the financial position of the *firm* and its~~

~~*group*; and~~

~~(2) the information in (1) and the transaction are easily comprehensible without the need for additional information about the *firm* and its *group*.~~ [deleted]

…

Deductions from tier one: Intangible assets

~~2.2.156~~ ~~G~~ ~~Intangible assets include goodwill as defined in accordance with the requirements referred to in *GENPRU 1.3.4 R* (General requirements: accounting principles to be applied) applicable to the *firm*. The treatment of deferred acquisition cost assets for *BIPRU investment firms* is dealt with in *GENPRU 1.3* (Valuation); they should not be deducted as an intangible asset.~~ [deleted]

2.2.156A G Intangible assets include goodwill as defined in accordance with the requirements referred to in *GENPRU 1.3.4 R* (General requirements: accounting principles to be applied) applicable to the *firm*.

…

General conditions for eligibility as tier two capital instruments

…

2.2.160 R ~~A holder of a non-deferred share of a *building society* must be treated as a senior unsecured creditor of that *building society* for the purpose of *GENPRU 2.2.159 R*.~~ [deleted]

…

Upper tier two capital: Revaluation reserves (BIPRU firm only)

2.2.185 R ~~(1) This *rule* applies to a *BIPRU firm*.~~

~~(2) A *BIPRU firm* must, in relation to equities held in the available-for-sale financial assets category:~~

~~(a) deduct any net losses at stage E of the calculation in the *capital resources table* (Deductions from tier one capital); and~~

~~(b) include any net gains (after deduction of deferred tax) in revaluation reserves at stage G of the calculation in the *capital resources table* (Upper tier two capital).~~

~~(3) A *BIPRU firm* must include any net gains, after deduction of deferred tax, on revaluation reserves of investment properties at stage G of the calculation in the *capital resources table*. A *firm* must include any losses on such revaluation reserves in profit and loss account and other reserves.~~

~~(4) A *BIPRU firm* must include any net gains, after deduction of deferred tax, on revaluation reserves of land and buildings at stage G of the calculation in the *capital resources table*. A *firm* must include any losses on such revaluation reserves in profit and loss account and other reserves.~~

(5) ~~(2) only applies to a *firm* to the extent that the category of asset referred to in that paragraph exists under the accounting framework that applies to the *firm* as referred to in *GENPRU 1.3.4 R* (General requirements: accounting principles to be applied).~~

(6) ~~(3) and (4) apply to a *firm* whatever the accounting treatment of those items is under the accounting framework that applies to the *firm* as referred to in *GENPRU 1.3.4 R*.~~ [deleted]

2.2.186 G ~~Subject to *GENPRU 2.2.185 R*, a *BIPRU firm* should value its revaluation reserves in accordance with the *rules* in *GENPRU 1.3* (Valuation).~~ [deleted]

Upper tier two capital: General/collective provisions (BIPRU firm only)

2.2.187 R ~~A *BIPRU firm* which adopts the *standardised approach* to credit risk may include general/collective provisions in its *tier two capital resources* only if:~~

(1) ~~they are freely available to the *firm*;~~

(2) ~~their existence is disclosed in internal accounting records; and~~

(3) ~~their amount is determined by the management of the *firm*, verified by independent auditors and notified to the *appropriate regulator*.~~ [deleted]

2.2.188 R ~~The value of general/collective provisions which a *firm* may include in its *tier two capital resources* as referred to in *GENPRU 2.2.187 R* may not exceed 1.25% of the sum of the following:~~

(1) ~~the sum of the *market risk capital requirement* and the *operational risk capital requirement* (if applicable), multiplied by a factor of 12.5; and~~

(2) ~~the sum of *risk weighted* assets under the *standardised approach* for credit risk.~~ [deleted]

2.2.189 R ~~Where a *firm* is unable to determine whether collective/general provisions relate only to *exposures* on either the *standardised approach* or the *IRB approach*, that *firm* must allocate them on a basis which is reasonable and consistent.~~ [deleted]

Upper tier two capital: Surplus provisions (BIPRU firm only)

2.2.190 R ~~A *BIPRU firm* calculating *risk weighted exposure amounts* under the *IRB approach* may include in its *upper tier two capital resources* positive amounts resulting from the calculation in *BIPRU 4.3.8 R* (Treatment of expected loss amounts), up to 0.6% of the *risk weighted exposure amounts* calculated under that approach.~~ [deleted]

2.2.191 R ~~A *BIPRU firm* calculating *risk weighted exposure amounts* under the *IRB approach* may not include in its *capital resources* value adjustments and provisions included in the calculation in *BIPRU 4.3.8 R* (Treatment of *expected loss* amounts under the *IRB approach* for *trading book exposures*) or value adjustments and provisions for *exposures* that would otherwise have been eligible for inclusion in general/collective provisions other than in accordance with *GENPRU 2.2.190 R*.~~ [deleted]

2.2.192 R ~~For the purpose of *GENPRU 2.2.190 R* and *GENPRU 2.2.191 R*, *risk weighted exposure amounts* must not include those calculated in respect of *securitisation positions* which have a *risk weight* of 1250%.~~ [deleted]

2.2.193 R ~~If a *BIPRU firm* calculates *risk weighted exposure amounts* under the *IRB approach* for the purposes of *BIPRU 14* (Capital requirements for settlement and counterparty risk) it must not include valuation adjustments referred to in *BIPRU 14.2.18 R (1)* (Treatment of expected loss amounts) in its *capital resources* except in accordance with that *rule*.~~ [deleted]

…

Deductions from tiers one and two: Qualifying holdings (bank or building society only)

2.2.202 R ~~*GENPRU 2.2.202 R* to *GENPRU 2.2.207 R* only apply to a *bank* or *building society*.~~ [deleted]

2.2.203 R ~~A *qualifying holding* is a direct or indirect holding of a *bank* or *building society* in a non-financial *undertaking* which represents 10% or more of the capital or of the voting rights or which makes it possible to exercise a significant influence over the management of that *undertaking*.~~ [deleted]

2.2.204 R ~~For the purpose of *GENPRU 2.2.203 R*, a non-financial *undertaking* is an *undertaking* other than:~~

(1) ~~a *credit institution* or *financial institution*;~~

(2) ~~an *undertaking* whose exclusive or main activities are a direct extension of banking or concern services ancillary to banking, such as leasing, factoring, the management of unit trusts, the management of data processing services or any other similar activity; or~~

(3) ~~an *insurer*.~~ [deleted]

2.2.205 R ~~The amount of *qualifying holdings* that a *bank* or *building society* must deduct in the calculation in the *capital resources table* is:~~

(1) ~~(if the *firm* has one or more *qualifying holdings* that exceeds 15% of its relevant *capital resources*) the sum of such excesses; and~~

(2) ~~to the extent not already deducted in (1), the amount by which the sum of each of that *firm's qualifying holdings* exceeds 60% of its relevant *capital resources*.~~ [deleted]

2.2.206 R ~~The relevant *capital resources* of a *firm* mean for the purposes of this *rule* the sum of the amount of *capital resources* calculated at stages L (Total tier one capital plus tier two capital) and Q (Total tier three capital) of the calculation in the *capital resources table* as adjusted in accordance with the following:~~

(1) ~~the *firm* must not take into account the items referred to in any of the following:~~

~~(a)~~ ~~*GENPRU 2.2.190 R* to *GENPRU 2.2.193 R* (surplus provisions); or~~

~~(b)~~ ~~*GENPRU 2.2.236 R* (*expected loss* amounts and other negative amounts); or~~

~~(c)~~ ~~*GENPRU 2.2.237 R* (*securitisation positions*);~~

(2) ~~the *firm* must make the deductions to be made at stage S of the calculation in the *capital resources table* (Deductions from total capital);~~

~~and~~

(3) ~~the *firm* need not deduct any *excess trading book position* under (2).~~ [deleted]

2.2.207 R ~~The following are not included as *qualifying holdings*:~~

(1) ~~*shares* that are not held as investments; or~~

(2) ~~*shares* that are held temporarily during the normal course of underwriting; or~~

(3) ~~*shares* held in a *firm's* name on behalf of others.~~ [deleted]

Deductions from tiers one and two: Material holdings (BIPRU firm only)

2.2.208 R ~~*GENPRU 2.2.208 R* to *GENPRU 2.2.216 G* only apply to a *BIPRU firm*.~~ [deleted]

2.2.209 R ~~(1)~~ ~~Subject to (2) and (3), a *material holding* is:~~

~~(a)~~ ~~a *BIPRU firm's* holdings of *shares* and any other interest in the capital of an individual *credit institution* or *financial institution* (held in the *non-trading book* or the *trading book* or both) exceeding 10% of the *share* capital of the issuer, and, where this is the case, any holdings of subordinated debt of the same issuer are also included as a *material holding*; the full amount of the holding is a *material holding*; or~~

~~(b)~~ ~~a *BIPRU firm's* holdings of *shares*, any other interest in the capital and subordinated debt in an individual *credit institution* or *financial institution* (held in the *non-trading book* or the *trading book* or both) not deducted under (a) if the total amount of such holdings exceeds 10% of that *firm's capital resources* at stage N (Total tier one capital plus tier two capital after deductions) of the calculation in the *capital resources table* (calculated before deduction of its *material holdings*); only the excess amount is a *material holding*; or~~

~~(c)~~ ~~a *bank* or *building society's* aggregate holdings in the *non-trading book* of *shares*, any other interest in the capital, and subordinated debt in all *credit institutions* or *financial institutions* not deducted under (a) or (b) if the total amount of such holdings exceeds 10% of that *firm's capital resources* at stage N of the calculation in the *capital resources table* (calculated before deduction of its *material holdings*); only the excess amount is a *material holding*; or~~

~~(d)~~ ~~a *material insurance holding*.~~

~~(2)~~ ~~If a *BIPRU firm* holds *shares* in the capital of Business Growth Fund plc or another *financial institution* which makes *venture capital investments* (in this section and its related annexes, a "Venture Capital Investor") and the following conditions are met:~~

~~(a)~~ ~~the sole business of the Venture Capital Investor is the making of *venture capital investments* together with the performance of *ancillary activities* in relation to the administration of the *venture capital investments*;~~

~~(b)~~ ~~none of the *venture capital investments* made by the Venture~~

~~Capital Investor is an investment (direct or indirect) in:~~

~~(i) a *credit institution*; or~~

~~(ii) a *financial institution* the principal activity of which is to perform any activity other than the acquisition of holdings in other *undertakings*;~~

~~(c) the relevant proportion of the Venture Capital Investor is included in the *firm's UK consolidation group* in accordance with *BIPRU 8.5*; and~~

~~(d) the *firm* assigns a *risk weight* to its *exposure* to the Venture Capital Investor as if it were an *equity exposure* to which the simple *risk weight* approach is applied as set out in *BIPRU 4.7.9 R* to *BIPRU 4.7.12 R* (and in calculating its *capital resources requirement* the *firm* must assign a *risk weight* to that *exposure* in accordance with those *rules* and notwithstanding that those *rules* would not otherwise apply to that calculation);the Venture Capital Investor may be ignored for the purposes of determining whether there is a *material holding*.~~

~~(3) If a *BIPRU firm* holds *shares* in the capital of a *subsidiary undertaking* which is a *financial institution* solely by reason of its principal activity being the acquiring of holdings and which in turn holds (directly or indirectly) *shares* in the capital of a Venture Capital Investor (in this section and its related annexes, a "Venture Capital Holding Company") and the following conditions are met:~~

~~(a) the Venture Capital Investor meets the conditions in (2)(a) and (b);~~

~~(b) the Venture Capital Holding Company is included in the *firm's UK consolidation group* in accordance with *BIPRU 8.5*;~~

~~(c) the proportion of the value of the Venture Capital Holding Company attributable to investment in Venture Capital Investors and the proportion of the value of the Venture Capital Holding Company attributable to investment in other investments can be identified and valued on a regular basis; and~~

~~(d) the *firm* assigns a *risk weight* to its *exposure* to the proportion of the Venture Capital Holding Company that represents the value of its investment in Venture Capital Investors as if it were an *equity exposure* to which the simple *risk weight* approach is applied as set out in *BIPRU 4.7.9 R* to *BIPRU 4.7.12 R* (and in calculating its *capital resources requirement* the *firm* must assign a *risk weight* to that *exposure* in accordance with those *rules* and notwithstanding that those *rules* would not otherwise apply to that calculation);the proportion of the *firm's* investment in the Venture Capital Holding Company that represents the value of its investment in Venture Capital Investors may be ignored for the purposes of determining whether there is a *material holding*. The proportion of the *firm's* investment in the Venture Capital Holding Company that represents the value of other investments is a *material holding*.~~ [deleted]

2.2.210 G ~~For the purpose of the definition of a *material holding*, *share* capital includes *preference shares*. *Share* premium should be taken into account when determining the amount of *share* capital.~~ [deleted]

2.2.211 R ~~When calculating the size of its *material holdings* a *firm* must only include an actual holding (that is, a long cash position). A *firm* must not net such holdings with a short position.~~ [deleted]

2.2.212 R ~~A *material insurance holding* means the holdings of a *BIPRU firm* of items of the type set out in *GENPRU 2.2.213 R* in any:~~

~~(1) *insurance undertaking*; or~~

~~(2) *insurance holding company*;~~

~~that fulfils one of the following conditions:~~

~~(3) it is a *subsidiary undertaking* of that *firm*; or~~

~~(4) that *firm* holds a *participation* in it.~~ [deleted]

2.2.213 R ~~An item falls into this provision for the purpose of *GENPRU 2.2.212 R* if it is:~~

~~(1) an *ownership share*; or~~

~~(2) subordinated debt or another item of capital that falls into Article 16(3) of the *First Non-Life Directive* or, as applicable, Article 27(3) of the *Consolidated Life Directive*.~~ [deleted]

2.2.214 R ~~The amount to be deducted with respect to each *material insurance holding* is the higher of:~~

~~(1) the book value of the *material insurance holding*; and~~

~~(2) the *solo capital resources requirement* for the *insurance undertaking* or *insurance holding company* in question calculated in accordance with Part 3 of *GENPRU 3 Annex 1 R* (Method 3 of the capital adequacy calculations for financial conglomerates).~~ [deleted]

2.2.215 R ~~For the purpose of the definition of a *material holding*, holdings must be valued using the valuation method which the holder uses for its external financial reporting purposes.~~ [deleted]

2.2.216 G ~~(1) This paragraph gives *guidance* on how the calculation under *GENPRU 2.2.214 R (1)* should be carried out where an *insurance undertaking* is accounted for using the embedded value method.~~

~~(2) On acquisition, any "goodwill" element (that is, the difference between the acquisition value according to the embedded value method and the actual investment) should be deducted from *tier one capital resources*.~~

~~(3) The embedded value should be deducted from the total of *tier one capital resources* and *tier two capital resources*.~~

~~(4) Post-acquisition, where the embedded value of the *undertaking* increases, the increase should be added to reserves, while the new embedded value is deducted from total *capital resources*.~~

~~(5) This means that the net impact on the level of total *capital resources* is zero, although *tier two capital resources* headroom will increase with any increase in *tier one capital resources* reserves.~~

~~(6)~~ ~~Embedded value is the value of the *undertaking* taking into account the present value of the expected future inflows from existing life assurance business.~~ [deleted]

2.2.216A G ~~(1)~~ ~~This paragraph gives *guidance* as to the amount to be deducted at Part 2 of stage M (Deductions from the totals of tier one and two) of *GENPRU 2 Annex 2 R* (Capital resources table for a bank) and *GENPRU 2 Annex 3 R* (Capital resources table for a building society) in respect of investments in *subsidiary undertakings* and *participations* (excluding any amount which is already deducted as *material holdings* or *qualifying holdings*).~~

~~(2)~~ ~~The effect of those *rules* is to achieve the deduction of all investments in *subsidiary undertakings* and *participations* for *banks* and *building societies* by ensuring that amounts not already deducted under other *rules* are accounted for at this stage of the calculation of *capital resources*, except where the investment has been made in:~~

~~(a)~~ ~~a Venture Capital Investor and the conditions in *GENPRU 2.2.209R (2)* are met; or~~

~~(b)~~ ~~a Venture Capital Holding Company and the conditions in *GENPRU 2.2.209R (3)* are met;~~

~~(3)~~ ~~The following investments in *subsidiary undertakings* and *participations* should be deducted at this stage:~~

~~(a)~~ ~~those not deducted in Part 1 of stage M because of the operation of the thresholds in *GENPRU 2.2.205 R* (on qualifying holdings) and *GENPRU 2.2.209 R* (on material holdings); and~~

~~(b)~~ ~~those which do not meet the definition of *qualifying holding* or *material holding*, but excluding investments in Venture Capital Investors which are ignored in accordance with *GENPRU 2.2.209R (2)* and investments in Venture Capital Holding Companies which are ignored in accordance with *GENPRU 2.2.209R (3)*, for the purposes of determining whether there is a *material holding*.~~

~~(4)~~ ~~For example, an investment in an *undertaking* which is not a *qualifying holding* under *GENPRU 2.2.204 R (2)* (on the definition of a non-financial undertaking), that is whose exclusive or main activities are a direct extension of banking or concern services ancillary to banking, such as leasing, factoring, the management of unit trusts, the management of data processing services or any other similar activity, should be deducted at this stage.~~ [deleted]

Deductions from tiers one and two: Reciprocal cross holdings (BIPRU firm only)

2.2.217 R ~~*GENPRU 2.2.217 R* to *GENPRU 2.2.220 R* apply to a *BIPRU firm*.~~ [deleted]

2.2.218 R ~~A *BIPRU firm* must deduct at stage M of the calculation in the *capital resources table* (Deductions from the totals of tier one and two) any *reciprocal cross-holdings*. However a *BIPRU firm* must not deduct such holdings to the extent that they fall to be deducted at Part 1 of stage M of the calculation in the *capital resources table* (Deductions for *material holdings*, *qualifying holdings* and certain other items).~~ [deleted]

2.2.219 R ~~A *reciprocal cross-holding* means a holding of the *BIPRU firm* of *shares*, any other interest in the capital, and subordinated debt, whether in the *trading* or~~

~~*non-trading* book, in:~~

~~(1) a *credit institution*; or~~

~~(2) a *financial institution*;~~

~~that satisfies the following conditions:~~

~~(3) the holding is the subject of an agreement or arrangement between the *BIPRU firm* and either the issuer of the instrument in question or a member of a *group* to which the issuer belongs;~~

~~(4) under the terms of the agreement or arrangement described in (3) the issuer invests in the *BIPRU firm* or in a member of the *group* to which that *BIPRU firm* belongs; and~~

~~(5) the effect of that agreement or arrangement on the capital position of the *BIPRU firm*, the issuer, or any member of a *group* to which either belongs, under any relevant rules is significantly more beneficial than it is in economic terms, taking into account the agreement or arrangement as a whole.~~ [deleted]

2.2.220 R ~~For the purpose of *GENPRU 2.2.219 R*, a relevant rule means a *rule* in *GENPRU*, *BIPRU* or *INSPRU* or any other capital adequacy or solvency requirements of the *appropriate regulator* or any other regulator, territory or country.~~ [deleted]

Deductions from tiers one and two: Connected lending of a capital nature (bank only)

2.2.221 R ~~(1) *GENPRU 2.2.221 R* to *GENPRU 2.2.235 G* only apply to a bank.~~

~~(2) If a *firm* has elected to ignore an investment in a Venture Capital Investor or a Venture Capital Holding Company in accordance with *GENPRU 2.2.209R (2)* or *(3)*, for the purposes of determining whether there is a *material holding*, *GENPRU 2.2.221 R* to *GENPRU 2.2.233 R* do not apply to any lending by the *firm* to that Venture Capital Investor or Venture Capital Holding Company, provided that any lending to the Venture Capital Holding Company is made to and deployed by the *firm* solely in connection with the Venture Capital Investor.~~ [deleted]

2.2.222 R ~~*Connected lending of a capital nature* means all lending within *GENPRU 2.2.227 R* or *GENPRU 2.2.229 R* and guarantees within *GENPRU 2.2.231 R* or *GENPRU 2.2.233 R*.~~ [deleted]

2.2.223 R ~~A *bank* must not deduct any item as *connected lending of a capital nature* to the extent that it falls to be deducted at Part 1 of stage M of the calculation in the *capital resources table* (Deductions for *material holdings*, *qualifying holdings* and certain other items) or as a *reciprocal cross-holding*.~~ [deleted]

2.2.224 R ~~For the purpose of the *rules* in this section about *connected lending of a capital nature* and in relation to a *bank*, a connected party means another *person* ("P") who fulfils at least one of the following conditions and is not solo-consolidated with the *bank* under *BIPRU 2.1* (Solo consolidation):~~

~~(1) P is *closely related* to the *bank*; or~~

~~(2) P is an *associate* of the *bank*; or~~

(3) ~~the same *persons* significantly influence the *governing body* of P and the *bank*.~~ [deleted]

2.2.225 R ~~For the purpose of *GENPRU 2.2.224 R*, in relation to a *person* ("P") to which a *bank* has an *exposure* when P is acting on his own behalf and also an *exposure* to P when P acts in his capacity as a trustee, custodian or general partner of an investment trust, unit trust, venture capital or other investment fund, pension fund or similar fund (a "fund") the *bank* may choose to treat this latter *exposure* as an *exposure* to the fund, unless such treatment would be misleading.~~ [deleted]

2.2.226 G ~~*BIPRU 10.3.13 G* (*Guidance* onexposures to trustees) applies to *GENPRU 2.2.225 R* .~~ [deleted]

2.2.227 R ~~A loan is *connected lending of a capital nature* if:~~

(1) ~~it is made by the *bank* to a connected party; and~~

(2) ~~it falls into *GENPRU 2.2.228 R*.~~ [deleted]

2.2.228 R ~~A loan falls into this *rule* for the purposes of *GENPRU 2.2.227 R (2)* if, whether through contractual, structural, reputational or other factors:~~

(1) ~~based on the terms of the loan and the other knowledge available to the *bank*, the borrower would be able to consider it from the point of view of its characteristics as capital as being similar to *share* capital or subordinated debt; or~~

(2) ~~the position of the lender from the point of view of maturity and repayment is inferior to that of the senior unsecured and unsubordinated creditors of the borrower.~~ [deleted]

2.2.229 R ~~A loan is also *connected lending of a capital nature* if:~~

(1) ~~it funds directly or indirectly a loan to a connected party of the *bank* falling into *GENPRU 2.2.228 R* or an investment in the capital of a connected party of the *bank*; and~~

(2) ~~it falls into *GENPRU 2.2.228 R*.~~ [deleted]

2.2.230 G ~~It is likely that a loan is not *connected lending of a capital nature* if:~~

(1) ~~it is secured by collateral that is eligible for the purposes of *credit risk mitigation* under the *standardised approach* to credit risk as set out in *BIPRU 5.4* (Financial collateral) and *BIPRU 5.5* (Other funded credit risk mitigation); or~~

(2) ~~it is repayable on demand (and should be treated as such for accounting purposes by the borrower and lender) and the *bank* can demonstrate that there are no potential obstacles to exercising the right to repay, whether contractual or otherwise.~~ [deleted]

2.2.231 R ~~A guarantee is *connected lending of a capital nature* if it is a guarantee by the *bank* of a loan from a third party to a connected party of the *bank* and:~~

(1) ~~the loan meets the requirements of *GENPRU 2.2.228 R*; or~~

(2) ~~the rights that the *bank* would have against the borrower with respect to the guarantee meet the requirements of *GENPRU 2.2.228 R (2)*.~~

[deleted]

2.2.232 R ~~A guarantee is also *connected lending of a capital nature* if it is a guarantee by the *bank* of a loan falling into *GENPRU 2.2.229 R (1)*; and~~

~~(1)~~ ~~the loan meets the conditions in *GENPRU 2.2.228 R*; or~~

~~(2)~~ ~~the guarantee meets the conditions in *GENPRU 2.2.231 R (2)*.~~ [deleted]

2.2.233 R ~~The amount of a guarantee that constitutes *connected lending of a capital nature* that a *firm* must deduct is the amount guaranteed.~~ [deleted]

2.2.234 G ~~A loan may initially fall outside the definition of *connected lending of a capital nature* but later fall into it. For example, if the initial lending to a connected party is subsequently downstreamed to another connected party the relationship between the *bank* and the ultimate borrower may be such that, looking at the arrangements as a whole, the *undertaking* to which the *bank* lends is able to regard the loan to it as being capable of absorbing losses.~~ [deleted]

2.2.235 G ~~Lending to a connected party will not normally be *connected lending of a capital nature* where that party:~~

~~(1)~~ ~~is acting as a vehicle to pass funding to an unconnected party; and~~

~~(2)~~ ~~has no other creditors whose claims could be senior to those of the lender.~~ [deleted]

Deductions from tiers one and two: Expected losses and other negative amounts (BIPRU firm only)

2.2.236 R ~~A *BIPRU firm* calculating *risk weighted exposure amounts* under the *IRB approach* must deduct:~~

~~(1)~~ ~~any negative amounts arising from the calculation in *BIPRU 4.3.8 R* (Treatment of expected loss amounts); and~~

~~(2)~~ ~~any *expected loss* amounts calculated in accordance with *BIPRU 4.7.12 R* (*Expected loss* amounts under the simple risk weight approach to calculating *risk weighted exposure amounts* for *exposures* belonging to the *equity exposure IRB exposure class*) or *BIPRU 4.7.17 R* (*Expected loss* amounts under the *PD/LGD approach*).~~ [deleted]

Deductions from tiers one and two: Securitisation positions (BIPRU firm only)

2.2.237 R ~~A *BIPRU firm* calculating *risk weighted exposure amounts* under the *IRB approach* or the *standardised approach* to credit risk must deduct from its *capital resources* the following:~~

~~(1)~~ ~~the exposure amount of *securitisation positions* which receive a *risk weight* of 1250% under *BIPRU 9* (Securitisation), unless the *firm* includes the *securitisation positions* in its calculation of *risk weighted exposure amounts* (see *BIPRU 9.10* (Reduction in risk-weighted exposure amounts)); and~~

~~(2)~~ ~~the exposure amount of *securitisation positions* in the *trading book* that would receive a *risk weight* of 1250% if they were in the *firm's non-trading book*.~~ [deleted]

Deductions from tiers one and two: Special treatment of material holdings and other items (BIPRU firm only)

2.2.238 R ~~*GENPRU 2.2.238 R* to *GENPRU 2.2.241 R* apply to a *BIPRU firm* and relate to the deductions in respect of:~~

~~(1) *material holdings*;~~

~~(2) *expected loss* amounts and other negative amounts referred to in *GENPRU 2.2.236 R*; and~~

~~(3) *securitisation positions* referred to in *GENPRU 2.2.237 R*.~~ [deleted]

2.2.239 R ~~(1) The treatment in the *capital resources table* of the deductions in *GENPRU 2.2.238 R* only has effect for the purpose of the *capital resources gearing rules*.~~

~~(2) In other cases (3) and (4) apply.~~

~~(3) A *BIPRU firm* making the deductions described in *GENPRU 2.2.238 R* must deduct 50% of the total amount of those deductions at stage E (Deductions from tier one capital) and 50% at stage J (Deductions from tier two capital) of the calculation in the *capital resources table* after the application of the *capital resources gearing rules*.~~

~~(4) To the extent that half of the total of:~~

~~(a) *material holdings*;~~

~~(b) *expected loss* amounts and other negative amounts; and~~

~~(c) *securitisation positions*;exceeds the amount calculated at stage I (Total tier two capital) of that calculation, a *firm* must deduct that excess from the amount calculated at stage F (Total tier one capital after deductions) of the *capital resources table*.~~ [deleted]

2.2.240 G ~~The alternative calculation in *GENPRU 2.2.239 R (3)* to *(4)* is only relevant to *BIPRU 11* (Pillar 3 disclosures) and certain reporting requirements under *SUP*. However the deduction of *material holdings* at Part 2 of stage E of the *capital resources table* in the case of a *BIPRU investment firm* with an *investment firm consolidation waiver* has effect for all purposes.~~ [deleted]

Tier three capital: upper tier three capital resources (BIPRU firm only)

2.2.241 R ~~*GENPRU 2.2.241 R* to *GENPRU 2.2.245 R* only apply to a *BIPRU firm*.~~ [deleted]

2.2.242 R ~~A *BIPRU firm* may include subordinated debt in its *upper tier three capital resources* only if:~~

~~(1) it has an original maturity of at least two years or is subject to at least two years' notice of repayment; and~~

~~(2) payment of interest or principal is permitted only if, after that payment, the *firm's capital resources* would be not less than its *capital resources requirement*.~~ [deleted]

2.2.243 R ~~A *BIPRU firm* which includes subordinated debt in its *tier three capital resources* must notify the *appropriate regulator* one month in advance of all~~

~~payments of either interest or principal made when the *firm's capital resources* are less than 120% of its *capital resources requirement*.~~ [deleted]

2.2.244 R ~~The *rules* in the table in *GENPRU 2.2.245 R* apply to short term subordinated debt that a *BIPRU firm* includes in its *tier three capital resources* in the same way that they apply to a *firm's tier two capital resources* with the adjustments in that table.~~ [deleted]

2.2.245 R ~~Table: Application of tier two capital rules to tier three debt~~
~~This table belongs to *GENPRU 2.2.244 R*~~

~~*Tier two capital rule*~~	~~Adjustment~~
~~*GENPRU 2.2.159 R* (General conditions for eligibility as tier two capital)~~	~~The references in *GENPRU 2.2.159 R (5)* (Capital must not become repayable prior to stated maturity date except in specified circumstances) to repayment at the option of the holder are replaced by a reference to *GENPRU 2.2.242 R (1)* (*Upper tier three capital* should have maturity or notice period of at least two years)~~ ~~The reference in *GENPRU 2.2.159 R (10)* (Description of *tier two capital* in marketing documents) to *GENPRU 2.2.271 R* (Other requirements: insurers carrying on with-profits business (Insurer only)) does not apply~~
~~*GENPRU 2.2.160 R* (Holder of a non-deferred share of a *building society* to be treated as a senior creditor)~~	~~-~~
~~*GENPRU 2.2.161 R* (Additional remedies)~~	~~-~~
~~*GENPRU 2.2.163 R* (Legal opinion where debt subject to a law of a country outside the *United Kingdom*)~~	~~-~~
~~*GENPRU 2.2.169 R* (Ineligibility as *tier two capital* owing to connected transactions)~~	~~The reference to *GENPRU 2.2.177 R* (General eligibility conditions for *upper tier two capital*) does not apply~~
~~*GENPRU 2.2.171 R* (Amendments to terms of the *capital instrument*)~~	~~-~~
~~*GENPRU 2.2.172 R* to *GENPRU 2.2.173 R* (Redeemability at the option of the issuer)~~	~~-~~
~~*GENPRU 2.2.174 R* (Notification of~~	~~-~~

~~redemption)~~	
~~References in the *rules* in the first column to the fifth anniversary are amended so as to refer to the second anniversary.~~	

[deleted]

Tier three capital: lower tier three capital resources (BIPRU firm only)

2.2.246 R ~~*GENPRU 2.2.246 R* to *GENPRU 2.2.249 R* only apply to a *BIPRU firm*.~~ [deleted]

2.2.247 R ~~A *BIPRU firm's* net interim *trading book* profits mean its net *trading book* profits adjusted as follows:~~

~~(1) they are net of any foreseeable charges or dividends and less net losses on its other business; and~~

~~(2) a *firm* must not take into account items that have already been included in the calculation of *capital resources* as part of the calculation of the following items:~~

~~(a) interim net profits (see stage (A) of the *capital resources table*); or~~

~~(b) interim net losses or material interim net losses (see stage (A) of the *capital resources table*); or~~

~~(c) profit and loss and other reserves (see stage (A) of the *capital resources table*).~~ [deleted]

2.2.248 R ~~*Trading book* profits and losses, other than those losses to which *GENPRU 2.2.86 R (2)* (Valuation adjustment and reserves) refers, originating from valuation adjustments or reserves as referred to in *GENPRU 1.3.29 R* to *GENPRU 1.3.35A G* (Valuation adjustments or reserves) must be included in the calculation of net interim *trading book* profits and be added to or deducted from *tier three capital resources*.~~ [deleted]

2.2.249 R ~~*Trading book* valuation adjustments or reserves as referred to in *GENPRU 1.3.29 R* to *GENPRU 1.3.35A G* which exceed those made under the accounting framework to which a *firm* is subject must be treated in accordance with *GENPRU 2.2.248 R* if not required to be treated under *GENPRU 2.2.86 R (2)*.~~ [deleted]

…

Deductions from total capital: Illiquid assets (BIPRU investment firm only)

2.2.259 R ~~*GENPRU 2.2.259 R* to *GENPRU 2.2.262 G* only apply to a *BIPRU investment firm*.~~ [deleted]

2.2.260 R ~~*Illiquid assets* means illiquid assets including~~

~~(1) tangible fixed assets (except land and buildings if they are used by a *firm* as security for loans, but this exclusion is only up to the value of the principal outstanding on the loans); or~~

~~(2) any holdings in the *capital resources* of *credit institutions* or *financial institutions*, except to the extent that:~~

~~(a) they have already been deducted as a *material holding*; or~~

~~(b) they are *shares* which are included in a *firm's trading book* and included in the calculation of the *firm's market risk capital requirement*; or~~

~~(3) holdings of other *securities* which are not *readily realisable securities*; or~~

~~(4) deficiencies of net assets in *subsidiary undertakings*; or~~

~~(5) deposits which are not repayable within 90 days (except for payments in connection with margined *futures* or *options* contracts); or~~

~~(6) loans and other amounts owed to a *firm* except where they are due to be repaid within 90 days; or~~

~~(7) physical stocks except for *positions* in *physical commodities* which are included in the calculation of a *firm's commodity PRR*.~~ [deleted]

2.2.261 G ~~If a loan or other amount owing to a *firm* was originally due to be paid more than 90 days from the date of the making of the loan or the incurring of the payment obligation, as the case may be, it may be treated as liquid for the purposes of *GENPRU 2.2.260 R (6)* where through the passage of time the remaining time to the contractual repayment date falls below 90 days.~~ [deleted]

2.2.262 G ~~If a loan or other amount is due to be paid within 90 days (whether measured by reference to original or remaining maturity), a *firm* should consider whether it can reasonably expect the amount owing to be paid within that period. If the *firm* cannot reasonably expect it to be paid within that period the *firm* should treat it as illiquid.~~ [deleted]

Deductions from total capital: Excess trading book position (bank or building society only)

2.2.263 R ~~*GENPRU 2.2.263 R* to *GENPRU 2.2.265 R* only apply to a *bank* or *building society*.~~ [deleted]

2.2.264 R ~~(1) The *excess trading book position* is the excess of:~~

~~(a) a *bank* or *building society's* aggregate net long (including notional) *trading book positions* in *shares*, subordinated debt or any other interest in the capital of *credit institutions* or *financial institutions*;over;~~

~~(b) 25% of that *firm's capital resources* calculated at stage T (Total capital after deductions) of the *capital resources table* (calculated before deduction of the *excess trading book position*).~~

~~(2) Only the excess amount calculated under (1) must be deducted.~~ [deleted]

2.2.265 R ~~The *standard market risk PRR rules* apply for establishing what is a net *position* and the amount and value of that *position* for the purposes of *GENPRU 2.2.264 R*, ignoring *rules* which would otherwise exclude such *positions* from *BIPRU 7.2* (Interest rate PRR) or *BIPRU 7.3* (Equity PRR and basic interest rate PRR for equity derivatives) on the basis that they are to be deducted from a *bank* or *building society's capital resources*, or for any other reason.~~ [deleted]

…

Public sector guarantees

2.2.276 R ~~A *BIPRU firm* may not include a guarantee from a state or public authority in its *capital resources*.~~ [deleted]

…

2 Annex 1 **Capital resources table for an insurer**

R

Capital resources calculation for an insurer		
Type of capital	**Related text**	**Stage**
Core tier one capital		**(A)**
…		
Profit and loss account and other reserves (taking into account interim net losses)	*GENPRU 2.2.85AR*; *GENPRU 2.2.87R* to *GENPRU 2.2.88 R*	
…		

~~**2 Annex 2**~~ ~~**Capital resources table for a bank**~~

GENPRU 2 Annex 2R is deleted in its entirety. The deleted text is not shown.

~~**2 Annex 3**~~ ~~**Capital resources table for a building society**~~

GENPRU 2 Annex 3R is deleted in its entirety. The deleted text is not shown.

~~**2 Annex 4**~~ ~~**Capital resources table for a BIPRU investment firm deducting material holdings**~~

GENPRU 2 Annex 4R is deleted in its entirety. The deleted text is not shown.

~~**2 Annex 5**~~ ~~**Capital resources table for a BIPRU investment firm deducting illiquid assets**~~

GENPRU 2 Annex 5R is deleted in its entirety. The deleted text is not shown.

