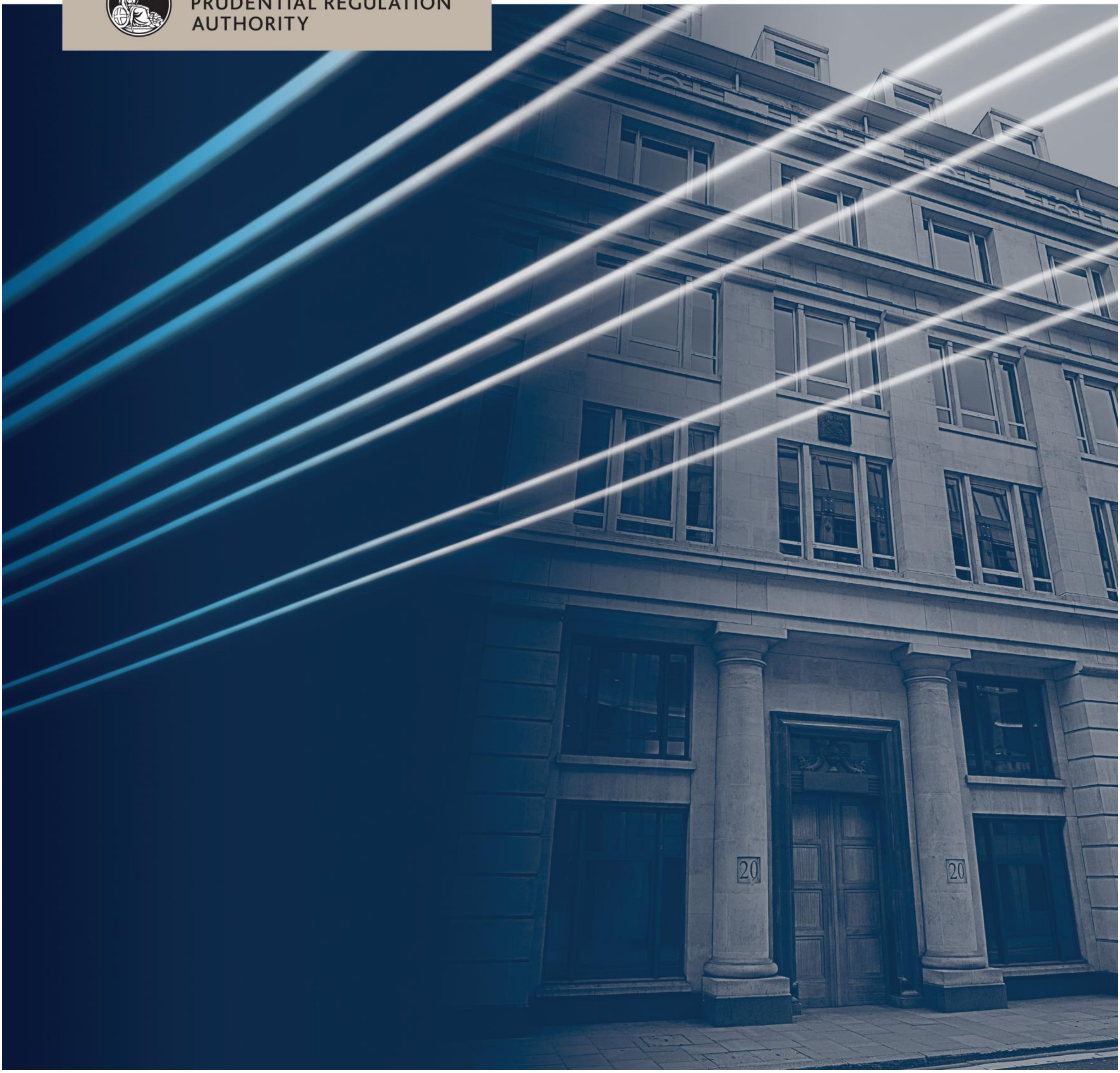
Supervisory Statement | SS45/15

The UK leverage ratio framework

December 2015

BANK OF ENGLAND
PRUDENTIAL REGULATION AUTHORITY



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1 Introduction

1.1 This supervisory statement (SS) is aimed at Capital Requirements Regulation (CRR) firms in scope of the UK leverage ratio framework. The purpose of this SS is to set out the expectations of the Prudential Regulatory Authority (PRA) on leverage ratio buffers and the reporting and disclosure of an averaged leverage ratio, as well as to provide some clarification on the PRA rules. It should be read alongside the Leverage Ratio, Reporting Leverage Ratio and Public Disclosure Parts of the PRA Rulebook. This statement complements the PRA's rules in implementing the FPC's Direction and Recommendation with regard to a UK leverage ratio framework. [1]

