General Prudential sourcebook
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1.1 Application

1.1.1 There is no overall application statement for GENPRU. Each chapter or section has its own application statement.

1.1.2 Broadly speaking however, GENPRU applies (except as provided in GENPRU 1.1.2-AAG) to:

(1) [deleted]

(2) [deleted]

(3) [deleted]

(4) a BIPRU firm; and

(5) groups containing such firms.

1.1.2-AA GENPRU 3 (Cross sector groups) applies to:

(1) an IFPRU investment firm;

(2) an insurer that is a “UK Solvency II firm“ as defined in the PRA Rulebook: Glossary; and

(3) a group containing both the firms in (1) and (2).

1.1.2-A

1.1.2-B GENPRU applies to a collective portfolio management investment firm that is a BIPRU firm in parallel with IPRU-INV-11 (see IPRU-INV-link-11.6).

1.1.2A A firm should refer to GEN 2.2.13A R (cross-references in the Handbook) and GEN 2.2.23 R to GEN 2.2.25 G (cutover: application of provisions made by both the FCA and the PRA) when applying the rules and guidance in GENPRU.

1.1.2B As the FCA does not have the power to impose prudential rules and guidance on PRA-authorised persons, references to PRA-authorised persons
or PRA rules that are included in FCA GENPRU provisions will not be relevant in the FCA’s application of that provision, unless otherwise stated.

Scope

1.1.3 GENPRU applies to a firm in relation to the whole of its business, except where a particular provision provides for a narrower scope.
1.2 Adequacy of financial resources

Application

1.2.1 R This section applies to a BIPRU firm.

(3) [deleted]

1.2.1A R [deleted]
The guidance in this section is drafted with respect to a firm to which this section and the other provisions of GENPRU and BIPRU (except ■ BIPRU 12) referred to in this section apply in full.

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 collective portfolio management investment firm, GENPRU 1.2.11 G means that this section also applies to its activities in relation to the management of AIFs and/or UCITS.

Purpose

Adequate financial resources and adequate systems and controls are necessary for the effective management of prudential risks. This section therefore has requirements relating to both of these topics.

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.

In the case of a BIPRU firm this section implements the third paragraph of article 95(2) of the UK CRR applying requirements that correspond to Article 34 of the Capital Adequacy Directive so far as that Article applies Article 123 of the Banking Consolidation Directive.
This section also has rules requiring a firm to identify and assess risks to its being able to meet its liabilities as they fall due, how it intends to deal with those risks, and the amount and nature of financial resources that the firm considers necessary. GENPRU 1.2.60 R provides that a firm should document that assessment. The FCA will review that assessment as part of its own assessment of the adequacy of a firm’s capital under its supervisory review and evaluation process (SREP). When forming a view of any individual capital guidance to be given to the firm, the appropriate regulator will also review the regulator’s risk assessment and any other issues arising from day-to-day supervision.

This section also has rules requiring a firm to carry out appropriate stress tests and scenario analyses for the risks it has previously identified and to establish the amount of financial resources needed in each of the circumstances and events considered in carrying out the stress tests and scenario analyses. In the case of a BIPRU firm, the FCA will consider as part of its SREP whether the BIPRU firm should hold a capital planning buffer and, in such a case, the amount and quality of that buffer. The capital planning buffer is an amount separate, though related to, the individual capital guidance, insofar as its purpose is to ensure that a BIPRU firm is able to continue to meet the overall financial adequacy rule throughout the relevant capital planning period in the face of adverse circumstances, after allowing for realistic management actions. Therefore, when forming its view on a BIPRU firm’s capital planning buffer, the FCA will take into account the assessment made in relation to the firm’s ICG.

The basic requirements in this section are drafted to apply to a firm on a solo basis. This section then goes on to describe when its requirements do and do not apply on a solo basis and on a consolidated basis (see GENPRU 1.2.45 R to GENPRU 1.2.47 R and GENPRU 1.2.57 R to GENPRU 1.2.58 R). It also sets out some details about how the solo requirements are adjusted when they are applied on a consolidated basis (see GENPRU 1.2.48 R to GENPRU 1.2.56 G and GENPRU 1.2.29 G).

Outline of other related provisions

1.2.18 GENPRU 2.1 sets out the minimum capital resources requirements for a firm.
GENPRU 2.2 sets out how capital resources are defined and measured for the purpose of meeting the requirements of GENPRU 2.1.

1.2.19
(1) BIPRU 2.2 (Internal capital adequacy standards) sets out detailed guidance on how a firm should carry out the assessment referred to in GENPRU 1.2.15 G. The more thorough, objective, and prudent a firm’s assessment is, and can be demonstrated as being, the more reliance the FCA will be able to place on the results of that assessment.

(2) BIPRU 2.2 also has information on how the FCA will review and respond to the assessments referred to in GENPRU 1.2.15G and GENPRU 1.2.16 G. In particular they deal with the giving of individual capital guidance to a firm, which is guidance about the amount and quality of capital resources that the FCA thinks a
Requirement to have adequate financial resources

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

1.2.26A ■ BIPRU 12 contains rules and guidance in relation to the adequacy of a BIPRU firm’s liquidity resources. Consistent with ■ GENPRU 1.2.2A R, 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.

1.2.27 G The liabilities referred to in the overall financial adequacy rule include a firm’s contingent and prospective liabilities. They exclude liabilities that might arise from transactions that a firm has not entered into and which it could avoid, for example, by taking realistic management actions such as...
ceasing to transact new business after a suitable period of time has elapsed. They include liabilities or costs that arise both in scenarios where the firm is a going concern and those where the firm ceases to be a going concern. They also include claims that could be made against a firm, which ought to be paid in accordance with fair treatment of customers, even if such claims could not be legally enforced.