…

2 Annex **Guidance on applications for waivers relating to Implicit items**

8

G G Implicit items under the Act

1	The *capital resources table* does not permit *implicit items* to be included in the calculation of a *firm's capital resources*, except subject to a *waiver* under section 138A of the *Act*. Article 27(4) of the *Consolidated Life Directive* states that *implicit items* can be included in the calculation of a *firm's capital resources*, within limits, provided that the supervisory authority agrees. Certain *implicit items*, however, are not eligible for inclusion beyond 31 December 2009 (see paragraph 5). The ~~*appropriate regulator*~~ <u>*PRA*</u> may be ~~prepared~~ to grant a *waiver* from the *capital resources table* to allow *implicit items*, in line with the purpose of the *Consolidated Life Directive*, and provided the conditions as set out in article 27(4) of the *Consolidated Life Directive* are met. Such a *waiver* would allow an *implicit item* to count towards the *firm's capital resources* available to count against its *capital resources requirement* (*CRR*) set out for *realistic basis life firms* in *GENPRU 2.1.18 R* and for *regulatory basis only life firms* in *GENPRU 2.1.23 R*. An *implicit item* may potentially count as *tier one capital* (but not *core tier one capital*) or *tier two capital*. Where a *waiver* is granted allowing an *implicit item* as *tier one capital*, the value of the *implicit item* so allowed must be included at stage B of the *capital resources table*. If the application of the value of the *implicit item* is restricted by *GENPRU 2.2.29 R*, which requires that at least 50% of a *firm's tier one capital resources* must be accounted for by *core tier one capital*, the remainder may be included at stage G of the calculation in the *capital resources table*, subject to *GENPRU 2.2.31 G*. An *implicit item* treated as *tier two capital* will also be included at stage G of the calculation, again subject to *GENPRU 2.2.81 R*. Article 29(1) of the *Consolidated Life Directive* requires that *implicit items* be excluded from the capital eligible to cover the *guarantee fund*. Under *GENPRU 2.2.33 R* a *firm* must meet the *guarantee fund* from the sum of the items listed at stages A, B, G and H of the *capital resources table* less the sum of the items listed at stage E of the *capital resources table*. The ~~*appropriate regulator*~~ <u>*PRA*</u> will only grant an *implicit items* <u>*waiver*</u> if the *waiver* includes a modification to *GENPRU 2.2.33 R* to ensure that the *implicit item* does not count towards meeting the *guarantee fund*.	
2	Under section 138A of the *Act*, the ~~*appropriate regulator*~~ <u>*PRA*</u> may, on the application of a *firm*, grant a *waiver* from *PRU*. There are general requirements that must be met before any *waiver* can be granted. As explained in *SUP 8*, the ~~*appropriate regulator*~~ <u>*PRA*</u> may not give a *waiver* unless the ~~*appropriate regulator*~~ <u>*PRA*</u> is satisfied that:	
	(1)	compliance by the *firm* with the *rules* will be unduly burdensome, or would not achieve the purpose for which the *rules* were made; and
	(2)	the *waiver* ~~would not result in undue risk to *persons* whose interests the *rules* are intended to protect.~~ <u>would not adversely affect the advancement of any of the *PRA*'s objectives.</u>
3	The ~~appropriate regulator~~ <u>*PRA*</u> will assess compliance with the requirements in the light of all the relevant circumstances. This will include consideration of the costs incurred by compliance with a particular *rule* or whether a *rule* is framed in a way that would make compliance difficult in view of the *firm's* circumstances. For example, the *firm* may demonstrate that if an *implicit item* were not allowed, the *firm* would either have to suffer increased (and unwarranted) costs in injecting further *capital resources* or operate with a lower equity backing ratio (see case studies in paragraph 43). Even if a *firm* can demonstrate a case for an *implicit item waiver*, it	

	should not assume that the ~~appropriate regulator~~ *PRA* will grant the *capital resources* requested, or that any *capital resources* will be granted for the full amount of the *implicit item* which could be granted, as set out in this annex. The ~~appropriate regulator~~ *PRA* will consider each application on its own merits, and taking into account all relevant circumstances, including the financial situation and business prospects of the *firm*.
	…
5	The *Consolidated Life Directive* (reflecting the changes introduced by the Solvency 1 Directive) requires member states to end a *firm's* ability to take into account future profits *implicit items* by (at the latest) 31 December 2009. Until then, the maximum amount of the *implicit item* relating to future profits permitted under the *Consolidated Life Directive* is limited to 50% of the product of the estimated annual profits and the average period to run (not exceeding six years) on the *policies* in the portfolio. The *Consolidated Life Directive* further limits the maximum amount of these economic reserves that can be counted to 25% of the lesser of the available solvency margin and the required solvency margin. The changes introduced by the *Solvency 1 Directive* take effect for financial years beginning on or after 1 January 2004. However, the *Consolidated Life Directive* allows for a transitional period of five years, which runs from 20 March 2002 (the publication date of the *Solvency 1 Directive*), for *firms* to become fully compliant with these new requirements. ~~*f*~~*Firms* will need to consider the potential impact of these changes when engaging in future capital planning. When applying for an *implicit item waiver* a *firm* should provide the ~~appropriate regulator~~ *PRA* with a plan showing how the *firm* intends to maintain its capital adequacy over the period to 31 December 2009. ~~*f*~~*Firms* should also be aware that the ~~appropriate regulator~~ *PRA* will typically only grant *waivers* for a maximum of 12 months.
…	
Zillmerisation	
7	*Zillmerisation* is an allowance for acquisition costs that are expected, under prudent assumptions, to be recoverable from future *premiums*. ~~*f*~~*Firms* can make a direct adjustment to their reserves for *zillmerisation*, subject to the *rules* on *mathematical reserves*. However, where no such adjustment has been made, the ~~appropriate regulator~~ *PRA* will consider an application for a *waiver* to take into account an *implicit item*.
…	
Process for applying for a waiver, including limits applicable when a waiver is granted	
9	This annex sets out the procedures to be followed and the form of calculations and data which should be submitted by *firms* to the ~~appropriate regulator~~ *PRA*. This *guidance* should also be read in conjunction with the general requirements relating to the *waiver* process described in *SUP 8*. The ~~appropriate regulator~~ *PRA* expects that applications for *waivers* in respect of future profits and *zillmerising* will not normally be considered to pass the ~~"not result in undue risk to persons whose interests the *rules* are intended to protect"~~ "would not adversely affect the advancement of any of the *PRA*'s objectives" test unless the relevant criteria set out in this *guidance* have been satisfied and an application for such a *waiver* may require further criteria to be satisfied for

	this test to be passed. As set out below, *waivers* in respect of either *zillmerising* or hidden reserves will not normally be given except in very exceptional circumstances.
Timing	
10	A *long-term insurer* may apply to the ~~appropriate regulator~~ *PRA* for a *waiver* in respect of *implicit items*. A *capital resources* *waiver* will not apply retrospectively (see *SUP 8.3.6 G*). Consequently, applications intended for a particular accounting reference date will normally need to be made well before that reference date. Applications by *firms* must be made to the ~~appropriate regulator~~ *PRA* in writing and include the relevant details specified under *SUP 8.3.3 D*. Given the uncertainty in predicting the future, *waivers* will normally be granted for a maximum of 12 months at a time and any further applications will need to be made accordingly.
11	The information that will be required to enable an application to be considered as set out below, should normally include a demonstration of how the *capital resources requirement* is to be met, with and without the *waiver*. Clearly, up-to-date information may not be available before the *financial year*-end. In some cases information from the previous year-end's *return* may be used, as long as any known significant changes in the structure of the *firm*, or the assumptions used, have been taken into account.
12	If the application for a *waiver* is granted, when a *firm* submits its next *return* the amount of the *implicit item* shown should not exceed that supported by the *firm's* calculations as at the valuation date. In the event that the amount of the future profits item calculated by the *firm* based on these updated assumptions is less than the amount calculated at the time of the *firm's* *waiver* application, the lower figure should be used in the *return*.
13	An *implicit item* *waiver* in respect of *zillmerising* or hidden reserves is related to the basis on which liabilities or assets have been valued. In the case of hidden reserves, as explained below, the granting of a *waiver* will be dependent on the overall *capital resources* of the *firm*. *Waivers* in respect of these *implicit items* will, therefore, only be made in relation to the position shown in a particular set of *returns* and it will be essential for *firms* to submit applications to the ~~appropriate regulator~~ *PRA* well in advance of the latest date for the submission of the relevant *return*.
14	*Waivers* may be withdrawn by the ~~appropriate regulator~~ *PRA* at any time (e.g. where the ~~appropriate regulator~~ *PRA* considers the amount in respect of which a *waiver* has been given can no longer be justified). This may be as a result of changes in the *firm's* position or as a result of queries arising on scrutiny of the *returns*.
Information to be submitted	
15	An application for a *capital resources* *waiver* (which includes an application for an extension to or other variation of a *waiver*) should be prepared using the standard application form for a *capital resources* (see *SUP 8 Annex 2 D*). In addition, the application should be accompanied by full supporting information to enable the ~~appropriate regulator~~ *PRA* to arrive at a decision on the merits of the case. In particular, the application should state clearly the nature and the amounts of the *implicit items* that a *firm* wishes to count against its *capital resources requirement* and whether it proposes to treat the *implicit item* as *tier one capital* or *tier two capital*. In order to assess an

	application, the ~~appropriate regulator~~ PRA needs information as to the make-up of the *firm's capital resources*, the quality of the capital items which have been categorised into each tier of capital and a breakdown of capital both within and outside the *firm's long-term insurance fund* or *funds* and between the *firm's with-profits funds* and *non-profit funds*. An explanation as to the appropriateness of the proposed treatment of the *implicit item* under the *capital resources table* should also be provided, including a demonstration that, in allowing for *implicit items*, there has been no double counting of future margins and that the basis for valuing such margins is prudent.
	…
17	As a minimum, applications for a future profits *implicit item* *waiver* should be supported by the information contained in Forms 13, 14, 18, 19, 40, 41, 42, 48, 49, the answers to questions 1 to 12 of the abstract of the valuation report, Appendix 9.4 of *IPRU(INS)*, the abstract of the valuation report for the realistic valuation, Appendix 9.4A of *IPRU(INS)* and Forms 51, 52, 53, 54 and 58. For a *zillmerisation* ~~implicit item~~ *implicit item* *waiver*, only those items noted above forming part of the abstract valuation report will normally be needed. Applications for a *waiver* in respect of a hidden reserves *implicit item* will normally be considered only if accompanied by the information which is contained in the annual regulatory *returns*. In particular, the balance sheet forms, *long-term insurance business* revenue accounts, and abstract of the valuation report as set out in Appendices 9.1, 9.3 and 9.4 of *IPRU(INS)* should be provided. This is not to say that a full regulatory *return* must be provided in the specified format, simply that the information contained in these forms should be provided. Where appropriate, the information may be summarised.
18	The following supporting information relating to the calculation of the amounts claimed should be supplied for each type of *implicit item* in respect of which a *waiver* is sought: Future profits: in addition to information related to the prospective calculation and retrospective calculation described below, the profits reported in each of the last five *financial years* up to the date of the most recent available valuation under *rule* 9.4 of *IPRU(INS)* which has been submitted to the ~~appropriate regulator~~ *PRA* prior to, or together with, the application, and the amounts and nature of any exceptional items left out of account; the method used for calculating the average period to run and the results for each of the main categories of business, both before and after allowing for premature termination (where the calculation has been made in two stages); and the basis on which this allowance has been made. *Zillmerising*: the categories of contracts for which an item has been calculated and the percentages of the *relevant capital sum* in respect of which an adjustment has been made. Hidden reserves: particulars, with supporting evidence, of the undervaluation of assets for which recognition is sought.
Continuous monitoring by firms	
19	*Firms* should take into account any material changes in financial conditions or other relevant circumstances that may have an impact on the level of future profits that can prudently be taken into account. ~~f~~*Firms* should also re-evaluate whether an application to vary an *implicit item waiver* should be made whenever circumstances have changed. In the event that circumstances have changed such that an amendment is appropriate, the *firm* must contact the ~~appropriate regulator~~ *PRA* as quickly as possible in accordance with Principle 11. (See *SUP 8.5.1 R*). In this context, the ~~appropriate regulator~~ *PRA* would expect notice of any matter that materially

	impacts on the *firm's* financial condition, or any *waivers* granted.
Future profits - factors to take into account when submitting calculations to support waiver applications	
	…
21	~~*f*~~*Firms* need to assess prospective future profit (i.e. how much can reasonably be expected to arise) and compare this to maximum limits (in article 27(4) of the *Consolidated Life Directive*), which relate to past profits.
Future profits - prospective calculation	
22	The application for a *waiver* should be supported by details of a prospective calculation of future profits arising from in-force business. The information supplied to the ~~appropriate regulator~~ *PRA* should include a description of the method used in the calculation and of the assumptions made, together with the results arising. From 31 December 2009 at the latest, future profits *implicit items* will no longer be permitted under the *Consolidated Life Directive*. Where a *firm* first applies for an *implicit item waiver* after *GENPRU 2.2* comes into effect, under the prospective calculation a *firm* should only take into consideration future profits that are expected to emerge in the period up to 31 December 2009. *Implicit item waivers* granted before *GENPRU 2.2* comes into effect will continue to operate under the terms of those *waivers*, but an application to vary the terms of such a *waiver*, for example to extend the effective period, is an application for a new *waiver* for which a *firm* should usually only take into consideration future profits that are expected to emerge in the period up to 31 December 2009.
Assumptions	
23	The assumptions made should be prudent, rather than best estimate, assumptions of future experience (that is, the prudent assumptions should allow for the fair market price for assuming that risk including associated expenses). In particular, it would not normally be considered appropriate for the projected return on any asset to be taken to be higher than the risk-free yield (that is, assessed by reference to the yield arrived at using a model of future risk free yields properly calibrated from the forward gilts market). It may also be appropriate to bring future withdrawals into account on a suitably prudent basis. For *with-profits business*, the assumptions for future investment returns should not capitalise future bonus loadings except where the with-profits *policyholders* share in risks other than the investment performance of the fund. Furthermore, the rate at which future profits are discounted should include an appropriate margin over a risk free rate of return. Calculations should also be carried out to demonstrate that the prospective calculation of the future profits arising from the in-force business supporting the application for the *implicit item* *waiver* would be sufficient to support the amount of the *implicit item* under each scenario described for use in determining the *resilience capital requirement* - where the *waiver* relates to an *implicit item* allocated to more than one fund, this should be demonstrated separately for that element of the *implicit item* allocated to each fund. For an *implicit item* allocated to a *with-profits fund*, proper allowance should be made for any shareholder transfers to ensure that the *implicit item* is not supported by future profits which will be required to support those transfers. To the extent, if any, that future profits are dependent on the levying of explicit expense related charges (for example as in the case of unit-linked business) the documentation submitted should

	include a demonstration of the prudence of the assumptions made as to the level at which future charges will be levied and expenses incurred.

Other limitations on the extent to which waivers for implicit items will be granted to a realistic basis life firm

24	Where a *waiver* in respect of an *implicit item* is granted to a *realistic basis life firm* additional limits may apply by reference to a comparison of *realistic excess capital* and *regulatory excess capital* including allowance for the effect of the *capital resources*. Where the *capital resources* <u>waiver</u> relates to an *implicit item* allocated partly or entirely to a *with-profits fund*, the *waiver* will contain a limitation to the effect that the *regulatory excess capital* for that *with-profits fund*, allowing for the effect of the *capital resources*, may not exceed that fund's *realistic excess capital*. This limitation will apply on an ongoing basis so that, for example, in the case of an *implicit item* allocated to a *with-profits fund*, the amount of the *implicit item* would be limited to zero whenever the *regulatory excess capital* exceeded the *realistic excess capital* of that fund.

Other charges to future profits

25	To avoid double counting, no account should be taken of any future surplus arising from assets corresponding to explicit items which have been counted towards the *capital resources requirement* such as shareholders funds, surplus carried forward or investment reserves. Deductions should be made in the calculation of future surpluses for the impact of any other arrangements which give rise to a charge over future surplus emerging (e.g. financial *reinsurance* arrangements, subordinated loan capital or contingent loan agreements). Deductions should also be made to the extent that any credit has been taken for the purposes of *INSPRU 1.4.45 R (2)* for the present value of future profits relating to non-profit business written in a *non-profit fund*. The information supplied to the ~~appropriate regulator~~ <u>*PRA*</u> should identify the amount and reason for any adjustments made to the calculation of the prospective amount of future profits.
26	The *firm* should confirm to the ~~appropriate regulator~~ <u>*PRA*</u> that the calculations have been properly carried out and that there are no other factors that should be taken into account.

Future profits - retrospective calculation

…

Definition of profits

28	The estimated annual profit should be taken as the average annual surplus arising in the *long-term insurance fund* over the last five *financial years* up to the date of the most recent available valuation which has been submitted to the ~~appropriate regulator~~ <u>*PRA*</u> prior to, or together with, the application. For this purpose, deficiencies arising should be treated as negative surpluses. Where a *firm's financial year* has altered, the surplus arising in a period falling partly outside the relevant five year period should be assumed to accrue uniformly over the period in question for the purpose of estimating the profits arising within the five year period. When there has been a transfer of a block of business into the *firm* (or out of the *firm*) during the period, surplus arising from the transferred block should be included (or excluded) for the full five year period. Where a portion of a block of business is transferred, the surplus included (or excluded) should

	be a reasonable estimate of the surplus arising from the portion transferred.
	…
Double counting	
31	The inclusion of investment income arising from the assets representing the explicit components of *capital resources* (as part of the estimated annual profit for the purpose of determining the future profits *implicit item*) would result in double-counting. If those assets were required to meet the effects of adverse developments, this would automatically result in the cessation of the contribution to profits from the associated investment income. It would clearly not be appropriate for the ~~appropriate regulator~~ *PRA* to grant a *capital resources* *waiver* which would enable a *firm* to meet the *capital resources requirement* on the basis of counting both the capital values of the assets and the value of the income flow which they can be expected to generate.
	…
33	Where there is reason to suspect that the elimination of any such double-counting would reduce a *firm's capital resources* to close to or below the required level, or would otherwise be significant, the ~~appropriate regulator~~ *PRA* will request this information with a view to taking account of this factor in determining the amount of the *implicit item*. Additional information concerning investment income should be furnished with an application for a *waiver*, if a *firm* believes that any double-counting would fall into one of the categories mentioned above.
Average period to run	
34	The average number of years remaining to run on *policies* should be calculated on the basis of the weighted average of the periods for individual *contracts of insurance*, using as weights the actuarial present value of the benefits payable under the contracts. A separate weighted average should be calculated for each of the various categories of contract and the results combined to obtain the weighted average for the portfolio as a whole. Approximate methods of calculation, which the *firm* considers will give results similar to the full calculation, will be accepted. In particular, the ~~appropriate regulator~~ *PRA* will normally accept the calculation of an average period to run for a specific category of contract on the basis of the average valuation factor for future benefits derived from data contained in the abstract of the valuation report in the regulatory *returns*. A *firm* will be asked to demonstrate the validity of the method adopted only where an abnormal distribution of the business in force gives grounds for doubt about its accuracy.
35	Calculations will normally be requested only for the main categories of *insurance business*, accounting for not less than 90% of the *mathematical reserves*, except where there are grounds for expecting that the exclusion of certain categories of *policies* under this provision might have a significant effect on the resulting average period to run. Detailed calculations will not be required where a *waiver* is sought in respect of a low multiple of the annual profits, well within the average period to run for the *firm*.

	…
Definition of period to run	
40	The definition of the period to run and the basis of the allowance for early termination should clearly be considered together. For certain types of contracts (e.g. pension contracts with a range of retirement ages or other options), there is inherent uncertainty about the likely term to run. In such circumstances any estimate for determining the amount of the future profits *implicit item* for which a *waiver* is sought should be based on prudent assumptions tending, if anything, to underestimate the average period to run.
Zillmerising	
41	The ~~appropriate regulator~~ *PRA* does not normally expect to grant a ~~*waivers*~~ *waiver* permitting *implicit items* due to *zillmerisation* except in very exceptional circumstances. *Zillmerisation* is an allowance for acquisition costs that are expected, under prudent assumptions, to be recoverable from future *premiums*. ~~*f*~~*Firms* can make a direct adjustment to their reserves for *zillmerisation*, subject to the requirements on *mathematical reserves* set out in *INSPRU 1.3.43 R*, and this is the usual approach. However, where no such adjustment has been made, or where the maximum adjustment has not been made in the *mathematical reserves*, the ~~appropriate regulator~~ *PRA* will consider an application for an *implicit item* waiver, if the amount is consistent with the amount that would have been allowed as an adjustment to *mathematical reserves* under *INSPRU 1.3.43 R*.
Hidden reserves	
42	The ~~appropriate regulator~~ *PRA* will grant *waivers* permitting *implicit items* due to hidden reserves only in very exceptional circumstances. These items relate to hidden reserves resulting from the underestimation of assets. The *rules* for the valuation of assets and liabilities (see *GENPRU 1.3*) which apply to assets and liabilities other than *mathematical reserves* are based on the valuation used by the *firm* for the purposes of its external accounts, with adjustments for regulatory prudence such as concentration limits for large holdings, and would not normally be expected to contain hidden reserves.
Case studies on "unduly burdensome"	
43	Some examples of situations where the existing *rules* might be considered to be unduly burdensome are given below:
•	A *firm* writes *with-profits business*. The *firm's* investment policy is affected by its published financial position. Application of the *rules* without an *implicit item* waiver would result in the *firm* adopting a lower equity backing ratio. It may be possible to demonstrate that, in the circumstances, it would be unduly burdensome to require the *firm* to incur costs (which might prejudice *policyholders*) resulting from the lower equity backing ratio, rather than take allowance for an *implicit item*.
	…

•	A *firm* has a block of in-force business, on which the future profits may be reasonably estimated. Application of the *rules* without an *implicit item* *waiver* would result in a need to obtain additional capital. It may be possible to demonstrate that it is unduly burdensome, having regard to the particular circumstances of the *firm*, to require it to incur the costs involved in the injection of further capital rather than take allowance for an *implicit item*.
	…
Publicity	
45	The ~~appropriate regulator~~ *PRA* will publish the *capital resources* (see *SUP 8.6* and *SUP 8.7*). Public disclosure is standard practice unless the ~~appropriate regulator~~ *PRA* is satisfied that publication is inappropriate or unnecessary (see section 138~~A~~B of the *Act*). Any request that a direction not be published should be made to the ~~appropriate regulator~~ *PRA* in writing with grounds in support, as set out in *SUP 8.6*. Disclosure of a *waiver* will normally be required in the *firm's* annual *returns*.

…

TP 7 ~~**Pillar 3 capital resources**~~

~~-~~	~~-~~	~~**Application**~~
~~7.1~~	~~R~~	~~This section applies to a *BIPRU firm*.~~
~~-~~	~~-~~	~~**Purpose**~~
~~7.2~~	~~G~~	~~This section implements Article 154(4) of the *Banking Consolidation Directive*.~~
~~-~~	~~-~~	~~**Duration**~~
~~7.3~~	~~R~~	~~This section applies until 31 December 2012.~~
~~-~~	~~-~~	~~**Transitional provision**~~
~~7.4~~	~~R~~	~~A *firm* may elect not to apply *GENPRU 2.2.239 R (2)* to *(4)* (50:50 split between deductions from *tier one capital* and *tier two capital*) to *material insurance holdings* acquired before 20 July 2006. If a *firm* elects not to apply *GENPRU 2.2.239 R (2)* to *(4)*, the *firm* must deduct such *material insurance holdings* from the total of *tier one capital* and *tier two capital*.~~ [deleted]

TP 8 **Miscellaneous capital resources definitions for BIPRU firms**

~~Miscellaneous capital resources definitions for BIPRU firms~~

~~-~~	~~-~~	~~**Application**~~	
~~8.1~~	~~R~~	~~This section applies to a *BIPRU firm*.~~	
~~8.2~~	~~R~~	~~Any provision of this section that applies on a consolidated basis under *GENPRU* TP 8.3R applies to any *firm* to which *BIPRU 8* (Group risk - consolidation) applies.~~	
~~-~~	~~-~~	~~**Consolidation**~~	
~~8.3~~	~~R~~	~~A provision of this section applies on a consolidated basis for the purpose of *BIPRU 8* (Group risk -consolidation) to the extent that, and in the same way that, the provision in *BIPRU* to which it relates applies on a consolidated basis.~~	
~~-~~	~~-~~	~~**Specific issues of TONS and other securities**~~	
~~8.4~~	~~R~~	~~A *bank* may treat a *security* forming part of an issue of *securities* listed in *GENPRU* TP 8.5R as eligible for inclusion within stage B of the *capital resources table* (Perpetual non cumulative preference shares) if it would not otherwise be eligible if:~~	
~~-~~	~~-~~	~~(1)~~	~~on 31 December 2006 the *bank* was subject to *IPRU(BANK)*;~~
~~-~~	~~-~~	~~(2)~~	~~the *bank* issued it on or before 31 December 2006; and~~
~~-~~	~~-~~	~~(3)~~	~~as at 31 December 2006 the *bank* included it, and was entitled to include it, in the calculation of its capital resources under *IPRU(BANK)* as permanent share capital and tier one capital as referred to in chapter CA of *IPRU(BANK)*.~~
~~8.5~~	~~R~~	~~The issues of *securities* referred to in *GENPRU* TP 8.4R are as follows:~~	
~~-~~	~~-~~	~~(1)~~	~~Barclays £400mn 6% perpetual TONs;~~
~~-~~	~~-~~	~~(2)~~	~~Abbey National £175m 6.984% perpetual TOPIC;~~
~~-~~	~~-~~	~~(3)~~	~~Northern Rock £200m 7.053% perpetual TONs;~~
~~-~~	~~-~~	~~(4)~~	~~Barclays $1bn 6.86% perpetual TONs;~~
~~-~~	~~-~~	~~(5)~~	~~Lloyds TSB $1000m 6.90% perpetual capital securities; and~~
~~-~~	~~-~~	~~(6)~~	~~Abbey National $500m 7.375% T1MBS.~~
~~-~~	~~-~~	~~**PIBS**~~	
~~8.6~~	~~R~~	~~A *building society* may treat a *PIBS* as eligible for inclusion within stage B of the *capital resources table* (Perpetual non-cumulative preference shares) if it would not otherwise be eligible if:~~	
~~-~~	~~-~~	~~(1)~~	~~on 31 December 2006 the *firm* was subject to *IPRU(BSOC)*;~~

-	-	~~(2)~~	~~the *building society* issued it before 18 November 2004; and~~
-	-	~~(3)~~	~~as at 31 December 2006 the *building society* included it, and was entitled to include it, in the calculation of its capital resources under *IPRU(BSOC)* as tier one capital as referred to in Annex 1A of chapter 1 of volume 1 of *IPRU(BSOC)*.~~
-	-	~~**Preference shares**~~	
~~8.7~~	~~R~~	~~A *bank* or *BIPRU investment firm* may treat a *preference share* as eligible for inclusion within stage B of the *capital resources table* (Perpetual non-cumulative preference shares) if it would not otherwise be eligible if:~~	
-	-	~~(1)~~	~~on 31 December 2006 the *firm* was subject to *IPRU(BANK)* or *IPRU(INV)*;~~
-	-	~~(2)~~	~~the *firm* issued it on or before 31 December 2006;~~
-	-	~~(3)~~	~~as at 31 December 2006 the *firm* included it, and was entitled to include it, in the calculation of its capital resources under *IPRU(BANK)* or *IPRU(INV)* as capital of a type that corresponded to *tier one capital resources*;~~
-	-	~~(4)~~	~~it would have been eligible for inclusion within stage B of the *capital resources table* except for the fact that it does not meet *GENPRU 2.2.64 R (4)(b)* (Restrictions on mandatory *coupons* for *tier one capital*) or *GENPRU 2.2.109 R (1)* (Restrictions on mandatory *coupons* for perpetual non-cumulative *preference shares*) or both of those *rules*;~~
-	-	~~(5)~~	~~the only reason that it does not meet *GENPRU 2.2.64 R (4)(b)* or *GENPRU 2.2.109 R (1)* is because a mandatory cash *coupon* is payable;~~
-	-	~~(6)~~	~~the *firm* has the right not to pay the cash *coupon* if it is in breach of any of the *main BIPRU firm Pillar 1 rules* or to the extent that paying such *coupon* would result in a breach of any of those *rules*; and~~
-	-	~~(7)~~	~~any amount not paid under (6) does not accumulate.~~
-	-	~~**Innovative tier one capital**~~	
~~8.8~~	~~R~~	~~A *bank* may treat an item of a *capital instrument* as eligible for inclusion within stage C of the *capital resources table* (Innovative tier one capital) if it would not otherwise be eligible if:~~	
-	-	~~(1)~~	~~on 31 December 2006 the *firm* was subject to *IPRU(BANK)*;~~
-	-	~~(2)~~	~~the *bank* issued it on or before 31 December 2006;~~
-	-	~~(3)~~	~~as at 31 December 2006 the *bank* included it, and was entitled to include it, in the calculation of its capital resources under *IPRU(BANK)* as innovative tier one capital as referred to in chapter CA of *IPRU(BANK)*;~~
-	-	~~(4)~~	~~it would have been eligible for inclusion within stage C of the *capital resources table* except for the fact that it does not meet *GENPRU*~~

			~~*2.2.64 R (4)(b)* (Restrictions on mandatory *coupons* for *tier one capital*);~~
~~-~~	~~-~~	~~(5)~~	~~the only reason that it does not meet *GENPRU 2.2.64 R (4)(b)* is because a mandatory cash *coupon* is payable;~~
~~-~~	~~-~~	~~(6)~~	~~the *bank* has the right not to pay the cash *coupon* if it is in breach of any of the *main BIPRU firm Pillar 1 rules* or to the extent that paying such *coupon* would result in a breach of any of those *rules*; and~~
~~-~~	~~-~~	~~(7)~~	~~any amount not paid under (6) does not accumulate.~~
~~-~~	~~-~~	~~**Upper tier 2 instruments: Deferral of interest**~~	
~~8.9~~	~~R~~	~~A *bank* or *BIPRU investment firm* may treat a *capital instrument* as eligible for inclusion within stage G of the *capital resources table* (Upper tier two capital) if it would not otherwise be eligible if:~~	
~~-~~	~~-~~	~~(1)~~	~~on 31 December 2006 the *firm* was subject to *IPRU(BANK)* or *IPRU(INV)*;~~
~~-~~	~~-~~	~~(2)~~	~~the *firm* issued it on or before 31 December 2006;~~
~~-~~	~~-~~	~~(3)~~	~~as at 31 December 2006 the *firm* included it, and was entitled to include it, in the calculation of its capital resources under *IPRU(BANK)* or *IPRU(INV)* as capital of a type that corresponded to *upper tier two capital resources*;~~
~~-~~	~~-~~	~~(4)~~	~~it would have been eligible for inclusion within stage G of the *capital resources table* except for the fact that it does not meet *GENPRU 2.2.177 R (2)* ;~~
~~-~~	~~-~~	~~(5)~~	~~the only reason that it does not meet *GENPRU 2.2.177 R (2)* is because a mandatory cash *coupon* is payable; and~~
~~-~~	~~-~~	~~(6)~~	~~the *firm* has the right not to pay the cash *coupon* if it is in breach of any of the *main BIPRU firm Pillar 1 rules* or to the extent that paying such *coupon* would result in a breach of any of those *rules* .~~
~~-~~	~~-~~	~~**Lower tier 2 instruments: Additional events of default for building societies**~~	
~~8.10~~	~~R~~	~~A *building society* may treat a *capital instrument* as eligible for inclusion within stage H of the *capital resources table* (Lower tier two capital) if it would not otherwise be eligible if:~~	
~~-~~	~~-~~	~~(1)~~	~~on 31 December 2006 the *building society* was subject to *IPRU(BSOC)*;~~
~~-~~	~~-~~	~~(2)~~	~~the *building society* issued it on or before 31 December 2006;~~
~~-~~	~~-~~	~~(3)~~	~~as at 31 December 2006 the *building society* included it, and was entitled to include it, in the calculation of its capital resources under *IPRU(BSOC)* as Term Subordinated Debt falling within its Tier Two Capital (as referred to in Annex 1A of Chapter 1 and Chapter 2 of *IPRU(BSOC)*);~~

~~-~~	~~-~~	~~(4)~~	~~it would have been eligible for inclusion within stage H of the *capital resources table* except for the fact that it does not meet *GENPRU 2.2.159 R (2)* (Events of default); and~~	
~~-~~	~~-~~	~~(5)~~	~~the only reason that it does not meet *GENPRU 2.2.159 R (2)* is because it contains an event of default permitted by paragraph 2.8.10G(3) of Volume 1 of *IPRU(BSOC)* (cancellation of a society's registration under the Building Societies Act 1986 otherwise than under section 103(1)(a) of that Act).~~	
~~-~~	~~-~~	~~**Conversion ratio**~~		
~~8.11~~	~~R~~	~~*GENPRU 2.2.138 R (2)* (Tier one capital: Conversion ratio) does not apply to a *capital instrument* issued by a *firm* if:~~		
~~-~~	~~-~~	~~(1)~~	~~on 31 December 2006 the *firm* was subject to *IPRU(BANK)*, *IPRU(BSOC)* or *IPRU(INV)*;~~	
~~-~~	~~-~~	~~(2)~~	~~the *firm* issued it on or before 31 December 2006; and~~	
~~-~~	~~-~~	~~(3)~~	~~as at 31 December 2006 the *firm* included it, and was entitled to include it, in the calculation of its capital resources under:~~	
~~-~~	~~-~~	~~-~~	~~(a)~~	~~(in the case of a *bank*) *IPRU (BANK)* as innovative tier one capital as referred to in chapter CA of *IPRU(BANK)*; or~~
~~-~~	~~-~~	~~-~~	~~(b)~~	~~(in the case of any other type of *firm*) *IPRU(BSOC)* or *IPRU(INV)* as capital of a type that corresponded to *tier one capital*.~~
~~-~~	~~-~~	~~**Legal opinions**~~		
~~8.12~~	~~R~~	~~*GENPRU 2.2.118 R* (Legal opinions for *innovative tier one capital*) does not apply to a *capital instrument* issued by a *firm* if:~~		
~~-~~	~~-~~	~~(1)~~	~~on 31 December 2006 the *firm* was subject to *IPRU(BANK)*, *IPRU(BSOC)* or *IPRU(INV)*;~~	
~~-~~	~~-~~	~~(2)~~	~~the *firm* issued the *capital instrument* on or before 31 December 2006;~~	
~~-~~	~~-~~	~~(3)~~	~~(in the case of a *bank*) as at 31 December 2006 the *bank* included the *capital instrument*, and was entitled to include it, in the calculation of its capital resources under *IPRU(BANK)* as innovative tier one capital as referred to in chapter CA of *IPRU(BANK)*; and~~	
~~-~~	~~-~~	~~(4)~~	~~(in any other case) the *firm* included the *capital instrument*, and was entitled to include it, in the calculation of its capital resources under *IPRU(BSOC)* or *IPRU(INV)* as capital of a type that corresponded to *tier one capital*.~~	
~~8.13~~	~~R~~	~~The following *rules*:~~		
~~-~~	~~-~~	~~(1)~~	~~*GENPRU 2.2.159 R (12)* (Legal opinions for *tier two capital*);~~	
~~-~~	~~-~~	~~(2)~~	~~*GENPRU 2.2.163 R* (Legal opinions for *tier two capital* governed by a~~	

			~~foreign law);~~		
-	-	~~(3)~~	~~*GENPRU 2.2.181 R* (Legal opinions for *upper tier two capital*); and~~		
-	-	~~(4)~~	~~*GENPRU 2.2.244 R* (Application of certain *rules* about *tier two capital* to *tier three capital*) so far as it applies the *rules* in (1) to (3);~~		
-	-	~~do not apply to a *capital instrument* issued by a *firm* if:~~			
-	-	~~(5)~~	~~on 31 December 2006 the *firm* was subject to *IPRU(BANK)*, *IPRU(BSOC)* or *IPRU(INV)*;~~		
-	-	~~(6)~~	~~the *firm* issued the *capital instrument* on or before 31 December 2006; and~~		
-	-	~~(7)~~	~~as at 31 December 2006 the *firm* included the *capital instrument*, and was entitled to include it, in the calculation of its capital resources under *IPRU(BANK)*, *IPRU(BSOC)* or *IPRU(INV)* as capital of the type that corresponds to:~~		
-	-	-	~~(a)~~	~~(where the *firm* disapplies the *rule* in (1) or (2)) *tier two capital*; or~~	
-	-	-	~~(b)~~	~~(where the *firm* disapplies the *rule* in (3)) *upper tier two capital*; or~~	
-	-	-	~~(c)~~	~~(where the *firm* disapplies the *rule* in (4)) *tier three capital*.~~	
-	-	~~**Version of IPRU**~~			
~~8.14~~	~~R~~	~~Any reference in this section to a type of capital in *IPRU* is to a type of capital in *IPRU* in the form *IPRU* was in on 31 December 2006.~~			
-	-	~~**Eligibility**~~			
~~8.15~~	~~G~~	~~If this section says that an item of capital is eligible for inclusion within a particular stage of the *capital resources table* this is still subject to the application of the *capital resources gearing rules*.~~			
-	-	~~**Waivers and concessions**~~			
~~8.16~~	~~G~~	~~A reference to a *firm* being entitled to include *capital instruments* in the calculation of its capital resources under *IPRU* at a particular level includes the *firm* being able to do this under a *waiver* or, in the case of *IPRU(BANK)* or *IPRU(BSOC)*, a written approval by the *appropriate regulator* .~~			
-	-	~~**Combinations of provisions**~~			
~~8.17~~	~~G~~	~~A *firm* may combine the use of two or more of the provisions in this section.~~			

[deleted]

TP 8A **Further miscellaneous capital resources definitions for BIPRU firms**

~~Further miscellaneous capital resources definitions for BIPRU firms~~

~~**Application and interpretation**~~				
~~8A.1~~	~~R~~	~~This section applies to a *BIPRU firm*. In this section a reference to 30 December 2010 means 23.59 on 30 December 2010.~~		
~~**Tier one capital**~~				
~~8A.2~~	~~R~~	~~Until 31 December 2040 a *BIPRU firm* may treat a *capital instrument* as eligible for inclusion as *hybrid capital*, if it would not otherwise be eligible, if:~~		
~~-~~	~~-~~	~~(1)~~	~~on 30 December 2010 the *BIPRU firm* was subject to *GENPRU*; and~~	
~~-~~	~~-~~	~~(2)~~	~~as at 30 December 2010 the *BIPRU firm* included it, and was entitled to include it, at stage B or C of the calculation in the *capital resources table*.~~	
~~8A.3~~	~~R~~	~~If a *BIPRU firm* treats a *capital instrument* as eligible for inclusion as *hybrid capital* under *GENPRU TP8A.2R* , then the *firm*:~~		
~~-~~	~~-~~	~~(1)~~	~~if it included the *capital instrument* as *innovative tier one capital* as at 30 December 2010, must treat the *capital instrument* as *hybrid capital* included at stage C of the calculation in the *capital resources table*;~~	
~~-~~	~~-~~	~~(2)~~	~~except where it is a *building society*, must apply the limit in *GENPRU 2.2.30A R (3)* to the aggregate of the *capital instruments* treated under (1) and the *hybrid capital* that is eligible under *GENPRU 2.2* for inclusion at stage C of the calculation in the *capital resources table*;~~	
~~-~~	~~-~~	~~(3)~~	~~in the case of a *building society*, must not include *hybrid capital* at stage C of the calculation in the *capital resources table* under *GENPRU 2.2*, except as provided by (4), if the amount of *PIBS* with incentives to redeem treated under *GENPRU TP8A.2R* exceeds the limit in *GENPRU 2.2.30A R (3)*;~~	
~~-~~	~~-~~	~~(4)~~	~~in the case of a *building society*, may include *hybrid capital* at stage C of the calculation in the *capital resources table*, notwithstanding (3), if the *firm* issued it after 30 December 2010 and:~~	
~~-~~	~~-~~	~~-~~	~~(a)~~	~~the *capital instrument* would otherwise be eligible for inclusion as *hybrid capital* at stage C of the calculation in the *capital resources table* under *GENPRU 2.2*; and~~
~~-~~	~~-~~	~~-~~	~~(b)~~	~~the *firm* issued it in order to replace a *PIBS* with an incentive to redeem that the *firm* treated as *hybrid capital* under *GENPRU TP8A.2R* ;~~
~~-~~	~~-~~	~~(5)~~	~~must not include *hybrid capital* at stage B2 of the calculation in the *capital resources table* under *GENPRU 2.2*, except as provided by *GENPRU TP8A.4R*, if and to the extent that the aggregate of the following exceeds the limit in *GENPRU 2.2.30A R (2)*~~	
~~-~~	~~-~~	~~-~~	~~(a)~~	~~*capital instruments* included at stage C in the *capital resources table* under (1) and *GENPRU 2.2* ; and~~
~~-~~	~~-~~	~~-~~	~~(b)~~	~~*capital instruments* included at stage B of the calculation in the *capital resources table* as at 30 December 2010 and treated under *GENPRU*~~

