

## Chapter 4

# Capital resources

## 4.2 Capital resources requirements

4.2.-1

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### General solvency requirement

4.2.1

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A *firm* must at all times ensure that it is able to meet its liabilities as they fall due.

4.2.1A

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Specific liquidity requirements for a *firm* carrying on any *home financing* or *home finance administration* connected to *regulated mortgage contracts* are set out in ■ MIPRU 4.2D.

### General capital resource requirement

4.2.2

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A *firm* must at all times maintain capital resources equal to or in excess of its relevant capital resources requirement.

### Capital resources: relevant accounting principles

4.2.3

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A *firm* must recognise an asset or liability, and measure its amount, in accordance with the relevant accounting principles applicable to it for the purpose of preparing its annual financial statements unless a *rule* requires otherwise.

### Capital resources: client assets

4.2.4

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In this chapter, "*client assets*" includes a *document* only if it has value, or is capable of having value, in itself (such as a bearer instrument)

### Capital resources requirement: firms carrying on regulated activities including designated investment business

4.2.5

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The capital resources requirement for a *firm* (other than a *credit union*) carrying on *regulated activities*, including *designated investment business* and to which *IPRU(INV)* does not apply, is the higher of:

- (1) the requirement which is applied by this chapter according to the activity or activities of the *firm* (treating the relevant *rules* as applying to the *firm* by disregarding its *designated investment business*); and
- (2) the financial resources requirement which is applied by the Prudential sourcebook for MiFID Investment Firms (*MIFIDPRU*).

**4.2.5A** **G** The capital resources requirement for a *firm* (other than a *credit union*) carrying on *regulated activities*, including *designated investment business*, which is also subject to the Interim Prudential sourcebook for investment businesses is the amount calculated in IPRU(INV) 13.13.3R.

**Capital resources requirement: social housing firms**

**4.2.7** **R** The capital resources requirement for a *social housing firm* whose *Part 4A permission* is limited to carrying on the *regulated activities* of:

- (1) *home financing*; or
- (2) *home finance administration* (or both);

is that the *firm's* net tangible assets must be greater than zero.

**4.2.8** **G** If a *social housing firm* is carrying on *home financing* or *home finance administration* (and no other *regulated activity*), its net tangible assets must be greater than zero. However, if it carries on *insurance distribution activity* or *home finance mediation activity*, there is no special provision and the capital resources requirement for *firms* carrying on *designated investment business*, *insurance distribution activity* or *home finance mediation activity* only applies to it as appropriate.

**Capital resources requirement: application according to regulated activities**

**4.2.9** **R** Unless any of the *rules* on capital resources for *firms* carrying on *designated investment business*, for *credit unions* or for *social housing firms* apply, the capital resources requirement for a *firm* varies according to the *regulated activity* or activities it carries on.

**4.2.10** **R** Table: Application of capital resources requirements

	Regulated activities	Provisions
1.	(a) <i>insurance distribution activity</i> ; or  (b) <i>home finance mediation activity</i> (or both); and no other <i>regulated activity</i> .	MIPRU 4.2.11 R
2.	(a) <i>home financing</i> not connected to <i>regulated mortgage contracts</i> ; or  (b) <i>home financing</i> and <i>home finance administration</i> (not connected to <i>regulated mortgage contracts</i> ); and no other <i>regulated activity</i> .	MIPRU 4.2.12 R to MIPRU 4.2.17 E
3.	<i>home finance administration</i> ; and no other <i>regulated activity</i> .	MIPRU 4.2.18 R to MIPRU 4.2.19 R

	Regulated activities	Provisions
4.	<i>insurance distribution activity; and</i> (a) <i>home financing; or</i> (b) <i>home finance administration (or both).</i>	MIPRU 4.2.20 R
5.	<i>home finance mediation activity; and</i> (a) <i>home financing, or</i> (b) <i>home finance administration (or both).</i>	MIPRU 4.2.21 R
7.	a) <i>home financing connected to regulated mortgage contracts; or</i>  (b) <i>home financing and home finance administration connected to regulated mortgage contracts; and no other regulated activity.</i>	[deleted] MIPRU 4.2.23 R
8.	any combination of <i>regulated activities</i> not within rows 1 to 7.	MIPRU 4.2.22 R

## 4.2.10A

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■ MIPRU 4.2.12 R to ■ MIPRU 4.2.23 R have the effect that a *firm* carrying on any *home financing* or *home finance administration* which is connected to *regulated mortgage contracts* will be subject to different capital requirements to a *firm* that carries on those activities without connection to *regulated mortgage contracts*. To identify which of the *rules* in ■ MIPRU 4.2.12 R to ■ MIPRU 4.2.23 R is applicable, a *firm* should consider which *regulated activities* it performs as part of its *home financing* and *home finance administration* activities and determine whether any of those *regulated activities* (no matter what proportion) are connected to *regulated mortgage contracts*.