1.2.28 A firm should therefore make its assessment of adequate financial resources on realistic valuation bases for assets and liabilities taking into account the actual amounts and timing of cash flows under realistic adverse projections.

1.2.29 Risks may be addressed through holding capital to absorb losses that unexpectedly materialise. The ability to pay liabilities as they fall due also requires liquidity. Therefore, in assessing the adequacy of a firm’s financial resources, both capital and liquidity needs should be considered. A firm should also consider the quality of its financial resources such as the loss-absorbency of different types of capital and the time required to liquidate different types of asset.

**Systems, strategies, processes and reviews**

1.2.30 A firm must have in place sound, effective and complete processes, strategies and systems:

1. to assess and maintain on an ongoing basis the amounts, types and distribution of financial resources, capital resources and internal capital that it considers adequate to cover:
   1. the nature and level of the risks to which it is or might be exposed;
   2. the risk in the overall financial adequacy rule; and
   3. the risk that the firm might not be able to meet its CRR in the future; and
(2) that enable it to identify and manage the major sources of risks 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 risk;
(b) market risk;
(c) liquidity risk;
(d) operational risk;
(e) insurance risk;
(f) concentration risk;
(g) residual risk;
(h) securitisation risk;
(i) business risk;
(j) interest rate risk (including, in the case of a BIPRU firm, interest rate risk in the non-trading book);
(k) pension obligation risk; and
(l) group risk.

1.2.31  
(1) This rule defines some of the terms used in the overall Pillar 2 rule.

(2) Residual risk means the risk that credit risk mitigation techniques used by the firm prove less effective than expected.

(3) Securitisation risk includes the risk that the capital resources 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.

(4) Business risk means any risk to a firm arising from changes in its business, including the risk that the firm may not be able to carry out its business plan and its desired strategy. It also includes risks arising from a firm's remuneration policy (see also the Remuneration Code which applies to BIPRU firms and the detailed application of which is set out in SYSC 19A.1).

(5) Pension obligation risk is 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). It also means the risk that the firm will make payments or other contribution 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.

1.2.32  
(1) This paragraph gives guidance on some of the terms used in the overall Pillar 2 rule.

(2) Insurance risk refers to the inherent uncertainties as to the occurrence, amount and timing of insurance liabilities.
1.2.33 R (1) This rule amplifies some of the obligations in the overall Pillar 2 rule.

(3) As part of its obligations in respect of market risk, a BIPRU 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.

1.2.34 G In the overall Pillar 2 rule, internal capital refers to the financial resources of a firm which it treats as being held against the risks listed in the overall Pillar 2 rule. The obligation in that rule to assess the distribution of such capital refers, in relation to a firm making an assessment on a solo basis, for example, to the need to take account of circumstances where part of a firm’s financial resources are held by a branch of that firm which are subject to restrictions on its ability to transfer that capital. An assessment of internal capital distribution might also take account of such of a firm’s financial resources as may be ring-fenced in the event of its insolvency.

1.2.35 R The processes, strategies and systems required by the overall Pillar 2 rule must be comprehensive and proportionate to the nature, scale and complexity of the firm’s activities.

1.2.36 R As part of its obligations under GENPRU 1.2.30R (1) (Main requirement relating to risk processes, strategies and systems), a firm must identify separately the amount of tier one capital, tier two capital, tier three capital, other capital eligible to form part of its capital resources and each category of capital (if any) that is not eligible to form part of its capital resources which it considers adequate for the purposes described in GENPRU 1.2.30R (1).
The processes and systems required by the overall Pillar 2 rule must:

1. include an assessment of how the firm intends to deal with each of the major sources of risk identified in accordance with GENPRU 1.2.30 R (2);

2. take into account the impact of diversification effects and how such effects are factored into the firm’s systems for measuring and managing risks; and

3. include an assessment of the firm-wide impact of the risks identified in accordance with GENPRU 1.2.30 R (2), to which end a firm must aggregate the risks across its various business lines and units, making appropriate allowance for the correlation between risks.

Certain risks such as systems and controls weaknesses may not be adequately addressed by, for example, holding additional capital and a more appropriate response would be to rectify the weakness. In such circumstances, the amount of financial resources required to address these risks might be zero. However, a firm should consider whether holding additional capital might be an appropriate response until the identified weaknesses are rectified. A firm, should, in accordance with GENPRU 1.2.60 R (Documentation of risk assessments), document the approaches taken to manage these risks.

A firm must:

1. carry out regularly the assessments required by the overall Pillar 2 rule; and

2. carry out regularly assessments of the processes, strategies and systems required by the overall Pillar 2 rule to ensure that they remain compliant with GENPRU 1.2.35 R.

A firm should carry out assessments of the sort described in the overall Pillar 2 rule and GENPRU 1.2.39 R at least annually, 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. The appropriateness of the internal process, and the degree of involvement of senior management in the process, will be taken into account by the FCA when reviewing a firm’s assessment as part of the FCA’s own assessment of the adequacy of a firm’s financial resources. The processes and systems should ensure that the assessment of the adequacy of a firm’s financial resources is reported to its senior management as often as is necessary.

### Stress and scenario tests

(1) As part of its obligation under the overall Pillar 2 rule, a firm must, for the major sources of risk identified in accordance with GENPRU 1.2.30 R (2), 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 and the CRR in 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.