				~~*TP8A.2R* ;~~
-	-	~~(6)~~		~~if it includes *hybrid capital* at stage B2 of the calculation in the *capital resources table* under *GENPRU 2.2*, except as provided by *GENPRU TP8A.4R*, must include *capital instruments* treated under *GENPRU TP8A.2R* in the calculation of the limit in *GENPRU 2.2.30A R (2)*;~~
-	-	~~(7)~~		~~must not include *hybrid capital* at stage B1 of the calculation in the *capital resources table* under *GENPRU 2.2*, except as provided by *GENPRU TP8A.5R*, if and to the extent that the aggregate of the following exceeds the limit in *GENPRU 2.2.30A R (1)* :~~
-	-	-	~~(a)~~	~~*capital instruments* included at stage C in the *capital resources table* under (1) and*GENPRU 2.2*; and~~
-	-	-	~~(b)~~	~~*capital instruments* included at stage B of the calculation in the *capital resources table* as at 30 December 2010 and treated under *GENPRU TP8A.2R* ; and~~
-	-	~~(8)~~		~~if it includes *hybrid capital* at stage B1 of the calculation in the *capital resources table* under *GENPRU 2.2*, except as provided by *GENPRU TP8A.5R*, must include *capital instruments* treated under*GENPRU TP8A.2R* in the calculation of the limit in *GENPRU 2.2.30A R (1)*.~~
~~8A.4~~	~~R~~	~~A *BIPRU firm* may include *hybrid capital* at stage B2 of the calculation in the *capital resources table*, notwithstanding *GENPRU TP8A.3R(5)*, if the *firm* issued it after 30 December 2010 and:~~		
-	-	~~(1)~~		~~the *capital instrument* would otherwise be eligible for inclusion as *hybrid capital* at stage B2 of the calculation in the *capital resources table* under *GENPRU 2.2*; and~~
-	-	~~(2)~~		~~the *firm* issued it in order to replace another *capital instrument* that the *firm* treated as *hybrid capital* under *GENPRU TP8A.2R*.~~
~~8A.5~~	~~R~~	~~A *BIPRU firm* may include *hybrid capital* at stage B1 of the calculation in the *capital resources table*, notwithstanding *GENPRU TP8A.3R(7)*, if the *firm* issued it after 30 December 2010 and:~~		
-	-	~~(1)~~		~~the *capital instrument* would otherwise be eligible for inclusion as *hybrid capital* at stage B1 of the calculation in the *capital resources table* under *GENPRU 2.2*; and~~
-	-	~~(2)~~		~~the *firm* issued it in order to replace another *capital instrument* that the *firm* treated as *hybrid capital* under *GENPRU TP8A.2R*.~~
~~8A.6~~	~~R~~	~~In relation to the *tier one capital resources* of a *BIPRU firm*, calculated at stage F of the calculation in the *capital resources table* (Total tier one capital after deductions):~~		
-	-	~~(1)~~		~~from 31 December 2020 until 30 December 2030:~~
-	-	-	~~(a)~~	~~no more than 20% may be accounted for by items treated under *GENPRU TP8A.2R* as *tier one capital*; and~~
-	-	-	~~(b)~~	~~in the case of a *building society*, any *PIBS* with an incentive to redeem~~

				~~treated under *GENPRU TP8A.2R* is to be treated as *hybrid capital* included at stage C of the calculation in the *capital resources table* and as subject to the limit in *GENPRU 2.2.30A R (3)*; and~~
-	-	~~(2)~~	~~from 31 December 2030 until 30 December 2040, no more than 10% may be accounted for by items treated under *GENPRU TP8A.2R* as *tier one capital*.~~	
~~8A.7~~	~~R~~	~~*BIPRU firms* which do not comply by 31 December 2010 with the limits set out in *GENPRU 2.2.29 R* to *GENPRU 2.2.30A R (3)* must develop strategies and processes on the necessary measures to resolve this situation before the dates set out in *GENPRU TP8A.6R* .~~		

[deleted]

TP 8B Miscellaneous capital resources definitions for BIPRU firms: Core tier one capital

~~Miscellaneous capital resources definitions for BIPRU firms: Core tier one capital~~

~~**Application**~~				
~~8B.1~~	~~R~~	~~This section applies to a *BIPRU firm*.~~		
~~**Core tier one capital**~~				
~~8B.2~~	~~R~~	~~A provision in this section applies on a consolidated basis for the purposes of *BIPRU 8* (Group risk - consolidation) to a *UK consolidation group* to the extent that, and in the same manner that, the provision in *GENPRU* to which it relates applies on a consolidated basis.~~		
~~8B.3~~	~~R~~	~~The Royal Bank of Scotland plc may treat a *share* falling within *GENPRU TP 8B.4R* as eligible for inclusion within stage A of the *capital resources table* (Core tier one capital) if it would not otherwise be eligible provided that:~~		
-	-	~~(1)~~	~~the *share*:~~	
-	-	-	~~(a)~~	~~had been issued on or before 30 December 2010; or~~
-	-	-	~~(b)~~	~~if issued after that date, is issued pursuant to a contractual obligation requiring its issue entered into on or before 30 December 2010;~~
-	-	~~(2)~~	~~as at 30 December 2010 The Royal Bank of Scotland plc was entitled (or would have been entitled, had the *share* then been issued) to include it in the calculation of its *capital resources* under *GENPRU* as *permanent share capital* and, in the case of a *share* which had been issued as at that date, did so include it; and~~	
-	-	~~(3)~~	~~the *share* is held by or on behalf of the Government of the *United Kingdom*.~~	
~~8B.4~~	~~R~~	~~The *shares* referred to in *GENPRU TP 8B.3R* are as follows:~~		
-	-	~~(1)~~	~~The Royal Bank of Scotland Group plc Series 1 Class B Shares of 1p each; and~~	

~~-~~	~~-~~	~~(2)~~	~~The Royal Bank of Scotland Group plc Series 1 Dividend Access Share of 1p;~~
~~-~~	~~-~~	~~either as separate instruments or considered together as connected instruments~~	
~~Voting rights~~			
~~8B.5~~	~~R~~	~~A *BIPRU firm* may treat an ordinary *share* that has different voting rights to other ordinary *shares* issued by the *firm* as eligible for inclusion within stage A of the *capital resources table* (Core tier one capital) without making a notification of issue or change in voting rights to the *appropriate regulator* under *GENPRU 2.2.83B R* if:~~	
~~-~~	~~-~~	~~(1)~~	~~on 30 December 2010 the *firm* was subject to *GENPRU*;~~
~~-~~	~~-~~	~~(2)~~	~~the *firm* issued the ordinary *share* on or before 30 December 2010 and the shareholders were bound by the differences in voting rights on or before 30 December 2010; and~~
~~-~~	~~-~~	~~(3)~~	~~as at 30 December 2010 the *firm* included the ordinary *share*, and was entitled to include it, in the calculation of *capital resources* under *GENPRU* as *permanent share capital*;~~
~~-~~	~~-~~	~~provided that by 30 June 2011 the *firm* provides the *appropriate regulator* with full details of the ordinary *shares*, their terms of issue and the differences in voting rights applicable to those ordinary *shares*.~~	

[deleted]

~~TP 9~~ **~~Individual capital guidance for BIPRU firms~~**

~~Individual capital guidance for BIPRU firms~~

~~-~~	~~-~~	**~~Application~~**	
~~9.1~~	~~G~~	~~This section applies to a *BIPRU firm* that is a *bank* or *building society* for which the *FSA* has given:~~	
~~-~~	~~-~~	~~(1)~~	~~(in the case of a *building society*) a threshold ratio under *IPRU(BSOC)*; or~~
~~-~~	~~-~~	~~(2)~~	~~(in the case of a *bank*) an individual capital ratio under *IPRU(BANK)*;~~
~~-~~	~~-~~	~~that was in effect on 31 December 2006 but to which the *FSA* has not yet given *individual capital guidance*.~~	
~~-~~	~~-~~	**~~Duration~~**	
~~9.2~~	~~G~~	~~This section applies to a *firm* until it receives *individual capital guidance*.~~	

~~9.3~~	~~G~~	~~GENPRU TP 9.4G - GENPRU TP 9.6G only apply until 31 December 2007. Thereafter (if they do not already apply) GENPRU TP 9.7G - GENPRU TP 9.10G apply.~~	
-	-	**~~Pre 2007 capital requirements~~**	
~~9.4~~	~~G~~	~~GENPRU TP 9.5G - GENPRU TP 9.6G apply if, and for as long as, a *firm* applies the treatment in *BIPRU TP 3* (Pre CRD capital requirements applying on a solo basis during 2007) to all its *exposures*.~~	
~~9.5~~	~~G~~	~~If GENPRU TP 9.4G applies, any threshold ratio or individual capital ratio remains in force. However compliance with such ratios should be measured by reference to *capital resources*.~~	
~~9.6~~	~~G~~	~~Where necessary, a *firm* should apply the adjustment set out in section 4.1.3 of chapter CO of *IPRU(BANK)* (CAD banks) as it stood on 31 December 2006 to its *trading book* capital requirements.~~	
-	-	**~~BIPRU capital requirements~~**	
~~9.7~~	~~G~~	~~GENPRU TP 9.8G - GENPRU TP 9.10G apply to a *firm* if GENPRU TP 9.5G - GENPRU TP 9.6G do not apply.~~	
~~9.8~~	~~G~~	~~Any threshold ratio or individual capital ratio remains in force adjusted as follows:~~	
-	-	~~(1)~~	~~the *firm* should work out the percentage of its *capital resources requirement* as at the date in GENPRU TP 9.10G represented by the absolute amount in GENPRU TP 9.9G; and~~
-	-	~~(2)~~	~~the *firm* should hold *capital resources* of an amount at least equal to the percentage specified in (1) of its *capital resources requirement* from time to time.~~
~~9.9~~	~~G~~	~~The absolute amount referred to in GENPRU TP 9.8G is:~~	
-	-	~~(1)~~	~~(if GENPRU TP 9.7G - GENPRU TP 9.10G apply to the *firm* on 1 January 2007) the amount of capital resources it had to hold under *IPRU* on 31 December 2006 in order to meet the ratio referred to in GENPRU TP 9.1G; and~~
-	-	~~(2)~~	~~(in any other case) the amount of *capital resources* it had to hold immediately prior to the date in GENPRU TP 9.10G in order to meet the ratio referred to in GENPRU TP 9.1G.~~
~~9.10~~	~~G~~	~~The date referred to in GENPRU TP 9.8G and GENPRU TP 9.9G is:~~	
-	-	~~(1)~~	~~(if GENPRU TP 9.9G(1) applies) 1 January 2007; and~~
-	-	~~(2)~~	~~(if GENPRU TP 9.9G(2) applies) the date on which GENPRU TP 9.7G - GENPRU TP 9.10G first apply to the *firm*.~~

~~9.11~~	~~G~~	~~The following illustrates how GENPRU TP 9.8G - GENPRU TP 9.10G work. This example relates to a *bank* to which GENPRU TP 9.7G - GENPRU TP 9.10G apply from 1 January 2007. The example is as follows (all figures in £millions):~~		
-	-	~~(1)~~	~~as at 31 December 2006:~~	
-	-	-	~~(a)~~	~~the *bank* has risk-weighted assets of £1250;~~
-	-	-	~~(b)~~	~~its Pillar 1 capital resources requirement was £100 (8% of £1250);~~
-	-	-	~~(c)~~	~~its individual capital ratio was 10%; and~~
-	-	-	~~(d)~~	~~its capital resources requirement expressed as an absolute amount and including the individual capital ratio is £125;~~
-	-	~~(2)~~	~~on 1 January 2007 its *capital resources requirement* is £80;~~	
-	-	~~(3)~~	~~the result is that the new individual capital ratio is 156.25% (£125m/£80m); and~~	
-	-	~~(4)~~	~~its capital resources requirement expressed as an absolute amount and including the individual capital ratio remains at £125 despite the fall in the Pillar 1 charge.~~	
~~9.12~~	~~G~~	~~Continuing the example, say that the *bank's capital resources requirement* falls to £70 on 31 July 2007. Its capital resources requirement, expressed as an amount and including the individual capital ratio, now falls to £109.375.~~		
-	-	~~**Adjustments**~~		
~~9.13~~	~~G~~	~~No adjustment should be made to take into account differences between the calculation of capital resources under *IPRU* and of *capital resources*.~~		
-	-	~~**Consolidation**~~		
~~9.14~~	~~G~~	~~This section also applies to threshold ratios and individual capital ratios that apply on a consolidated basis.~~		

[deleted]

…

Sch 2 **Notification and reporting requirements**

G

…

3 Table

Handbook reference	Matter to be notified	Contents of notification	Trigger events	Time allowed
…				
~~*GENPRU 2.2.19 R*~~	~~Intention to deduct *illiquid assets* rather than *material holdings*~~	~~Fact of intention~~	~~Intention to start or stop using method in column 2~~	~~One month prior to change of method~~ [deleted]
…				
~~*GENPRU 2.2.79G R*~~	~~Intention to purchase a *tier one instrument* in accordance with *GENPRU 2.2.79A R*~~	~~Fact of intention and details of the *firm's* position after the purchase in order to show how, over an appropriate timescale, adequately stressed, and without planned recourse to the capital markets, it will meet its *capital resources requirement* and have sufficient financial resources to meet the *overall financial adequacy rule*~~	~~Intention to purchase~~	~~At least one month prior to becoming committed to purchase~~ [deleted]
~~*GENPRU 2.2.83B R*~~	~~Intention to include in stage A of the *capital resources table* different classes of the same *share* type that meet the conditions in *GENPRU 2.2.83 R* and *GENPRU 2.2.83A R* but have differences in voting rights.~~	~~Fact of intention.~~	~~Intention to include in stage A of the *capital resources table* classes of the same *share* type that have different voting rights.~~	~~At least one month before the *shares* are issued or (in the case of existing issued *shares*) the differences in voting rights take effect.~~ [deleted]
~~*GENPRU 2.2.83F R*~~	~~Intention by a *building society* to issue a *capital instrument* that includes a *coupon* limit in its terms of issuance in accordance with *GENPRU 2.2.83E*~~	~~Fact of intention.~~	~~Intention to issue a *capital instrument* that includes a *coupon* limit.~~	~~At least one month before the intended date of issue.~~ [deleted]

	~~*R.*~~			
~~*GENPRU 2.2.135 R*~~	~~Intention to include an unusual transaction in capital under *GENPRU 2.2.124 R*~~	~~Fact of intention.~~	~~Intention to include in capital~~	~~At least one month prior to inclusion of that capital in *capital resources*~~ [deleted]
…				
~~*GENPRU 2.2.243 R*~~	~~Intention to pay interest or principal on subordinated debt included in *tier three capital resources* if the *firm's capital resources* are less than 120% of its *capital resources requirement*~~	~~Fact of intention~~	~~Intention to pay~~	~~One month prior to any payment of interest or principal~~ [deleted]
~~*GENPRU 2.2.245 R*~~	~~Intention to repay (other than on contractual repayment date) *tier three capital resources*~~	~~Fact of intention and details of how the *firm* will meet its *capital resources requirement* after such repayment~~	~~Intention to repay~~	~~One month prior to repayment~~ [deleted]

Annex B

Amendments to the Prudential sourcebook for Banks, Building Societies and Investment Firms (BIPRU)

The entirety of BIPRU is deleted save for:

- BIPRU 12;
- BIPRU, Schedule 3; and
- BIPRU Schedule 6.

Appendix 2

Supervisory Statements

Introduction

This appendix sets out proposed supervisory statements which, alongside the proposed rules (in Appendix 1), form part of the Prudential Regulation Authority's (PRA's) implementation of CRD IV, consisting of the Capital Requirements Regulation(1) (CRR) and the Capital Requirements Directive(2) (CRD).

The statements are aimed at firms to whom the CRD IV package applies — banks, building societies and PRA-designated investment firms respectively. Each statement sets out the relevant articles of the CRR and/or CRD that form the basis of the explanatory material and refers to any relevant proposed rules. Firms are advised to read these statements in conjunction with the related CRR and CRD material and proposed rules in order to fully understand the PRA's proposed approach to implementing CRD IV.

Firms should note that PRA Rulebook references are made as follows: [Part] [Rule] eg Internal Capital Adequacy Assessment 3.1.

(1) Regulation (EU) No 575/2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms.
(2) Directive 2013/36/EU of the European Parliament and of the Council on the access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms.

1 Pillar 2

The Internal Capital Adequacy Assessment Process (ICAAP) and the Supervisory Review and Evaluation Process (SREP)

1 Introduction

1.1 This supervisory statement is aimed at firms to which CRD IV applies.

1.2 The purpose of this supervisory statement is to set out the expectations that the PRA has in relation to the Internal Capital Adequacy Assessment Process (ICAAP) and the requirements set out in the PRA Rulebook in the Internal Capital Adequacy Assessment rules.

1.3 It provides further detail in relation to the high-level expectations outlined in *The PRA's approach to banking supervision* (April 2013).

1.4 The PRA will review a firm's ICAAP as part of its SREP, and this supervisory statement also sets out some of the factors that the PRA will take into consideration during the SREP.

1.5 In addition, this supervisory statement sets out the PRA's expectations with regard to firms' coverage and treatment of interest rate risk arising in the non-trading book, group risk and operational risk.

2 Expectations of firms undertaking an ICAAP

2.1 A firm must carry out an ICAAP in accordance with the PRA's ICAAP rules. These include requirements on a firm to undertake a regular assessment of the amounts, types and distribution of capital that it considers adequate to cover the level and nature of the risks to which it is or might be exposed. This assessment should cover the major sources of risks to the firm's ability to meet its liabilities as they fall due and incorporate stress testing and scenario analysis. The ICAAP should be documented and updated annually by the firm or more frequently if changes in the business, strategy, nature or scale of its activities or operational environment suggest that the current level of financial resources is no longer adequate.

2.2 The PRA expects firms in the first instance to take responsibility for ensuring that the capital they have is adequate, with the ICAAP being an integral part of meeting this expectation. The PRA expects the ICAAP to be the responsibility of a firm's governing body, that it is reviewed and signed-off by the governing body, and that it is used as an integral part of the firm's management process and decision-making culture. The processes and systems used to produce the ICAAP should ensure that the assessment of the adequacy of a firm's financial resources is reported to its governing body and senior management as often as is necessary.

2.3 The ICAAP, and supporting processes and systems, should be proportionate to the nature, scale and complexity of the activities of a firm, as set out in Internal Capital Adequacy Assessment 3.3. Where a firm has identified risks as not being material, it should be able to provide evidence of the assessment process that determined this and discuss why that conclusion has been reached.

2.4 Liquidity risk should also be assessed, including in relation to potential losses arising from the liquidation of assets and increases in the cost of funding during periods of stress. The requirements in relation to liquidity risk may be found in BIPRU 12.

2.5 As outlined in the supervisory statement on stress testing, the PRA expects firms to develop a framework for stress testing, scenario analysis and capital management that captures the full range of risks to which they are exposed and enables these risks to be assessed against a range of plausible yet severe scenarios. The ICAAP should outline how stress testing supports capital planning for the firm.

2.6 Where a firm uses a model to aid its assessment of the level of adequate capital, it should be appropriately conservative and should contribute to prudent risk management and measurement. The firm should expect the PRA to investigate the structure, parameterisation and governance of the model, and the PRA will seek reassurance that the firm understands the attributes, outputs and limitations of the model, and that it has the appropriate skills and expertise to operate, maintain and develop the model.

3 The SREP

3.1 The SREP is a process by which the PRA will, taking into account the nature, scale and complexity of the firm's activities: review the arrangements, strategies, processes and mechanisms implemented by a firm to comply with its regulatory requirements laid down in PRA rules and the CRR; evaluate the risks to which the firm is or might be exposed; and assess the risks that a firm poses to the financial system and the risks revealed by stress testing.

3.2 As part of its SREP, the PRA will review the firm's ICAAP and have regard to the risks outlined in the overall Pillar 2 rule in Internal Capital Adequacy Assessment 3.1, the governance arrangements of the firm, its corporate culture and values, and the ability of members of the management body to perform their duties. The degree of involvement of the governing body of the firm will be taken into account by the PRA when assessing the ICAAP, as will the appropriateness of the internal processes and systems for supporting and producing the ICAAP.

3.3 When the PRA reviews an ICAAP as part of the SREP, it does so in order to determine whether all of the material risks have been identified and that the amount and quality of capital identified by the firm is sufficient to cover the nature and level of the risks to which it is or might be exposed.

3.4 The SREP will also consider:

(a) the results of stress tests carried out in accordance with the CRR by firms that use the IRB approach or internal models for market risk capital requirements;

(b) the exposure to and management of concentration risk by firms, including their compliance with the requirements set out in Part Four of the CRR and Chapter 6 of the ICAAP rules;

(c) the robustness, suitability and manner of application of policies and procedures implemented by firms for the management of the residual risk associated with the use of credit risk mitigation techniques;

(d) the extent to which the capital held by firms in respect of assets which it has securitised are adequate, having regard to the economic substance of the transaction, including the degree of risk transfer achieved;

(e) the exposure to and management of liquidity risk by firms, including the development of alternative scenario analyses, the management of risk mitigants (including the level, composition and quality of liquidity buffers), and effective contingency plans;

(f) the impact of diversification effects and how such effects are factored into the firm's risk measurement system;

(g) the geographical location of firms' exposures;

(h) the exposure of firms to the risk of excessive leverage; and

(i) whether a firm has provided implicit support to a securitisation.

3.5 The PRA will also assess as part of the SREP the risks that the firm poses to the financial system.

3.6 The PRA may need to request further information and meet with the governing body and other representatives of the firm in order to evaluate fully the comprehensiveness of the ICAAP. The management of the firm, including the governing body, should therefore be prepared to discuss all aspects of the ICAAP, covering both quantitative and qualitative components. Additionally, the PRA will consider the business model of the firm and the advocated rationale for the model, as well as the firm's expectations regarding the future market and economic environment and how they might affect its business model.

3.7 The SREP will generally be the same across all types of firms, but will be proportionate given the nature, scale and complexity of a firm's activities. There may also be a different emphasis depending on the type of firm or its potential risk to the financial system. For example, banks and building societies may be more exposed to credit concentration risk and interest rate risk in the non-trading book, with investment firms being more likely to be exposed to market risk; these potentially different areas of emphasis will be reflected in the conduct of the SREP, where applicable, for relevant firms.

3.8 On the basis of the SREP, the PRA will determine whether the arrangements implemented by the firm and the capital held by it provide sound management and adequate coverage of its risks. If necessary, the PRA will require the firm to take appropriate actions or steps at an early stage to address any future, potential failure to meet its prudential regulatory requirements.

4 The setting of Individual Capital Guidance (ICG) and the Capital Planning Buffer (CPB)

4.1 Following the SREP, including both a review of the ICAAP and any further interactions with a firm, the PRA will normally give the firm Individual Capital Guidance (ICG), advising the firm of the amount and quality of capital that the PRA considers the firm should hold to meet the overall financial adequacy rule in Internal Capital Adequacy Assessment 2.1.

4.2 The PRA will give ICG on a consolidated basis and on an individual basis when appropriate.

4.3 Where the PRA gives ICG to a firm it will generally specify an amount and quality of capital (Pillar 2A) that the firm should hold at all times in addition to the capital it must hold to comply with the CRR (Pillar 1). The PRA will usually do so by stating that the firm should hold capital of an amount at least equal to a specified percentage of that firm's capital requirement under the CRR, plus one or more static add-ons in relation to specific risks in accordance with the overall Pillar 2 rule in Internal Capital Adequacy Assessment 3.1.

4.4 It is for firms to ensure that they comply with the overall financial adequacy rule in Internal Capital Adequacy Assessment 2.1: however, if a firm holds the level of capital recommended as its ICG that does not necessarily mean that it is complying with the overall financial adequacy rule. Deviation by a firm from the terms of the ICG given to it by the PRA does not automatically mean that the firm is in breach of the overall financial adequacy rule or that the PRA will consider that the firm is failing or is likely to fail to satisfy the Threshold Conditions. However, firms should expect the PRA to investigate whether any firm is failing or likely to fail to satisfy the Threshold Conditions, with a view to taking further action as necessary.

4.5 The PRA does not expect a firm to meet the CRD IV buffers with any CET1 capital maintained to meet its ICG. If a firm agrees with its ICG, the PRA will expect the firm to apply for a requirement under s55M(5) of FSMA preventing the firm from meeting any of the CRD IV buffers that apply to the firm with any CET1 capital maintained to meet its ICG. A firm will normally be invited to apply for such a requirement at the same time as it is advised of its ICG. If a firm does not apply for such a requirement the PRA will consider using its powers under s55M(3) to impose one of its own initiative. Where applicable to a firm, global and other systemically important institution buffers will also be set by the PRA using its powers under s55M of FSMA to increase the size of the firm's combined buffer.

4.6 Following a SREP, the PRA may also notify the firm of an amount and quality of capital that it should hold as a Capital Planning Buffer (CPB), over and above the level of capital recommended as its ICG, and will generally do so at the same time as advising the firm of its ICG. The CPB, based on a firm-specific supervisory assessment, should be of sufficient amount and adequate quality to allow the firm to continue to meet the overall financial adequacy rule in Internal Capital Adequacy Assessment 2.1, in the face of adverse circumstances, after allowing for realistic management actions that a firm could and would take in a stress scenario. Utilisation of the CPB is not of itself a breach of capital requirements or the Threshold Conditions. The automatic distribution constraints associated with the CRD IV buffers do not apply to the CPB.

4.7 The PRA may set a firm's CPB either as an amount of capital which it should hold from the time of the PRA's notification following the firm's SREP or, in exceptional cases, as a forward-looking target that a firm should build up over time. More information on setting the CPB is outlined in the supervisory statement on stress testing. Where the general stress and scenario testing rule, as part of the ICAAP rules, applies to a firm on consolidated basis the PRA may notify the firm that it should hold a group CPB.

4.8 Where the amount or quality of capital which the PRA considers a firm should hold to meet the overall financial adequacy rule in Internal Capital Adequacy Assessment 2.1 or as a CPB is different from that identified by the firm through its ICAAP, the PRA usually expects to discuss any such difference with the firm and may consider the use of its powers under s166 of FSMA to assist in such circumstances.

4.9 If a firm considers that the ICG or the CPB advised to it by the PRA is inappropriate to its circumstances it should notify the PRA of this, consistent with Principle 11 (Relations with regulators). If, after discussion, the PRA and the firm do not agree on an adequate level of capital, the PRA may consider using its powers under s55M of FSMA to impose a requirement on the firm to hold capital in accordance with the PRA's view of the capital necessary to comply with overall financial adequacy rule in Internal Capital Adequacy Assessment 2.1. In deciding whether it should use its powers under section 55M, the PRA will take into account the amount and quality of the capital that the firm should hold for its CPB.

5 Failure to meet ICG and use of the CPB

5.1 The PRA expects every firm to hold at least the level of capital advised to it via its ICG at all times. If a firm's capital resources have fallen or are expected to fall below that level it should inform the PRA as soon as practicable (even if the firm has not accepted the ICG given by the PRA), explaining why this has happened or is expected to happen. The firm will also be expected to discuss the actions that it intends to take to increase its capital resources and/or reduce its risks (and therefore capital requirements), and any potential modification that it considers should be made to the ICG.

5.2 Where this has happened, the PRA may ask the firm for alternative and more detailed proposals or further assessments of capital adequacy and risks faced by the firm. The PRA will seek to agree with the firm appropriate timescales and the scope for any such additional work.

5.3 Where a firm has a CPB in place, it should only use that buffer to absorb losses or meet increased capital requirements if certain adverse circumstances materialise. These should be circumstances beyond the firm's normal and direct control, whether relating to a deteriorating external environment or periods of stress such as macroeconomic downturns or financial/market shocks, or firm-specific circumstances.

5.4 Consistent with Principle 11 (Relations with regulators), a firm should notify the PRA as early as possible in advance where it has identified that it would need to use its CPB (even if the firm has not accepted the PRA's assessment of the amount or quality of the capital required for the CPB). The firm's notification should state as a minimum:

- what adverse circumstances are likely to force the firm to draw down its CPB;

- how the CPB will be used up in line with the firm's capital planning projections; and

- what plan is in place for the eventual restoration of the CPB.

5.5 Following discussions with the firm, the PRA may put in place additional reporting arrangements to monitor the firm's use of its CPB in accordance with the plan agreed to restore that buffer. The PRA may also identify specific trigger points as the CPB is being used up by the firm, which may lead to additional supervisory actions.

5.6 Where a firm's CPB is being drawn down due to circumstances other than those arising from a deteriorating external environment or periods of stress (eg macroeconomic downturns or financial/market shocks), or firm-specific circumstances (eg poor planning), the PRA may ask the firm for more detailed plans for it to restore its CPB. In light of the relevant circumstances, the PRA may consider taking other remedial actions, which may include using its powers under section 55M of FSMA to require the firm to take specified action to restore its CPB within an appropriate timeframe.

5.7 Where a firm has started to use its CPB in circumstances where it was not possible to notify the PRA in advance, it should notify the PRA and provide information about the cause, the current and projected usage of the buffer, and its eventual restoration as soon as practicable afterwards.

6 Interest rate risk in the non-trading book

6.1 Firms must have appropriate systems and processes, proportionate to the nature, scale and complexity of their business, to evaluate and manage interest rate risk in the non-trading book. Examples of interest rate risk in the non-trading book include:

- the mismatch of repricing of assets and liabilities and off balance sheet short and long-term positions (termed 'repricing risk');

- hedging exposure to one interest rate with exposure to a rate which reprices under slightly different conditions ('basis risk');

- the uncertainties of occurrence of transactions, eg where actual transactions do not equal those that were expected in the future ('pipeline risk'); and

- consumers redeeming fixed rate products when market rates change ('optionality risk').

6.2 The systems and processes should allow the firm to include:

- the ability to measure the exposure and sensitivity of the firm's activities, if material, to repricing risk, yield curve risk, basis risk and risks arising from embedded optionality (eg pipeline risk, prepayment risk) as well as changes in assumptions (eg those about customer behaviour);

- consideration as to whether a purely static analysis of the impact on their current portfolio of a given shock or shocks should be supplemented by a more dynamic simulation approach; and

- scenarios in which different interest rate paths are computed and in which some of the assumptions (eg about behaviour, contribution to risk and balance sheet size and composition) are themselves functions of interest rate level.

6.3 Under Internal Capital Adequacy Assessment 13.1, a firm is required to make a written record of its assessments made under those rules. A firm's record of its approach to evaluating and managing interest rate risk as it affects the firm's non-trading activities should cover the following issues:

- the internal definition of the boundary between 'banking book' and 'trading activities';

- the definition of economic value and its consistency with the method used to value assets and liabilities (eg discounted cash flows);

- the size and the form of the different shocks to be used for internal calculations;

- the use of a dynamic and/or static approach in the application of interest rate shocks;

- the treatment of commonly called 'pipeline transactions' (including any related hedging);

- the aggregation of multi-currency interest rate exposures;

- the inclusion (or not) of non-interest bearing assets and liabilities (including capital and reserves);

- the treatment of current and savings accounts (ie the maturity attached to exposures without a contractual maturity);

- the treatment of fixed rate assets (liabilities) where customers still have a right to repay (withdraw) early;

- the extent to which sensitivities to small shocks can be scaled up on a linear basis without material loss of accuracy (ie covering both convexity generally and the non-linearity of pay-off associated with explicit option products);

- the degree of granularity employed (for example offsets within a time bucket); and

- whether all future cash flows or only principal balances are included.

6.4 In accordance with Internal Capital Adequacy Assessment 9.2, a firm should apply a 200 basis point shock in both directions to each major currency exposure. The PRA will periodically review whether the level of the shock is appropriate in light of changing circumstances, in particular the general level of interest rates (for instance, during periods of very low interest rates) and their volatility. The level of shock required may also be changed in accordance with EBA guidelines. A firm's internal systems should, therefore, be flexible enough to compute its sensitivity to any standardised shock that is prescribed. If a 200 basis point shock would imply negative interest rates, or if such a shock would otherwise be considered inappropriate, the PRA will consider adjusting the requirements accordingly.

6.5 Alongside the requirement to monitor and evaluate the potential impact of changes in interest rates on economic value, the PRA expects firms to monitor the potential impact on earnings volatility. This should be assessed on an appropriate timeframe of three to five years, and factor in the firm's forward-looking view of product volumes, based on its proposed business model, and the projected path of interest rates.

7 Group risk

7.1 Under SYSC 12.1.8R a firm is required to have adequate, sound and appropriate risk management processes and internal control mechanisms for the purpose of assessing and managing its own exposure to group risk, including sound administrative and accounting procedures.

8 Operational risk

8.1 In meeting the general standard referred to in Internal Capital Adequacy Assessment 10.1, a firm that undertakes market-related activities should be able to demonstrate to the PRA:

- in the case of a firm calculating its Operational Risk Capital Requirement using the basic indicator approach or standardised approach, that it has considered; or
- in the case of a firm with an Advanced Measurement Approach (AMA) permission, compliance with;

the Committee of European Banking Supervisors' *Guidelines on the management of operational risk in market-related activities*,[1] published in October 2010.

8.2 In meeting the general standards referred to in Internal Capital Adequacy Assessment 10.1, a firm with an AMA approval should be able to demonstrate to the appropriate regulator that it has considered and complies with Section III of the European Banking Authority's *Guidelines on the Advanced Measurement Approach (AMA) — Extensions and Changes*,[2] published in January 2012.

8.3 The matters dealt with in a business continuity plan should include:

(a) resource requirements such as people, systems and other assets, and arrangements for obtaining these resources;

(b) the recovery priorities for the firm's operations;

(c) communication arrangements for internal and external concerned parties (including the PRA, clients and the press);

(d) escalation and invocation plans that outline the processes for implementing the business continuity plans, together with relevant contact information;

(e) processes to validate the integrity of information affected by the disruption; and

(f) regular testing of the business continuity plan in an appropriate and proportionate manner.

(1) www.eba.europa.eu/regulation-and-policy/operational-risk/guidelines-on-the-management-of-operational-risk-in-market-related-activities.
(2) www.eba.europa.eu/-/guidelines-on-ama-extensions-and-chang-1.

Supervisory statement — stress testing, scenario analysis and capital planning

1 Introduction

1.1 This supervisory statement is aimed at firms to which CRD IV applies.

1.2 This statement sets out the PRA expectations of firms in relation to stress testing, scenario analysis and capital planning, and the requirements set out in the PRA Rulebook in Chapter 12 of the Internal Capital Adequacy Assessment rules.

1.3 It provides further detail on the high-level expectations outlined in *The PRA's approach to banking supervision* (April 2013).

1.4 Stress testing typically refers to shifting the values of individual parameters that affect the financial position of a firm and determining the effect on the firm's financial position.

1.5 Scenario analysis typically refers to a wider range of parameters being varied at the same time. Scenario analyses often examine the impact of adverse events on the firm's financial position, for example, simultaneous movements in a number of risk categories affecting all of a firm's business operations, such as business volumes, investment values and interest rate movements.

2 Expectations of firms

2.1 There are three broad purposes of stress testing and scenario analysis. First, it can be used as a means of quantifying how much capital might be absorbed if an adverse event or events occurred. This might be a proportionate approach to risk management for an unsophisticated business. Second, it can be used to provide a check on the outputs and accuracy of risk models, particularly in identifying non-linear effects when aggregating risks. Third, it can be used to explore the sensitivities in longer-term business plans and how capital needs might change over time.

2.2 The general stress test and scenario analysis rule in Internal Capital Adequacy Assessment 12.1 requires a firm to carry out stress tests and scenario analyses as part of its obligations under the overall Pillar 2 rule in Internal Capital Adequacy Assessment 3.1. Both stress tests and scenario analyses are undertaken by a firm to further and better its understanding of the vulnerabilities that it faces under adverse conditions. They are based on the analysis of the impact of a range of events of varying nature, severity and duration. These events can be financial, operational or legal, or relate to any other risk that might have an economic impact on the firm.

3 Overall approach

3.1 As part of its obligation under the general stress and scenario testing rule in Internal Capital Adequacy Assessment 12.1, a firm should undertake a broad range of stress tests which reflect a variety of perspectives, including sensitivity analysis, scenario analysis and stress testing on individual portfolios as well as at a firm-wide level.

3.2 Stress tests and scenario analyses should be carried out at least annually. A firm should, however, consider whether the nature of the major sources of risks identified by it in accordance with the overall Pillar 2 rule in Internal Capital Adequacy Assessment 3.1 and their possible impact on its financial resources suggest that such tests and analyses should be carried out more frequently. For instance, a sudden change in the economic outlook may prompt a firm to revise the parameters of some of its stress tests and scenario analyses. Similarly, if a firm has recently become exposed to a particular sectoral concentration, it may wish to amend and/or add some stress tests and scenario analyses in order to reflect that concentration.

3.3 The firm should document its stress testing and scenario analysis policies and procedures, as well as the results of its tests in accordance with Internal Capital Adequacy Assessment 13.1. These results should be included within the firm's ICAAP document.

Governance

3.4 The PRA expects a firm's senior management and governing body to be actively involved and engaged in all relevant stages of the firm's stress testing and scenario analysis programme. This would include establishing an appropriate stress testing programme, reviewing the programme's implementation (including the design of scenarios) and challenging, approving and taking action based on the results of the stress tests. The PRA expects firms to assign adequate resources, including IT systems, to stress testing and scenario analysis, taking into account the stress testing techniques employed, so as to be able to accommodate different and changing stress tests at an appropriate level of granularity.