### Capital resources requirement: insurance distribution activity or home finance mediation activity only

## 4.2.11

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- (1) If a *firm* carrying on *insurance distribution activity* or *home finance mediation activity* (and no other *regulated activity*) does not hold *client money* or other *client assets* in relation to these activities, its capital resources requirement is the higher of:
- £5,000; and
  - 2.5% of the *annual income* from its *insurance distribution activity* or *home finance mediation activity* (or both).
- (2) If a *firm* carrying on *insurance distribution activity* or *home finance mediation activity* (and no other *regulated activity*) holds *client money* or other *client assets* in relation to these activities, its capital resources requirement is the higher of:

- (a) £10,000; and
- (b) 5% of the *annual income* from its *insurance distribution activity* or *home finance mediation activity* (or both).

### Capital resources requirement: home financing and home finance administration not connected to regulated mortgage contracts

4.2.12

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- (1) The capital resources requirement for a *firm* carrying on only *home financing*, which is not connected to *regulated mortgage contracts*, or *home financing* and *home finance administration* which is not connected to *regulated mortgage contracts* (and no other *regulated activity*) is the higher of:
- (a) £100,000; and
  - (b) 1% of:
    - (i) its total assets plus total undrawn commitments and unreleased amounts under the *home reversion plan*; less:
    - (ii) excluded loans or amounts plus intangible assets (see Note 1 in the table in ■ MIPRU 4.4.4 R).
- (2) Undrawn commitments and unreleased amounts means the total of those amounts which a *customer* has the right to draw down or to receive from the *firm* but which have not yet been drawn down or received, excluding those under an agreement:
- (a) which has an original maturity of up to one year; or
  - (b) which can be unconditionally cancelled at any time by the lender or provider.

4.2.13

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When considering what is an undrawn commitment or unreleased amount, the *appropriate regulator* takes into account an amount which a *customer* has the right to draw down or to receive under a *home finance transaction*, but which has not yet been drawn down or received, whether the commitment or obligation is revocable or irrevocable, conditional or unconditional.

4.2.14

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When calculating total assets, the *firm* may exclude a loan or plan which has been transferred to a third party only if it meets the following conditions:

- (1) the first condition is that the loan or the plan has been transferred in a legally effective manner by:
  - (a) novation; or
  - (b) legal or equitable assignment; or
  - (c) sub-participation; or
  - (d) declaration of trust; and
- (2) the second condition is that the *home finance provider*:
  - (a) retains no material economic interest in the loan or the plan; and
  - (b) has no material exposure to losses arising from it.

- 4.2.15 **E** (1) When seeking to rely on the second condition, a *firm* should ensure that the loan or plan qualifies for the 'linked presentation' accounting treatment under Financial Reporting Standard 5 (Reporting the substance of transactions) issued in April 1994, and amended in December 1994 and September 1998 (if applicable to the *firm*).
- (2) Compliance with (1) may be relied upon as tending to establish compliance with the second condition.

4.2.16 **G** The requirement that the loan qualifies for the 'linked presentation' accounting treatment under FRS 5 is aimed at those *firms* which report according to FRS 5. Other *firms* which report under other standards, including *UK-adopted international accounting standards*, need not adopt FRS 5 in order to meet the second condition.

- 4.2.17 **E** (1) When seeking to rely on the second condition, a *firm* should not provide material credit enhancement in respect of the loan or plan unless it deducts the amount of the credit enhancement from its capital resources before meeting its capital resources requirement.
- (2) Credit enhancement includes:
- (a) any holding of subordinated loans or notes in a transferee that is a special purpose vehicle; or
  - (b) over collateralisation by transferring loans or plans to a larger aggregate value than the *securities* to be issued; or
  - (c) any other arrangement with the transferee to cover a part of any subsequent losses arising from the transferred loan or plan.
- (3) Contravention of (1) may be relied upon as tending to establish contravention the second condition.

### Capital resources requirement: home finance administration only

- 4.2.18 **R** The capital resources requirement for a *firm* carrying on *home finance administration* only, which has all or part of the *home finance transactions* that it administers on its balance sheet, is:
- (1) in the case of a *firm* carrying on only *home finance administration* which is not connected to *regulated mortgage contracts*, the amount which is applied to a *firm* under ■ MIPRU 4.2.12 R; or
  - (2) in the case of a *firm* carrying on any *home finance administration* which is connected to *regulated mortgage contracts*, the amount which is applied to a *firm* under ■ MIPRU 4.2.23 R.