(5) As part of its obligation under the overall Pillar 2 rule, a BIPRU firm must also incorporate and take into account any stress tests and scenario analyses that it is required to carry out under BIPRU. In particular, a BIPRU firm with an IRB permission must incorporate and take into account the stress test required to be carried out under BIPRU 4.3.40 R (2).

1.2.42A In order to comply with the general stress and scenario testing rule, 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 an individual portfolio as well as a firm-wide level.

1.2.42B A BIPRU firm with an IRB permission which has any material credit exposures excluded from its IRB models should also include these exposures in its stress and scenario testing to meet its obligations under the general stress and scenario testing rule. A BIPRU firm without an IRB permission, should conduct analyses to assess risks to the credit quality of its counterparties, including any protection sellers, considering both on and off-balance sheet exposures.
In carrying out the stress tests and scenario analyses required by GENPRU 1.2.42R (1), a firm should also consider any impact of the adverse circumstances on its capital resources. In particular, a firm should consider the capital resources gearing rules where its tier one capital is eroded by the event.

A firm should 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.

GENPRU 1.2.63 G to GENPRU 1.2.78 G provide additional guidance on stress testing and scenario analyses. In particular, GENPRU 1.2.73A G provides specific guidance on capital planning.

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 GENPRU 1.2.30R (2) (Main requirement relating to risk processes, strategies and systems) 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 add some stress tests and scenario analyses in order to reflect that concentration.

Application of this section on a solo and consolidated basis:

General

(1) GENPRU 1.2.45 R – GENPRU 1.2.56 G explain when the ICAAP rules apply on a solo basis and when they apply on a consolidated basis. This material also explains how the ICAAP rules are adjusted to apply on a consolidated basis.

(2) GENPRU 1.2.57 R – GENPRU 1.2.59 R provide that the overall financial adequacy rule always applies on a solo basis. They also explain when and how it applies on a consolidated basis.

Application of this section on a solo and consolidated basis:

Processes and tests

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 8.2.1 R (Basic consolidation rule for a UK consolidation group); or

(2) apply on a sub-consolidated basis under BIPRU 8.3.1 R (Basic consolidation rule for a non-UK sub-group).

The ICAAP rules apply on a solo basis:

(1) [deleted]
(2) to a BIPRU firm to which those rules do not apply on a consolidated or sub-consolidated basis as referred to in GENPRU 1.2.46 R (including a BIPRU investment firm with an investment firm consolidation waiver).

(3) [deleted]

1.2.47A  R

1.2.48  R

The requirements of the ICAAP rules as they apply on a consolidated basis must be carried out on the basis of the consolidated position of:

(1) [deleted]

(2) (if ■ BIPRU 8.2.1 R (Basic consolidation rule for a UK consolidation group) applies) the UK consolidation group of which the firm is a member; and

(3) (if ■ BIPRU 8.3.1 R (Basic consolidation rule for a non-UK sub-group) applies) the non-UK sub-group of which the firm is a member.

1.2.49  R

(1) In accordance with the general principles in GENPRU 1.2.48 R and BIPRU 8 (Group risk – consolidation), for the purpose of the ICAAP rules as they apply on a consolidated basis:

(a) the firm must ensure that the relevant group as defined in (2) have the processes, strategies and systems required by the overall Pillar 2 rule;

(b) the risks to which the overall Pillar 2 rule and the general stress and scenario testing rule refer are those risks as they apply to each member of the relevant group;

(c) the reference in the overall Pillar 2 rule to amounts and types of financial resources, capital resources 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 relevant group as defined in (2);

(d) other references to resources must be read as being to resources of the members of the relevant group as defined in (2);

(e) references to the CRR are to the consolidated capital requirements applicable to the relevant group under BIPRU 8 (Group risk - consolidation);

(f) the reference in the overall Pillar 2 rule to the distribution of resources must be read as including a reference to the distribution between members of the relevant group as defined in (2); and

(g) the reference in the overall Pillar 2 rule to the overall financial adequacy rule must be read as being to that rule as adjusted.
under GENPRU 1.2.59 R (Application of the overall financial adequacy rule on a consolidated basis).

(2) For the purpose of this rule the relevant group is the group referred to in GENPRU 1.2.48 R and the members of that group are those undertakings that are included in the scope of consolidation with respect to the UK consolidation group or, as the case may be, non-UK sub-group in question.

1.2.50 GENPRU 1.2.49 R means that non-financial members of the firm's group are excluded from the group assessment. Notwithstanding the scope of GENPRU 1.2.49 R, a firm should nevertheless take account of risks arising from the activities of those excluded members in its overall assessment of risk.

1.2.51 (1) This rule relates to the assessment of the amounts, types and distribution of financial resources, capital resources and internal capital (referred to in this rule as "resources") under the overall Pillar 2 rule as applied on a consolidated basis and to the assessment of diversification effects as referred to in GENPRU 1.2.37 R (2) as applied on a consolidated basis.

(2) A firm must be able to explain how it has aggregated the risks referred to in the overall Pillar 2 rule and the resources required by each member of the relevant group as referred to in GENPRU 1.2.49 R (2) and how it has taken into account any diversification benefits with respect to the group in question.

(3) 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 and scenario testing rule.

1.2.52 (1) A firm must allocate the total amount of financial resources, capital resources and internal capital identified as necessary under the overall Pillar 2 rule (as applied on a consolidated basis) between different parts of the relevant group (as defined in GENPRU 1.2.49 R). GENPRU 1.2.36 R (Identifying different tiers of capital) does not apply to this allocation.