Scenarios

3.5 In identifying scenarios, and assessing their impact, the PRA expects a firm to take into account, where material, how changes in circumstances might impact upon:

- the nature, scale and mix of its future activities; and
- the behaviour of counterparties, and of the firm itself, including the exercise of choices (for example, options embedded in financial instruments or contracts of insurance).

3.6 Firms should develop a range of firm-wide scenarios including some based on macroeconomic and financial market shocks for the purposes of their own stress testing. These scenarios should be developed so as to be relevant to the circumstances of the firm, including its business model, and the market(s) in which it operates. When the PRA publishes macroeconomic scenarios, firms are expected to consider their severity to inform the design of its own stress testing framework. In addition, the PRA may also ask a firm to apply specific scenarios directly in its ICAAP submission. More information on ICAAP expectations is outlined in the supervisory statement on the ICAAP and the SREP.

3.7 The calibration of the stress and scenario analyses should be reconciled to a clear statement setting out the premise upon which the firm's internal capital assessment under the overall Pillar 2 rule in Internal Capital Adequacy Assessment 3.1 is based.

3.8 In identifying adverse circumstances and events in accordance with Internal Capital Adequacy Assessment 12.1, a firm should consider the results of any reverse stress-testing conducted in accordance with SYSC 20. Reverse stress-testing may be expected to provide useful information about the firm's vulnerabilities and variations around the most likely scenarios for the purpose of meeting the firm's obligations under Internal Capital Adequacy Assessment 12.1. In addition, such a comparison may help a firm to assess the sensitivity of its financial position to different stress calibrations.

Impact on resources

3.9 In carrying out the stress tests and scenario analyses required by the general stress and scenario testing rule in Internal Capital Adequacy Assessment 12.1, the PRA expects a firm to also consider any impact of the adverse circumstances on its capital resources. In determining whether it would have adequate financial resources in the event of each identified realistic adverse scenario, the firm should:

- only include financial resources that could reasonably be relied upon as being available in the circumstances of the identified scenario; and
- take account of any legal or other restriction on the use of financial resources.

3.10 In identifying an appropriate range of adverse circumstances and events in accordance with Internal Capital Adequacy Assessment Rules 12.1, a firm will need to consider:

(a) the nature, scale and complexity of its business and of the risks that it bears;

(b) its risk appetite, including in light of the adverse conditions through which it expects to remain a going concern;

(c) the cycles it is most exposed to and whether these are general economic cycles or specific to particular markets, sectors or industries; and

(d) for the purposes of Internal Capital Adequacy Assessment 12.1, the amplitude and duration of the relevant cycle should include a severe downturn scenario based on forward-looking hypothetical events, calibrated against the most adverse movements in individual risk drivers experienced over a long historical period.

Time horizon

3.11 Both stress testing and scenario analysis are forward-looking analysis techniques, which seek to anticipate possible losses that might occur if an identified economic downturn or risk event crystallises.

3.12 In making the estimate required by Internal Capital Adequacy Assessment 12.1(3), a firm should project both its capital resources and its required capital resources over a time horizon of three to five years, taking account of its business plan and the impact of relevant adverse scenarios. In making the estimate, the firm should consider both the capital resources required to meet its capital requirements under the CRR and the capital resources needed to meet the overall financial adequacy rule. The firm should make these projections in a manner consistent with its risk management processes and systems as set out in Internal Capital Adequacy Assessment 3.1.

3.13 When deciding the planning horizon over which to conduct their analysis, firms should consider how long it might take to recover from any loss. The time horizon over which stress tests and scenario analyses should be carried out will depend on, among other things, the maturity and liquidity of the positions stressed. For example, for the market risk arising from the holding of investments, this will depend upon the extent to which there is a regular, open and transparent market in those assets, which would allow fluctuations in the values of the investments to be more readily and quickly identified.

3.14 In projecting its financial position over the relevant time horizon, the firm should:

(a) reflect how its business plan would 'flex' in response to the adverse events being considered, taking into account factors such as changing consumer demand and changes to new business assumptions;

(b) consider the potential impact on its stress testing of dynamic feedback effects and second-order effects of the major sources of risk identified in accordance with the overall Pillar 2 rule in Internal Capital Adequacy Assessment 3.1;

(c) estimate the effects on the firm's financial position of the adverse event without adjusting for management actions;

(d) separately, identify any realistic management actions that the firm could and would take to mitigate the adverse effects of the stress scenario; and

(e) estimate the effects of the stress scenario on the firm's financial position after taking account of realistic management actions.

Management actions

3.15 The PRA expects firms to identify any realistic management actions intended to maintain or restore capital adequacy. These could include ceasing to transact new business after a suitable period has elapsed, balance sheet shrinkage, restricting distribution of profits or raising additional capital. A firm should reflect management actions in its projections only where it could and would take such actions, taking account of factors such as market conditions in the stress scenario and any effects upon the firm's reputation with its counterparties and investors. The combined effect on capital and retained earnings should be estimated.

3.16 In order to assess whether prospective management actions in a stress scenario would be realistic, and to determine which actions the firm could and would take, the PRA expects a firm to take into account any preconditions that might affect the value of management actions as risk mitigants. It should then analyse the difference between the estimates of its financial position over the time horizon, both gross and net of management actions, in sufficient detail to understand the implications of taking different management actions at different times, particularly where they represent a significant divergence from the firm's business plan.

3.17 A firm should use the results of its stress testing and scenario analysis not only to assess capital needs, but also to decide if measures should be put in place to minimise the adverse effect on the firm if the risks covered by the stress or scenario test actually materialise. Such measures might be a contingency plan or more concrete risk mitigation steps.

4 PRA review: the SREP

4.1 The PRA will review the firm's records referred to in Internal Capital Adequacy Assessment 13.1 as part of its SREP to enable it to judge whether a firm will be able to continue to meet its CRR and the overall financial adequacy rule in Internal Capital Adequacy Assessment 2.1 throughout the time horizon used for the capital planning exercise.

4.2 If a firm's stress testing management plan shows that the firm's projected capital resources are less than those required to continue to meet its ICG or less than those needed to continue to meet the overall financial adequacy rule over the appropriate time horizon, the PRA may require the firm to set out additional countervailing measures and off-setting actions to reduce such differences or to restore the firm's capital adequacy after the stress event.

2 Definition of capital

CRD IV and capital

1 Introduction

1.1 This statement is aimed at firms to which CRD IV applies.

1.2 This statement sets out the PRA's expectations on the regulatory capital resources that firms are required to hold, of an appropriate quality, under CRD and the CRR. This statement supplements the requirements set out in Part 2 of the CRR, in the Capital rules of the PRA Rulebook and the high-level expectations on capital as outlined in *The PRA's approach to banking supervision* (April 2013) ('the banking approach document').

2 Quality and composition of capital

2.1 As set out in the banking approach document, the PRA expects a significant part of a firm's capital to be ordinary shares and reserves. These are the highest-quality form of capital, as they allow firms to absorb losses unambiguously on a going concern basis. When assessing firms, the PRA will be mindful of the fact that quality of capital is not purely about whether a firm meets each sub-tier of the capital rules. For example, even if two firms have identical Common Equity Tier 1 (CET1) positions, the PRA may view the quality of their capital differently due to the nature of the items underlying their CET1 position.

2.2 As set out in the banking approach document, the PRA also expects firms to comply with the clearly stated internationally agreed criteria around the definition of capital, in spirit as well as to the letter, when structuring capital instruments. This includes an expectation that firms ensure their marketing of proposed capital instruments does not undermine their compliance with the spirit of these criteria. The PRA expects firms to refrain from innovation to structure new capital instruments if these may be ineffective (or less effective) in absorbing losses. For example, the PRA would expect firms to refrain from complex structures, including transactions involving several legs or side agreements, where the same prudential aim can be achieved more simply.

3 Additional Tier 1 Triggers

3.1 Under CRR Article 54, Additional Tier 1 capital instruments (AT1) are required to have a convertibility trigger in order to be eligible as part of a firm's regulatory capital resources. Conversion will result in a boost to a firm's CET1 ratio at a trigger point (as a result of the instrument being written-down or converted into equity). The minimum required trigger in the CRR is 5.125% CET1.

3.2 The aim of the trigger and conversion is to contribute to the firm's recovery following a significant stress. Therefore, if UK firms, especially those whose failure may have systemic consequences for the United Kingdom, issue AT1 instruments, the PRA expects them to set AT1 triggers at a level that is unambiguously consistent with being able to recover from a stress without entering into resolution. This may be at a level higher than 5.125% CET1. The PRA also expects the conversion or write-down to be for the full amount of the instrument and to be permanent.

4 Preference

4.1 Where possible, the PRA expects firms to meet their CET1 requirements entirely with voting common shares and associated reserves. The PRA strongly discourages firms from including non-voting shares in CET1, particularly if such shares have higher dividends than common shares. The main reason for the PRA's concern is that it is imperative that the composition of a firm's CET1 is as straightforward and transparent as possible. There should also be no doubt that a firm's CET1 only includes the highest quality capital. The inclusion of instruments other than voting common shares in CET1 could lead to concerns that such instruments may not have the same capital quality.

5 Subordination, remedies, events of default and set-off

5.1 Under CRR, all regulatory capital must be capable of absorbing losses either on a going or gone concern basis. Therefore, all capital instruments as a minimum must be subordinated to all senior creditors, including depositors. In particular, building societies must ensure that any capital instruments issued by them are subordinated to retail depositors (as per the rule in Capital 10.2).

5.2 It is also important that subordination is not made less effective by granting additional rights to holders of subordinated instruments for example in respect of events of default, remedies and rights of set-off. The PRA expects events of default to be restricted to non-payment of any amount falling due under the terms of the instrument or on the winding-up of the firm. This ensures that the subordinated creditor cannot force early repayment while the issuer may still be technically solvent. This is important so as not to hinder the efforts of the authorities in the context of recovery or resolution actions in relation to the issuer.

5.3 In the event that default occurs, the PRA expects remedies to be restricted, to the fullest extent permitted under the laws of the relevant jurisdictions, to petitioning for the winding-up of the firm or proving for the debt in liquidation or administration. Limiting remedies in this way prevents holders of subordinated instruments using other remedies to receive payment, potentially ahead of senior creditors. Also, to the fullest extent permitted under the laws of the relevant jurisdictions, the PRA expects subordinated creditors to waive any rights to set off amounts they owe the issuer against subordinated amounts owed to them by the issuer. Waiving rights of set-off helps to maintain the creditor hierarchy so that subordinated creditors are not treated in the same way as senior creditors.

6 Regulatory capital and subordinated swaps

6.1 CRR requires that the full amount of regulatory capital is subordinated. If a firm chooses to hedge the valuation volatility associated with a capital instrument that it has issued under fair value hedge accounting, then to maintain consistency with the CRR capital regime the PRA expects the hedging instrument to also be subordinated. For example, if the value of a subordinated debt instrument falls from 100 to 90, then the hedge must also be subordinated in order to continue to count 100 of subordinated debt as regulatory capital. If the hedge is not subordinated, then only 90 of subordinated debt would be eligible to count as regulatory capital. This is because the ten contributed by the swap would not be subordinated and therefore would not meet the minimum eligibility criteria specified in CRR.

The Basel I floor

1 Introduction

1.1 This statement is aimed at firms to which CRD IV applies.

1.2 This statement sets out the PRA's expectations regarding the application of the Basel 1 floor. This statement supplements the requirements set out in the CRR and replaces the requirements in BIPRU TP 2 which set out how the capital floor provisions were to be applied.

2 Calculation of capital requirements

2.1 Firms should apply the requirements in CRR Article 500(1) to its portfolio as it changes over time. For example, if a firm is calculating its capital requirements as at 31 December 2014 it will have two calculations. The first is carried out in accordance with CRR Article 92 (disregarding Article 500) and the second takes 80% of the requirements of IPRU(1) as it stood on 31 December 2006. Both calculations are applied to the firm's figures as at 31 December 2014, and the firm's capital requirement is the greater of these two calculations. Firms should take into account the impact of expected loss, credit risk adjustments and other similar adjustments as defined in Article 159 in these calculations.

2.2 This section provides an illustrative example.(2) In this example:

(a) the own funds required by Article 92 (disregarding Article 500) would be £5.4 million, and the sum of credit risk and similar adjustments are £0.25 million less than expected losses; and

(b) under IPRU, the firm's capital resources requirement would be £8.0 million and this would be met in part by general credit risk adjustments of £0.5 million.

2.3 Expected losses should be taken into account in undertaking the first calculation. For these purposes, if expected losses less value adjustments and provisions is negative, then the absolute value of that amount should be added to the capital resources requirement. If the result is positive then that amount should be deducted from the capital resources requirement. In this example, the result is negative, and so a capital requirement of £5.65 million should be calculated. In this example, a capital requirement of £6.0 million, which is 80% multiplied by (£8.0 million less £0.5 million), should be used for the second calculation.

2.4 As the Article 92 calculation is still less than the floor-adjusted IPRU capital resources requirement of £6.0 million, the effect of CRR Article 500 is that the firm is subject to the (higher) IPRU-based requirement. If the Article 92 had been greater than £6.0 million, the effect of CRR Article 500 is that the firm would have been subject to the Article 92 requirement at that time. See: (CRR Article 500(1).)

3 Permission to apply floor based on non-modelled CRR approaches(3)

3.1 The PRA expects that it will only grant permission to apply a floor based on non-modelled CRR approaches in place of the Basel 1 floor in accordance with CRR Article 500(2) in the following circumstances:

(a) the firm has first used an advanced approach on 1 January 2010 or later; and

(b) the firm does not have access to systems and data that would allow it to calculate capital requirements based on IPRU without incurring materially greater costs than if it were to use non-modelled CRR approaches for the floor instead; and

(c) the firm can demonstrate, based on the latest available information at the time it applies for permission, that its floored capital requirements based on non-modelled CRR approaches are not materially less than those based on IPRU. (See: CRR Article 500(2).)

4 Permission to not apply floor

4.1 The PRA does not expect that it will waive the application of the Basel 1 floor in accordance with CRR Article 500(5).

(1) 'The Interim Prudential Sourcebook', comprising IPRU(BANK), IPRU(BSOC), IPRU(FSOC), IPRU(INS) and IPRU(INV), which formed part of the *FSA Handbook*.
(2) This example assumes that a firm does not have permission under CRR Article 500(2) to apply the floor based on non-modelled CRR approaches.
(3) CP10/22 section 3.10.

3 Credit risk

Securitisation

1 Introduction

1.1 This statement is aimed at firms to which CRD IV applies.

1.2 This statement sets out the PRA's expectations of firms in respect of securitisation in the following sections:

(2) 'High-level Significant Risk Transfer considerations' — general expectations of firms seeking to obtain significant risk transfer (SRT) through securitisation;

(3) 'Significant Risk Transfer notifications and permissions' — process for notifying us of SRT transactions and for obtaining permission to undertake own assessments of SRT;

(4) 'Regulatory capital calculation methodology and SRT' — methodologies firms use to calculate post-securitisation risk weights in SRT transactions;

(5) 'Implicit Support and SRT' — the PRA's approach to implicit support;

(6) 'High cost credit protection and other SRT considerations' — factors likely to affect the assessment of SRT transactions; and

(7) 'Mapping of External Credit Assessment Institutions' (ECAIs) credit assessments to credit quality steps' — the PRA's view of interim mapping of rating agency grades to credit quality steps for the purposes of securitisation positions under the Ratings Based Approach to Securitisation.

1.3 The statement supplements the CRR and rules in the Benchmarking of Internal Approaches and Credit Risk Part of the PRA Rulebook.

2 High-level Significant Risk Transfer considerations

2.1 CRR requires any reduction in capital requirements achieved through securitisation to be justified by a commensurate transfer of risk to third parties. Where the PRA determines that the reduction in risk-weighted exposure amounts (RWEA), which would be achieved through a particular securitisation transaction, is not justified by a commensurate transfer of risk then SRT shall not be considered to have been achieved by that transaction.

2.2 SRT is an on-going requirement. Accordingly, the PRA expects firms to ensure that any reduction in capital requirements achieved through securitisation continues to be matched by a commensurate transfer of risk throughout the life of the transaction. The PRA expects firms to take a substance over form approach to assessing SRT. Firms should be able to demonstrate that the capital relief post-transaction adequately captures the economic substance of the entire transaction, and is commensurate to the retained risks.

2.3 One indication of whether or not risk transfer is commensurate is whether the RWEA post-securitisation is commensurate with the RWEA that would apply if the firm acquired the securitised exposures from a third party. The PRA expects firms purchasing risk transfer products to give adequate consideration to all relevant factors when assessing SRT, including the size of premiums paid.

2.4 When risk transfer transactions are structured as a group of linked transactions rather than a single transaction, the PRA expects the aggregate effect of linked transactions to comply with the CRR. The PRA expects firms to ensure that analysis of risk transfer incorporates all linked transactions, particularly if certain transactions within a group of linked transactions are undertaken at off-market rates.

2.5 The PRA expects the instruments used to transfer credit risk not to contain provisions which materially limit the amount of risk transferred. For example, should losses or defaults occur in the pool — ie deterioration in the credit quality of the underlying pool — the PRA expects the originator's net cost of protection or the yield payable to investors should not increase as a result.

2.6 In order to ensure their continuing appropriateness, the PRA expects firms to update the opinions of qualified legal counsel, required by CRR, as necessary to ensure their continuing validity. For example, an opinion may need to be updated if relevant statutory provisions are amended, or where a new decision or judgment of a court has a bearing on the continuing validity of counsel's opinion.

2.7 The PRA expects relevant senior management of a firm to be appropriately engaged in the execution of securitisation transactions that lead to a reduction in RWEA, where the firm is providing or purchasing structured trades.

2.8 The PRA does not operate a pre-approval process for securitisation transactions. The PRA nevertheless expects a firm to discuss with its supervisor at an early stage securitisation transactions that are material or have complex features. Where a firm claims a regulatory capital reduction from securitisation transactions in its disclosures to the market, the PRA expects such disclosures to include caveats making clear the risk of full or partial recharacterisation where this risk is material in the light of our stated policy.

2.9 Although this supervisory statement sets out the PRA's expectations regarding securitisation, these expectations are also relevant for other similar credit protection arrangements.

2.10 The PRA will seek to ensure that the securitisation framework is not used to undermine or arbitrage other parts of the prudential framework. In relation to other similar credit protection arrangements, including those subject to credit risk mitigation or trading book rules, the impact of certain features (eg significant premiums or call options) may cast doubt on the extent of risk transferred and the resulting capital assessment.(1) Features which result in inadequate capital requirements compared to the risks a firm is running may result in the credit protection not being recognised or the firm being subject to extra capital charges in their Individual Capital Guidance (ICG) in the form of Pillar 2 add-ons. Credit protection arrangements in general are subject to the same overarching principles as those in the securitisation framework.

2.11 Where a firm achieves SRT for a particular transaction, the PRA expects it to continue to monitor risks related to the transaction to which it may still be exposed. The PRA expects firms to consider the capital planning implications of securitised assets returning onto their balance sheets. CRR requires firms to conduct regular stress testing of their securitisation activities and off-balance sheet exposures. The PRA expects those stress tests to consider the firm-wide impact of stressed market conditions on those activities and exposures and the implications for other sources of risk, for example, credit risk, concentration risk, counterparty risk, market risk, liquidity risk and reputational risk. The PRA expects a firm's stress testing of securitisation activities to take into account existing securitisations and pipeline transactions. The PRA expects a firm to have in place procedures to assess and respond to the results of that stress testing and would expect them to be taken into account under Pillar 2.

(CRR Articles 243 and 244)

3 Significant Risk Transfer notifications and permissions

Requirements for originators to use securitisation risk weights

3.1 An originator of a securitisations is able to use the securitisation risk weights (and not calculate capital requirements on the assets underlying their securitisation) in either of the following cases:

(a) the firm transfers significant credit risk associated with the securitised exposures to third parties; or

(b) the firm deducts from Common Equity Tier 1, or applies a 1,250% risk weight to, all positions it holds in that securitisation.

3.2 The CRR provides three options for firms to demonstrate how they transfer significant credit risk for any given securitisation transaction:

1. the originator does not retain more than 50% of the risk weighted exposure amounts of mezzanine securitisation positions, where these are:

    (i) positions to which a risk weight lower than 1,250% applies; and

    (ii) more junior than the most senior position in the securitisation and more junior than any position in the securitisation rated Credit Quality Step 1 or 2.

2. where there is no mezzanine position, the originator does not hold more than 20% of the exposure values of securitisation positions that are subject to a deduction or 1,250% risk weight and where the originator can demonstrate that the exposure value of such securitisation positions exceeds a reasoned estimate of the expected loss on the securitised exposures by a substantial margin; and

3. the competent authority may grant permission to an originator to make its own assessment if it is satisfied that the originator can meet certain requirements.

SRT under options (1) and (2)

3.3 Credit Risk 4.1 in the PRA Rulebook requires a firm to notify the PRA of each transaction on which it seeks capital relief under options 1 and 2.

3.4 Where the PRA considers that the possible reduction in RWEA, achieved via the securitisation is not justified by a commensurate transfer of risk to third parties, then the PRA

(1) Article 194(2) of the CRR requires firms to, 'take all appropriate steps to ensure the effectiveness of the credit protection arrangement and to address the risks related to that arrangement'.

will find SRT has not been achieved. Consequently, firms will not be able to recognise any reduction in RWEA from the transaction.

(CRR Articles 243 and 244)

SRT option 3

3.5 The PRA intends to grant permission for an originator to make its own assessment of SRT only where it is satisfied that:

- in every relevant case, the reduction in capital requirements achieved would be justified by a commensurate transfer of risk to third parties;
- the firm has in place appropriately risk-sensitive policies and methodologies to assess the transfer of risk; and
- such transfer of risk to third parties is also recognised for the purposes of the firm's internal risk management and internal capital allocation.

3.6 Where the PRA grants permission for multiple transactions, then that permission will cover a defined scope of potential transactions. The permission will enable a firm (within certain limits) to carry out these transactions without notifying the PRA in each individual instance.

(CRR Articles 243 and 244)

Deduction or 1,250% risk weighting

3.7 A firm seeking to achieve capital relief by deducting or applying a 1,250% risk weight to all retained positions would not need to notify the PRA or obtain permission. In such cases, a firm should consider whether the characteristics of the transaction are such that the PRA would reasonably expect prior notice of it.

(CRR Articles 243 and 244)

SRT notifications

Process for submitting notifications

3.8 When informing the PRA of a transaction in accordance with Credit Risk 4.1, the information should be sent simultaneously via email to the SRT notifications inbox (SRT@bankofengland.co.uk) and to the firm's usual supervisory contact.

Information to be provided

3.9 A firm's notification should include sufficient information to enable the PRA to assess whether the possible reduction in RWEA which would be achieved by the securitisation is justified by a commensurate transfer of credit risk to third parties. The PRA expects such information to include at least the following:

(a) details of the securitisation positions, including rating, exposure value and RWEA broken down by securitisation positions sold and retained;

(b) a copy of the SRT policy applied to the transaction, including details of the methodology and any models used to assess risk transfer;

(c) a statement of how all relevant risks are incorporated into the SRT assessment and how the full economic substance of the transaction is taken into consideration;

(d) the SRT calculation, setting out why the firm believes the capital relief proposed is commensurate with the credit risk transferred to third parties;

(e) details of reliance on external credit assessment institutions (ECAIs) in the SRT assessment;

(f) a description of the risks being retained;

(g) key transaction documentation and any relevant supporting documents (eg a summary of the transaction);

(h) copies of investor and internal presentations on the transaction;

(i) details of the underlying assets (including asset class, geography, tenor, rating, spread, collateral, exposure size);

(j) details of the transaction structure;

(k) details of any termination options (eg call options)

(l) details of the cash flow between parties involved in the transaction;

(m) details of the ratings and pricing of bonds issued in the transaction;

(n) details of any connected parties involved in the transaction;

(o) details of the rationale for the transaction;

(p) details of the CRR rules the firm is relying on; and

(q) details of the governance process for the transaction, including details of any committees involved in approving the transaction.

Communicating PRA decisions on notified transactions

3.10 Following review of sufficient information provided by the firm, the PRA will inform the firm of its view on commensurate risk transfer. The PRA's review will focus on the proportion of credit risk transferred — including any transaction features which undermine effective risk transfer — compared to the proportion by which RWEA is reduced as a result of the transaction. Where the PRA judge the reduction in RWEA not to be justified by a commensurate transfer of credit risk to third parties, it will inform the firm that SRT has not been achieved by this transaction. Otherwise the PRA will inform the firm that it does not object to the transaction.

3.11 The PRA does not intend to pre-approve transactions. Instead, the PRA will provide a view on whether it considers that commensurate risk transfer to have been achieved at a point in time, which may be provided after a transaction has closed. The PRA may reassess its judgement of the achievement of commensurate risk transfer if the level of credit risk transfer in a transaction changes materially.

Permissions for own assessment of SRT

3.12 Firms may apply for permission to consider SRT to have been achieved without needing to rely on option (1) or (2). The scope of such permission can be defined to cover a number of transactions or an individual transaction.

(CRR Articles 243 and 244)

Multiple transaction permissions

3.13 Where a firm applies for such permission, the PRA expects the scope to be defined according to a range of characteristics, including the type of asset class and the structural features of the transaction. The characteristics that the PRA expects a firm to consider when defining the scope of a permission application include:

(a) asset class (eg residential or commercial mortgages, credit card receivables, leasing, loans to corporates or small and medium-sized enterprises, consumer loans, trade receivables, securitisations, Private Finance Initiative, insurance, covered bonds, other assets);

(b) further asset class distinction (eg geography and asset quality); and

(c) structural features (eg distinguishing between securitisation and resecuritisation, traditional and synthetic securitisation and non-revolving structures and revolving structures).

3.14 It is likely for it to be more straightforward for the PRA to assess relatively narrowly scoped permissions than those covering a wide range of assets and/or with complex structural features.

PRA areas of review and information to be submitted by firms

3.15 In order to assess a firm's ability to use its own policies and methodologies for assessing SRT, the PRA's permission reviews will focus on the following factors:

- the firm's understanding of the risk of potential transactions within permission scope, including for potential underlying assets, securitisation structures and other relevant factors that affect the economic substance of risk transfer;
- the firm's governance around SRT assessment (including sign-off procedures) and systems and controls relating to risk-transfer assessment and determination of SRT;
- SRT calculation policies and methodologies, including models used;
- the firm's historical experience with relevant securitisation origination; and
- the use of third-party risk assessments (eg external ECAI ratings) and the relationship with internal assessments.

3.16 The information the PRA expects a firm to provide in a permission application includes the following:

(a) details of the firm's governance processes for SRT, including details of any relevant committees and the seniority and expertise of key persons involved in sign-off;

(b) a copy of the firm's SRT policy, including details of the SRT calculation policies, methodologies and any models used to assess risk transfer (this should set out how the firm ensures it only takes capital relief in proportion to the amount of risk transferred on any given transaction);

(c) a statement of how all relevant risks are incorporated in the SRT calculations and how the full economic substance of transactions is taken into consideration;

(d) details of the firm's systems and controls regarding risk transfer in securitisations;

(e) a copy of the firm's capital allocation strategy;

(f) details of any securitised assets that have come back on the firm's balance sheet and the reason why; and

(g) details of reliance on ECAIs in determining SRT.

Limits attached to multiple transaction permissions

Materiality

3.17 The PRA will apply two materiality limits to the proportion of RWEA reduction that can be taken under any permission covering multiple transactions:

(a) transaction level limit — any transaction that would in principle be within the scope of the permission, but that resulted in an RWEA reduction exceeding 1% of the firm's credit risk related RWEAs, as at the date of the firm's most recent regulatory return, will fall outside the scope of a multiple transaction permission and will require a separate permission or require notification (if the transaction would satisfy option 1 or 2); and

(b) aggregate limit — once the aggregate RWEA reduction on all SRT transactions executed within the scope of a permission exceeds 5% of the firm's credit risk-related RWEAs as at the date of the firm's most recent regulatory return, no additional transactions may be executed within scope of the permission. In such circumstances, a firm should take one of the following actions:

   (i) apply to renew the multiple transaction permission;

   (ii) apply for a new permission covering the specific transactions exceeding the RWEA limit; or

   (iii) notify the PRA of the transaction, following the SRT notification procedure (if the transactions would satisfy option 1 or 2).

Length of permission

3.18 Multiple transaction permissions will be granted for a period of one year. The PRA's review of permission renewal will focus on changes to the firm's SRT policies and methodologies since the previous review.

Individual transaction permissions

3.19 Permissions relating to individual transactions need not be granted prior to the execution of a transaction. The PRA does not intend to specify the timeframe in which a firm should submit an individual transaction permission, but firms should note that capital relief from a specific transaction will not be available until a firm has obtained permission covering the SRT assessment and capital treatment (unless the transaction is being notified under option 1 or 2, or falls within scope of a multiple transaction permission).

3.20 The information the PRA expects to receive in an individual transaction permission includes the items set out in paragraph 3.9 points d to p, and paragraph 3.16 points a to c.

Limits attached to individual transaction permissions

3.21 The PRA may grant an individual permission for the full duration of a transaction, or may impose a shorter time limit on the permission. Where a firm seeks to take capital relief on a transaction beyond the expiry date of the relevant permission, the permission will require renewal prior to expiry.

3.22 As SRT should be met on a continuing basis, permissions will typically include a requirement to notify the PRA of changes in circumstances from those under which the permission was granted. Any reduction in credit risk transfer subsequent to the permission being granted will require the firm to make a commensurate reduction in the extent of RWEA reduction that is recognised. If a firm does not effect a commensurate reduction in the RWEA relief in such circumstances, the PRA may revoke the relevant permission.

(CRR Articles 243 and 244)

4 Regulatory capital calculation methodology and SRT

4.1 Originators must transfer a significant amount of credit risk associated with securitised exposures to third parties to be able to apply the securitisation risk weights set out in Chapter 5 of the CRR, and any associated reduction in capital requirements must be matched by a commensurate transfer of risk to third parties.

4.2 As part of the notification and permissions process, the PRA expects a firm to inform it of the methodology it intends to use to calculate securitisation capital requirements. The PRA will generally be more sceptical of the achievement of commensurate risk transfer for transactions where the regulatory capital calculation used produces very low capital requirements. Where the method used to calculate regulatory capital requirements post-securitisation results in a particularly significant reduction in capital requirements, the PRA will apply a high degree of scrutiny in its assessment of whether commensurate risk transfer is achieved.

(CRR Articles 243 and 244)

5 Implicit support and SRT

5.1 The PRA will monitor the support provided by a firm to its securitisation transactions, and will consider this carefully in the assessment of commensurate risk transfer. As part of firms' on-going consideration of risk transfer, the PRA expects them to consider the support they have provided to securitisation transactions.

5.2 If a firm is found to have provided support to a securitisation, the expectation that the firm will provide future support to its securitisations is increased. The PRA will take account of this increased expectation in future assessments of commensurate risk transfer for that firm.

5.3 The PRA expects securitisation documentation to make clear, where applicable, that repurchase of securitisation positions by the originator beyond its contractual obligations is not mandatory and may only be made at fair market value.

5.4 Where a firm provides support which it is entitled, but not obliged, to provide under the contractual documentation of the securitisation, the PRA will consider the following factors in assessing if that support has been appropriately reflected in the assessment of SRT:

(a) whether the fact that the firm may provide such support was expressly set out in the contractual and marketing documents for the securitisation;

(b) whether the nature of the support that the firm may give is precisely described in the documentation;

(c) whether the maximum degree of support that could be provided could be ascertained at the time of the securitisation by the firm and by a person whose only information came from the marketing documents for the securitisation;

(d) whether the assessment of whether SRT was achieved and the amount of that risk transferred was made on the basis that the firm would provide support to the maximum degree possible; and

(e) whether the firm's own funds and own funds requirements were appropriately adjusted at the time of the securitisation on the basis that the firm provided support to the maximum degree possible.

5.5 If a firm failed to comply with CRR Article 248(1), the PRA may require it to disclose publically that it has provided non-contractual support to its transaction.

(CRD Article 98(3) CRR Articles 243, 244 and 248 and CRD4 Article 98)

6 High-cost credit protection and other SRT considerations

6.1 Some transactions transfer little or no economic risk from the protection buyer to the protection seller, but may nevertheless result in a reduction in regulatory capital requirements. An example of such a transaction-type is one in which protection is purchased on a junior tranche and a high premium is paid for that protection.

6.2 Generally, the amount of premium paid will not materially affect the assessment of whether significant risk transfer is achieved. This is because either:

- the protection payment payable upon default from protection seller to protection buyer is significantly larger than the overall premium payable to the protection seller; or

- the payment of premium leads to an immediate incurred cost.

6.3 However, there comes a point at which the premium payable for protection can reduce significantly the economic risk that is transferred from the protection buyer to protection seller. A premium payable of 100% of the protection amount could leave the protection buyer in a position over the life of the transaction that was no better than if protection had not been purchased.

6.4 The PRA expects originators seeking to apply the securitisation risk weights to synthetic securitisations to take into account all relevant factors to assess the extent of risk transferred. As well as the size and timing of amounts payable to the protection seller, the circumstances in which those amounts are payable can undermine the effectiveness of risk transfer. The PRA expects firms seeking capital relief through synthetic securitisations to incorporate premiums in their assessment of SRT. In particular, the following transaction features may have a significant impact on the extent of risk transfer:

- premium which is guaranteed in all or almost all circumstances, eg premium which is payable upfront or deferred;

- those that could result in the amount of premium payable for protection being significantly greater than the spread income on the assets in the portfolio or similar to the size of the hedged position; and

- those under which the protection buyer retains the expected loss through higher transaction costs to the counterparty, in the form of premium or otherwise.

6.5 Originators should have regard to the statement on high cost credit protection issued by the Basel Committee on Banking Supervision (www.bis.org/publ/bcbs_nl16.htm).

6.6 CRR requires maturity to be assessed in considering SRT. When considering the effective maturity of synthetic securitisations, the PRA expects firms to consider whether the transaction contained an option to terminate the protection at the discretion of the protection buyer. The PRA will consider the following to be examples of features which generally indicate a positive incentive for the protection buyer to call a transaction, or at least to constitute grounds for discussion with the PRA prior to the conclusion of the transaction:

- the transaction contains terms, such as payments at maturity or payments upon early termination or significant premiums, which may reduce risk transfer;

- the transaction includes a requirement for the protection buyer to incur additional costs or obligations if they do not exercise their option to terminate the protection; and

- there are pre-agreed mechanisms, for example 'at-market unwinds', where the protection seller and protection buyer agree that the transaction can be terminated in the future at a 'market' value and specifies aspects of how the value is calculated.

(CRR Articles 243 and 244)

7 Mapping of ECAI credit assessments to credit quality steps

7.1 The CRR requires the European Banking Authority (EBA) to produce implementing technical standards (ITS) mapping the credit assessments of ECAIs to the credit quality steps specified in the CRR for the purposes of calculating risk-weighted exposure amounts under the ratings-based approach.

7.2 EBA is required to submit those draft ITS to the European Commission by 1 July 2014. Prior to adoption of the EBA's ITS, the PRA would expect firms to continue to use the PRA mapping of ECAI credit assessments to credit quality steps, as set out in **Tables 3.A–3.D** below. These tables will be superseded by the EBA's mapping once that mapping has been adopted by the Commission.

Table 3.A Long-term mapping: standardised approach

Credit quality step	Risk weights	Fitch	Moody's	S&P	DBRS
1	20%	AAA to AA-	Aaa to Aa3	AAA to AA-	AAA to AAL
2	50%	A+ to A-	A1 to A3	A+ to A-	AH to AL
3	100%	BBB+ to BBB-	Baa1 to Baa3	BBB+ to BBB-	BBBH to BBBL
4	350%	BB+ to BB-	Ba1 to Ba3	BB+ to BB-	BBH to BBL
5	1,250%	B+ and below	B1 and below	B+ and below	BH and below

Table 3.B Long-term mapping: IRB approach

Credit quality step	Risk weights			Credit assessments			
	Most senior tranche	Base	Non-granular pool	Fitch	Moody's	S&P	DBRS
1	7%	12%	20%	AAA	Aaa	AAA	AAA
2	8%	15%	25%	AA	Aa	AA	AA1
3	10%	18%	35%	A+	A1	A+	AH
4	12%	20%	35%	A	A2	A	A
5	20%	35%	35%	A-	A3	A-	AL
6	35%	50%	50%	BBB+	Baa1	BBB+	BBBH
7	60%	75%	75%	BBB	Baa2	BBB	BBB
8	100%	100%	100%	BBB-	Baa3	BBB-	BBBL
9	250%	250%	250%	BB+	Ba1	BB+	BBH
10	425%	425%	425%	BB	Ba2	BB	BB
11	650%	650%	650%	BB-	Ba3	BB-	BBL
Below 11	1,250%	1,250%	1,250%	Below BB-	Below Ba3	Below BB-	Below BBL

Table 3.C Short-term mapping: standardised approach

Credit quality step	Risk weights	Fitch	Moody's	S&P	DBRS
1	20%	F1+, F1	P-1	A-1+, A-1	R-1 (high), R-1 (middle), R-1 (low)
2	50%	F2	P-2	A-2	R-2 (high), R-2 (middle), R-2 (low)
3	100%	F3	P-3	A-3	R-3
All other credit assessments	1,250%	Below F3	NP	All short-term ratings below A3	All short-term ratings below R-3

Table 3.D Short-term mapping: IRB approach

Credit quality step	Risk weights			Credit assessments			
	Most senior tranche	Base	Non-granular pool	Fitch	Moody's	S&P	DBRS
1	7%	12%	20%	F1+, F1	P-1	A-1+, A-1	R-1 (high), R-1 (middle), R-1 (low)
2	12%	20%	35%	F2	P-2	A-2	R-2 (high), R-2 (middle), R-2 (low)
3	60%	75%	75%	F3	P-3	A-3	R-3
All other credit assessments	1,250%	1,250%	1,250%	Below F3	All short-term ratings below A3, P3 and F3	All short-term ratings below A3	All short-term ratings below R-3

Standardised approach

1 Introduction
1.1 This statement is aimed at firms to which CRDIV applies.

1.2 The purpose of this statement is to set out the PRA's expectations in respect of certain aspects of a firm's implementation of the Standardised Approach to credit risk.

1.3 This statement supplements CRR Articles 119, 123, 124, 125, 128, 129, 136 and 208.

2 Exposures to institutions
2.1 The PRA confirms that, in relation to the concessionary treatment set out in CRR Article 119(5), there are no financial institutions currently authorised and supervised by it — other than those to which the CRR applies directly — that are subject to prudential requirements that the PRA considers to be comparable in terms of robustness to those applied to institutions under CRR.