2 Leverage Ratio Buffers

2.1 Firms that do not hold an amount of Common Equity Tier 1 (CET1) equal to or greater than their applicable leverage ratio buffers will not face automatic restrictions on their distributions.

2.2 Where a firm does not hold an amount of CET1 capital that is equal to or greater than its countercyclical leverage ratio buffer (CCLB), it must notify the PRA immediately in accordance with Leverage Ratio 5.1 and prepare a capital plan and submit it to the PRA, including the information required in Leverage Ratio 6.2.

2.3 The global systemically important institution (G-SII) additional leverage ratio buffer (ALRB) is firm specific. Where applicable to a firm, the G-SII ALRB and related reporting and disclosure requirements will be set by the PRA using its powers under section 55M of the Financial Services and Markets Act (2000). If a G-SII does not hold an amount of CET1 capital that is equal to or greater than its G-SII ALRB, it will be required to notify the PRA immediately and prepare a capital plan and submit it to the PRA.

2.4 The PRA will assess a firm's capital plan to determine whether, if implemented, it would be reasonably likely to secure that the amount of the firm's CET1 will be equal to or greater than the firm's leverage ratio buffers within a period which the PRA considers appropriate. When exercising its judgement on what constitutes a reasonable time to rebuild buffers drawn down in stress, the PRA will take into account the drivers of the firm's shortfall, including in the context of current and forecasted macroeconomic and financial conditions.

2.5 In determining the appropriate period for a firm to satisfy its CCLB, the PRA will have regard to the period of time the firm had to meet the increase in its Countercyclical Capital Buffer rate(s). The PRA expects any increase in the CCLB rate to follow the transitional periods set for the increase in the relevant CCB rate(s), which will generally become effective twelve months after an announcement. This approach would ensure consistency and complementarity between the CCB and CCLB.

2.6 When calculating its CCLB, a firm is expected to take into account any decrease in relevant CCB rate(s) immediately.

3 Averaged leverage ratio calculation

3.1 The PRA expects firms not to engage in short-term balance sheet management activities with a view to boosting their leverage ratio temporarily at any point in time.

1 Financial Stability Report, July 2015; www.bankofengland.co.uk/publications/Documents/fsr/2015/fsrfull1507.pdf.

3.2 For the purpose of calculating an averaged leverage ratio over a reporting quarter, the PRA rules require firms to calculate the exposure measure based on firms' daily on-balance sheet assets averaged over the quarter and monthly (at the last day of the month) off-balance sheet exposures averaged over the quarter, in accordance with Reporting Leverage Ratio 3.2. The capital measure and relevant deductions and adjustments should be calculated with the same frequency as the off-balance sheet exposures.

3.3 During the transitional period for daily averaged reporting, the PRA permits firms to calculate the exposure measure based on monthly (at the last day of the month) exposure measures averaged over a quarter, for both on- and off-balance sheet exposures, in accordance with Reporting Leverage Ratio 4.2. The capital measure and relevant deductions and adjustments should be calculated in the same way. The same methodology should apply to the computation of the averaged leverage ratio disclosed during the transitional period for disclosures.

3.4 The PRA recognises that there might be difficulties in valuing certain accounting assets at the end of each day and therefore intends to adopt a pragmatic approach to the implementation of the averaging requirement. The PRA considers that 'best estimates' are acceptable so long as they are measured consistently and prudently. For the purpose of daily valuation of balance sheet assets, firms should apply methodologies and a valuation basis that are consistent with those used for quarter-end reporting. The PRA expects firms to have appropriate governance and procedures to ensure the accuracy and representativeness of the averaged leverage ratio and its components which are reported and disclosed. Firms should provide an explanation of the assumptions used in their calculations.