(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 group is subject and the effect of any diversification benefits.

1.2.53 A firm must also allocate the total amount of financial resources, capital resources and internal capital (referred to in this rule as "resources") identified as necessary under the overall Pillar 2 rule as applied on a consolidated basis between each firm which is a member of the relevant group (as defined in GENPRU 1.2.49 R) on the following basis:

(1) the amount allocated to each firm must be decided on the basis of the principles in GENPRU 1.2.52 R (2); and
(2) if the process in (1) were carried out for each group member, the total so allocated would equal the total amount of resources identified as necessary under the overall Pillar 2 rule as applied on a consolidated basis.

1.2.54 A firm to which the ICAAP rules apply on a consolidated basis need not prepare a consolidated basis assessment if such an assessment has been prepared by another member of its group. Where that is the case, a firm may adopt such an assessment as its own. A firm nevertheless remains responsible for the assessment.

The purpose of GENPRU 1.2.51 R – GENPRU 1.2.53 R is to enable the FCA to assess the extent, if any, to which a firm's assessment, calculated on a consolidated basis, is lower than it would be if each separate legal entity were to assess the amount of capital it would require to mitigate its risks (to the same level of confidence) were it not part of a group subject to consolidated supervision under BIPRU 8 (Group risk - consolidation). The reason the FCA wishes to make this assessment is so that individual capital guidance which it gives is fair and comparable as between different firms and groups. Group diversification benefits which a firm might assert exist can be a material consideration in a capital adequacy assessment. Understanding the methods used to aggregate the different risks (for example, the correlation assumptions) is crucial to a proper evaluation of such benefits.

1.2.56 Whereas a single legal entity can generally use its capital to absorb losses wherever they arise, there are often practical and legal restrictions on the ability of a group to do so. For instance:

   (1) capital which is held by overseas regulated firms may not be capable of being remitted to a firm in the UK which has suffered a loss;

   (2) a firm which is insolvent or likely to become so may be obliged to look to the interests of its creditors first before transferring capital to other group companies; and

   (3) a parent company may have to balance the interests of its shareholders against the protection of the creditors of a subsidiary undertaking which is or might become insolvent and may, rationally, conclude that a subsidiary undertaking should be allowed to fail rather than provide capital to support it.

Application of this section on a solo and consolidated basis: Adequacy of resources

1.2.57 The overall financial adequacy rule applies to a firm on a solo basis whether or not it also applies to the firm on a consolidated basis.

1.2.58 The overall financial adequacy rule applies to a firm on a consolidated basis if the ICAAP rules apply to it on a consolidated basis.
(1) When the overall financial adequacy rule applies on a consolidated basis, the firm must ensure that at all times its group maintains overall financial resources, including capital resources 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 group cannot be met as they fall due.

(2) The group referred to in (1) is the relevant group as defined in GENPRU 1.2.49 R.

(3) The members of the group referred to in (1) must be identified in accordance with GENPRU 1.2.49 R.

Documentation of risk assessments

A firm must make a written record of the assessments required under this section. These assessments include assessments carried out on a consolidated basis and on a solo basis. In particular it must make a written record of:

(1) the major sources of risk identified in accordance with GENPRU 1.2.30R (Main requirement relating to risk processes, strategies and systems);

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

(3) 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 and scenario testing rule.

A firm must retain the records of its assessments referred to in GENPRU 1.2.60 R for at least three years.

Where a firm assesses the adequacy of its CRR in its particular circumstances in accordance with BIPRU 2.2 (Internal capital adequacy standards) as a basis for deciding what financial resources are adequate, it should include this in the documentation produced in accordance with GENPRU 1.2.60 R.

Additional guidance on stress tests and scenario analyses

The general stress and scenario testing rule requires a firm to carry out stress tests and scenario analyses as part of its obligations under the overall Pillar 2 rule. Both stress tests and scenario analyses are undertaken by a firm to further a better 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.

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.
1.2.65 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.

1.2.66 There are three broad purposes of stress testing and scenario analysis. Firstly, it can be used as a means of quantifying how much capital might be absorbed if an adverse event or events occurred. As such it represents a simple 'what if' approach to estimating exposure to risks. This might be a proportionate approach to risk management for an unsophisticated business. Secondly, 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. Thirdly, it can be used to explore the sensitivities in longer term business plans and how capital needs might change over time.

1.2.67 [deleted]

1.2.68 Subject to \textbf{GENPRU 1.2.76 G}, the purpose of stress tests and scenario analyses under the \textit{general stress and scenario testing rule} is to test the adequacy of overall financial resources. Scenarios need only be identified, and their impact assessed, in so far as this facilitates that purpose. In particular, the nature, depth and detail of the analysis depend, in part, upon the firm's capital strength and the robustness of its risk prevention and risk mitigation measures.

1.2.69 Both stress testing and scenario analyses are forward-looking analysis techniques, which seek to anticipate possible losses that might occur if an identified risk crystallises. In applying them, a firm should decide how far forward to look. This should depend upon:

(1) how quickly it would be able to identify events or changes in circumstances that might lead to a risk crystallising resulting in a loss; and

(2) after it has identified the event or circumstance, how quickly and effectively it could act to prevent or mitigate any loss resulting from the risk crystallising and to reduce exposure to any further adverse event or change in circumstance.