(CRR Article 119(5))

3 Retail exposures
3.1 Where an exposure is denominated in a currency other than the euro, the PRA expects firms to use appropriate and consistent exchange rates to determine compliance with relevant CRR thresholds. Accordingly, the PRA expects a firm to calculate the euro equivalent value of the exposure for the purposes establishing compliance with the aggregate monetary limit of €1 million for retail exposures using a set of exchange rates the firm considers to be appropriate. The PRA expects a firm's choice of exchange rate to have no obvious bias and to be derived on the basis of a consistent approach.

(See CRR: Article 123(c))

4 Exposures fully and completely secured by mortgages on residential property
Ijara mortgages
4.1 The PRA considers an Ijara mortgage to be an example of an exposure to a tenant under a property leasing transaction concerning residential property under which the firm is the lessor and the tenant has an option to purchase.

4.2 Accordingly, the PRA expects exposures to Ijara mortgages to be subject to all of the requirements applicable to exposures secured by mortgages on residential property including in respect of periodic property revaluation.

(CRR Articles 124 and 125)

Lifetime mortgages
4.3 The PRA expects firms with lifetime mortgage exposures to inform the PRA of the difference in the capital requirements on those exposures under the CRR and the credit risk capital requirement that would have applied under BIPRU 3.4.56A. The PRA will use this information in its consideration of relevant risks in the PRA's supervisory assessments of firms.

(CRR Articles 124, 125 and 208)

5 Exposures in default
5.1 When determining the portion of a past due item that is secured, the PRA expects the secured portion of an exposure covered by a mortgage indemnity product that is eligible for credit risk mitigation purposes under Chapter 4 of the CRR potentially to qualify as an eligible guarantee.

(CRR Article 129(2))

6 Items associated with particular high risk
6.1 When determining whether exposures in the form of units or shares in a CIU are associated with particularly high risk, the PRA expects the following features would be likely to give rise to such risk:

(a) an absence of external credit assessment of the CIU from an ECAI recognised under the provisions of Article 132(2) of the CRR, and where the CIU has specific features (such as high levels of leverage or lack of transparency) that prevent it from meeting the eligibility criteria set out in Article 132(3) of the CRR; and

(b) a substantial element of the CIU's property is made up of items that would be subject to a risk weight of more than 100%, or the mandate of a CIU would permit it to invest in a substantial amount of such items.

6.2 The PRA would expect a firm's assessment of whether types of exposure referred to in Article 128(3) of the CRR are associated with particularly high risk to include consideration of exposures arising out of a venture capital business (whether the firm itself carries on the venture capital business or not) to be associated with particularly high risk. The PRA considers 'venture capital business' to include the business of carrying on any of the following:

(a) advising on investments which are, managing investments which are, arranging (bringing about) transactions in, or making arrangements with a view to transactions in, venture capital investments;

(c) advising on investments or managing investments in relation to portfolios, or establishing, operating or winding up collective investment schemes, where the portfolios or collective investment schemes (apart from funds awaiting investment) invest only in venture capital investments;

Table 3.E Mapping of ECAIs' credit assessments to credit quality steps for the purposes of the standardised approach

Long-term mapping

Credit quality step	Fitch's assessments	Moody's assessments	S&P's assessments	DBRS assessments	Corporate	Institution (includes banks)			Sovereign
							Credit assessment		
						Sovereign method	Maturity > three months	Maturity three months or less	
1	AAA to AA-	Aaa to Aa3	AAA to AA-	AAA to AAL	20%	20%	20%	20%	0%
2	A+ to A-	A1 to A3	A+ to A-	AH to AL	50%	50%	50%	20%	20%
3	BBB+ to BBB-	Baa1 to Baa3	BBB+ to BBB-	BBBH to BBBL	100%	100%	50%	20%	50%
4	BB+ to BB-	Ba1 to Ba3	BB+ to BB-	BBH to BBL	100%	100%	100%	50%	100%
5	B+ to B-	B1 to B3	B+ to B-	BH to BL	150%	100%	100%	50%	100%
6	CCC+ and below	Caa1 and below	CCC+ and below	CCCH and below	150%	150%	150%	150%	150%

Short-term mapping

Credit quality step	Fitch	Moody's	S&P	DBRS	Risk weights
1	F1+, F1	P-1	A-1+, A-1	R-1 (high), R-1 (middle), R-1 (low)	20%
2	F2	P-2	A-2	R-2 (high), R-2 (middle), R-2 (low)	50%
3	F3	P-3	A-3	R-3	100%
4	Below F3	NP	B-1, B-2, B-3, C	R-4, R-5	150%
5					150%
6					150%

Collective investment undertakings (CIUs)

Credit quality step	Risk weights	Fitch	Moody's	S&P	S&P
				Principal stability funds ratings	Fund credit quality ratings
1	20%	AAA to AA-	Aaa to Aa3	AAAm to AA-m	AAAf to AA-f
2	50%	A+ to A-	A1 to A3	A+m to A-m	A+f to A-f
3	100%	BBB+ to BBB-	Baa1 to Baa3	BBB+m to BBB-m	BBB+f to BBB-f
4	100%	BB+ to BB-	Ba1 to Ba3	BB+m to BB-m	BB+f to BB-f
5	150%	B+ to B-	B1 to B3	B+m to B-m	B+f to B-f
6	150%	CCC+ and below	Caa1 and below	CCC+ m and below	CCC+f and below

(d) any custody activities provided in connection with the activities in (a) or (b); and

(e) any related ancillary activities.

(CRR Article 128)

7 Mapping of ECAI credit assessments

7.1 Until such time as the Commission adopts ITS drafted by the ESA's Joint Committee, which specify for all ECAIs the relevant credit assessments of the ECAI that correspond to credit quality steps that are set out in the CRR, the PRA expects firms to continue to have regard to **Table 3.E** above mapping the credit assessments of certain ECAIs to credit quality steps.

(CRR Article 136(1))

Credit risk mitigation

1 Introduction

1.1 This supervisory statement is aimed at firms to which CRD IV applies.

1.2 The purpose of this supervisory statement is to provide clarification to firms of the PRA's expectations in respect of the recognition of credit risk mitigation in the calculation of risk-weighted exposure amounts. The statement supplements CRR Article 119(5), 202 and 227.

2 Eligibility of protection providers under all approaches

2.1 The PRA does not consider that there are any other eligible providers of unfunded credit protection in the form of financial institutions for which exposures to those financial institutions are treated as exposures to institutions according to Article 119(5) of the CRR. Accordingly, the PRA has no list of such providers to publish.

(CRR Article 119(5) and 202)

3 Conditions for applying a 0% volatility adjustment under the Financial Collateral Comprehensive method

3.1 For the purposes of repurchase transactions and securities lending or borrowing transactions, the PRA does not consider that there are any core market participants apart from those entities listed in Article 227(3) of the CRR.

(CRR Article 227)

Internal ratings based approaches

1 Introduction

1.1 This supervisory statement is aimed at firms to which CRD IV applies.

1.2 Article 143(1) of the CRR requires the PRA to grant permission to use the IRB Approach where it is satisfied that the requirements of Title II Chapter 3 of the CRR are met. The purpose of this supervisory statement is to provide explanation, where appropriate, of the PRA's expectations when assessing whether they meet those requirements, including in respect of the conservatism applied.

1.3 Responsibility for ensuring that internal models are appropriately conservative and are CRR compliant rests with firms themselves. The PRA stated in *The PRA's approach to banking supervision* that 'if a firm is to use an internal model in calculating its regulatory capital requirements, the PRA will expect the model to be appropriately conservative'.

1.4 Firms should be aware that where approval to use the IRB approach is subject to a joint decision under CRR Article 20, the expectations set out in this supervisory statement will be subject to discussion between the PRA and other EEA regulators regarding the joint decision.

1.5 Some parts of this supervisory statement will require revision in due course as a result of the development by the EBA of binding technical standards required by the CRR. The PRA would expect to amend or delete these parts of this supervisory statement when those technical standards enter into force.

1.6 The PRA expects that this document will be revised on a periodic basis.

2 Application of requirements to EEA groups applying the IRB approach on a unified basis

2.1 The CRR provides that where the IRB approach is used on a unified basis by an EEA group, the PRA is required to permit certain IRB requirements to be met on a collective basis by members of that group. The PRA considers that where a firm is reliant upon a rating system or data provided by another member of its group it will not meet the condition that it is using the IRB approach on a unified basis unless:

(a) the firm only does so to the extent that it is appropriate, given the nature and scale of the firm's business and portfolios and the firm's position within the group;

(b) the integrity of the firm's systems and controls is not adversely affected;

(c) the outsourcing of these functions meets the requirements of SYSC;[1] and

(d) the abilities of the PRA and the lead regulator of the group to carry out their responsibilities under the CRR are not adversely affected.

(CRR Article 20(6))

2.2 Prior to reliance being placed by a firm on a rating system, or data provided by another member of the group, the PRA expects the proposed arrangements to have been explicitly considered, and found to be appropriate, by the governing body of the firm.

2.3 If a firm uses a rating system or data provided by another group member, the PRA expects the firm's governing body to delegate those functions formally to the persons or bodies that are to carry them out.

(CRR Article 20(6))

3 Materiality of non-compliance

3.1 Where a firm seeks to demonstrate to the PRA that the effect of its non-compliance with the requirements of CRR Title II Chapter 3 is immaterial under CRR Article 146(b), the PRA expects a firm to have taken into account all instances of non-compliance with the requirements of the IRB approach and to have demonstrated that the overall effect of non-compliance is immaterial.

(CRR Article 146(b))

4 Corporate governance

4.1 Where the firm's rating systems are used on a unified basis pursuant to CRR Article 20(6), the PRA considers that the governance requirements in CRR Article 189 can be met only if the subsidiary undertakings have delegated to the governing body or designated committee of the EEA parent institution, EEA parent financial holding company or EEA parent mixed financial holding company responsibility for approval of all material aspects of rating and estimation processes.

(1) *Senior Management Arrangements, Systems and Controls*, as contained in the PRA Handbook.

4.2 The PRA expects an appropriate individual in a Significant Influence Function role to provide to the PRA on an annual basis written attestation that the rating system approvals required by the CRR have been carried out appropriately.

(CRR Article 189, CRR Article 20(6), CRD Article 3(1)(7))

5 Permanent partial use

Policy for identifying exposures

5.1 The PRA expects a firm that is seeking to apply the Standardised Approach on a permanent basis to certain exposures to have a well-documented policy, explaining the basis on which exposures would be selected for permanent exemption from the IRB approach. This policy should be provided to the PRA when the firm applies for permission to use the IRB approach and maintained thereafter. Where a firm also wishes to undertake sequential implementation, the PRA expects the firm's roll-out plan to provide for the continuing application of that policy on a consistent basis over time.

(CRR Article 143(1), CRR Article 148(1), CRR Article 150(1))

Exposures to sovereigns and institutions

5.2 The PRA may permit the exemption of exposures to sovereigns and institutions under CRR Articles 150(1)(a) and 150(1)(b) respectively, only if the number of material counterparties is limited and it would be unduly burdensome to implement a rating system for such counterparties.

5.3 The PRA considers that the 'limited number of material counterparties' test is unlikely to be met if for the UK group total exposures to 'higher-risk' sovereigns and institutions exceed either £1 billion or 5% of total assets (other than in the case of temporary fluctuations above these levels). For these purposes, 'higher-risk' sovereigns and institutions are considered to be those that are unrated or carry ratings of BBB+ (or equivalent) or lower. In determining whether to grant this exemption, the PRA will also consider whether a firm incurs exposures to 'higher-risk' counterparties which are below the levels set out below, but are outside the scope of its core activities.

5.4 In respect of the 'unduly burdensome' condition, the PRA considers that an adequate, but not perfect, proxy for the likely level of expertise available to a firm is whether its group has a trading book. Accordingly, if a firm's group does not have a trading book, the PRA is likely to accept the argument that it would be unduly burdensome to implement a rating system.

(CRR Article 150(1)(a) and CRR Article 150(1)(b))

Non-significant business units and immaterial exposures classes and types

5.5 Where a firm wishes permanently to apply the Standardised Approach to certain business units on the grounds that they are non-significant, and/or certain exposure classes or types of exposures on the grounds that they are immaterial in terms of size and perceived risk profile, the PRA expects to permit this exemption only to the extent that the risk-weighted exposure amounts calculated under paragraphs (a) and (f) of CRR Article 92(3) that are based on the Standardised Approach (insofar as they are attributable to the exposures to which the Standardised Approach is permanently applied) — would be no more than 15% of the risk-weighted exposure amounts calculated under paragraphs (a) and (f) of CRR Article 92, based on whichever of the Standardised Approach and the IRB Approach would apply to the exposures at the time the calculation was made.

5.6 The following points set out the level at which the PRA would expect the 15% test to be applied for firms that are members of a group:

(a) if a firm were part of a group subject to consolidated supervision in the EEA and for which the PRA was the lead regulator, the calculations in part (a) would be carried out with respect to the wider group;

(b) if a firm were part of a group subject to consolidated supervision in the EEA and for which the PRA was not the lead regulator the calculation set out in part (a) would not apply but the requirements of the lead regulator related to materiality would need to be met in respect of the wider group;

(c) if the firm were part of a subgroup subject to consolidated supervision in the EEA, and part of a wider third-country group subject to equivalent supervision by a regulatory authority outside of the EEA, the calculation set out in part (a) would not apply but the requirements of the lead regulator related to materiality would need to be met in respect of both the subgroup and the wider group; and

(d) if the firm is part of a subgroup subject to consolidated supervision in the EEA, and is part of a wider third-country group that is not subject to equivalent supervision by a regulatory authority outside of the EEA, then the calculation in part (a) would apply in respect of the wider group if supervision by analogy (as referred to in CRR) is applied and in respect of the subgroup if other alternative supervisory techniques are applied.

5.7 Whether a third-country group is subject to equivalent supervision, whether it is subject to supervision by analogy, as referred to in the CRR, or whether other alternative supervisory techniques apply, is decided in accordance with Article 126 of the CRD.

(CRR Article 150(1)(c) and CRD Article 126)

Identification of connected counterparties

5.8 Where a firm wished permanently to apply the Standardised Approach to exposures to connected counterparties in accordance with CRR Article 150(1)(e), the PRA will normally grant permission to do so only if the firm has a policy that identifies connected counterparty exposures that would be permanently exempted from the IRB approach and also identifies connected counterparty exposures (if any) that would not be permanently exempted. The PRA expects a firm to use the IRB approach either for all of its intra-group exposures or for none of them.

(CRR Article 150(1)(e))

6 Sequential implementation following significant acquisition

6.1 In the event that a firm with an IRB permission acquires a significant new business, it should discuss with the PRA whether sequential roll-out of the firm's IRB approach to these exposures would be appropriate. In addition, the PRA would expect to review any existing time period and conditions for sequential roll-out and determine whether these remain appropriate.

(CRR Article 148)

7 Classification of retail exposures

7.1 CRR Article 154(4)(d) specifies that for an exposure to be treated as a Qualified Revolving Retail Exposure (QRRE), it needs to exhibit relatively low volatility of loss rates. The PRA expects firms to assess the volatility of loss rates for the qualifying revolving retail exposure portfolio relative to the volatilities of loss rates of other relevant types of retail exposures for these purposes. Low volatility should be demonstrated by reference to data on the mean and standard deviation of loss rates over a time period that can be regarded as representative of the long-run performance of the portfolios concerned.

7.2 CRR Article 154(4)(e) specifies that for an exposure to be treated as a QRRE this treatment should be consistent with the underlying risk characteristics of the subportfolio. The PRA considers that a subportfolio consisting of credit card or overdraft obligations will usually meet this condition and that it is unlikely that any other type of retail exposure would do so. If a firm wishes to apply the treatment in CRR Article 154 (4) to product types other than credit card or overdraft obligations the PRA expects it to discuss this with the PRA before doing so.

(CRR Article 154(4))

8 Documentation

8.1 The PRA expects a firm to ensure that all documentation relating to its rating systems (including any documentation referenced in this Supervisory Statement or required by the CRR requirements that relate to the IRB approach) is stored, arranged and indexed in such a way that it could make them all, or any subset thereof, available to the PRA immediately on demand or within a short time thereafter.

9 Overall requirements for estimation

High-level expectations for estimation

9.1 In order to be able to determine that the requirements in CRR Article 144(1) have been met, the PRA would typically have the high level expectations set out in this subsection.

9.2 The PRA expects the information that a firm produces or uses for the purpose of the IRB approach to be reliable and take proper account of the different users of the information produced (customers, shareholders, regulators and other market participants).

9.3 The PRA expects firms to establish quantified and documented targets and standards, against which it should test the accuracy of data used in its rating systems. Such tests should cover:

(a) a report and accounts reconciliation, including whether every exposure has a PD, LGD and, if applicable, conversion factor for reporting purposes;

(b) whether the firm's risk control environment has key risk indicators for the purpose of monitoring and ensuring data accuracy;

(c) whether the firm has an adequate business and information technology infrastructure with fully documented processes;

(d) whether the firm has clear and documented standards on ownership of data (including inputs and manipulation) and timeliness of current data (daily, monthly, real time); and

(e) whether the firm has a comprehensive quantitative audit programme.

9.4 The PRA expects that in respect of data inputs, the testing for accuracy of data, including the reconciliation referred to above, should be sufficiently detailed so that, together with other available evidence, it provides reasonable assurance that data input into the rating system is accurate, complete and appropriate. The PRA considers that input data would not meet the required standard if it gave rise to a serious risk of material misstatement in the capital requirement, either immediately or subsequently.

9.5 In respect of data outputs, as part of the reconciliation referred to above, the PRA expects a firm to be able to identify and explain material differences between the outputs produced under accounting standards and those produced under the requirements of the IRB approach, including in relation to areas that address similar concepts in different ways (for example expected loss and accounting provisions).

9.6 The PRA expects a firm to have clear and documented standards and policies about the use of data in practice (including information technology standards) which should in particular cover the firm's approach to the following:

(a) data access and security;

(b) data integrity, including the accuracy, completeness, appropriateness and testing of data; and

(c) data availability.

(CRR Article 144(1)(a))

Ratings systems: policies

9.7 In order for the PRA to be satisfied that a firm documents its ratings systems appropriately in accordance with CRR Article 144(1)(e) the PRA expects a firm to be able to demonstrate that it has an appropriate policy in respect of its ratings systems in relation to:

(a) any deficiencies caused by its not being sensitive to movements in fundamental risk drivers or for any other reason;

(b) the periodic review and action in the light of such review;

(c) providing appropriate internal guidance to staff to ensure consistency in the use of the rating system, including the assignment of exposures or facilities to pools or grades;

(d) dealing with potential weaknesses of the rating system;

(e) identifying appropriate and inappropriate uses of the rating system and acting on that identification;

(f) novel or narrow rating approaches; and

(g) ensuring the appropriate level of stability over time of the rating system.

(CRR Article 144(1)(a) and CRR Article 144(1)(e))

Collection of data

9.8 In order to be satisfied that the requirements in CRR Article 179(1) are met, the PRA expects a firm to collect data on what it considers to be the main drivers of the risk parameters of Probability of Default (PD), Loss Given Default (LGD), Conversion Factor (CFs) and Expected Loss (EL), for each group of obligors or facilities, to document the identification of the main drivers of risk parameters, and to be able to demonstrate that the process of identification is reasonable and appropriate.

9.9 In its processes for identifying the main drivers of risk parameters, the PRA expects that a firm should set out its reasons for concluding that the data sources chosen provide in themselves sufficient discriminative power and accuracy, and why additional potential data sources do not provide relevant and reliable information that would be expected materially to improve the discriminative power and accuracy of its estimates of the risk parameter in question. The PRA would not expect this process necessarily to require an intensive analysis of all factors.

(CRR Article 179(1)(a), Article 179(1)(d), CRR Article 179(1)(e))

Data quality

9.10 In order to demonstrate that rating systems provide for meaningful assessment, the PRA expects that a firm's documentation relating to data include clear identification of responsibility for data quality. The PRA expects a firm to set standards for data quality, aim to improve them over time and measure its performance against those standards. Furthermore, the PRA expects a firm to ensure that its data are of sufficiently high quality to support the firm's risk management processes and the calculation of its capital requirements.

(CRR Article 144(1)(a))

Use of models and mechanical methods to produce estimates of parameters

9.11 Further detail of standards that the PRA would expect firms to meet when it assesses compliance with CRR Article 174 are set out in the sections on Probability of Default (PD), Loss Given Default (LGD) and Exposure at Default (EAD).

9.12 In assessing whether the external data used by a firm to build models are representative of its actual obligors or exposures, the PRA expects a firm to consider whether the data are appropriate to its own experience and whether adjustments are necessary.

(CRR Article 174, CRR Article 174(c))

Calculation of long-run averages of PD, LGD and EAD

9.13 In order to estimate PDs that are long-run averages of one year default rates for obligor grades or pools, the PRA expects firms to estimate expected default rates for the grade/pool over a representative mix of good and bad economic periods, rather than simply taking the historic average of default rates actually incurred by the firm over a period of years. The PRA expects that a long-run estimate would be changed when there is reason to believe that the existing long-run estimate is no longer accurate, but that it would not be automatically updated to incorporate the experience of additional years, as these may not be representative of the long-run average.

(CRR Article 180)

9.14 In order to be able to demonstrate compliance with CRR Article 144(1)(1), the PRA expects a firm to take into account the following factors in understanding differences between their historic default rates and their PD estimates, and in adjusting the calibration of their estimates as appropriate:

(a) the rating philosophy of the system and the economic conditions in the period over which the defaults have been observed;

(b) the number of defaults, as a low number is less likely to be representative of a long-run average. Moreover, where the number of internal defaults is low, there is likely to be a greater need to base PDs on external default data as opposed to purely internal data;

(c) the potential for under-recording of actual defaults; and

(d) the level of conservatism applied.

9.15 The PRA expects that a firm that is not able to produce a long-run estimate, as described above, to consider what action it would be appropriate for it to take to comply with CRR Article 180(1)(a). In some circumstances, it may be appropriate for firms to amend their rating system so that the PD used as an input into the IRB capital requirement is an appropriately conservative estimate of the actual default rate expected over the next year. However, such an approach is not likely to be appropriate where default rates are dependent on the performance of volatile collateral.

(CRR Article 179(1)(f) and CRR Article 180(1)(a))

9.16 In accordance with CRR Article 181(1)(b) and CRR Article 182(1)(b), where the estimates appropriate for an economic downturn are more conservative than the long-run average, we would expect the estimate for each of these parameters to represent the LGD or CF expected, weighted by the number of defaults, over the downturn period. Where this was not the case we would expect the estimate to be used to be the expected LGD or CF, weighted by the number of defaults, over a representative mix of good and bad economic periods.

(CRR Article 179, 181 and 182)

Assignment to grades or pools

9.17 In order to demonstrate that a rating system provided for a meaningful differentiation of risk and accurate and consistent quantitative estimates of risk the PRA expects that a firm would have regard to the sensitivity of the rating to movements in fundamental risk drivers, in assigning exposures to grades or pools within a rating system.

(CRR Article 171)

10 Definition of default

Identification of obligors

10.1 The PRA expects that if a firm ordinarily assigns exposures in the corporate, institution or central government and central bank exposure classes to a member of a group substantially on the basis of membership of that group and a common group rating, and the firm does so in the case of a particular obligor group, the firm should consider whether members of that group should be treated as a single obligor for the purpose of the definition of default set out in CRR Article 178(1).

10.2 The PRA would not expect a firm to treat an obligor as part of a single obligor under the preceding paragraph if the firm rated its exposures on a stand alone basis or if its rating was notched. (For these purposes a rating is notched if it takes into account individual risk factors, or otherwise reflects risk factors that are not applied on a common group basis.) Accordingly, if a group has two members which are separately rated, the PRA would not expect that the default of one would necessarily imply the default of the other.

Days past due

10.3 Under CRR Article 178(2)(d) the PRA is empowered to replace 90 days with 180 days in the days past due component of the definition of default for exposures secured by residential or SME commercial real estate in the retail exposure class, as well as exposures to public sector entities (PSEs).

10.4 We would expect to replace 90 days with 180 days in the days past due component of the definition of default for exposures secured by residential real estate in the retail exposure class where this was requested by the firm. Where this occurred, it would be specified in a firm's IRB permission.

Unlikeliness to pay: distressed restructuring

10.5 The PRA expects that a credit obligation be considered a distressed restructuring if an independent third party, with expertise in the relevant area, would not be prepared to provide financing on substantially the same terms and conditions.

(See CRR Article 178(2)(d))

Return to performing status

10.6 In order to be satisfied that a firm complies with the documentation requirements set out in CRR Article 175(3) the PRA expects that a firm should have a clear and documented policy for determining whether an exposure that has been in default should subsequently be returned to performing status.

(CRR Article 175(3))

11 Probability of default in IRB approaches

Rating philosophy[1]

11.1 'Rating philosophy' describes the point at which a rating system sits on the spectrum between the stylised extremes of a point in time (PiT) rating system and a through the cycle (TTC) rating system. Points (a) and (b) explain these concepts further:

(a) PiT: firms seek explicitly to estimate default risk over a fixed period, typically one year. Under such an approach the increase in default risk in a downturn results in a general tendency for migration to lower grades. When combined with the fixed estimate of the long-run default rate for the grade, the result is a higher capital requirement. Where data are sufficient, grade level default rates tend to be stable and relatively close to the PD estimates; and

(b) TTC: firms seek to remove cyclical volatility from the estimation of default risk, by assessing borrowers' performance across the economic cycle. TTC ratings do not react to changes in the cycle, so there is no consequent volatility in capital requirements. Actual default rates in each grade diverge from the PD estimate for the grade, with actual default rates relatively higher at weak points in the cycle and relatively lower at strong points.

11.2 Most rating systems sit between these two extremes. Rating philosophy is determined by the cyclicality of the drivers/criteria used in the rating assessment, and should not be confused with the requirement for grade level PDs to be 'long run'. The calibration of even the most PiT rating system needs to be targeted at the long-run default rates for its grades; the use of long-run default rates does not convert such a system into one producing TTC ratings or PDs.

11.3 Firms should understand where their rating systems lie on the PiT/TTC spectrum to enable them to estimate how changes in economic conditions will affect their IRB capital requirements. The PRA also expects firms to be able to compare the actual default rates incurred against the default rate expected over the same period given the economic conditions pertaining, as implied by their PD estimate.

Variable scalar approaches[2]

Use of variable scalar approaches

11.4 We use the term 'variable scalar' to describe approaches in which the outputs of an underlying, relatively PiT, rating system are transformed to produce final PD estimates used for regulatory capital requirements that are relatively non-cyclical. Typically this involves basing the resulting requirement on the long-run default rate of the portfolio or segments thereof.

11.5 CRR Article 169(3) allows the use of direct estimates of PDs, though such a measure could be assessed over a variety of different time horizons which CRR does not specify. Accordingly, the PRA considers it acceptable in principle to use methodologies of this type in lieu of estimation of long-run averages for the grade/pool/score of the underlying rating system where conditions set out below are met. Meeting these conditions would require firms using the variable scalar approach to have a deep understanding of how and why their default rates varied over time.

(a) firms meet the following four principles which address the considerable conceptual and technical challenges to be overcome in order to carry out variable scalar adjustments in an appropriate way:

Principle 1: both the initial calculations of and subsequent changes to the scalar should be able to take account of changes in default risk that are not purely related to the changes in the cycle;

Principle 2: a firm should be able accurately to measure the long-run default risk of its portfolio; this must include an assumption that there are no changes in the business written;

Principle 3: a firm should use a data series of appropriate length in order to provide a reasonable estimate of the long-run default rate referred to in paragraph 9.13; and

Principle 4: a firm should be able to demonstrate the appropriateness of the scaling factor being used across a portfolio.

(b) stress testing includes a stress test covering the downturn scenarios outlined by the PRA, based on the PDs of the underlying PiT rating system, in addition to the stress test based on the parameters used in the Pillar 1 capital calculation (ie the portfolio level average long-run default rates); and

(1) CP4/13 11–12.
(2) CP4/13 13–17.

(c) firms are able to understand and articulate upfront how the scaling factor would vary over time in order to achieve the intended effect.

11.6 The PRA will not permit firms using a variable scalar approach to revert to using a PiT approach during more benign economic conditions.

11.7 Principle 1 is the most important and challenging to achieve as it requires an ability to be able to distinguish movements not related to the economic cycle, from changes purely related to the economic cycle, and not to average these away. This is because a variable scalar approach removes the ability of a rating system to take account automatically of changes in risk through migration between its grades.

11.8 Accordingly, the PRA expects firms using a variable scalar approach to adopt a PD that is the long-run default rate expected over a representative mix of good and bad economic periods, assuming that the current lending conditions including borrower mix and attitudes and the firm's lending policies remain unchanged. If the relevant lending conditions or policies change, then we would expect the long-run default rate to change.

(CRR Article 180(1)(a), CRR Article 180(1)(b) and CRR Article 180(2)(a))

Variable scalar considerations for retail portfolios[1]

11.9 The PRA considers that until more promising account level arrears data is collected, enabling firms to better explain the movement in their arrears rate over time, the likelihood of firms being able to develop a compliant variable scalar approach for non-mortgage retail portfolios is low. This is because of the difficulty that firms have in distinguishing between movements in default rates that result from cyclical factors and those that result from non-cyclical reasons for these portfolios. In practice therefore the rest of this section applies to residential mortgage portfolios.

11.10 For the purposes of this subsection 'non-mortgage retail portfolios' refers to non-mortgage lending to individuals (eg credit cards, unsecured personal loans, auto-finance) but does not include portfolios of exposures to small and medium-sized entities (SMEs in the retail exposure class).

11.11 The PRA considers that one variable scalar approach, potentially compliant with the four principles set out above, could involve:

(a) segmenting a portfolio by its underlying drivers of default risk; and

(b) estimating separate long-run default rates for each of these segmented pools.

Segmentation

A firm that applied a segmentation approach properly could satisfy both Principle 1 and Principle 4. The choice of the basis of segmentation and the calibration of the estimated long-run default rate for the segments would both be of critical importance.

The PRA expects segmentation to be done on the basis of the main drivers of both willingness and ability to pay. In the context of residential mortgages, an example of the former is the amount of equity in the property and an example of the latter is the ratio of debt to income of the borrower. The PRA expects firms to:

- incorporate an appropriate number of drivers of risk within the segmentation to maximise the accuracy of the system;

- provide detailed explanations supporting their choices of drivers, including an explanation of the drivers they have considered but chosen not to use; and

- ensure that the drivers reflect their risk processes and lending policy, and are not be chosen using only statistical criteria (ie a judgemental assessment of the drivers chosen is applied).

(CRR Article 179(1)(d))

11.12 To the extent that the basis of segmentation is not sufficient completely to explain movements in non-cyclical default risk, the long-run default rate for that segment will not be stable (eg a change in the mix of the portfolio within the segment could change the long-run default rate). In such cases, we expect firms to make a conservative compensating adjustment to the calibration of the long-run average PD for the affected segments and to be able to demonstrate that the amount of judgement required to make such adjustments is not excessive. Where judgement is used, considerable conservatism may be required. The PRA expects conservatism applied for this reason not to be removed as the cycle changes.

Long-run default rate

11.13 The PRA expects firms to review and amend as necessary the long-run default rate to be applied to each segment on a regular (at least an annual) basis. When reviewing the long-run default rate to be applied to each segment, the PRA expects firms to consider the extent to which:

(a) realised default rates are changing due to cyclical factors and the scaling factors needs to be changed;

(b) new information suggests that both the PiT PDs and the long-run PDs should be changed; and

(1) CP4/13 18–38 (in part).

(c) new information suggests that the basis of segmentation should be amended.

11.14 The PRA expects that over time the actual default rates incurred in each segment would form the basis of PD estimates for the segments. However at the outset the key calibration issue is likely to be the setting of the initial long-run default rate for each segment, as this will underpin the PD of the entire portfolio for some years to come. The PRA expects firms to apply conservatism in this area and this is something on which the PRA is likely to focus on in particular in PRA model reviews.

Governance

11.15 The PRA expects firms to put in place a governance process to provide a judgemental overlay to assess their choices of segments, PD estimates and scalars, both initially and on a continuing basis. Moreover, where the basis of their estimation is a formulaic approach, we would consider that the act of either accepting or adjusting the estimate suggested by the formula would represent the exercise of judgement.

11.16 The PRA expects firms to consider what use they can make of industry information. However, we would expect firms to seek to measure the absolute level of and changes to their own default risk, rather than changes in default risk relative to the industry. Given the potential for conditions to change across in the market as a whole, the PRA expects a firm should not to draw undue comfort from the observation that its default risk is changing in the same way as the industry as a whole. Doing so would not allow them to meet Principle 1.

11.17 The PRA expects firms to be able to demonstrate that they have adequate information and processes in order to underpin the decisions outlined above on choice of segmentation, source of data, and adequacy of conservatism in the calibration, and that this information is reflected in the reports and information being used to support the variable scalar governance process. Given that, for retail business, these decisions would be likely to affect only the regulatory capital requirements of the firm and not the day-to-day running of its business, we will be looking for a high level of reassurance and commitment from firms' senior management to maintain an adequate governance process.

Data considerations

11.18 The PRA expects firms to consider the following issues when seeking to apply a variable scalar approach for UK mortgages:

(a) in respect of Principle 2, the commonly used Council for Mortgage Lenders database was based on arrears data and not defaults during a period, and the use of these data without further analysis and adjustment can undermine the accuracy of any calculations; and

(b) in respect of Principle 3, the historical data time period chosen for use in the calculations will vary the long-run PDs, and thus capital requirements, when there is no change in the underlying risk.

11.19 The PRA expects firms that are including mortgage arrears data as a proxy for default data to:

(a) carry out sensitivity analysis identifying the circumstances in which the assumption that arrears may be used as a proxy for default would produce inaccuracy in long-run PD estimates;

(b) set a standard for what might constitute a potentially significant level of inaccuracy, and demonstrate why in practice the use of this proxy would not result in any significant inaccuracy;

(c) establish a process for assessing the on-going potential for inaccuracy, including thresholds beyond which the level of inaccuracy may no longer be insignificant; and

(d) consider the use of conservative adjustments to address the potential inaccuracy.

11.20 When using historical mortgage data as a key input into variable scalar models the PRA expects firms to:

(a) carry out sensitivity analysis identifying the implications of using different cut-off dates for the start of the reference data set; and

(b) justify the appropriateness of their choice of cut-off date.

Retail exposures: obligor level definition of default

11.21 Where a firm has not chosen to apply the definition of default at the level of an individual credit facility in accordance with CRR Article 178(1), the PRA expects it to ensure that the PD associated with unsecured exposures is not understated as a result of the presence of any collateralised exposures.

11.22 The PRA expects the PD of a residential mortgage would typically be lower than the PD of an unsecured loan to the same borrower.

(CRR Article 178(1))

Retail exposures: facility level definition of default

11.23 Where a firm chooses to apply the definition of default at the level of an individual credit facility in accordance with CRR Article 178(1) and a customer has defaulted on a facility, then default on that facility is likely to influence the PD assigned to that customer on other facilities. The PRA expects firms to take this into account in its estimates of PD.

(CRR Article 178(1))

Multi-country mid-market corporate PD models[1]

11.24 In order to ensure that a rating system provides a meaningful differentiation of risk and accurate and consistent quantitative estimates of risk, the PRA would expect firms to develop country-specific mid-market PD models. Where firms develop multi-country mid-market PD models, we would expect firms to be able to demonstrate that the model rank orders risk and predicts default rates for each country where it is to be used for regulatory capital calculation.

11.25 The PRA expects firms to have challenging standards in place to meaningfully assess whether a model rank orders risk and accurately predict default rates. These standards should specify the number of defaults that are needed for a meaningful assessment to be done.

11.26 We would expect firms to assess the model's ability to predict default rates using a time series of data (ie not only based on one year of default data).

11.27 In our view a model is not likely to be compliant where the firm cannot demonstrate that it rank orders risk and predicts default rates for each country regardless of any apparent conservatism in the model.

Use of external ratings agency grades[2]

11.28 We would expect firms using a rating agency grades as the primary driver in their IRB models to be able to demonstrate (and document) compliance with the following criteria:

(a) the firm has its own internal rating scale;

(b) the firm has a system and processes in place that allow it continuously to collect and analyse all relevant information, and the 'other relevant information' considered by the firm in accordance with CRR Article 171(2) reflects the information collected and analysed by the firm when extending credit to new or existing obligors;

(c) the 'other relevant information' considered by the firm is included in an IRB model in a transparent and objective way and is subject to challenge. We would expect the firm to be able to demonstrate what information was used and why, and, how it was included; and if no additional information is included, to be able to document what information was discarded and why;

(d) the development of final grades includes the following steps:

   (i) the firm takes into account all available information (eg external agency grades and any 'other relevant information') prior to allocating obligors to internal grades. The firm does not automatically assign obligors to grades based on the rating agency grade;

   (ii) any overrides are applied to these grades; and

   (iii) the firm has a system and processes in place that allows it to continuously collect and analyse final rating overrides.

(e) the grades to which obligors are assigned is reassessed at least annually. The firm is able to demonstrate how the grades are reassessed on a more frequent than annual basis when new relevant information becomes available; and

(f) firms can demonstrate that a modelling approach is being applied, both in terms of the choice of the rating agency grade as the primary driver and, where information is found materially and consistently to add to the accuracy or predictive power of the internal rating grade, that they have incorporated this information as an additional driver. The PRA expects this work to be analytical (rather than entirely subjective) and could form part of the annual independent review of the model.

11.29 In the PRA's view, if a firm does not have any additional information to add to the external ratings for the significant part of its portfolio then the PRA expects it will not meet the requirements for using an IRB approach.

Low default portfolios[3]

11.30 The PRA expects a firm to estimate PD for a rating system in accordance with this section where a firm's internal experience of defaults for that rating system was 20 or fewer, and reliable estimates of PD cannot be derived from external sources of default data including the use of market price related data. In PD estimation for all exposures covered by that rating system, the PRA expects firms to:

(a) use a statistical technique to derive the distribution of defaults implied by the firm's experience, estimating PDs (the 'statistical PD') from the upper bound of a confidence interval set by the firm in order to produce conservative estimates of PDs in accordance with CRR Article 179(f);

(1) CP4/13 35–38.
(2) CP4/13 39–40.
(3) BIPRU 4.3.95R.