4.2.19 **R** The capital resources requirement for a *firm* carrying on *home finance administration* only, which has all the *home finance transactions* that it administers off its balance sheet, is the higher of:

- (1) £100,000; and
- (2) 10% of its *annual income*.

#### Capital resources requirement: insurance distribution activity and home financing or home finance administration

4.2.20

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The capital resources requirement for a *firm* carrying on *insurance distribution activity* and *home financing* or *home finance administration* is the sum of :

- (1) the capital resources requirement for a *firm* carrying on *insurance distribution activity* or *home finance mediation activity* (and no other *regulated activity*) (see ■ MIPRU 4.2.11 R); and
- (2) (a) in the case of a *firm* carrying on *home financing* which is not connected to *regulated mortgage contracts*, or *home finance administration* which is not connected to *regulated mortgage contracts*, the amount which is applied to a *firm* under ■ MIPRU 4.2.12 R; or
  - (aa) in the case of a *firm* carrying on any *home financing* which is connected to *regulated mortgage contracts* or any *home finance administration* that it administers on its balance sheet which is connected to *regulated mortgage contracts*, the amount which is applied to a *firm* under ■ MIPRU 4.2.23 R; or
  - (b) in the case of a *firm* carrying on *home finance administration* with all the *home finance transactions* that it administers off balance sheet, the amount which is applied to a *firm* under ■ MIPRU 4.2.19 R.

#### Capital resources requirement: home finance mediation activity and home financing or home finance administration

4.2.21

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- (1) If a *firm* carrying on *home finance mediation activity* and *home financing* or *home finance administration* does not hold *client money* or other *client assets* in relation to its *home finance mediation activity*, the capital resources requirement is:
  - (a) in the case of a *firm* carrying on *home financing* which is not connected to *regulated mortgage contracts* or *home finance administration* which is not connected to *regulated mortgage contracts*, the amount applied to a *firm* under ■ MIPRU 4.2.12 R; or
  - (aa) in the case of a *firm* carrying on any *home financing* which is connected to *regulated mortgage contracts* or any *home finance administration* that it administers on its balance sheet which is connected to *regulated mortgage contracts*, the amount applied to a *firm* under ■ MIPRU 4.2.23 R; or
  - (b) in the case of a *firm* carrying on *home finance administration* with all the *home finance transactions* that it administers off balance sheet, the amount applied to a *firm* under ■ MIPRU 4.2.19 R
- (2) If the *firm* holds *client money* or other *client assets* in relation to its *home finance mediation activity*, the capital resources requirement is:

- (a) the amount calculated under (1); plus
- (b) the amount which is applied to a *firm* carrying on *insurance distribution activity* or *home finance mediation activity* (and no other *regulated activity*) that holds *client money* or other *client assets* in relation to these activities (see ■ MIPRU 4.2.11R (2)).

#### Capital resources requirement: other combinations of activities

4.2.22

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The capital resources requirement for a *firm* carrying on any combination of *regulated activities* which is not set out in ■ MIPRU 4.2.10 R to ■ MIPRU 4.2.21 R and ■ MIPRU 4.2.23 R is:

- (1) if the combination of *regulated activities* includes carrying on any *home financing* connected to *regulated mortgage contracts* or *home finance administration* connected to *regulated mortgage contracts*, the sum of the amounts which are applied to a *firm* under:
  - (a) ■ MIPRU 4.2.20R (1); and
  - (b) ■ MIPRU 4.2.23 R; or
- (2) in all other cases, the sum of the amounts which are applied to a *firm* under:
  - (a) ■ MIPRU 4.2.20R (1); and
  - (b) ■ MIPRU 4.2.12 R.

#### Capital resources requirement: home financing and home finance administration connected to regulated mortgage contracts

4.2.23

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The *capital resources requirement* for a *firm* carrying on any *home financing* which is connected to *regulated mortgage contracts*, or *home financing* and *home finance administration* which is connected to *regulated mortgage contracts* (and no other *regulated activity*), is the higher of:

- (1) £100,000; and
- (2) the sum of:
  - (a) the *credit risk capital requirement* calculated in accordance with ■ MIPRU 4.2A; and
  - (b) 1% of:
    - (i) its total assets plus total undrawn commitments and unreleased amounts under the *home reversion plan*; less
    - (ii) intangible assets (see Note 1 in the table in ■ MIPRU 4.4.4 R) plus loans, *securitisation positions* and *fund positions* subject to ■ MIPRU 4.2A.4 R.