1.2.70 Where a firm is exposed to \textit{market risk}, 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 \textit{market risk} arising from the holding of investments, this will depend upon:

(1) the extent to which there is a regular, open and transparent market in those assets, which would allow fluctuations in the value of the investment to be more readily and quickly identified; and

(2) the extent to which the market in those assets is sufficiently liquid (and would remain liquid in the changed circumstances contemplated in the stress test or scenario analysis) to allow the firm, if needed, to
sell, hedge or otherwise mitigate the risks relating to its holding so as to prevent or reduce exposure to future price fluctuations. In devising stress tests and scenario analyses for market risk, a BIPRU firm should also take into account BIPRU 7.1.17 R to BIPRU 7.1.20 G.

1.2.71 In identifying scenarios, and assessing their impact, a firm should take into account, where material, how changes in circumstances might impact upon:

1. the nature, scale and mix of its future activities; and

2. 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).

1.2.72 In determining whether it would have adequate financial resources in the event of each identified realistic adverse scenario, a firm should:

1. only include financial resources that could reasonably be relied upon as being available in the circumstances of the identified scenario; and

2. take account of any legal or other restriction on the use of financial resources.

1.2.73 (1) [deleted]

(1A) [deleted]

(2) [deleted]

(3) [deleted]

(4) [deleted]

(5) [deleted]

Capital planning

1.2.73A (1) In identifying an appropriate range of adverse circumstances and events in accordance with GENPRU 1.2.42R (2):

(a) a firm will need to consider the cycles it is most exposed to and whether these are general economic cycles or specific to particular markets, sectors or industries;

(b) for the purposes of GENPRU 1.2.42R (2)(a), 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;

(c) the adverse scenarios considered should in general be acyclical and, accordingly, the scenario should not become more severe during a downturn and less severe during an upturn. However, the FCA does expect scenarios to be updated with relevant new economic data on a pragmatic basis to ensure that the scenario continues to be relevant; and
(d) the adverse scenarios considered should reflect a firm's risk tolerance of the adverse conditions through which it expects to remain a going concern.

(2) In making the estimate required by GENPRU 1.2.42R (3), a firm should project both its capital resources and its required capital resources over a time horizon of 3 to 5 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 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 GENPRU 1.2.37 R.

(3) 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 GENPRU 1.2.30R (2);
   (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.

(4) A firm should identify any realistic management actions intended to maintain or restore its 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. In order to assess whether prospective management actions in a stress scenario would be realistic and to determine which actions the firm would and could take, the firm should take into account any preconditions that might affect the value of management actions as risk mitigants and analyse the difference between the estimates in (3)(c) and (3)(e) 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.

(5) The firm should document its stress testing and scenario analysis policies and procedures, as well as the results of its tests in accordance with GENPRU 1.2.60 R. These records should be included within the firm’s ICAAP submission document.
(6) The FCA will review the firm’s records referred to in (5) as part of its SREP. The purpose of examining these is to enable the FCA to judge whether a firm will be able to continue to meet its CRR and the overall financial adequacy rule throughout the projection period.

(7) If, after taking account of realistic management actions, 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 CRR or less than those needed to continue to meet the overall financial adequacy rule over the projection period, the FCA may require the firm to set out additional countervailing measures and off-setting actions to reduce such difference or to restore the firm’s capital adequacy after the stress event.

(8) The firm’s senior management or governing body should 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 actioning the results of the stress tests.

(9) [deleted]

1.2.73B G The FCA may formulate macroeconomic and financial market scenarios which a firm may use as an additional input to its ICAAP submission. In addition, the FCA may also ask a firm to apply specific scenarios directly in its ICAAP submission.

1.2.73C G [deleted]

1.2.74 G A firm may consider scenarios in which expected future profits will provide capital reserves against future risks. However, it would only be appropriate to take into account profits that can be foreseen with a reasonable degree of certainty as arising before the risk against which they are being held could possibly arise. In estimating future reserves, a firm should deduct future dividend payment estimates from projections of future profits.

1.2.75 G (1) [deleted]

(2) Stress and scenario analyses should, in the first instance, be aligned with the risk appetite of the firm, as well as the nature, scale and complexity of its business and of the risks that it bears. 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 is based.

(3) [deleted]

(4) In identifying adverse circumstances and events in accordance with GENPRU 1.2.42R (2), 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 ruin scenarios for the purpose of meeting the firm’s obligations under...
1.2.76 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 risk covered by the stress or scenario test actually materialises. Such measures might be a contingency plan or might be more concrete risk mitigation steps.

1.2.77 Additional guidance on stress tests and scenario analyses for the assessment of capital resources is available in BIPRU 2.2 (Internal capital adequacy standards).

1.2.78 [deleted]

1.2.78A BIPRU 12 sets out the main Handbook provisions in relation to liquidity risk for a BIPRU firm.

Pension obligation risk

1.2.79 GENPRU 1.2.80 G to GENPRU 1.2.86 G contain guidance on the assessment required by GENPRU 1.2.30R (2)(k) for a firm exposed to pension obligation risk as defined in GENPRU 1.2.31R (5).

1.2.80 The pension scheme itself (i.e. the scheme's assets and liabilities) is not the focus of the risk assessment but rather the firm's obligations towards the pension scheme. A firm should include in its estimate of financial resources...
both its expected obligations to the pension scheme and any increase in obligations that may arise in a stress scenario.

1.2.81 If a firm has a current funding obligation in excess of normal contributions or there is a risk that such a funding obligation will arise then, when calculating available capital resources, it should reverse out any accounting deficit and replace this in its capital adequacy assessment with its best estimate, calculated in discussion with the scheme’s actuaries or trustees, of the cash that will need to be paid into the scheme in addition to normal contributions over the foreseeable future. This may differ from the approach taken in assessing pension scheme risks for the purposes of calculating resources to meet the CRR, where a firm may not need to consider funding obligations beyond the next five years.