(b) use a statistical technique to derive the distribution of default which takes account, as a minimum, of the following modelling issues:

(i) the number of defaults and number of obligor years in the sample;

(ii) the number of years from which the sample was drawn;

(iii) the interdependence between default events for individual obligors;

(iv) the interdependence between default rates for different years; and

(v) the choice of the statistical estimators and the associated distributions and confidence intervals.

(c) further adjust the statistical PD to the extent necessary to take account of the following:

(i) any likely differences between the observed default rates over the period covered by the firm's default experience and the long-run PD for each grade required by CRR Article 180(1)(a) and CRR Article 180(2)(a); and

(ii) any other information that indicates (taking into account the robustness and cogency of that information) that the statistical PD is likely to be an inaccurate estimate of PD.

11.31 The PRA expects firms to take into account only defaults that occurred during periods that are relevant to the validation under the CRR of the model or other rating system in question when determining whether there are 20 defaults or fewer.

Supervisory slotting criteria for specialised lending

11.32 The PRA expects firms to assign exposures to the risk weight category for specialised lending exposures based on the criteria set out in the tables in Appendix A. Draft EBA regulatory technical standards due to be developed by 31 December 2014 will specify these assignments.

12 Loss Given Default in IRB approaches

Negative LGDs

12.1 The PRA expects firms to ensure that no LGD estimate is less than zero.

Low LGDs

12.2 The PRA does not expect firms to be using zero LGD estimates in cases other than where they had cash collateral supporting the exposures.

12.3 The PRA expects firms to justify any low LGD estimates using analysis on volatility of sources of recovery, notably on collateral, and cures (as outlined below). This includes:

(a) recognising that the impact of collateral volatility on low LGDs is asymmetric as surpluses over amounts owed need to be returned to borrowers and that this effect may be more pronounced when estimating downturn rather than normal period LGDs; and

(b) recognising the costs and discount rate associated with realisations and the requirements of CRR Article 181(1)(e).

12.4 In order to ensure that the impact of collateral volatility is taken into account, the PRA expects firms' LGD framework to include non-zero LGD floors which are not solely related to administration costs.

(CRR Article 179(1)(f))

Treatment of cures[1]

12.5 Where firms wish to include cures in their LGD estimates, the PRA expects them to do so on a cautious basis with reference to both their current experience and how this is expected to change in downturn conditions. In particular, this involves being able to articulate clearly both the precise course of events that will allow such cures to take place and any consequences of such actions for other elements of their risk quantification. For example:

(a) Where cures are driven by the firm's own policies, we would expect firms to consider whether this is likely to result in longer realisation periods and larger forced sale discounts for those exposures that do not cure, and higher default rates on the book as a whole, relative to those that might be expected to result from a less accommodating attitude. To the extent feasible, the PRA expects cure assumptions in a downturn to be supported by relevant historical data.

(b) The PRA expects firms to be aware of and properly account for the link between cures and subsequent defaults. In particular, an earlier cure definition is, other things being equal, likely to result in a higher level of subsequent defaults.

(CRR Article 5(2))

Incomplete workouts

12.6 In order to ensure that estimates of LGDs take into account the most up to date experience, we would expect firms to take account of data in respect of relevant incomplete

(1) CP4/13 51.

workouts (ie defaulted exposures for which the recovery process is still in progress, with the result that the final realised losses in respect of those exposures are not yet certain).

(CRR Article 179(1)(c))

LGD — sovereign floor[1]

12.7 To ensure that Sovereign LGD models are sufficiently conservative in view of the estimation error that may arise from the lack of data on losses to sovereigns, the PRA expects firms to apply a 45% LGD floor to each unsecured exposure in the sovereign asset class.

(CRR Articles 144(1) and 179(1)(a)

LGD — UK retail mortgage property sales reference point[2]

12.8 The PRA believes that an average reduction in property sales prices of 40% from their peak price, prior to the market downturn, forms an appropriate reference point when assessing downturn LGD for UK mortgage portfolios. This reduction captures both a fall in the value of the property due to house price deflation as well as a distressed forced sale discount.

12.9 Where firms adjust assumed house price values within their LGD models to take account of current market conditions (for example with reference to appropriate house price indices) we recognise that realised falls in market values may be captured automatically. Firms adopting such approaches may remove observed house price falls from their downturn house price adjustment so as not to double count. The PRA expects all firms wishing to apply such an approach to seek the consent of the PRA and to be able to demonstrate that the following criteria are met:

(a) the adjustment applied to the market value decline element of a firm's LGD model is explicitly derived from the decrease in indexed property prices (ie the process is formulaic, not judgemental);

(b) the output from the adjusted model has been assessed against the 40% peak-to-trough property sales prices decrease reference point (after inclusion of a forced sale discount);

(c) a minimum 5% market value decline applies at all times in the LGD model; and

(d) the firm has set a level for reassessment of the property market price decline from its peak. For example, if a firm had initially assumed a peak-to-trough market decline of 15%, then it will have set a level of market value decline where this assumption will be reassessed.

CRR Article 181(1)(b))

Downturn LGDs

12.10 In order to ensure that their LGD estimates are oriented towards downturn conditions, the PRA expects firms to have a process through which they:

(a) identify appropriate downturn conditions for each IRB exposure class within each jurisdiction;

(b) identify adverse dependencies, if any, between default rates and recovery rates; and

(c) incorporate adverse dependencies, if identified, between default rates and recovery rates in the firm's estimates of LGD in a manner that meets the requirements relating to an economic downturn.

(CRR Article 181(1)(b))

Discounting cash flows

12.11 In order to ensure that their LGD estimates incorporate material discount effects, the PRA expects firms' methods for discounting cash flows to take account of the uncertainties associated with the receipt of recoveries with respect to a defaulted exposure, for example by adjusting cash flows to certainty equivalents or by using a discount rate that embodies an appropriate risk premium; or by a combination of the two.

12.12 If a firm intends to use a discount rate that does not take full account of the uncertainty in recoveries, we would expect it to be able to explain how it has otherwise taken into account that uncertainty for the purposes of calculating LGDs. This can be addressed by adjusting cash flows to certainty equivalents or by using a discount rate that embodies an appropriate risk premium for defaulted assets; or by a combination of the two.

12.13 In addition to the above measures the PRA expects firms to ensure that no discount rate used to estimate LGD is less than 9%.

(CRR Article 5(2))

Wholesale LGD[3]

12.14 The PRA expects firms using AIRB approaches to have done the following in respect of wholesale LGD estimates:

(a) applied LGD estimates at transaction level;

(b) ensured that all LGD estimates (both downturn and non-downturn) are cautious, conservative and justifiable, given the paucity of observations. In

(1) CP4/13 41.
(2) CP4/13 43–44.
(3) CP4/13 45–47.

accordance with Article 179(1)(a), estimates must be derived using both historical experience and empirical evidence, and not be based purely on judgemental consideration. We expect the justification as to why the firm thinks the estimates are conservative to be documented;

(c) identified and explained at a granular level how each estimate has been derived. This should include an explanation of how internal data, external data, expert judgement or a combination of these has been used to produce the estimate;

(d) clearly documented the process for determining and reviewing estimates, and the parties involved in the process in cases where expert judgement was used;

(e) demonstrated an understanding of the impact of the economic cycle on collateral values and be able to use that understanding in deriving their downturn LGD estimates;

(f) demonstrated sufficient understanding of any external benchmarks used and identified the extent of their relevance and suitability to the extent that the firm can satisfy itself that they are fit for purpose;

(g) evidenced that they are aware of any weaknesses in their estimation process and have set standards, for example related to accuracy, that their estimates are designed to meet;

(h) demonstrated that they have sought and utilised relevant and appropriate external data, including through identifying all relevant drivers of LGD and how these will be affected by a downturn;

(i) ensured, in most cases, estimates incorporate effective discrimination on the basis of at least security type and geography. In cases where these drivers are not incorporated into LGD estimates then we would expect the firm to be able to demonstrate why they are not relevant;

(j) have put in place an on-going data collection framework to collect all relevant internal loss and exposure data required for estimating LGD and a framework to start using these data as soon as any meaningful information becomes available; and

(k) ensured it can articulate the data the firm intends to use from any industry-wide data collection exercises in which it is participating, and how the data will be used.

(CRR Section 6)

12.15 We have developed a framework for assessing the conservatism of firms' wholesale LGD models for which there are a low number of defaults. The framework is set out in Appendix C and does not apply to sovereign LGD estimates which are floored at 45%. We are in the process of using this framework to assess the calibration of firms' material LGD models for low-default portfolios.

12.16 In the following cases, the PRA expects firms to determine the effect of applying the framework set out in Appendix C to models which include LGD values that are based on fewer than 20 'relevant' data points (as defined in Appendix C):

(a) the model is identified for review by the PRA; or

(b) the firm submits a request for approval for a material change to its LGD model.

12.17 In such cases firms should contact their supervisor to obtain the relevant data templates that should be populated and submitted to the PRA.

Unexpected loss on defaulted assets[1]

12.18 The CRR is unclear in how UL should be calculated for defaulted assets. This was also the case for the BCD. The answer to transposition group question 655 on the calculation of UL for defaulted assets under the BCD referred to two approaches:

(a) the independent calculation approach, in which possible losses are estimated over the recovery period that are additional to the best estimate; and

(b) subtraction of the best estimate of expected loss from post-default LGD.

12.19 The PRA considers that both of the approaches set out in the CRD transposition group answer are acceptable in principle.

12.20 Where an independent calculation approach is adopted for the calculation of unexpected loss on defaulted assets the PRA expects firms to ensure that estimates are at least equal, at a portfolio level, to a 100% risk-weight/8% capital requirement on the amount outstanding net of provisions.

(CRR Article 181(1)(h))

(1) CP4/13 48–50.

Unsecured LGDs where the borrowers' assets are substantially used as collateral[1]

12.21 The extent to which a borrower's assets are already given as collateral will affect the recoveries available to unsecured creditors. If the degree to which assets are pledged is substantial this will be a material driver of LGDs on such exposures. Although potentially present in all transactions, the PRA expects firms to be particularly aware of this driver in situations in which borrowing on a secured basis is the normal form of financing, leaving relatively few assets available for the unsecured debt. Specialist lending (including property), hedge funds, some SME/mid-market lending are examples of such cases.

12.22 The PRA expects firms to take into account the effect of assets being substantially used as collateral for other obligations estimating LGDs for borrowers for which this is the case. The PRA expects firms not to use unadjusted data sets that ignore this impact, and note that it is an estimate for downturn conditions that is normally required. In the absence of relevant data to estimate this effect, conservative LGDs — potentially of 100% — are expected to be used.

(CRR Articles 171(2), 179(1)(a))

13 Own estimates of exposure at default (EAD) in IRB approaches

Estimation of EAD in place of conversion factors[2]

13.1 The PRA considers that a firm may provide own estimates of EAD in place of the own estimates of conversion factors (CFs) that it is permitted or required to provide under CRR Article 151.

13.2 In this supervisory statement references to EAD refer to both direct estimates of EAD and CFs unless specified otherwise.

(CRR Article 151)

General expectations for estimating EAD[3]

13.3 The PRA expects that EAD estimates should not be less than current drawings (including interest accrued to date). Consequently, the PRA expects CF estimates not to be less than zero.

13.4 The EAD required for IRB purposes is the exposure(s) expected to be outstanding under a borrower's current facilities should it go into default in the next year, assuming that economic downturn conditions occur in the next year and a firm's policies and practices for controlling exposures remain unchanged other than changes that result from the economic downturn conditions.

13.5 In order to achieve sufficient coverage of the EAD, the PRA expects firms to take into account all facility types that may result in an exposure when an obligor defaults, including uncommitted facilities.

13.6 To the extent that a firm makes available multiple facilities, the PRA expects firms to be able to demonstrate:

(a) how they deal with the fact that exposures on one facility may become exposures under another on which the losses are ultimately incurred; and

(b) the impact of its approach on its capital requirements.

13.7 The PRA expects firms using own estimates of EAD to have done the following in respect of EAD estimates:

(a) applied EAD estimates at the level of the individual facility;

(b) where there is a paucity of observations, ensured that all EAD estimates are cautious, conservative and justifiable. In accordance with Article 179(1)(a), estimates must be derived using both historical experience and empirical evidence, and must not be based purely on judgemental consideration. The PRA would expect the justification as to why the firm thinks the estimates are conservative to be documented;

(c) identified and explained at a granular level how each estimate has been derived. This should include an explanation of how internal data, any external data, expert judgement or a combination of these has been used to produce the estimate.

(d) ensured that where expert judgement has been used there is clear documentation of the process for arriving at and reviewing the estimates, and identifying the parties involved;

(e) demonstrated an understanding of the impact of the economic cycle on exposure values and be able to use that understanding in deriving downturn EAD estimates;

(f) demonstrated sufficient understanding of any external benchmarks used and identified the extent of their relevance and suitability to the extent that the firm can satisfy itself that they are fit for purpose;

(g) evidenced that they are aware of any weaknesses in their estimation process and have set standards that their estimates are designed to meet (eg related to accuracy);

(1) CP4/13 54–56.
(2) CP4/13 65.
(3) CP4/13 57–61.

(h) ensured, in most cases, that estimates incorporate effective discrimination on the basis of at least product features and customer type. In cases where these drivers are not incorporated into EAD estimates then the PRA expects the firm to be able to demonstrate why they are not relevant;

(i) have an on-going data collection framework in place to collect all relevant internal exposure data required for estimating EAD and a framework to start using this data as soon as any meaningful information becomes available;

(j) made use of the data they are collecting to identify all relevant drivers of EAD and to understand how these drivers will be affected by a downturn; and

(k) identified dependencies between default rates and conversion factors for various products and markets when estimating downturn EADs. Firms are expected to consider how they expect their own policies regarding exposure management to evolve in a downturn.

13.8 The PRA has developed a framework for assessing the conservatism of firms' wholesale EAD models for which there are a low number of defaults. The PRA is in the process of using this framework to assess the calibration of firms' material EAD models for low-default portfolios.

13.9 In the following cases, the PRA expects firms to determine the effect of applying the framework set out in Appendix C to models which include EAD values that are based on fewer than 20 'relevant' data points (as defined in Appendix C):

(a) the model is identified for review by the PRA; or

(b) the firm submits a request for approval for a material change to its EAD model.

13.10 In such cases firms should contact their supervisor to obtain the relevant data templates that should be populated and submitted to the PRA.

(CRR Articles 4(56), 166, Section 6)

Time horizon[1]

13.11 The PRA expects firms to use a time horizon of one year for EAD estimates, unless they can demonstrate that another period would be more conservative.

13.12 EAD estimates can be undertaken on the basis that default occurs at any time during the time horizon (the 'cohort approach'), or at the end of the time horizon (the 'fixed-horizon approach'). The PRA considers that either approach is acceptable in principle.

13.13 The PRA expects the time horizon for additional drawings to be the same as the time horizon for defaults. In effect this means that EAD estimation need cover only additional drawings that might take place in the next year, such that:

(a) no capital requirement need be held against facilities, or proportions of facilities that cannot be drawn down within the next year; and

(b) where facilities can be drawn down within the next year, firms may in principle reduce their estimates to the extent that they can demonstrate that they are able and willing, based on a combination of empirical evidence, current policies, and documentary protection to prevent further drawings.

(CRR Article 182)

Direct estimates of EAD[2]

13.14 There are a range of approaches that focus on the total amount that will be drawn down at the time of default and directly estimate EAD. Typically, but not in all cases, these will estimate EAD as a percentage of Total Limit. These approaches can be described collectively as 'momentum' approaches.

13.15 A 'momentum' approach can be used either:

(a) by using the drawings/limit percentage to formulaically derive a conversion factor on the undrawn portion of the limit; or

(b) by using the higher of percentage of the limit and the current balance as the EAD.

13.16 The PRA considers that the use of momentum approaches in both of the ways outlined above is acceptable in principle as an alternative to direct estimation of conversion factors.

(CRR Article 4(56))

Distortions to conversion factor estimates caused by low undrawn limits[3]

13.17 In cases where firms estimate conversion factors (CFs) directly, using a reference data set that includes a significant number of high CFs as a result of very low undrawn limits at the observation date, the PRA expects firms to:

(1) CP4/13 61–64.
(2) CP4/13 65–69.
(3) CP4/13 71–77.

(a) investigate the distribution of realised CFs in the reference data set;

(b) base the estimated CF on an appropriate point along that distribution that results in the choice of a CF appropriate for the exposures to which it is being applied and consistent with the requirement in Article 179 for estimates to include a margin of conservatism related to errors; and

(c) be cognisant that while the median of the distribution might be a starting point, they should not assume without analysis that the median represents a reasonable unbiased estimate. The PRA expects firms to consider whether the pattern of distribution in realised CFs means that some further segmentation is needed (eg treating facilities that are close to full utilisations differently).

(CRR Article 182(1)(a))

Identification of exposures for which an EAD must be estimated

13.18 The PRA expects firms to treat a facility as an exposure from the earliest date at which a customer is able to make drawings under it.

13.19 Where the facility is of the type that it is customary not to advise the borrower of its availability, the PRA expects an EAD/CF to be applied from the time that the existence of the facility is recorded on the firm's systems in a way that would allow the borrower to make a drawing.

13.20 If the availability of a facility is subject to a further credit assessment by the firm, an EAD/CF may not be required. However, the PRA expects this to be the case only if the subsequent credit assessment were of substantially equivalent rigour to that of the initial credit approval, and if this includes a re-rating or a confirmation of the rating of the borrower.

13.21 Firms are not expected to include in their EAD/CF estimates the probability of increases in limits between observation and default date. If the reference data set included the impact of such increases, the PRA expects firms to be able to adjust their estimates accordingly with the aim of assessing what the exposure would have been at default if the limit had not been increased.

13.22 The PRA expects firms to investigate the incidence of exposures existing at default that arise from products or relationships that are not intended to result in a credit exposure and, consequently, have no credit limit established against them and are not reflected in their estimates of EAD. Unless such exposures are immaterial, the PRA expects firms to apply a Pillar 1 capital charge on a portfolio basis to such exposures.

13.23 The PRA expects firms to investigate how their EAD estimates are impacted by exposures that are in excess of limits at either the observation date (if in the reference data set) or at the current reporting date (for the existing book to which estimates need to be applied). Unless a momentum approach is being used exposures in excess of limit should be excluded from the reference data set (as the undrawn limit is negative and nonsensical answers would result from their inclusion). The PRA expects firms to ensure that their EAD estimation includes the risk of further drawings on accounts that are in excess of their limits.

(CRR Article 4(56))

Accrued interest[1]

13.24 Exposures include not only principal amounts borrowed under facilities but also interest accrued which will fluctuate between payment dates. In order to ensure proper coverage of interest, we would expect firms to take the following approach:

(a) accrued interest to date should be included in current exposure for performing exposures;

(b) firms may choose whether estimated increases in accrued interest up to the time of default should be included in LGD or EAD;

(c) in the estimation of EAD increases in accrued interest may be offset against reductions in other outstandings;

(d) estimation of changes in accrued interest needs to take account of changes in the contractual interest rate over the time horizon up to default, and in a way consistent with the scenario envisaged in the calculation of the downturn/default weighted average;

(e) inclusion of estimates of future post-default interest is not necessary in either EAD or LGD; and

(f) firms' accounting policies will determine the extent to which interest accrued to date is reflected in current exposure as opposed to LGD for defaulted exposures.

(CRR Article 166(1))

Netting[2]

13.25 As regards current balances, netting may be applied in those cases where a firm meets the general conditions for on balance sheet netting set out in the CRR.

(1) CP4/13 78.
(2) CP4/13 79–81.

13.26 As regards the CF on undrawn limits, this may be applied on the basis of the net limit provided the conditions in the CRR for the use of net limits are met. However, firms are reminded that the purpose of the measure is to estimate the amount that would be outstanding in the event of a default. This implies that their ability in practice to constrain the drawdown of credit balances will be particularly tested. Moreover the PRA expects the appropriate conversion factor to be higher as a percentage of a net limit than of a gross limit.

13.27 The lower the net limit as a percentage of gross limits or exposures, the greater will be the need on the part of the firm to ensure that it is restricting exposures below net limits in practice and that it will be able to continue to do so should borrowers encounter difficulties. The application of a zero net limit is acceptable in principle, but there is a consequently a very high obligation on the firm to ensure that breaches of this are not tolerated.

(CRR Article 166(3))

Underwriting commitments[1]

13.28 Estimation of CFs on underwritten facilities in the course of primary market syndication may take account of anticipated sell down to other parties.

13.29 Firms are reminded that since the basis of EAD estimation is that default by the borrower is expected to take place in a one-year time horizon, and quite possibly in downturn conditions, the PRA expects any reduction in their CF in anticipation of syndication to take account of this scenario.

(CRR Article 4(56))

14 Stress tests used in assessment of capital adequacy

14.1 In order to be satisfied that the credit risk stress test undertaken by a firm pursuant to CRR Article 177(2) is meaningful and considers the effects of severe, but plausible, recession scenarios the PRA would expect that the stress test would be based on an economic cycle that is consistent with the Supervisory Statement on the SREP.

(CRR Article 177(2))

15 Validation

15.1 The PRA expects a firm to have a validation process that includes the following:

(a) standards of objectivity, accuracy, stability and conservatism that it designs its ratings systems to meet and processes that establish whether its rating systems meet those standards;

(b) standards of accuracy of calibration (ie whether outcomes are consistent with estimates) and discriminative power (ie the ability to rank-order risk) that it designs its rating systems to meet and processes that establish whether its rating systems meet those standards;

(c) policies and standards that specify the actions to be taken when a rating system fails to meet its specified standards of accuracy and discriminative power.

(d) a mix of developmental evidence, benchmarking and process verification and policies on how this mixture varies between different rating systems;

(e) use of both quantitative and qualitative techniques;

(f) policies on how validation procedures are expected to vary over time; and

(g) ensuring independent input into and review of its rating systems.

(CRR Article 188)

15.2 In the paragraph above:

(a) developmental evidence means evidence that substantiates whether the logic and quality of a rating system (including the quantification process) adequately discriminates between different levels of, and delivers accurate estimates of PD, EL, LGD and conversion factors (as applicable); and

(b) process verification means the process of establishing whether the methods used in a rating system to discriminate between different levels of risk and to quantify PD, EL, LGD and conversion factors are being used, monitored and updated in the way intended in the design of the rating system.

(CRR Article 188)

15.3 The PRA expects a firm to be able to explain the performance of its rating systems against its chosen measure (or measures) of discriminative power. In making this comparison a firm should rely primarily on actual historic default experience where this is available. In particular, the PRA expects a firm be able to explain the extent of any potential inaccuracy in these measures, caused in particular by small sample size and the potential for divergence in the future, whether caused by changing economic conditions or other factors. Firms' assessment of discriminative power

(1) CP4/13 82.

should include appropriate use of external benchmarks where available.

15.4 The PRA will take into consideration the sophistication of the measure of discrimination chosen when assessing the adequacy of a rating system's performance.

15.5 In the case of a portfolio for which there is insufficient default experience to provide any confidence in statistical measures of discriminative power, the PRA expects a firm to use other methods. For example, analysis of whether the firm's rating systems and an external measurement approach, eg external ratings, rank common obligors in broadly similar ways. The PRA expects a firm to be able to explain the methodology it uses and the rationale for its use

16 Income-producing real estate portfolios

CRR compliance(1)

16.1 The PRA considers income-producing real estate (IPRE) to be a particularly difficult asset class for which to build effective rating systems that are compliant with the CRR's requirements for the IRB approach.

16.2 As with all asset classes, firms should assess whether their IPRE model is CRR compliant and not whether it is the nearest they can get to compliance given the constraints imposed on their model development (eg lack of data or resource constraints).

16.3 Where material non-compliance is identified and cannot be remediated in a timely fashion, firms should adopt a compliant approach for calculating regulatory capital. In most cases this is likely to be the slotting approach.

(CRR Article 144(1))

Drivers of risk(2)

16.4 The PRA expects firms to be able to demonstrate that the model drivers selected offer sufficient discriminatory power and to justify why other potential data sources are not expected to materially improve the discriminatory power and accuracy of estimates.

16.5 The PRA expects that an IPRE rating system will only be compliant if a firm is able to demonstrate the following in respect of its treatment of cash flows (except where the firm can demonstrate that this is not an appropriate risk driver):

(a) the difference in deal ratings when tenant ratings are altered is intuitive;

(b) the transformation of ratings into non-rent payment probability is intuitive. Even where tenants are rated by the firm the PD will not usually represent a direct read across to probability of non-payment due to, for example, model philosophy issues. Addressing this is likely to be a key area since many firms struggle with defining what divergence is expected between observed default rate and PD in different economic conditions in the mid corporate space;

(c) selection of parameter values and/or distributions, and their impact on deal ratings, is well supported and intuitive;

(d) impact on the deal rating is intuitive for such features as: type of building, geographical location and building quality; and

(e) where data are missing or unavailable the treatment is conservative.

16.6 The PRA expects that an IPRE rating system will only be compliant if a firm is able to demonstrate the following in respect of its treatment of interest rate risk (IRR):

(a) IRR is included as a relevant risk driver (unless the portfolio is exclusively hedged);

(b) the way in which interest rate risk is included in the deal rating is intuitive with respect to model philosophy. For example a 'point in time' rating should consider the current interest rate and likely change over a one-year time horizon, whereas a 'through the cycle' model needs to consider the interest rate risk averaged over an economic cycle; and

(c) the model rates deals where IRR is hedged by the firm differently from deals where IRR is unhedged and the magnitude of the difference in these ratings is intuitive.

16.7 The PRA expects that an IPRE rating system will only be compliant if a firm is able to demonstrate the following in respect of its treatment of refinance risk:

(a) refinance risk is included as a relevant risk driver (unless the portfolio contains only amortising loans);

(b) the model rates interest only and amortising deals differently in the final year and that the magnitude of the difference in these ratings is intuitive;

(c) given the time horizon associated with IRB estimates (ie twelve months) the refinance risk could have a zero weight until the deal enters its final year for point in time models. In these cases the risk should be captured in stress testing and Pillar 2; and

(1) CP4/13 86–88.
(2) CP4/13 39–92.

(d) the firm is able to report by borrowers that have previously had a distressed restructuring unlikeliness to pay indicator (even if they are now performing) by number, EAD and RWA.

Calibration[1]

16.8 The PRA expect that firms will not be compliant with the calibration requirements relating to use of a long-run default rate unless it can demonstrate that:

(a) the internal data series is the longest relevant and accurate data series, on a CRR compliant definition of default, that is available;

(b) the determination of long-run default rate includes reference to an appropriate source of downturn data. This may require the use of external data;

(c) the relevance of any external data used is analysed, and the relationship between internal default data and the external data used is considered over a multi-year period; and

(d) where uncertainty is introduced due to, for example, the quality of internal data or shortcomings in the relevance of external data a conservative adjustment to the estimates should be made.

16.9 The PRA expects that a firm will only be compliant with the calibration requirements relating to model philosophy if it can demonstrate that:

(a) model philosophy is clearly articulated and justified. Justification should include analysis of the performance of assets, and the corresponding ratings assigned, over a change in economic conditions (ie as long a period as possible); and

(b) in addition to encapsulating this information in a coherent way in the calibration, the impact of capturing risks such as IRR and refinance risk is clearly documented.

Low default portfolios[2]

16.10 Where the rating system is classed as a low default portfolio in accordance with this supervisory statement firms should be able to demonstrate that the framework applied adequately considers:

(a) economic environment of data used;

(b) changes in portfolio composition over time;

(c) parameter choices; and

(d) model philosophy.

Constructed theoretically[3]

16.11 Under CRR Article 144(1) all models, including those constructed from a theoretical basis without reference to any empirical default data (such as Monte Carlo cash flow simulation models) must meet the IRB requirements that are set out in CRR Title II Chapter 3.

16.12 The PRA considers that to meet these requirements it will be necessary for firms to demonstrate that a firm has a good understanding of PD models that are constructed theoretically and that the parameter estimates reflect a one-year PD. In addition, even if empirical data were not used to determine the PD estimate it should, where available, be used to back-test the estimates.

16.13 The PRA expects that, as most models of this type will be able to produce one-year estimates of PD that correspond closely to 'point in time' estimates, firms should conduct robust back-testing as such estimates by comparing them with realised default rates. Firms would need to demonstrate that the results of such back-testing meets pre-defined and stringent standards in order for the PRA to be satisfied that the IRB requirements are met.

16.14 Because assumptions in the model build process are likely materially to impact the resulting PDs, the PRA expects these choices to be clearly justified in the model documentation and to have been subject to independent review. In order to be satisfied that a firm is complying with CRR Article 176(1)(d) the PRA expects a firm to support justification for all assumptions with analysis of the sensitivity of the model outputs to changes in the assumptions.

16.15 Where the firm has less than 20 defaults in their internal data set, the PRA expects it to be necessary for firms to perform a statistical low default portfolio calibration, as set out in this Supervisory Statement.

Validation[4]

16.16 The PRA expects that a firm will not be compliant with the validation requirements unless it can demonstrate in respect of discriminatory power that:

(a) appropriate minimum standards that the rating system is expected to reach are defined together with reasoning behind the adoption of such standards and that the factors considered when determining the tests are clearly documented;

(b) an objective rank ordering metric, measured using an appropriate time horizon (eg using ratings one year prior

(1) CP4/13 93–94.
(2) CP4/13 35.
(3) CP4/13 96–102.
(4) CP4/13 103–105.

to default) or cohort approach), such as Gini or Accuracy Ratio of 50% is achieved over time;

(c) where there are sufficient defaults from different time periods the discriminatory power is shown to have reached the appropriate minimum standard over an extended time period (ie longest period possible including most recent data); and

(d) any concentrations in ratings from the model are demonstrated to be appropriate.

16.17 The PRA expects that a firm will not be compliant with the validation requirements unless it can demonstrate in respect of the calibration that:

(a) observed default rate versus PD is considered at grade level and across a range of economic environments (ie as long as period as possible);

(b) where the PD does not relates to a pure point in time estimate either the PD or the observed default rate is transformed such that comparison between the two is meaningful. This transformation should be consistent with the model philosophy and calibration technique applied; and

(c) pre-defined tolerances for the degree of divergence, and the associated actions for what should happen when they are not met, are set.

16.18 The PRA also expects that firms will not be compliant with the validation requirements unless it can demonstrate that:

(a) appropriate stability metrics are considered across a range of economic environments (ie longest period possible including most recent data);

(b) the tolerances for the degree of divergence, and associated actions for what should happen when they are not met, is pre-defined; and

(c) subsections of portfolios by characteristics affecting risk profile, and therefore potentially model performance, are investigated. Such subsections could include:

(i) loan type (amortising/interest only);

(ii) degree of hedging;

(iii) building type; and

(iv) other factors such as non-SPV lending in a predominately SPV lending book or *vice versa*.

(CRR Article 188)

Other requirements[1]

16.19 The PRA expects that a firm would not be able to comply with certain other CRR requirements unless it could demonstrate that:

(a) in relation to CRR Article 144(1)(e), where more than one model was used, the rationale and the associated boundary issues were clearly articulated and justified. The PRA expects the criteria for assigning an asset to a rating model are objective and clear;

(b) in relation to CRR Article 173(1)(c), the firm has a process in place to ensure valuations of the property are appropriate and up to date;

(c) in relation to CRR Article 171(2), the firm makes reference to information available from the Investment Property Databank where relevant. Where this data is utilised at a broad level when more granular data is available this is fully justified with appropriate analysis;

(d) in relation to CRR Article 173(1)(b), the rating histories demonstrate that deals are re-rated every time material information becomes available, for example where the deal enters its final year (and refinance risk becomes relevant) or a tenant defaults, is replaced or has their rating changed;

(e) in relation to CRR Article 189(3), management information covering all aspects required by the CRR is produced and reviewed regularly by senior management and the tolerances for the degree of divergence, and associated actions for what should happen when they are not met, are pre-defined; and

(f) in relation to CRR Article 177(2), the impact on PDs and RWAs in a firm's credit risk stress test is consistent with model philosophy (although ratings should be affected by events such as tenant defaults even if they are TTC) and impairment projections are justified with reference to past internal data.

17 Notification and approval of changes to approved models

Changes to approved models[2]

17.1 This section sets out the PRA's expectations in respect of the notifications and changes to approved models. For clarification, the term 'approved model' refers to all aspects of the IRB rating system that were in place at the time that the model was approved and implemented. This would include

(1) CP4/13 106.
(2) CP4/13 110–111.

any judgemental overlays or conservatism that were put in place or processes for manually overriding the model outputs, updating house price indices or ongoing recalibrations for point in time PD models.

17.2 Where a firm intends to make changes to an approved model these must be pre-notified to the PRA if they are significant and post-notified otherwise. Firms may nominate certain models for exclusion from these notification requirements on the grounds of immateriality. In addition, in certain circumstances temporary adjustments may be made to capital requirements outside of this framework. Further details are set out below.

Pre-notification of significant changes(1)

17.3 Model changes may necessitate a modification to the IRB approval originally granted. For the avoidance of doubt, any change that requires a revision to the IRB permission and/or joint decision must be pre-notified.

17.4 In addition, firms must notify the PRA of significant changes to IRB models prior to these changes being implemented. A firm's IRB permission offers some broad guidelines around the factors that constitute significant change.

17.5 In addition to these broad guidelines, the following are examples of factors which constitute significant change (please note that this is not an exhaustive list):

(a) Rating system development eg changes to the ratings philosophy of a material rating system.

(b) Extension of rating systems or development of new rating systems for new products and where partial use provisions were employed to migrate standardised portfolios to IRB.

(c) Mergers and acquisitions — a firm with IRB model approval may acquire rating systems which are not IRB compliant, or firms may have legacy capital models that they wish to amalgamate.

(d) Upgrades to IRB approaches — for example, from Foundation to Advanced IRB.

(e) A change resulting in a change in credit risk capital requirements for the UK consolidation group that is greater than 1%. In assessing changes to credit risk capital requirements firms should take into account changes in expected loss and treatment of securitisation positions as well as changes arising from RWAs.

(f) A recalibration that results in a reduction in portfolio level credit risk capital requirements greater than 5%. If a recalibration has an impact below 5% at the portfolio level but above 1% at the group level then such a recalibration would count as a significant reduction by virtue of (e) above. 'Portfolio level' should be interpreted as the portion of the group's overall exposures covered by the ratings system that the firm is proposing to modify. In assessing changes to credit risk capital requirements firms should take into account changes in expected loss and treatment of securitisation positions as well as changes arising from RWAs.

(g) A significant change to the outputs of the ratings system resulting from a series of changes that in isolation may not be significant but cumulatively have a significant effect.

17.6 In relation to paragraph 17.5(e) and 17.5(f) above, in the context of a CRR Article 20 joint decision, it should be open for the PRA and other EEA regulators to agree to the parameter for defining a significant change, so that there is consensus on how these cases are dealt with within the CRR Article 20 framework. Where the PRA is the consolidated supervisor, it will attempt to agree the thresholds for significance with other EEA regulators.

17.7 Firms should implement a formal internal policy which governs the IRB changes that require pre and post-notification, or are *de minimis* and require no notification.

17.8 An IRB permission may specify that one or more rating systems is to be rolled out within a time window and may specify that the PRA will review the rating system prior to rollout. Where the PRA has not indicated in the permission that it will review the ratings system prior to rollout, firms should nonetheless follow the above approach in determining whether pre-notification of a model change is necessary.

Process for pre-notifying a change(2)

17.9 Firms should follow the process outlined below to pre-notify a change:

Step 1. Submit the information set out in the *pro-forma* in Appendix B.

Step 2. The firm should advise its PRA supervisor about future proposed changes as far in advance as possible. Formal pre-notification to the PRA of specific changes in more detail may follow. Such advance notice might take the form of a periodic report setting out the firm's current thinking on future changes, in aggregate across the group.

(1) CP4/13 112–117.
(2) CP4/13 118.

Advance notice is particularly important in the case of firms with an IRB permission that is subject to joint decision under CRR Article 20, where the PRA may need to revise the joint decision in consultation with other EEA regulators, or more generally where a proposed change impacts on overseas jurisdictions where it may be appropriate to consult with other regulators. The common decision by the PRA and other regulators must be reached within six months.

Step 3. Conduct a self-assessment of the change against the relevant CRR requirements and guidance in this Supervisory Statement, noting any areas of CRR non-compliance with details of how these gaps will be closed.

Step 4. If the change affects a rating system, then, in addition to the information provided in the *pro-forma* in Appendix B, the firm should also comment on the following areas:

(a) the way in which the rating system complies with the use test;

(b) what the internal governance arrangements and sign-off procedures were for the rating system;

(c) what validation work has been performed on the ratings system or is planned; and

(d) how the firm's Pillar 1 stress-testing practices, including the impact on the quantitative results of stress testing, have been affected by the change.

Step 5. Send the material from Steps 1, 2 and 4 to its PRA supervisor. The material needs to be sent sufficiently far in advance of the proposed change to allow the PRA time to review it prior to implementation. If the PRA chooses to review the change, it may ask for additional information and, if necessary, meetings or on-site visits. The PRA is content for firms to provide internal documentation for this purpose, provided this addresses clearly and sufficiently the process requirements set out above.

Process for post-notifying a change(1)

17.10 Where a change to an approved model may be notified to the PRA after it has occurred, firms should prepare and submit the following information:

(a) the information set out in the *pro-forma* in Appendix B;

(b) confirmation that the change has been reviewed through the firm's internal governance processes; and

(c) confirmation that a self-assessment of the change against the relevant CRR requirements and guidance in this Supervisory Statement has been completed and has not identified any areas of CRR non-compliance.

17.11 After the post-notification, the PRA may request additional information to assist in any review that the PRA may undertake.

Immaterial models(2)

17.12 The PRA will normally permit firms to nominate a number of models, which in total account for no more than 1% of the credit risk capital requirement of the UK consolidation group, for which neither pre-notification nor post-notification is ordinarily necessary.

Fees(3)

17.13 There will be some circumstances where a fee may be applied, for example, where a firm is upgrading from FIRB to AIRB, or a special project fee in the case of a merger or acquisition.

Self-assessment(4)

17.14 The self-assessment process described above need only be an assessment against the CRR requirements and guidance in this supervisory statement that are relevant to the change in question. While it is the firm's responsibility to decide on the method of conducting the self-assessment, this should be sufficiently rigorous to allow the firm to identify areas of non-compliance.

17.15 A high-level 'gap analysis' or a process that places reliance on the firm's governance process or on the firm's developmental process to deliver a compliant approach is unlikely to form an adequate self-assessment, at least in the early years of IRB operation.

Temporary adjustments to approved models(5)

17.16 Firms should address identified model issues in a timely fashion with suitable model changes, and ensure that such changes are implemented in accordance with the model changes process outlined above. The PRA recognises, however, that there are instances where it is prudent and correct for firms to adjust the capital requirements produced by their models on a temporary basis. The PRA does not expect any such adjustment to be in place for a period longer than six months and firms should take any action required to remove an adjustment (including notifying the PRA of a model change where appropriate) within that period.

(1) CP4/13 119–120.
(2) CP4/13 121.
(3) CP4/13 122.
(4) CP4/13 123–124.
(5) CP4/13 125–127.

17.17 Firms should meet the following criteria in respect of any temporary adjustments to approved models:

(a) The framework must be applied at a portfolio level. For this a 'portfolio' is defined as the group of assets covered by the IRB model the adjustment is being made for. If adjustments are being made to more than one model (eg PD and LGD) which cover overlapping assets (eg a global LGD model and regional PD models), then a portfolio(s) must be defined as the subset of assets covered by the same models (eg in the example above the assets covered by the regional PD model would be classified as a single portfolio).

(b) Irrespective of what model component the adjustment is for (eg PD, LGD or EAD) the RWA and EL adjustments are made as a portfolio level add-on to the requirements produced by the approved models (ie the underlying models must not be recalibrated or changed to give the desired capital outcome).

(c) Firms' PD, LGD and EAD models remain in place until the correct level of approval has been obtained for any changes. These models continue to be monitored as required by the CRR.

(d) Only adjustments that increase RWA and EL are made and there should be no netting of adjustments across portfolios (eg if there are two data issues, in separate portfolios, one which increases RWA by £200 million and one that decreased RWA by £100 million, only the adjustment increase of £200 million is applied). Where netting of impacts is proposed, this is applied in the relevant portfolio (ie where a model covers a number of portfolios, netting can only be done at a portfolio level).

(e) A list of all model adjustments is included in the firm's model monitoring information presented to senior management, containing the following information as a minimum:

    (i) the portfolio and model component affected;

    (ii) a description of the issue and why it requires the adjustment;

    (iii) the date when the issue was first identified;

    (iv) what action is being taken to address the issue and the timeline for this action; and

    (v) the increase to RWA and EL as a result of the adjustment.

(f) Firms may make adjustments across model components (eg PD, LGD and EAD), however if the PRA judges that a firm is not applying the netting across components appropriately, or with the correct degree of conservatism, then it will require that netting is permitted only within a model component (eg if the adjustment to PD increases capital and to LGD decreases capital, the firm would only apply the increased capital that results from the PD adjustment).

17.18 Firms should include any EL and RWA adjustments in their regulatory returns. In respect of the FSA004 return, uplifts should be made by adjusting the total figures within the relevant IRB asset classes. In respect of the FSA045 return the total RWA and EL figures for each of the PD grades should be increased proportionally.

18 Appendix A: Slotting criteria

Table 3A.1 Supervisory rating grades for project finance exposures

	Strong	Good	Satisfactory	Weak
Financial strength				
Market conditions.	Few competing suppliers or substantial and durable advantage in location, cost, or technology. Demand is strong and growing.	Few competing suppliers or better than average location, cost, or technology but this situation may not last. Demand is strong and stable.	Project has no advantage in location, cost, or technology. Demand is adequate and stable.	Project has worse than average location, cost, or technology. Demand is weak and declining.
Financial ratios (eg debt service coverage ratio (DSCR), loan life coverage ratio (LLCR), project life coverage ratio (PLCR), and debt-to-equity ratio).	Strong financial ratios considering the level of project risk; very robust economic assumptions.	Strong to acceptable financial ratios considering the level of project risk; robust project economic assumptions.	Standard financial ratios considering the level of project risk.	Aggressive financial ratios considering the level of project risk.
Stress analysis.	The project can meet its financial obligations under sustained, severely stressed economic or sectoral conditions.	The project can meet its financial obligations under normal stressed economic or sectoral conditions. The project is only likely to default under severe economic conditions.	The project is vulnerable to stresses that are not uncommon through an economic cycle, and may default in a normal downturn.	The project is likely to default unless conditions improve soon.
Financial structure				
Duration of the credit compared to the duration of the project.	Useful life of the project significantly exceeds tenor of the loan.	Useful life of the project exceeds tenor of the loan.	Useful life of the project exceeds tenor of the loan.	Useful life of the project may not exceed tenor of the loan.
Amortisation schedule.	Amortising debt.	Amortising debt.	Amortising debt repayments with limited bullet payment.	Bullet repayment or amortising debt repayments with high bullet repayment.
Political and legal environment				
Political risk, including transfer risk, considering project type and mitigants.	Very low exposure; strong mitigation instruments, if needed.	Low exposure; satisfactory mitigation instruments, if needed.	Moderate exposure; fair mitigation instruments.	High exposure; no or weak mitigation instruments.
Force majeure risk (war, civil unrest, etc).	Low exposure.	Acceptable exposure.	Standard protection.	Significant risks, not fully mitigated.
Government support and project's importance for the country over the long term.	Project of strategic importance for the country (preferably export-oriented). Strong support from Government.	Project considered important for the country. Good level of support from Government.	Project may not be strategic but brings unquestionable benefits for the country. Support from Government may not be explicit.	Project not key to the country. No or weak support from Government.
Stability of legal and regulatory environment (risk of change in law).	Favourable and stable regulatory environment over the long term.	Favourable and stable regulatory environment over the medium term.	Regulatory changes can be predicted with a fair level of certainty.	Current or future regulatory issues may affect the project.
Acquisition of all necessary supports and approvals for such relief from local content laws.	Strong	Satisfactory	Fair	Weak
Enforceability of contracts, collateral and security.	Contracts, collateral and security are enforceable.	Contracts, collateral and security are enforceable.	Contracts, collateral and security are considered enforceable even if certain non-key issues may exist.	There are unresolved key issues in respect if actual enforcement of contracts, collateral and security.

	Strong	Good	Satisfactory	Weak
Transaction characteristics				
Design and technology risk.	Fully proven technology and design.	Fully proven technology and design.	Proven technology and design — start-up issues are mitigated by a strong completion package.	Unproven technology and design; technology issues exist and/or complex design.
Construction risk				
Permitting and siting.	All permits have been obtained.	Some permits are still outstanding but their receipt is considered very likely.	Some permits are still outstanding but the permitting process is well defined and they are considered routine.	Key permits still need to be obtained and are not considered routine. Significant conditions may be attached.
Type of construction contract.	Fixed-price date-certain turnkey construction EPC (engineering and procurement contract).	Fixed-price date-certain turnkey construction EPC.	Fixed-price date-certain turnkey construction contract with one or several contractors.	No or partial fixed-price turnkey contract and/or interfacing issues with multiple contractors.
Completion guarantees.	Substantial liquidated damages supported by financial substance and/or strong completion guarantee from sponsors with excellent financial standing.	Significant liquidated damages supported by financial substance and/or completion guarantee from sponsors with good financial standing.	Adequate liquidated damages supported by financial substance and/or completion guarantee from sponsors with good financial standing.	Inadequate liquidated damages or not supported by financial substance or weak completion guarantees.
Track record and financial strength of contractor in constructing similar projects.	Strong.	Good.	Satisfactory.	Weak.
Operating risk				
Scope and nature of operations and maintenance (O&M) contracts.	Strong long-term O&M contract, preferably with contractual performance incentives, and/or O&M reserve accounts.	Long-term O&M contract, and/or O&M reserve accounts.	Limited O&M contract or O&M reserve account.	No O&M contract: risk of high operational cost overruns beyond mitigants.
Operator's expertise, track record, and financial strength.	Very strong, or committed technical assistance of the sponsors.	Strong.	Acceptable.	Limited/weak, or local operator dependent on local authorities.
Off-take risk				
(a) If there is a take-or-pay or fixed-price off-take contract:	Excellent creditworthiness of off-taker; strong termination clauses; tenor of contract comfortably exceeds the maturity of the debt.	Good creditworthiness of off-taker; strong termination clauses; tenor of contract exceeds the maturity of the debt.	Acceptable financial standing of off-taker; normal termination clauses; tenor of contract generally matches the maturity of the debt.	Weak off-taker; weak termination clauses; tenor of contract does not exceed the maturity of the debt.
(b) If there is no take-or-pay or fixed-price off-take contract:	Project produces essential services or a commodity sold widely on a world market; output can readily be absorbed at projected prices even at lower than historic market growth rates.	Project produces essential services or a commodity sold widely on a regional market that will absorb it at projected prices at historical growth rates.	Commodity is sold on a limited market that may absorb it only at lower than projected prices.	Project output is demanded by only one or a few buyers or is not generally sold on an organised market.
Supply risk				
Price, volume and transportation risk of feed-stocks; supplier's track record and financial strength.	Long-term supply contract with supplier of excellent financial standing.	Long-term supply contract with supplier of good financial standing.	Long-term supply contract with supplier of good financial standing — a degree of price risk may remain.	Short-term supply contract or long-term supply contract with financially weak supplier — a degree of price risk definitely remains.
Reserve risks (eg natural resource development).	Independently audited, proven and developed reserves well in excess of requirements over lifetime of the project.	Independently audited, proven and developed reserves in excess of requirements over lifetime of the project.	Proven reserves can supply the project adequately through the maturity of the debt.	Project relies to some extent on potential and undeveloped reserves.
Strength of sponsor				
Sponsor track record, financial strength, and country/sector experience.	Strong sponsor with excellent track record and high financial standing.	Good sponsor with satisfactory track record and good financial standing.	Adequate sponsor with adequate track record and good financial standing.	Weak sponsor with no or questionable track record and/or financial weaknesses.
Sponsor support, as evidenced by equity, ownership clause and incentive to inject additional cash if necessary.	Strong. Project is highly strategic for the sponsor (core business — long-term strategy).	Good. Project is strategic for the sponsor (core business — long-term strategy).	Acceptable. Project is considered important for the sponsor (core business).	Limited. Project is not key to sponsor's long-term strategy or core business.

	Strong	Good	Satisfactory	Weak
Security package				
Assignment of contracts and accounts.	Fully comprehensive.	Comprehensive.	Acceptable.	Weak.
Pledge of assets, taking into account quality, value and liquidity of assets.	First perfected security interest in all project assets, contracts, permits and accounts necessary to run the project.	Perfected security interest in all project assets, contracts, permits and accounts necessary to run the project.	Acceptable security interest in all project assets, contracts, permits and accounts necessary to run the project.	Little security or collateral for lenders; weak negative pledge clause.
Lender's control over cash flow (eg cash sweeps, independent escrow accounts).	Strong.	Satisfactory.	Fair.	Weak.
Strength of the covenant package (mandatory prepayments, payment deferrals, payment cascade, dividend restrictions...).	Covenant package is strong for this type of project. Project may issue no additional debt.	Covenant package is satisfactory for this type of project. Project may issue extremely limited additional debt.	Covenant package is fair for this type of project. Project may issue limited additional debt.	Covenant package is Insufficient for this type of project. Project may issue unlimited additional debt.
Reserve funds (debt service, O&M, renewal and replacement, unforeseen events, etc).	Longer than average coverage period, all reserve funds fully funded in cash or letters of credit from highly rated bank.	Average coverage period, all reserve funds fully funded.	Average coverage period, all reserve funds fully funded.	Shorter than average coverage period, reserve funds funded from operating cash flows.

Table 3A.2 Supervisory rating grades for income-producing real estate expo

	Strong	Good	Satisfactory	Weak
Financial strength				
Market conditions.	The supply and demand for the project's type and location are currently in equilibrium. The number of competitive properties coming to market is equal or lower than forecasted demand.	The supply and demand for the project's type and location are currently in equilibrium. The number of competitive properties coming to market is roughly equal to forecasted demand.	Market conditions are roughly in equilibrium. Competitive properties are coming on the market and others are in the planning stages. The project's design and capabilities may not be state of the art compared to new projects.	Market conditions are weak. It is uncertain when conditions will improve and return to equilibrium. The project is losing tenants at lease expiration. New lease terms are less favourable compared to those expiring.
Financial ratios and advance rate.	The property's debt service coverage ratio (DSCR) is considered strong (DSCR is not relevant for the construction phase) and its loan to value ratio (LTV) is considered low given its property type. Where a secondary market exists, the transaction is underwritten to market standards.	The DSCR (not relevant for development real estate) and LTV are satisfactory. Where a secondary market exists, the transaction is underwritten to market standards.	The property's DSCR has deteriorated and its value has fallen, increasing its LTV.	The property's DSCR has deteriorated significantly and its LTV is well above underwriting standards for new loans.
Stress analysis.	The property's resources, contingencies and liability structure allow it to meet its financial obligations during a period of severe financial stress (eg interest rates, economic growth).	The property can meet its financial obligations under a sustained period of financial stress (eg interest rates, economic growth). The property is likely to default only under severe economic conditions.	During an economic downturn, the property would suffer a decline in revenue that would limit its ability to fund capital expenditures and significantly increase the risk of default.	The property's financial condition is strained and is likely to default unless conditions improve in the near term.
Cash-flow predictability				
(a) For complete and stabilised property.	The property's leases are long-term with creditworthy tenants and their maturity dates are scattered. The property has a track record of tenant retention upon lease expiration. Its vacancy rate is low. Expenses (maintenance, insurance, security, and property taxes) are predictable.	Most of the property's leases are long-term, with tenants that range in creditworthiness. The property experiences a normal level of tenant turnover upon lease expiration. Its vacancy rate is low. Expenses are predictable.	Most of the property's leases are medium rather than long-term with tenants that range in creditworthiness. The property experiences a moderate level of tenant turnover upon lease expiration. Its vacancy rate is moderate. Expenses are relatively predictable but vary in relation to revenue.	The property's leases are of various terms with tenants that range in creditworthiness. The property experiences a very high level of tenant turnover upon lease expiration. Its vacancy rate is high. Significant expenses are incurred preparing space for new tenants.
(b) For complete but not stabilised property.	Leasing activity meets or exceeds projections. The project should achieve stabilisation in the near future.	Leasing activity meets or exceeds projections. The project should achieve stabilisation in the near future.	Most leasing activity is within projections; however, stabilisation will not occur for some time.	Market rents do not meet expectations. Despite achieving target occupancy rate, cash flow coverage is tight due to disappointing revenue.
(c) For construction phase.	The property is entirely pre-leased through the tenor of the loan or pre-sold to an investment grade tenant or buyer, or the bank has a binding commitment for take-out financing from an investment-grade lender.	The property is entirely pre-leased or pre-sold to a creditworthy tenant or buyer, or the bank has a binding commitment for permanent financing from a creditworthy lender.	Leasing activity is within projections but the building may not be pre-leased and there may not exist a take-out financing. The bank may be the permanent lender.	The property is deteriorating due to cost overruns, market deterioration, tenant cancellations or other factors. There may be a dispute with the party providing the permanent financing.

	Strong	Good	Satisfactory	Weak
Asset characteristics				
Location.	Property is located in highly desirable location that is convenient to services that tenants desire.	Property is located in desirable location that is convenient to services that tenants desire.	The property location lacks a competitive advantage.	The property's location, configuration, design and maintenance have contributed to the property's difficulties.
Design and condition.	Property is favoured due to its design, configuration, and maintenance, and is highly competitive with new properties.	Property is appropriate in terms of its design, configuration and maintenance. The property's design and capabilities are competitive with new properties.	Property is adequate in terms of its configuration, design and maintenance.	Weaknesses exist in the property's configuration, design or maintenance.
Property is under construction.	Construction budget is conservative and technical hazards are limited. Contractors are highly qualified.	Construction budget is conservative and technical hazards are limited. Contractors are highly qualified.	Construction budget is adequate and contractors are ordinarily qualified.	Project is over budget or unrealistic given its technical hazards. Contractors may be under qualified.
Strength of sponsor/developer				
Financial capacity and willingness to support the property.	The sponsor/developer made a substantial cash contribution to the construction or purchase of the property. The sponsor/developer has substantial resources and limited direct and contingent liabilities. The sponsor/developer's properties are diversified geographically and by property type.	The sponsor/developer made a material cash contribution to the construction or purchase of the property. The sponsor/developer's financial condition allows it to support the property in the event of a cash flow shortfall. The sponsor/developer's properties are located in several geographic regions.	The sponsor/developer's contribution may be immaterial or non-cash. The sponsor/developer is average to below average in financial resources.	The sponsor/developer lacks capacity or willingness to support the property.
Reputation and track record with similar properties.	Experienced management and high sponsors' quality. Strong reputation and lengthy and successful record with similar properties.	Appropriate management and sponsors' quality. The sponsor or management has a successful record with similar properties.	Moderate management and sponsors' quality. Management or sponsor track record does not raise serious concerns.	Ineffective management and substandard sponsors' quality. Management and sponsor difficulties have contributed to difficulties in managing properties in the past.
Relationships with relevant real estate actors.	Strong relationships with leading actors such as leasing agents.	Proven relationships with leading actors such as leasing agents.	Adequate relationships with leasing agents and other parties providing important real estate services.	Poor relationships with leasing agents and/or other parties providing important real estate services.
Security package				
Nature of lien.	Perfected first lien.(a)	Perfected first lien.(a)	Perfected first lien.(a)	Ability of lender to foreclose is constrained.
Assignment of rents (for projects leased to long-term tenants).	The lender has obtained an assignment. They maintain current tenant information that would facilitate providing notice to remit rents directly to the lender, such as a current rent roll and copies of the project's leases.	The lender has obtained an assignment. They maintain current tenant information that would facilitate providing notice to the tenants to remit rents directly to the lender, such as current rent roll and copies of the project's leases.	The lender has obtained an assignment. They maintain current tenant information that would facilitate providing notice to the tenants to remit rents directly to the lender, such as current rent roll and copies of the project's leases.	The lender has not obtained an assignment of the leases or has not maintained the information necessary to readily provide notice to the building's tenants.
Quality of the insurance coverage.	Appropriate.	Appropriate.	Appropriate.	Substandard.

(a) Lenders in some markets extensively use loan structures that include junior liens. Junior liens may be indicative of this level of risk if the total LTV inclusive of all senior positions does not exceed a typical first loan LTV.

Table 3A.3 Supervisory rating grades for object finance exposures

	Strong	Good	Satisfactory	Weak
Financial strength				
Market conditions.	Demand is strong and growing, strong entry barriers, low sensitivity to changes in technology and economic outlook.	Demand is strong and stable. Some entry barriers, some sensitivity to changes in technology and economic outlook.	Demand is adequate and stable, limited entry barriers, significant sensitivity to changes in technology and economic outlook.	Demand is weak and declining, vulnerable to changes in technology and economic outlook, highly uncertain environment.
Financial ratios (debt service coverage ratio and loan to value ratio)	Strong financial ratios considering the type of asset. Very robust economic assumptions.	Strong/acceptable financial ratios considering the type of asset. Robust project economic assumptions.	Standard financial ratios for the asset type.	Aggressive financial ratios considering the type of asset.
Stress analysis.	Stable long-term revenues, capable of withstanding severely stressed conditions through an economic cycle.	Satisfactory short-term revenues. Loan can withstand some financial adversity. Default is only likely under severe economic conditions.	Uncertain short-term revenues. Cash flows are vulnerable to stresses that are not uncommon through an economic cycle. The loan may default in a normal downturn.	Revenues subject to strong uncertainties; even in normal economic conditions the asset may default, unless conditions improve.
Market liquidity.	Market is structured on a worldwide basis; assets are highly liquid.	Market is worldwide or regional; assets are relatively liquid.	Market is regional with limited prospects in the short term, implying lower liquidity.	Local market and/or poor visibility. Low or no liquidity, particularly on niche markets.

	Strong	Good	Satisfactory	Weak
Political and legal environment				
Political risk, including transfer risk.	Very low; strong mitigation instruments, if needed.	Low; satisfactory mitigation instruments, if needed.	Moderate; fair mitigation instruments.	High; no or weak mitigation instruments.
Legal and regulatory risks.	Jurisdiction is favourable to repossession and enforcement of contracts.	Jurisdiction is favourable to repossession and enforcement of contracts.	Jurisdiction is generally favourable to repossession and enforcement of contracts, even if repossession might be long and/or difficult.	Poor or unstable legal and regulatory environment. Jurisdiction may make repossession and enforcement of contracts lengthy or impossible.
Transaction characteristics				
Financing term compared to the economic life of the asset.	Full payout profile/minimum balloon. No grace period.	Balloon more significant, but still at satisfactory levels.	Important balloon with potentially grace periods.	Repayment in fine or high balloon.
Operating risk				
Permits/licensing.	All permits have been obtained; asset meets current and foreseeable safety regulations.	All permits obtained or in the process of being obtained; asset meets current and foreseeable safety regulations.	Most permits obtained or in process of being obtained, outstanding ones considered routine, asset meets current safety regulations.	Problems in obtaining all required permits, part of the planned configuration and/or planned operations might need to be revised.
Scope and nature of O&M contracts.	Strong long-term O&M contract, preferably with contractual performance incentives, and/or O&M reserve accounts (if needed).	Long-term O&M contract, and/or O&M reserve accounts (if needed).	Limited O&M contract or O&M reserve account (if needed).	No O&M contract: risk of high operational cost overruns beyond mitigants.
Operator's financial strength, track record in managing the asset type and capability to remarket asset when it comes off-lease.	Excellent track record and strong remarketing capability.	Satisfactory track record and remarketing capability.	Weak or short track record and uncertain remarketing capability.	No or unknown track record and inability to remarket the asset.
Asset characteristics				
Configuration, size, design and maintenance (ie age, size for a plane) compared to other assets on the same market.	Strong advantage in design and maintenance. Configuration is standard such that the object meets a liquid market.	Above average design and maintenance. Standard configuration, maybe with very limited exceptions — such that the object meets a liquid market.	Average design and maintenance. Configuration is somewhat specific, and thus might cause a narrower market for the object.	Below average design and maintenance. Asset is near the end of its economic life. Configuration is very specific; the market for the object is very narrow.
Resale value.	Current resale value is well above debt value.	Resale value is moderately above debt value.	Resale value is slightly above debt value.	Resale value is below debt value.
Sensitivity of the asset value and liquidity to economic cycles.	Asset value and liquidity are relatively insensitive to economic cycles.	Asset value and liquidity are sensitive to economic cycles.	Asset value and liquidity are quite sensitive to economic cycles.	Asset value and liquidity are highly sensitive to economic cycles.
Strength of sponsor				
Operator's financial strength, track record in managing the asset type and capability to remarket asset when it comes off-lease	Excellent track record and strong remarketing capability.	Satisfactory track record and remarketing capability.	Weak or short track record and uncertain remarketing capability.	No or unknown track record and inability to remarket the asset.
Sponsors' track record and financial strength.	Sponsors with excellent track record and high financial standing.	Sponsors with good track record and good financial standing.	Sponsors with adequate track record and good financial standing.	Sponsors with no or questionable track record and/or financial weaknesses.
Security package				
Asset control.	Legal documentation provides the lender effective control (eg a first perfected security interest, or a leasing structure including such security) on the asset, or on the company owning it.	Legal documentation provides the lender effective control (eg a perfected security interest, or a leasing structure including such security) on the asset, or on the company owning it.	Legal documentation provides the lender effective control (eg a perfected security interest, or a leasing structure including such security) on the asset, or on the company owning it.	The contract provides little security to the lender and leaves room to some risk of losing control on the asset.
Rights and means at the lender's disposal to monitor the location and condition of the asset.	The lender is able to monitor the location and condition of the asset, at any time and place (regular reports, possibility to lead inspections).	The lender is able to monitor the location and condition of the asset, almost at any time and place.	The lender is able to monitor the location and condition of the asset, almost at any time and place.	The lender is able to monitor the location and condition of the asset are limited.
Insurance against damages.	Strong insurance coverage including collateral damages with top quality insurance companies.	Satisfactory insurance coverage (not including collateral damages) with good quality insurance companies.	Fair insurance coverage (not including collateral damages) with acceptable quality insurance companies.	Weak insurance coverage (not including collateral damages) or with weak quality insurance companies.

Table 3A.4 Supervisory rating grades for commodities finance exposures

	Strong	Good	Satisfactory	Weak
Financial strength				
Degree of over-collateralisation of trade.	Strong.	Good.	Satisfactory.	Weak.
Political and legal environment				
Country risk.	No country risk.	Limited exposure to country risk (in particular, offshore location of reserves in an emerging country).	Exposure to country risk (in particular, offshore location of reserves in an emerging country).	Strong exposure to country risk (in particular, inland reserves in an emerging country).
Mitigation of country risks.	Very strong mitigation: Strong offshore Mechanisms. Strategic commodity. 1st class buyer.	Strong mitigation: Offshore mechanisms. Strategic commodity. Strong buyer.	Acceptable mitigation: Offshore mechanisms. Less strategic commodity. Acceptable buyer.	Only partial mitigation: No offshore mechanisms. Non-strategic commodity. Weak buyer.
Asset characteristics				
Liquidity and susceptibility to damage.	Commodity is quoted and can be hedged through futures or OTC instruments. Commodity is not susceptible to damage.	Commodity is quoted and can be hedged through OTC instruments. Commodity is not susceptible to damage.	Commodity is not quoted but is liquid. There is uncertainty about the possibility of hedging. Commodity is not susceptible to damage.	Commodity is not quoted. Liquidity is limited given the size and depth of the market. No appropriate hedging instruments. Commodity is susceptible to damage.
Strength of sponsor				
Financial strength of trader.	Very strong, relative to trading philosophy and risks.	Strong.	Adequate.	Weak.
Track record, including ability to manage the logistic process.	Extensive experience with the type of transaction in question. Strong record of operating success and cost efficiency.	Sufficient experience with the type of transaction in question. Above average record of operating success and cost efficiency.	Limited experience with the type of transaction in question. Average record of operating success and cost efficiency.	Limited or uncertain track record in general. Volatile costs and profits.
Trading controls and hedging policies.	Strong standards for counterparty selection, hedging, and monitoring.	Adequate standards for counterparty selection, hedging, and monitoring.	Past deals have experienced no or minor problems.	Trader has experienced significant losses on past deals.
Quality of financial disclosure.	Excellent.	Good.	Satisfactory.	Financial disclosure contains some uncertainties or is insufficient.
Security package				
Asset control.	First perfected security interest provides the lender legal control of the assets at any time if needed.	First perfected security interest provides the lender legal control of the assets at any time if needed.	At some point in the process, there is a rupture in the control of the assets by the lender. The rupture is mitigated by knowledge of the trade process or a third party undertaking as the case may be.	Contract leaves room for some risk of losing control over the assets. Recovery could be jeopardised.
Insurance against damages.	Strong insurance coverage including collateral damages with top quality insurance companies.	Satisfactory insurance coverage (not including collateral damages) with good quality insurance companies.	Fair insurance coverage (not including collateral damages) with acceptable quality insurance companies.	Weak insurance coverage (not including collateral damages) or with weak quality insurance companies.

19 Appendix B: Model change *pro-forma* required when pre or post-notifying changes to a ratings system[1]

Firm:	
Date notification sent to PRA:	
Pre or post change notification:	
Rating system:	Name: Asset type: PD/LGD/EAD
Brief description of change(s):	
Portfolio information: *[Credit risk capital information on the ratings system that the firm is proposing to change — this information should be prior to the application of the proposed change.]*	EAD £xxx (date) RWA £xxx (date) EL £xxx (date)
Group information: *[Credit risk capital information for UK consolidation group.]*	EAD £xxx (date) RWA £xxx (date) EL £xxx (date)
Materiality of change:	RWA impact £xxx RWA % change % EL impact £xxx EL % change %
Reason change is pre/post notified: *[Explain here why the change is classed as pre or post notified.]*	
Relevant committee approval: *[Committee responsible for approval of change.]*	Name: Date of approval:
Proposed implementation date: *[Date from which changes are intended to affect capital calculations, subject to approval received in the case of material pre-notified changes.]*	
Attach supporting documentation here: *[Including the following where available: development document(s); validation document(s); materials presented to approval committee; approval committee minutes; other supplementary materials.]*	

(1) CP4/13 Appendix A.

20 Appendix C: Wholesale LGD and EAD framework[1]

20.1 The following framework should be used to assess wholesale LGD models in the circumstances set out in paragraph 12.15 of this supervisory statement:

(a) For unsecured recoveries, if a firm has fewer than 20 relevant default observations of recoveries in a specific country for an individual type of exposure, then the maximum recovery a firm can assume must be equivalent to that which would give a 45% LGD for senior unsecured exposures, 75% for subordinated exposures and 11.25% for covered bonds.

(b) If a firm is taking account of non-financial collateral which is not eligible under the foundation approach, where they do not have 20 or more relevant data points of recovery values for that type of collateral or do not have a reliable time series of market price data for the collateral in a specific country, then the LGD for the exposure to which the collateral is applied must be floored at 45%.

(c) If a firm is taking account of non-financial collateral, which is eligible under the foundation approach, where they do not have 20 or more relevant data points of recovery values for that type of collateral or do not have a reliable time series of market price data for that collateral in a specific country, then the LGD for the exposure to which the collateral is applied must be floored at 35%.

20.2 Firms should note the following when applying the framework to LGD models:

(a) The 20 or more relevant data points can include internal or external data, however the PRA expects firms to ensure that each data point is independent, representative and an accurate record of the recovery for that exposure or collateral type in that specific country.

(b) We would anticipate firms being able to use market price data within the framework where they have less than 20 defaults only in exceptional circumstances. As a minimum, firms would need to demonstrate that the market price data being used is representative of their collateral and that it is over a long enough time period to ensure that an appropriate downturn and forced sale haircut can be estimated.

(c) The framework does not affect the use of financial collateral.

(d) The framework does not affect the use of unfunded credit protection.

(e) Where a model takes account of multiple collateral types, if this only includes collateral that is eligible under the foundation approach then LGDs must be floored at 35%, and if any collateral type is not eligible under the foundation approach then LGDs must be floored at 45%.

(f) The effect of this framework is to floor bank and non-bank financial institution (NBFI) exposures at foundation values unless sufficient country-specific recovery data is available. This floor should be applied where the exposures are to types of banks and NBFIs that are not sufficiently represented in the available historic data (eg if the historic recovery data only relates to small banks then the floor will affect large banks).

(g) When applying the framework the PRA expects firms to assess whether the 11.25% LGD floor for covered bonds is sufficient given the quality of the underlying assets.

20.3 Firms should select the most appropriate of the following three options when using the framework to assess wholesale EAD models in the circumstances set out in paragraph 13.8 of this supervisory statement:

(a) Rank-order the off balance sheet product types (separately for lending and trade finance) according to their drawdown risk. The EAD parameter for a product with 20 or more default observations can then be applied to low-default products with a lower drawdown risk; or

(b) For product types where the firm has the defaults needed to estimate the EAD for committed credit lines (or an estimate derived from the option above) but less than 20 defaults for uncommitted credit lines, use 50% of the committed credit line conversion factor as an estimate of the uncommitted credit line conversion factor; or

(c) Apply the foundation parameters.

20.4 Firms should note the following when applying the framework to EAD models:

(a) Firms may select more than one option when applying the framework providing that they can demonstrate that their chosen combination is appropriate, reflecting their particular mix of products and risks, and is not selected in order to minimise their capital requirements.

(b) As we believe that the EAD experienced by firms is dependent on their own credit management processes

(1) CP4/13 Appendix B.

we would expect only internal data to be used to estimate EAD. However, where firms can convincingly demonstrate to the PRA's satisfaction that the credit process are consistent across countries then we would accept that data sourced from these countries could be combined to estimate the EAD for each product (ie the 20 default data points do not have to be country specific for the purposes of estimating EAD).

(c) Firms using the option in paragraph 20.3(a) above should be able to demonstrate that a sufficiently robust approach has been taken to rank-ordering their product types by drawdown risk. This approach must be fully documented and assessed by an independent reviewer.

4 Counterparty credit risk

CRD IV and counterparty credit risk

1 Introduction

1.1 This supervisory statement is aimed at firms to which CRD IV applies.

1.2 This statement sets out the factors which the PRA expects such firms to take into account when applying for certain permissions related to the counterparty credit risk regulatory framework. This statement also provides some clarifications about the scope of the own funds requirements for credit valuation adjustment risk.

1.3 This statement should be considered in addition to the requirements in CRR Article 162 and 382, in the Counterparty Credit Risk rules of the PRA Rulebook and the high-level expectations outlined in *The PRA's approach to banking supervision* (April 2013).

2 Use of 'Internal CVA model' for the calculation of the maturity factor 'M'

2.1 This section sets out the PRA's expectations for granting a firm permission to use its own one-sided credit valuation adjustment internal models (an 'Internal CVA model') for the purpose of estimating the Maturity factor 'M', as proposed under CRR Article 162(2), paragraph (h).

2.2 In the context of counterparty credit risk, the Maturity factor 'M' is intended to increase the own funds requirements to reflect potentially higher risks associated with medium and long-term OTC derivative portfolios, more specifically when the exposure profile of these contracts is significant beyond one year. This adjustment is only applicable to firms using the Internal Model Method (IMM) for the calculation of exposure values.

2.3 Firms are permitted to replace the formula for the Maturity factor 'M', as set out in CRR Article 162(2), paragraph (g), with the 'effective credit duration' derived by a firm's Internal CVA model, subject to permission being granted by the PRA, as the relevant competent authority.

2.4 Internal CVA models are complex by nature and modelling practises vary significantly across the industry. The PRA considers the creation an acceptable model resulting in an appropriate credit duration to be challenging and so would require extensive review. Accordingly, the PRA will require firms to demonstrate a strong case for the granting of such permission.

2.5 A firm that wishes to make an application under Article 162(2), paragraph (h) will have to provide a satisfactory justification for the use of an internal CVA model for estimating the maturity factor M. The purpose of reducing the own funds requirements for counterparty credit risk will not in itself be considered as a reasonable justification. The PRA will also require highly conservative modelling assumptions within a firm's Internal CVA model for the purpose of Article 162(2), paragraph (h).

2.6 Any firm which wants to apply for the permission proposed under 162(2), paragraph (h) should contact the PRA.

3 Permission to set the maturity factor 'M' to 1 for the CCR default charge

3.1 This section sets out the PRA's expectations for permitting firms with the permission to use the Internal Model Method (IMM) and the permission to use an internal VaR model for specific risk associated with traded debt instruments to set to 1 the Maturity factor 'M' defined in CRR Article 162.

3.2 In the context of counterparty credit risk, the Maturity factor 'M' is intended to increase the own funds requirements to reflect the potential higher risks associated with medium and long-term OTC derivative portfolios, more specifically when the exposure profile of these contracts is significant beyond one year. This adjustment is only applicable to firms using the Internal Model Method (IMM) for the calculation of exposure values.

3.3 Article CRR 162(2), paragraph (i) allows a firm to set the Maturity factor 'M' to 1 for a firm using the IMM provided that the firm's internal VaR model for specific risk associated with traded debt instruments reflects the effect of rating migration, and subject to the permission of the PRA, as the relevant competent authority.

3.4 Internal VaR models for specific risk associated with traded debt instruments are not specifically designed to capture the effects of rating migrations. The risk captured by these models is based on a ten-days time horizon which cannot appropriately reflect the dynamics of rating migrations, which occurs on an irregular, infrequent basis. This deficiency was one of the main reasons underlying the introduction of a separate risk measure for the capture of both credit default and rating migration risks, based on a one-year time horizon (the 'IRC' models, CRR Article 372).

3.5 Since the challenges of appropriately capturing credit rating migrations in an internal VaR model are high, the PRA will require firms to demonstrate a strong case for the granting of the permission set out in CRR Article 162(2), paragraph (i).

3.6 A firm that wishes to make an application under CRR Article 162(2), paragraph (i) will have to provide a satisfactory justification for use of their internal VaR to capture the risks associated with ratings migration. The purpose of reducing the own funds requirements for counterparty credit risk will not be considered as a reasonable justification.

3.7 The PRA will require highly conservative modelling assumptions for the capture of rating migrations within a firm's internal VaR models for specific risk associated with traded debt instruments for the purpose of CRR Article 162(2), paragraph (i).

3.8 Any firm who wants to apply for the permission proposed under CRR 162(2), paragraph (i) should apply to the PRA.

4 Inclusion of securities financing transactions in the scope of the CVA capital charge

4.1 This section sets out the PRA's requirements for inclusion of securities financing transactions (SFTs) in the scope of the own funds requirements for credit valuation adjustment (CVA) risk where the PRA deems that CVA risk arising from these transactions is material (CRR Article 382(2)).

4.2 Securities financing transactions (SFTs) are not defined in the regulation. However, the PRA considers that, for these purposes, SFTs should be taken as meaning repurchase transactions or securities or commodities lending or borrowing transactions.

4.3 Transactions which are in substance regarded as SFTs for accounting purposes should not bear CVA risks since they are not subject to the accounting requirement to apply a CVA.

4.4 Therefore, the PRA believes that, in general, SFTs should not be included in the scope of the CVA charge. However, the PRA wants to prevent firms taking advantage of this treatment by structuring transactions which are in substance OTC derivative transactions but in the form of SFTs in order to exclude those transactions from the application of the own funds requirements for credit valuation adjustment risk.

4.5 Therefore, the PRA will pay close attention to SFT portfolios with features that give rise to very similar risks to those that the CVA charge for OTC derivatives is designed to mitigate. The PRA will require firms to identify such transactions and compute the impact of including them in the scope of the own funds requirements for credit valuation adjustment (CVA) risk. This impact should be communicated to the PRA which will decide whether this impact is sufficiently material to warrant inclusion of these transactions in the scope of the own funds requirements for credit valuation adjustment (CVA) risk. This will be determined on the basis of the materiality of the CVA risk exposures of these SFT portfolios.

5 Market risk

CRD IV and market risk

1 Introduction

1.1 This supervisory statement is aimed at firms to which CRD IV applies.

1.2 This statement sets out the PRA expectations of firms in relation to market risk. This statement should be considered in addition to requirements set out in CRD IV Articles 325–377, in the Market Risk rules of the PRA Rulebook and the high-level expectations outlined in *The PRA's approach to banking supervision* (April 2013).

1.3 This statement details the PRA's expectations with regard to the following:

- Material deficiencies in risk capture by an institution's internal approach.
- Standardised approach for options.
- Netting a convertible with its underlying instrument.
- Offsetting derivative instruments.
- Exclusion of backtesting exceptions when determining multiplication factor addends.
- Derivation of notional positions for standardised approaches.
- Qualifying debt instruments.
- Expectations relating to internal models.
- VaR and stressed VaR calculation.
- Requirement to have an internal IRC model.