1.2.82 A firm should also assess the risks that may increase its current funding obligations towards the pension scheme and that might lead to the firm not being able to pay its other liabilities as they fall due.

1.2.83 A firm may wish to consider the following scenarios:

(1) one in which the firm gets into difficulties with an effect on its ability to fund the pension scheme; and

(2) one in which the pension scheme position deteriorates (for example, because investment returns fall below expected returns or because of increases in life expectancy) with an effect on the firm’s funding obligations; taking into account the management actions the firm could and would take.

1.2.83A A firm is expected to determine where the scope of any stress test impacts upon its pension obligation risk and estimate how the relevant measure of pension obligation risk will change in the scenario in question. For example, in carrying out stress tests under GENPRU 1.2.42 R a firm must consider how a stress scenario, such as an economic recession, would impact on the firm’s current obligations towards its pension scheme and any potential increase in those obligations. Risks such as interest rate risk or reduced investment returns may have a direct impact on a firm’s financial position as well as an indirect impact resulting from an increase in the firm’s pension scheme obligations. Both effects should be taken into account in a firm’s estimate of financial resources under GENPRU 1.2.30 R.

1.2.84 Scenarios in which a firm’s employees suffer a loss or members of a pension scheme suffer a loss do not necessarily affect the firm’s ability to pay its liabilities as they fall due.

1.2.85 A firm should consider issues such as:

(1) the extent to which trustees of the pension scheme or a pension regulator (such as the one created under the Pensions Act 2004) can compel a certain level of contributions or a one-off payment in adverse financial situations or in order to meet the minimum legal...
requirements under the scheme’s trust deed and rules or under the applicable laws relating to the pension scheme;

(2) whether the valuation bases used to set pension scheme contribution rates are consistent with the firm’s current business plans and anticipated changes in the workforce; and

(3) which valuation basis is appropriate given the expected investment return on scheme assets and actions the firm can take if those returns do not materialise.

1.2.86 A firm should carry out analyses only to a degree of sophistication and complexity which is commensurate with the materiality of its pension risks.

Group risk (BIPRU firm only)

1.2.87 ■ GENPRU 1.2.88G to ■ GENPRU 1.2.91G contain additional guidance on the assessment required by ■ GENPRU 1.2.30R (2)(l) (Group risk).

1.2.88 A firm should include in the written record referred to in ■ GENPRU 1.2.60 R a description of the broad business strategy of the UK consolidation group or the non-UK sub-group of which it is a member, the group’s view of its principal risks and its approach to measuring, managing and controlling the risks. This description should include the role of stress testing, scenario analysis and contingency planning in managing risk at the solo and consolidated level.

1.2.89 A firm should satisfy itself that the systems (including IT) of the UK consolidation group or the non-UK sub-group of which it is a member are sufficiently sound to support the effective management and, where applicable, the quantification of the risks that could affect the UK consolidation group or the non-UK sub-group, as the case may be.

1.2.90 In performing stress tests and scenario analyses, a firm should take into account the risk that its group may have to bring back on to its consolidated balance sheet the assets and liabilities of off-balance sheet entities as a result of reputational contagion, notwithstanding the appearance of legal risk transfer.

1.2.91 A firm should carry out stress tests and scenario analyses to a degree of sophistication which is commensurate with the complexity of its group and the nature of its group risk.
1.3 Valuation

Application

1.3.1 (1) [deleted]

(2) This section of the Handbook applies to a BIPRU firm.

(3) [deleted]

1.3.1A (1) [deleted]

Purpose

1.3.2 This section sets out, for the purposes of GENPRU and BIPRU, rules and guidance as to how a firm should recognise and value assets, liabilities, exposures, equity and income statement items.

1.3.3 (1) This section corresponds to 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.

(2) [deleted]

General requirements: Accounting principles to be applied

1.3.4 Subject to GENPRU 1.3.9 R to GENPRU 1.3.10 R and GENPRU 1.3.36 R, except where a rule in GENPRU, BIPRU or INSIPRU provides for a different method of recognition or valuation, whenever a rule in GENPRU or BIPRU 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:

(1) [deleted]

(2) Financial Reporting Standards issued by the Financial Reporting Council;

(3) Statements of Recommended Practice, issued by industry or sectoral bodies recognised for this purpose by the Financial Reporting Council;

(4) [deleted]
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(5) UK-adopted international accounting standards;

(6) the Companies Act 1985 and

(7) the Companies Act 2006;

as applicable to the firm for the purpose of its external financial reporting (or as would be applicable if the firm was a company with its head office in the United Kingdom).

1.3.5 [G] Except where a rule in GENPRU or BIPRU makes a different provision, GENPRU 1.3.4 R applies whenever a rule in GENPRU or BIPRU refers to the value or amount of an asset, liability, exposure, equity or income statement item, including:

(1) whether, and when, to recognise or de-recognise an asset or liability;

(2) the amount at which to value an asset, liability, exposure, equity or income statement item; and

(3) which description to place on an asset, liability, exposure, equity or income statement item.

1.3.6 [G] In particular, unless an exception applies, GENPRU 1.3.4 R should be applied for the purposes of GENPRU or BIPRU to determine how to account for:

(1) netting of amounts due to or from the firm;

(2) the securitisation of assets and liabilities (see also GENPRU 1.3.7 G);

(3) leased tangible assets;

(4) assets transferred or received under a sale and repurchase or stock lending transaction; and

(5) assets transferred or received by way of initial or variation margin under a derivative or similar transaction.

General requirements: Adjustments to accounting values

1.3.9 [R] For the purposes of GENPRU or BIPRU, except where a rule in GENPRU or BIPRU provides for a different method of recognition or valuation:
(1) when a firm, upon initial recognition, designates its liabilities as at fair value through profit or loss, it must always adjust any value calculated in accordance with GENPRU 1.3.4 R by subtracting any unrealised gains or adding back in any unrealised losses which are not attributable to changes in a benchmark interest rate;

(2) in respect of a defined benefit occupational pension scheme:
   (a) a firm must derecognise any defined benefit asset;
   (b) a firm may substitute for a defined benefit liability the firm’s deficit reduction amount.

1.3.10 An election made under GENPRU 1.3.9R (2) must be applied consistently for the purposes of GENPRU or BIPRU in respect of any one financial year.

1.3.11 A firm should keep a record of and be ready to explain to its supervisory contacts in the appropriate regulator the reasons for any difference between the deficit reduction amount and any commitment the firm has made in any public document to provide funding in respect of a defined benefit occupational pension scheme.

1.3.12 The provisions of GENPRU 1.3.9 R to GENPRU 1.3.10 R and GENPRU 1.3.36 R apply only to the extent that the items referred to in those paragraphs would otherwise be recognised under the accounting requirements applicable to the firm. Some of those requirements may only be relevant to a firm subject to UK-adopted international accounting standards.

General requirements: Methods of valuation and systems and controls

1.3.13 (1) Except to the extent that GENPRU or BIPRU provide for another method of valuation, GENPRU 1.3.14 R to GENPRU 1.3.34 R (Marking to market, Marking to model, Independent price verification or Valuation adjustments) apply:
   (a) for the purposes set out in GENPRU 1.3.41 R;
   (b) for the purposes set out in GENPRU 1.3.39 R; and
   (c) to any balance sheet position measured at market value or fair value.

(2) A firm must establish and maintain systems and controls sufficient to provide prudent and reliable valuation estimates.

(3) Systems and controls under (2) must include at least the following elements:
   (a) documented policies and procedures for the process of valuation, including clearly defined responsibilities of the various areas involved in the determination of the valuation, sources of market information and review of their appropriateness, frequency of independent valuation, timing of closing prices, procedures for adjusting valuations, month-end and ad-hoc verification procedures, and, in the case of a BIPRU firm, guidelines for the
use of unobservable inputs reflecting the firm's assumptions of what market participants would use in pricing the position; and

(b) reporting lines for the department accountable for the valuation process that are:

(i) clear and independent of the front office; and

(ii) ultimately to a main board executive director.

General requirements: Marking to market

1.3.14 Wherever possible, a firm must use mark to market in order to measure the value of the investments and positions to which this rule applies under GENPRU 1.3.13 R and GENPRU 1.3.38 R to GENPRU 1.3.41 R. Marking to market is valuation (on at least a daily basis in the case of the trading book positions of a BIPRU firm) at readily available close out prices from independent sources.

1.3.15 For the purposes of GENPRU 1.3.14 R, examples of readily available close out prices include exchange prices, screen prices, or quotes from several independent reputable brokers.

1.3.16 (1) When marking to market, a firm must use the more prudent side of bid/offer unless the firm is a significant market maker in a particular position type and it can close out at the mid-market price.

(2) When calculating the current exposure value of a credit risk exposure for counterparty credit risk purposes:

(a) a firm must use the more prudent side of bid/offer or the mid-market price and the firm must be consistent in the basis it chooses; and

(b) where the difference between the more prudent side of bid/offer and the mid-market price is material, the firm must consider making adjustments.

General requirements: Marking to model

1.3.17 Where marking to market is not possible, a firm must (in the case of a BIPRU firm, conservatively) use mark to model in order to measure the value of the investments and positions to which this rule applies under GENPRU 1.3.13 R and GENPRU 1.3.38 R to GENPRU 1.3.41 R. Marking to model is any valuation which has to be benchmarked, extrapolated or otherwise calculated from a market input. GENPRU 1.3.18 R to GENPRU 1.3.25 R apply when marking to model.

1.3.18 When the model used is developed by the firm, that model must be:

(1) based on appropriate assumptions which have been assessed and challenged by suitably qualified parties independent of the development process;
A firm must ensure that its senior management are aware of the positions which are subject to mark to model and understand the materiality of the uncertainty this creates in the reporting of the performance of the business of the firm and the risks to which it is subject.

A firm must source market inputs in line with market prices so far as possible and assess the appropriateness of the market inputs for the position being valued and the parameters of the model on a frequent basis.

A firm must use generally accepted valuation methodologies for particular products where these are available.

A firm must establish formal change control procedures, hold a secure copy of the model, and periodically use that model to check valuations.

A firm must ensure that its risk management functions are aware of the weaknesses of the models used and how best to reflect those in the valuation output.

A firm must periodically review the model to determine the accuracy of its performance.

Examples of periodical review are assessing the continued appropriateness of the assumptions, analysis of profit and loss versus risk factors and comparison of actual close out values to model outputs.

General requirements: Independent price verification

In addition to marking to market or marking to model, a firm must perform independent price verification. This is the process by which market prices or model inputs are regularly verified for accuracy and independence.