2 Material deficiencies in risk capture by an institution's internal approach

2.1 This section sets out the PRA's requirements for the calculation of additional own funds for the purposes of implementing CRD Article 101, which applies where a firm has permission to calculate own funds requirements for one or more categories of market risk under CRR Part 3 Title IV Chapter 5. It requires firms to identify any material risks (or risks which are in aggregate material) which are not adequately captured by those models and to hold additional own funds against those risks. The methodology for the identification of those risks and the calculation of those additional own funds for VaR and sVaR models is referred to as the 'RNIV framework'.

2.2 Firms are responsible for identifying these additional risks, and this should be seen as an opportunity for risk managers and management to better understand the shortcomings of the firm's models. Following this initial assessment, the PRA will engage with the firm to provide challenge and so ensure an appropriate outcome.

Scope of the RNIV framework

2.3 The RNIV framework is intended to ensure that own funds are held to meet all material risks (and all risks that, when considered in aggregate, are material) which are not captured, or not captured adequately, by the firm's VaR and sVaR models. These include, but are not limited to, missing and/or illiquid risk factors such as cross-risks, basis risks, higher-order risks, and calibration parameters. The RNIV Framework is also intended to cover event risks that could adversely affect the relevant business.

Identification and measurement framework

2.4 The PRA expects firms to systematically identify and measure all non-captured or poorly captured risks that fall within the scope of the RNIV framework. This analysis should be updated at least quarterly, or more frequently at the request of the PRA. The measurement of these risks should capture the losses that could arise due to the risk factor(s) of all products that are within the scope of the relevant internal model permission, but are not adequately captured by the relevant internal models.

Identification of risk factors

2.5 The PRA expects firms to, on a quarterly basis, identify and assess individual risk factors covered by the RNIV framework. The PRA will review the results of this exercise and may require that firms identify additional risk factors as being eligible for measurement.

Measurement of risk factors

2.6 Where sufficient data is available, and where it is appropriate to do so, the PRA expects firms to calculate a VaR and sVaR metric for each risk factor within scope of the framework. The stressed period for the RNIV sVaR should be consistent with that used for sVAR. No offsetting or diversification may be recognised across risk factors included in the RNIV framework. The multipliers used for VaR and sVaR should be applied to generate an own funds requirement.

2.7 If it is not appropriate to calculate a VaR and sVaR metric for a risk factor, a firm should instead measure the size of the risk based on a stress test. The confidence level and capital horizon of the stress test should be commensurate with the liquidity of the risk, and should be at least as conservative as comparable risk factors under the internal model approach. The capital charge should be at least equal to the losses arising from the stress test.

3 Standardised approach for options

3.1 Firms that need to use own estimates of delta for the purposes of the standardised approach for options, should provide the PRA with confirmation that they meet the minimum standards set out below for each type of option for which they calculate delta. Firms should only provide this confirmation if they meet the minimum standards. A firm that is able to provide confirmation will be permitted to use own estimates of delta for the relevant option.

3.2 If a firm is unable to provide assurance with regard to a particular option type which is currently within its permissions, a capital add-on may be applied and a rectification plan agreed. If a firm is unable to comply with the rectification plan within the mandated time-frame, further supervisory measures may be taken. This may include variation of permissions so that they are no longer allowed to trade those particular types of option for which they do not meet the minimum standards.

Minimum standards

3.3 The level of sophistication of the pricing models, which are used to calculate own estimates of delta for use in the standardised approach for options, should be proportionate to the complexity and risk of each option and the overall risk of the firm's options trading business. In general, it is considered that the risk of sold options will be higher than the risk of the same options when bought.

3.4 Delta should be recalculated at least daily. Firms should also recalculate delta promptly following significant movements in the market parameters used as inputs to calculate delta.

3.5 The pricing model used to calculate delta should be:

- based on appropriate assumptions which have been assessed and challenged by suitably qualified parties independent of the development process;
- independently tested, including validation of the mathematics, assumptions, and software implementation; and
- developed or approved independently of the trading desk.

3.6 A firm should use generally accepted industry standard pricing models for the calculation of own deltas where these are available, such as for relatively simple options.

3.7 The IT systems used to run the calculation of delta should be sufficient to ensure that delta can be reliably calculated accurately and frequently.

3.8 Firms should have adequate systems and controls in place when using pricing models to calculate deltas. This should include the following documented policies and procedures:

- clearly defined responsibilities of the various areas involved in the calculation;
- frequency of independent testing; and
- guidelines for the use of unobservable inputs, where relevant.

3.9 Reporting lines for the department accountable for calculating delta should be:

- clear and independent of the front office; and
- ultimately to a main board executive director.

3.10 A firm should ensure its risk management functions are aware of weaknesses of the model used to calculate deltas. Where weaknesses are identified, the firm should ensure that estimates of delta result in prudent capital requirements being held. The outcome should be prudent across the whole portfolio of options and underlying positions at a given time.

4 Netting a convertible with its underlying instrument

4.1 For the purposes of CRR Article 327(2), the netting of a convertible bond and an offsetting position in the instrument underlying is permitted. The convertible bond should be:

- treated as a position in the equity into which it converts; and
- the firm's equity own funds requirement should be adjusted by making:
  - (i) an addition equal to the current value of any loss which the firm would make if it did convert to equity; or
  - (ii) a deduction equal to the current value of any profit which the firm would make if it did convert to equity (subject to a maximum deduction equal to the own funds requirements on the notional position underlying the convertible).

5 Offsetting derivative instruments

5.1 CRR Article 331(2) states conditions that should be met before firms not using interest rate pre-processing models can fully offset interest rate risk on derivative instruments. One of the conditions is that the reference rate (for floating rate positions) or coupon (for fixed rate positions) should be 'closely matched'. The PRA would normally consider a difference of less than 15 basis points as indicative of the reference rate or coupon being ‘closely matched’ for the purposes of this rule.

6 Exclusion of overshootings when determining multiplication factor addends

6.1 The PRA’s starting assumption will be that all overshootings should be taken into account for the purpose of the calculation of addends. If a firm believes that an overshooting should not count for that purpose, then it should seek a variation of its VaR model permission in order to exclude that particular overshooting. We will then decide whether to agree to such a variation.

6.2 One example of when a firm’s overshooting might properly be disregarded is when it has arisen as a result of a risk that is not captured in its VaR model, but against which capital resources are already held.

7 Derivation of notional positions for standardised approaches

Futures, forwards or synthetic futures on a basket or index of debt securities

7.1 These should be converted into forwards on single debt securities as follows:

1. futures, synthetic futures or forwards on a single currency basket or index of debt securities should be treated as either:
   (a) a series of forwards, one for each of the constituent debt securities in the basket or index, of an amount which is a proportionate part of the total underlying the contract according to the weighting of the relevant debt security in the basket; or
   (b) a single forward on a notional debt security;

and

2. futures, synthetic futures or forwards on multiple currency baskets or indices of debt securities should be treated as either:
   (a) a series of forwards (using the method described in 1.(a)); or
   (b) a series of forwards, each one on a notional debt security to represent one of the currencies in the basket or index, of an amount which is a proportionate part of the total underlying the contract according to the weighting of the relevant currency in the basket.

7.2 Notional debt securities derived through this treatment should be assigned a specific risk position risk adjustment and a general market risk position risk adjustment equal to the highest that would apply to the debt securities in the basket or index.

7.3 The debt security with the highest specific risk position risk adjustment within the basket might not be the same as the one with the highest general market risk position risk adjustment. A firm should select the highest percentages even where they relate to different debt securities in the basket or index, and regardless of the proportion of those debt securities in the basket or index.

Bonds where the coupons and principal are paid in different currencies

7.4 Where a debt security pays coupons in one currency, but will be redeemed in a different currency, it should be treated as:

(i) a debt security denominated in the coupon's currency; and

(ii) a foreign currency forward to capture the fact that the debt security’s principal will be repaid in a different currency from that in which it pays coupons, specifically:
   (a) a notional forward sale of the coupon currency and purchase of the redemption currency, in the case of a long position in the debt security; or
   (b) a notional forward purchase of the coupon currency and sale of the redemption currency, in the case of a short position in the debt security.

Interest rate risk on other futures, forwards and swaps

7.5 Other futures, forwards, and swaps where a treatment is not specified in Article 328 should be treated as positions in zero-specific-risk securities, each of which:

(i) has a zero coupon;

(ii) has a maturity equal to that of the relevant contract; and

(iii) is long or short according to the following table:

Instrument	Notional positions		
Foreign currency forward or future	A long position denominated in the currency purchased	*and*	A short position denominated in the currency sold
Gold forward	A long position if the forward or future involves an actual (or notional) sale of gold	*or*	A short position if the forward or future involves an actual (or notional) purchase of gold
Equity forward or future	A long position if the contract involves an actual (or notional) sale of the underlying equity	*or*	A short position if the contract involves an actual (or notional) purchase of the underlying equity

Deferred start interest rate swaps or foreign currency swaps

7.6 Interest rate swaps or foreign currency swaps with a deferred start should be treated as the two notional positions (one long, one short). The paying leg should be treated as a short position in a zero specific risk security with a coupon equal to the fixed rate of the swap. The receiving leg should be treated as a long position in a zero specific risk security, which also has a coupon equal to the fixed rate of the swap.

7.7 The maturities of the notional positions are shown in the following table:

	Paying leg	Receiving leg
Receiving fixed and paying floating	The maturity equals the start date of the swap	The maturity equals the maturity of the swap
Paying fixed and receiving floating	The maturity equals the maturity of the swap	The maturity equals the start date of the swap

Swaps where only one leg is an interest rate leg

7.8 For the purposes of interest rate risk, a firm should treat a swap (such as an equity swap) with only one interest rate leg as a notional position in a zero-specific-risk security:

(a) with a coupon equal to that on the interest rate leg;

(b) with a maturity equal to the date that the interest rate will be reset; and

(c) which is a long position if the firm is receiving interest payments and short if making interest payments.

Foreign exchange forwards, futures, CFDs and synthetic futures

7.9 A firm should treat a foreign currency forward, future, synthetic future or CFD as two notional currency positions as follows:

(a) a long notional position in the currency which the firm has contracted to buy; and

(b) a short notional position in the currency which the firm has contracted to sell.

7.10 The notional positions should have a value equal to either:

(a) the contracted amount of each currency to be exchanged in the case of a forward, future, synthetic future or CFD held in the non-trading book; or

(b) the present value of the amount of each currency to be exchanged in the case of a forward, future, synthetic future or CFD held in the trading book.

Foreign currency swaps

A firm should treat a foreign currency swap as:

(a) a long notional position in the currency in which the firm has contracted to receive interest and principal; and

(b) a short notional position in the currency in which the firm has contracted to pay interest and principal.

The notional positions should have a value equal to either:

(a) the nominal amount of each currency underlying the swap if it is held in the non-trading book; or

(b) the present value amount of all cash flows in the relevant currency in the case of a swap held in the trading book.

Futures, forwards, and CFDs on a single commodity

7.12 Where a forward, future, CFD or synthetic future settles according to:

1. the difference between the price set on trade date and that prevailing at contract expiry, then the notional position should:

   (a) equal the total quantity underlying the contract; and

   (b) have a maturity equal to the expiry date of the contract;

and

2. the difference between the price set on trade date and the average of prices prevailing over a certain period up to contract expiry, then a notional position should be derived for each of the reference dates used in the averaging period to calculate the average price, which:

   (a) equals a fractional share of the total quantity underlying the contract; and

   (b) has a maturity equal to the relevant reference date.

Buying or selling a single commodity at an average of spot prices prevailing in the future

7.13 Commitments to buy or sell at the average spot price of the commodity prevailing over some period between trade date and maturity should be treated as a combination of:

1. a position equal to the full amount underlying the contract with a maturity equal to the maturity date of the contract, which should be:

   (a) long, where the firm will buy at the average price; or

   (b) short, where the firm will sell at the average price;

and

2. a series of notional positions, one for each of the reference dates where the contract price remains unfixed, each of which should:

   (a) be long if the position under (1) is short, or short if the position under (1) is long;

(b) equal to a fractional share of the total quantity underlying the contract; and

(c) have a maturity date of the relevant reference date.

8 Qualifying debt instruments

8.1 CRR Article 336(4)(a) states that positions listed on a stock exchange in a third country, where the exchange is recognised by the competent authorities, qualify for the specific risk own funds requirements in the second row of the table in CRR Article 336.

8.2 For the purposes of this rule, we recognise the following stock exchanges in third countries:

- American Stock Exchange.
- Australian Securities Exchange Limited.
- Bermuda Stock Exchange.
- Bolsa Mexicana de Valores.
- Bourse de Montreal Inc.
- Channel Islands Stock Exchange.
- Chicago Board of Trade.
- Chicago Board Options Exchange.
- Chicago Board of Trade (CBOT).
- Chicago Stock Exchange.
- Coffee, Sugar and Cocoa Exchange, Inc.
- EUREX (Zurich).
- Euronext Amsterdam Commodities Market.
- Hong Kong Exchanges and Clearing Limited.
- ICE Futures US, Inc.
- International Securities Market Association.
- Johannesburg Stock Exchange.
- Kansas City Board of Trade.
- Korea Stock Exchange.
- Mid-America Commodity Exchange.
- Minneapolis Grain Exchange.
- National Association of Securities Dealers Automated Quotations (NASDAQ).
- New York Cotton Exchange.
- New York Futures Exchange.
- New York Stock Exchange.
- New York Mercantile Exchange Inc (NYMEX Inc.).
- New Zealand Stock Exchange.
- NYSE Liffe US.
- Osaka Securities Exchange.
- Pacific Exchange.
- Philadelphia Stock Exchange.
- Singapore Exchange.
- SIX Swiss Exchange AG.
- South African Futures Exchange.
- The Chicago Mercantile Exchange (CME).
- Tokyo International Financial Futures Exchange.
- Tokyo Stock Exchange.
- Toronto Stock Exchange.

9 Expectations relating to internal models

9.1 CRR Article 363 states that permission for an institution to use internal models to calculate capital is subject to competent authorities verifying compliance with:

- the general requirements;
- requirements particular to specific risk modelling; and
- requirements for an internal model for incremental default and migration risk

9.2 The standards that the PRA expects to be met to consider that an institution is compliant with these requirements are set out below.

High-level standards

9.3 A firm should be able to demonstrate that it meets the risk management standards set out in CRR Article 368 on a legal entity and business line basis where appropriate. This is particularly important for a subsidiary undertaking in a group subject to matrix management, where the business lines cut across legal entity boundaries.

Categories of Position

9.4 A VaR model permission will generally set out the broad classes of position within each risk category within its scope. It may also specify how individual products within one of those broad classes may be brought into or taken out of scope of the VaR model permission. These broad classes of permission are as follows:

1. Linear products, which comprise securities with linear pay-offs (such as bonds and equities), and derivative products which have linear pay-offs in the underlying risk factor (such as interest rate swaps, FRAs, and total return swaps).

2. European, American and Bermudan put and call options (including caps, floors, and swaptions) and investments with these features.

3. Asian options, digital options, single barrier options, double barrier options, look back options, forward starting options, compound options and investments with these features.

4. All other option based products (such as basket options, quantos, outperformance options, timing options, and correlation-based products) and investments with these features.

Data standards

9.5 The PRA expects a firm to ensure that the data series used by its VaR model is reliable. Where a reliable data series is not available, proxies or any other reasonable value-at-risk measurement may be used when the firm can demonstrate that the requirements of CRR Article 367(2)(e) are met. A firm should be able to demonstrate that the technique is appropriate and does not materially understate the modelled risks.

9.6 Data may be deemed insufficient if, for example, it contains missing data points, or data points which contain stale data. With regard to less-liquid risk factors or positions, the PRA expects the firm make a conservative assessment of those risks, using a combination of prudent valuation techniques and alternative VaR estimation techniques to ensure there is a sufficient cushion against risk over the close out period, which takes account of the illiquidity of the risk factor or position.

9.7 A firm is expected to update data sets to ensure standards of reliability are maintained in accordance with the frequency set out in its VaR model permission, or more frequently if volatility in market prices or rates necessitates more frequent updating. This is in order to ensure a prudent calculation of the VaR measure.

Aggregating VaR measures

9.8 In determining whether it is appropriate for an institution to use empirical correlations within risk categories and across risk categories within a model, the PRA expects certain features to be observed in assessing whether such an approach is sound and implemented with integrity. In general the PRA expects a firm to determine the aggregate VaR measure by adding the relevant VaR measure for each category, unless the firm's permission provides for a different method of aggregating VaR measures which is empirically sound.

9.9 The PRA does not expect a firm to use the square root of the sum of the squares approach when aggregating measures across risk categories or within risk categories unless the assumption of zero correlation between these categories is empirically justified. If correlations between risk categories are not empirically justified, the VaR measures for each category should simply be added in order to determine its aggregate VaR measure. However, to the extent that a firm's VaR model permission provides for a different way of aggregating VaR measures:

1. that method applies instead; and

2. if the correlations between risk categories used for that purpose cease to be empirically justified then the firm must notify the appropriate regulator at once.

Testing prior to model validation

9.10 A firm is expected to provide evidence of its ability to comply with the requirements for a VaR model permission. In general it will be required to demonstrate this by having a backtesting programme in place and should provide three months of backtesting history.

9.11 A period of initial monitoring or live testing is required before a VaR model can be recognised. This will be agreed on a firm by firm basis.

9.12 In assessing the firm's VaR model and risk management, the results of internal model validation procedures used by the firm to assess the VaR model will be taken into account.

Backtesting

9.13 For clarity, the backtesting requirements of CRR Article 366 should be implemented as follows:

- If the day on which a loss is made is day n, the value-at-risk measure for that day will be calculated on day n-1, or overnight between day n-1 and day n. Profit and loss figures are produced on day n+1, and backtesting also takes place on day n+1. The firm's supervisor should be notified of any overshootings by close of business on day n+2.

- Any overshooting initially counts for the purpose of the calculation of the plus factor even if subsequently the PRA agrees to exclude it. Thus, where the firm experiences an overshooting and already has four or more overshootings for the previous 250 business days, changes to the multiplication factor arising from changes to the plus factor become effective at day n+3.

9.14 A longer time period generally improves the power of backtesting. However a longer time period may not be desirable if the VaR model or market conditions have changed to the extent that historical data is no longer relevant.

9.15 The PRA will review, as part of a firm's VaR model permission application, the processes and documentation relating to the derivation of profit and loss used for backtesting. A firm's documentation should clearly set out the basis for cleaning profit and loss. To the extent that certain profit and loss elements are not updated every day (for example certain reserve calculations) the documentation should clearly set out how such elements are included in the profit and loss series.

Planned changes to the VaR model

9.16 In accordance with CRR Article 363(3), the PRA expects a firm to provide and discuss with us details of any significant planned changes to the VaR model before those changes are implemented. These details must include detailed information about the nature of the change, including an estimate of the impact on VaR numbers and the incremental risk charge.

Bias from overlapping intervals for ten-day VaR and sVaR

9.17 The use of overlapping intervals of ten-day holding periods for the purposes of CRR Article 365 introduces an autocorrelation into the data that would not exist should truly independent ten-day periods be used. This may give rise to an underestimation of the volatility and the VaR at the 99% confidence level. To obtain clarity on the materiality of the bias, a firm should measure the bias arising from the use of overlapping intervals for ten-day VaR and sVaR when compared to using independent intervals. A report on the analysis, including a proposal for a multiplier on VaR and sVaR to adjust for the bias, should be submitted to the PRA for review and approval.

10 VaR and stressed VaR calculation

10.1 CRR Article 365 requires firms that use an internal model for calculating their own funds requirement to calculate at least weekly a 'stressed value-at-risk' (sVaR) of their current portfolio. When the PRA considers a firm's application to use a sVaR internal model, we would expect the following features to be present prior to permission being granted as indicative that the conditions for granting permission have been met.

Quantile estimator

10.2 The firm should calculate the sVaR measure to be greater than or equal to the average of the second and third worst loss in a twelve-month time series comprising of 250 observations. The PRA expects as a minimum that a corresponding linear weighting scheme should be applied if the firm use a larger number of observations.

Meaning of 'period of significant financial stress relevant to the institution's portfolio'

10.3 The firm should ensure that the sVaR period chosen is equivalent to the period that would maximise VaR given the firm's portfolio. There is an expectation that a stressed period should be identified at each legal entity level at which capital is reported. Therefore, group-level sVaR measures should be based on a period that maximises the group-level VaR, whereas entity-level sVaR should be based on a period that maximises VaR for that entity.

Antithetic data

10.4 The PRA expects firms to consider whether the use of antithetic data in the calculation of the sVaR measure is appropriate to the firm's portfolio. A justification for using or not using antithetic data should be provided to the PRA.

Absolute and relative shifts

10.5 The PRA expects firms to explain the rationale for the choice of absolute or relative shifts for both VaR and sVaR methodologies. In particular, statistical processes driving the risk factor changes need to be evidenced for both VaR and sVaR.

10.6 The following information is expected to be submitted quarterly:

- analysis to support the equivalence of the firm's current approach to a VaR-maximising approach on an ongoing basis;
- the rationale behind the selection of key major risk factors;
- summary of ongoing internal monitoring of stressed period selection with respect to current portfolio;
- analysis to support capital equivalence of upscaled one-day VaR and sVaR measures to corresponding full ten-day VaR and sVaR measures;
- graphed history of sVaR/VaR ratio;
- analysis to demonstrate accuracy of partial revaluation approaches specifically for sVaR purposes (for firms using revaluation ladders or spot/vol-matrices). This should include a review of the ladders/matrices or spot/vol-matrices, ensuring that they are extended to include wider shocks to risk factors that incur in stress scenarios; and
- minutes of Risk Committee meeting or other form of evidence to reflect governance and senior management oversight of stressed VaR methodology.

11 Requirement to have an internal IRC model

11.1 CRR Article 372 requires firms that use an internal model for calculating own funds requirements for specific risk of traded debt instruments to also have an internal incremental default and migration risk (IRC) model in place. This model should capture the default and migration risk of its trading book positions that are incremental to the risks captured by its VaR model.

11.2 When the PRA considers a firm's application to use an IRC internal model, the PRA expects that the following matters would be included as demonstrating compliance with the standards set in CRR Article 372.

Basis risks for migration

11.3 The PRA expects the IRC model to capitalise pre-default basis risk. In this respect, the model should reflect that in periods of stress the basis could widen substantially. Firms should disclose to the PRA their material basis risks that are incremental to those already captured in existing market risk capital measures (VaR-based and others). This must take actual close-out periods during periods of illiquidity into account.

Price/spread change model

11.4 The price/spread change model used to capture the profit and loss impact of migration should calibrate spread changes to long-term averages of differences between spreads for relevant ratings. These should either be conditioned on actual rating events, or using the entire history of spreads regardless of migration. Point-in-time estimates are not considered acceptable, unless they can be shown to be as conservative as using long-term averages.

Dependence of the recovery rate on the economic cycle

11.5 To achieve a soundness standard comparable to those under the IRB approach, LGD estimates should reflect the economic cycle. The PRA therefore expects firms to incorporate dependence of the recovery rate on the economic cycle into the IRC model. Should the firm use a conservative parameterisation to comply with the IRB standard of the use of downturn estimates, evidence of this will be required to be submitted in quarterly reporting to the PRA, bearing in mind that for trading portfolios, which contain long and short positions, downturn estimates would not in all cases be a conservative choice.

6 Operational risk

Operational risk

1 Introduction

1.1 This supervisory statement is aimed at firms to which CRD IV applies.

1.2 This statement sets out the PRA's expectations on the extent to which the Advanced Measurement Approach (AMA) should capture the firms' operational risks where the firm has, or is about to, implement AMA. This is relevant where the AMA is applied across only part of a firm's operations and is used in conjunction with either the Basic Indicator Approach (BIA), or the Standardised Approach (TSA).

1.3 This statement should be read in conjunction with CRR Article 314(3) and the high-level expectations outlined in *The PRA's approach to banking supervision* (April 2013).

2 The PRA's expectations in relation to AMA

2.1 A firm may use an AMA in combination with either the BIA or TSA provided it obtains permission from the PRA.

2.2 In granting such permission, the PRA is required by CRR Article 314(3) to impose the following conditions when the AMA is used in combination with BIA or TSA:

(a) On the date of first implementation of an AMA, a '**significant**' part of the institution's operational risk are captured by that Approach; and

(b) The institution to commit to apply the AMA across a '**material**' part of its operations within a time schedule approved by the PRA.

2.3 For the purposes of these conditions, the PRA considers that:

- a 'significant' part of operational risk is approximately 50% or more; and
- a 'material' part of its operations is around 85% (or more).

7 Groups and large exposures

Groups

1 Introduction

1.1 This supervisory statement is aimed at firms to which CRD IV applies who are part of a group.

1.2 This statement sets out the PRA's expectations with regards to applications relating to:

(a) approach to consolidation, in particular individual consolidation (CRR Article 9) and the method of consolidation for entities falling within CRR Article 18(5); and

(b) excluding certain entities from consolidation (CRR Article 19(2)).

1.3 This statement should be read in conjunction with the CRR articles listed, the requirements in the Groups Part of the PRA Rulebook and the high-level expectations outlined in *The PRA's approach to banking supervision* (April 2013).

2 Approach to consolidation

Application process

2.1 Where a parent institution wishes to apply for individual consolidation, it will be expected to make a formal application to the PRA. The PRA expects the application to demonstrate how the conditions set out in CRR Article 9 and 396(2) are met.

2.2 The PRA will assess individual consolidation applications against CRR Article 9 and 396(2) on a case by case basis. Where the conditions in CRR Article 9 and 396(2) are met, the PRA will assess whether it is still appropriate to permit the treatment, if doing so risks conflict with its statutory objectives. The PRA will apply a high level of scrutiny to applications under CRR Article 9 as per the PRA's previous solo consolidation regime.

2.3 Where a parent institution does not wish to fully consolidate its undertakings subject to CRR Article 18(5), it will be expected to make a formal application to the PRA. The application should seek to demonstrate how fully consolidating those undertakings is disproportionate to the risk carried by the firm.

Application of criteria

2.4 CRR Article 9(2) requires parent institutions to demonstrate fully to the PRA, as competent authority, that there are no material practical or legal impediments to the prompt transfer of own funds or repayment of liabilities when due by the subsidiary to its parent undertaking.

2.5 When making this assessment, the PRA will consider whether any minority interest may represent an impediment of any kind to the prompt transfer of own funds or repayment of liabilities from subsidiary undertaking to parent. To reassure the PRA, the parent institution should demonstrate that any minority interest in a subsidiary institution will not result in the potential blocking or delay of prompt transfer of own funds or repayment of liabilities.

2.6 It may therefore be possible for a firm to meet the condition in CRR Article 7(1)(d) but not meet the condition in CRR Article 9(2).

2.7 The PRA will consider the non-exhaustive list below when determining whether the conditions in CRR Article 9(2) are met:

(a) the speed with which funds can be transferred or liabilities repaid to the firm and the simplicity of the method for the transfer or repayment;

(b) whether there are any interests other than those of the firm in the subsidiary undertaking and what impact those other interests may have on the firm's control over the subsidiary undertaking and on the ability of the firm to require a transfer of funds or repayment of liabilities. As part of our overall assessment, we would consider one of the indicators to achieving prompt transfer as being ownership of 75%[(1)] or more of the subsidiary undertaking;

(c) whether the prompt transfer of funds or repayment of liabilities to the firm might harm the reputation of the firm or its subsidiary undertakings;

(d) whether there are any tax disadvantages for the firm or the subsidiary undertaking as a result of the transfer of funds or repayment of liabilities;

(1) 75% or more shareholders can pass a special resolution.

(e) whether there are any exchange controls that may have an impact on the transfer of funds or repayment of liabilities;

(f) whether there are assets in the subsidiary undertaking available either to be transferred or liquidated for the purposes of the transfer of funds or repayment of liabilities;

(g) whether any regulatory requirements impact on the ability of the subsidiary undertaking to transfer funds or repay liabilities promptly;

(h) whether the purpose of the subsidiary undertaking prejudices the prompt transfer of funds or repayment of liabilities;

(i) whether the legal structure of the subsidiary undertaking prejudices the prompt transfer of funds or repayment of liabilities;

(j) whether the contractual relationships of the subsidiary undertaking with the firm and other third parties prejudices the prompt transfer of funds or repayment of liabilities;

(k) whether past and proposed flows of funds between the subsidiary undertaking and the firm demonstrate the ability to make prompt transfer of funds or repayment of liabilities; and

(l) whether the degree of solo consolidation by the firm undermines the appropriate regulator's ability to assess the soundness of the firm as a legal entity.

3 CRR Article 19(2) — entities excluded from the scope of prudential consolidation

Application process

3.1 Where a firm wishes to exclude entities from the scope of prudential consolidation, it will be expected to make a formal application to the PRA. This application should seek to articulate how one of the conditions set out in CRR Article 19(2) (a), (b), or (c) is met.

3.2 The PRA will assess applications to exclude entities from the scope of prudential consolidation under CRR Article 19(2) on a case by case basis. The PRA will only grant this treatment with respect to undertakings where one of the conditions in CRR Article 19(2) is met. Note that the PRA will still make a judgement as to whether it is appropriate to grant this treatment even where one of the conditions in CRR Article 19(2) is met.

Application of criteria

3.3 CRR Article 19(2) allows the consolidating supervisor to decide that an institution, financial institution or ancillary services undertaking, which is a subsidiary or in which a participation is held, need not be included in the consolidation in the following cases:

(a) where the undertaking concerned is situated in a third country where there are legal impediments to the transfer of necessary information; or

(b) where the undertaking concerned is of negligible interest only with respect to the objectives of monitoring credit institutions; or

(c) where, in the opinion of the competent authorities responsible for exercising supervision on a consolidated basis, the consolidation of the financial situation of the undertaking concerned would be inappropriate or misleading as far as the objectives of the supervision of credit institutions are concerned.

3.4 If several undertakings meet the criteria in (b) above, and are collectively of non-negligible interest with respect of the specified objectives, the PRA may not agree to exclude them all from the consolidation.

3.5 The PRA may request a firm to provide information about the undertakings excluded from consolidation.

Large exposures

1 Introduction

1.1 This supervisory statement is aimed at firms to which CRD IV applies.

1.2 This statement outlines the PRA's expectations in relation to large exposures requirements within the CRR. It covers:

(a) Applications to incorporate undertakings within a core UK group (CRR Article 113(6)) and non-core large exposure group (CRR 400(2)(c)).

(b) Sovereign large exposures exemptions (CRR Article 400(2)(g-h)) and exposures to trustees.

1.3 This statement should be read in conjunction with the specified CRR articles, the requirements in the Large Exposures Part of the PRA Rulebook and the high-level expectations outlined in *The PRA's approach to banking supervision* (April 2013).

2 CRR Article 400(1)(f): core UK group applications

2.1 CRR Article 113(6) permits a firm, subject to conditions, to apply a 0% risk weight for exposures to certain entities within its consolidation group, namely its parent undertaking, its own subsidiaries, and subsidiaries of its parent.

2.2 CRR Article 400(1)(f) then requires that exposures that are assigned a 0% risk weight under CRR Article 113(6) are fully exempted from the large exposures limit stipulated in CRR Article 395(1).

Application process

2.3 Firms wishing to apply a 0% risk weight to relevant exposures should make a formal application to the PRA, through which they should seek to demonstrate how the conditions set out in CRR Article 113(6)(a)-(e) are met.

2.4 The PRA will assess individual applications against CRR Article 113(6) on a case-by-case basis. The PRA will only approve applications where the conditions stipulated in CRR Article 113(6) are met.

2.5 Firms should note that the PRA will still make a wider judgement whether it is appropriate to grant this treatment even where the conditions in CRR Article 113(6) are met.

2.6 It is the PRA's intention to continue to apply a high level of scrutiny to applications under CRR Article 113(6).

Application of criteria

2.7 In relation to CRR Article 113(6)(d), the PRA will deem the condition to have been satisfied if:

- it is incorporated in the United Kingdom; or

- it is an undertaking of a type that falls within the scope of the Council Regulation of 29 May 2000 on insolvency proceedings (Regulation 1346/2000/EC); and

- it is established in the United Kingdom other than by incorporation; and

- the firm can demonstrate that the counterparty's centre of main interests is situated in the United Kingdom.

2.8 In relation to CRR Article 113(6)(e), the PRA will consider the following non-exhaustive list of factors when assessing whether this condition has been met:

- the speed with which funds can be transferred or liabilities repaid to the firm and the simplicity of the method for the transfer or repayment. As part of our overall assessment, we would consider one of the indicators to achieving prompt transfer as being ownership of 100% of the subsidiary undertaking;

- whether there are any interests other than those of the firm in the undertaking, and what impact those other interests may have on the firm's control over the undertaking and the ability of the firm to require a transfer of funds or repayment of liabilities;

- whether there are any tax disadvantages for the firm or the undertaking as a result of the transfer of funds or repayment of liabilities;

- whether the purpose of the undertaking prejudices the prompt transfer of funds or repayment of liabilities;

- whether the legal structure of the undertaking prejudices the prompt transfer of funds or repayment of liabilities;

- whether the contractual relationships of the undertaking with the firm and other third parties prejudices the prompt transfer of funds or repayment of liabilities; and

- whether past and proposed flows of funds between the undertaking and the firm demonstrate the ability to make prompt transfer of funds or repayment of liabilities.

2.9 When demonstrating how CRR Article 113(6)(e) is met, the PRA considers that in the case of a counterparty which is not a firm, the formal application should include a legally binding agreement between the firm and the counterparty. This agreement will be to promptly, on demand by the firm, increase the firm's capital resources by an amount required to ensure that the firm complies with the provisions contained in CRR Part Two (Own funds) and any other requirements relating to capital resources or concentration risk imposed on a firm by or under the regulatory system.

2.10 For the purpose of demonstrating compliance with CRR Article 113(6)(e), the PRA considers that the agreement to increase the firm's capital resources may be limited to capital resources available to the undertaking. It may reasonably exclude such amount of capital resources that, if transferred to the firm, would cause the undertaking to become balance sheet insolvent, in the manner contemplated in section 123(2) of the Insolvency Act 1986.

2.11 The PRA does not expect a firm to which this section applies to use any member of its core UK group (which is not a firm) to route lending, or to have exposures to any third party in excess of the limits stipulated in Article 395(1).

3 CRR Article 400(2)(c) — non-core large exposures groups

3.1 CRR 400(2)(c) permits the PRA to fully or partially exempt exposures incurred by an institution to intra-group undertakings from the large exposures limit stipulated in CRR Article 395(1). The PRA will consider exempting non-trading book and trading book exposures to intra-group undertakings that meet specified conditions (set out below and in the large exposures rules).

3.2 The PRA expects that applications for exemptions under CRR 400(2)(c) will be for institutions established in the United Kingdom where the intra-group undertakings to which it is exposed meet the criteria for the core UK group (CRR Article 113(6)) except for CRR Article 113(6)(d).

Application process

3.3 Where firms wish to apply for a non-core large exposures group exemption, the PRA expects them to make a formal application through which they should seek to demonstrate:

- how the conditions set out in CRR Article 400(2)(c) are met;
- how the counterparties to be included in the non-core large exposures group meet the conditions for the core UK group except CRR Article 113(6)(d); and
- compliance with the conditions set out in the large exposures instrument.

3.4 Firms should note that the PRA will still make a wider judgement whether it is appropriate to grant this treatment even where the above conditions are met.

4 CRR Article 400(2)(g)-(h) — sovereign large exposures exemption

4.1 CRR Article 400(2)(g)-(h) allows the PRA to exempt exposures which constitute claims on central banks in the form of minimum reserves held at central banks and denominated in their national currencies, and claims on central governments in the form of statutory liquidity requirements held in government securities, which are denominated and funded in their national currencies.

Application process

4.2 Where firms wish to apply a sovereign large exposures exemption, they will be expected to make a formal application to the PRA through which they should seek to demonstrate the way in which the relevant conditions set out CRR Article 400(2)(g)-(h) are met. The application should also demonstrate how the relevant conditions set out in the large exposures instrument are met.

4.3 The PRA will assess individual sovereign large exposures exemption applications against CRR Article 400(2)(g)-(h) on a case-by-case basis. The PRA will only approve this treatment where the conditions stipulated in CRR Article 400(2)(g)-(h) are met. Firms should note that the PRA will still make a wider judgement whether it is appropriate to grant this treatment even where the conditions in CRR Article 400(2)(g)-(h) are met.

Application of criteria

4.4 It is the PRA's intention to continue to apply a high level of scrutiny to applications under CRR Article 400(2)(g)-(h).

4.5 As part of the process of applying for a sovereign large exposure exemption, the PRA expects the firm to agree on the amount of the exposures that may be exempted. In general, the PRA expects the likelihood of the firm's liabilities (that fund the particular exempt exposure) falling alongside a fall in that exposure in an event of default to form one of the key considerations in discussions with the firm regarding the total amount of such exempt exposures.

4.6 The PRA will expect the firm to demonstrate that, taking into account the aggregate of all exposures exempted under other sovereign large exposure exemptions granted to the firm, the exemption being sought would not result in an undue risk to the safety and soundness of the firm.

5 Exposures to trustees

5.1 This section clarifies the PRA's expectations on firms when considering exposures to counterparties which act as a trustee, custodian or general partner of an investment trust, unit trust, venture capital or other investment fund, pension fund or a similar fund.

5.2 If a firm has an exposure to a person ('A') when A is acting on his own behalf, and also an exposure to A when A acts in his capacity as trustee, custodian or general partner of an investment trust, unit trust, venture capital or other investment fund, pension fund or a similar fund (a 'fund'), the firm may treat the latter exposure as if it was to the fund. This treatment may be adopted unless such a treatment would be misleading.

5.3 When considering whether the treatment described is misleading, factors a firm should consider include:

(a) the degree of independence of control of the fund, including the relation of the fund's board and senior management to the firm or to other funds or to both;

(b) the terms on which the counterparty, when acting as trustee, is able to satisfy its obligation to the firm out of the fund of which it is trustee;

(c) whether the beneficial owners of the fund are connected to the firm, or related to other funds managed within the firm's group, or both; and

(d) for a counterparty that is connected to the firm itself, whether the exposure arises from a transaction entered into on an arm's length basis.

5.4 In deciding whether a transaction is at arm's length, the PRA expects the following factors to be taken into account:

(a) the extent to which the person to whom the firm has an exposure ('A') can influence the firm's operations, through eg the exercise of voting rights;

(b) the management role of A where A is also a director of the firm; and

(c) whether the exposure would be subject to the firm's usual monitoring and recovery procedures if repayment difficulties emerged.