For independent price verification, where independent pricing sources are not available or pricing sources are more subjective (for example, only one available broker quote), prudent measures such as valuation adjustments may be appropriate.

In the case of the trading book positions of a BIPRU firm, while daily marking to market may be performed by dealers, verification of market prices and model inputs must be performed by a unit independent of the dealing room, at least monthly (or, depending on the nature of the market/trading activity, more frequently).
General requirements: Valuation adjustments

1.3.29 R The recognition of any gains or losses arising from valuations subject to GENPRU 1.3.13 R and GENPRU 1.3.38 R to GENPRU 1.3.41 R must be recognised for the purpose of calculating capital resources in accordance with GENPRU 1.3.14 R to GENPRU 1.3.34 R (Marking to market, Marking to model, Independent price verification or Valuation adjustments). However if GENPRU or BIPRU provide for another treatment of such gains or losses, that other treatment must be applied.

1.3.30 R A firm must establish and maintain procedures for considering valuation adjustments. These procedures must be compliant with the requirements set out in GENPRU 1.3.33 R.

1.3.31 R A firm using third-party valuations, or marking to model, must consider whether valuation adjustments are necessary.

1.3.32 R A firm must consider the need for making adjustments for less liquid positions and, on an ongoing basis, review their continued appropriateness in accordance with the requirements set out in GENPRU 1.3.33 R. Less liquid positions could arise from both market events and institution-related situations e.g. concentration positions and/or stale positions.

1.3.33 R (1) This paragraph sets out the requirements referred to in GENPRU 1.3.30 R and GENPRU 1.3.32 R.

(2) A firm must consider the following adjustments: unearned credit spreads, close-out costs, operational risks, early termination, investing and funding costs, future administrative costs and, where appropriate, model risk.

(3) (a) In the case of a BIPRU firm, a firm must establish and maintain procedures for calculating adjustments to the current valuation of less liquid positions. Those adjustments must, where necessary, be in addition to any changes to the value of the position required for financial reporting purposes and must be designed to reflect the illiquidity of the position.

(b) A firm must consider several factors when determining whether a valuation adjustment is necessary for less liquid positions. These factors include the amount of time it would take to hedge out the position/risks within the position; the average and volatility of bid/offer spreads; the availability of market quotes (number and identity of market makers); the average and volatility of trading volumes; market concentrations; the ageing of positions; the extent to which valuation relies on marking to model and the impact of other model risks.
(4) With regard to complex products including, but not limited to, securitisation exposures and nth-to-default credit derivatives, a BIPRU firm must explicitly consider the need for valuation adjustments for model risk arising from using a valuation which may be incorrect or the risk from using unobservable calibration parameters in the valuation model.

1.3.34 If the result of making adjustments under GENPRU 1.3.29 R to GENPRU 1.3.33 R is a valuation which differs from the fair value determined in accordance with GENPRU 1.3.4 R, a firm must reconcile the two valuations.

1.3.35 Reconciliation differences under GENPRU 1.3.34 R should not be reflected in the valuations under GENPRU 1.3 but should be disclosed to the FCA in prudential returns. Firms which are subject to the reporting requirement under SUP 16.16 should disclose those reconciliation differences in the Prudent Valuation Return which they are required to submit to the FCA under SUP 16.16.4 R.

1.3.35A Specific requirements: BIPRU firms

1.3.36 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 1.3.4 R in addition to those required by GENPRU 1.3.9 R to GENPRU 1.3.10 R.

(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 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.

1.3.37 Provisions for equity instruments held in the available-for-sale category can be found in GENPRU 2.2.185 R.

1.3.38 Trading book and other fair-valued positions, and revaluations to GENPRU 1.3.40 R apply only to a BIPRU firm.
1.3.39 Both trading book positions and other fair-valued positions are subject to prudent valuation rules as specified in GENPRU 1.3.14 R to GENPRU 1.3.34 R (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.

1.3.40 Trading book positions must be re-valued at least daily.
1.4 Actions for damages

General insurance business: Community co-insurance operations

1.4.1 A contravention of the rules in GENPRU does not give rise to a right of action by a private person under section 138D of the Act (and each of those rules is specified under section 138D(3) of the Act as a provision giving rise to no such right of action).
Chapter 2

Capital
2.1 Calculation of capital resources requirements

Application

2.1.1 This section applies to a BIPRU firm.

Purpose

2.1.6 Principle 4 requires a firm to maintain adequate financial resources. GENPRU 2 sets out provisions that deal specifically with the adequacy of that part of a firm's financial resources that consists of capital resources. The
adequacy of a firm's capital resources needs to be assessed both by that firm and the appropriate regulator. Through its rules, the FCA sets minimum capital resources requirements for firms. It also reviews a firm's own assessment of its capital needs, and the processes and systems by which that assessment is made, in order to see if the minimum capital resources requirements are appropriate (see GENPRU 1.2 (Adequacy of financial resources) and BIPRU 2.2 (Internal capital adequacy standards)).

2.1.7 This section sets capital resources requirements for a firm. GENPRU 2.2 (Capital resources) sets out how, for the purpose of meeting capital resources requirements, the amounts or values of capital, assets and liabilities are to be determined. More detailed rules relating to capital, assets and liabilities are set out in GENPRU 1.3 (Valuation) and, for a BIPRU firm, BIPRU.

2.1.8 (1) [deleted]

(2) This section also implements the third paragraph of article 95(2) of the UK CRR applying requirements that correspond to the 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 corresponds (in part) to article 75 of the Banking Consolidation Directive and Articles 5, 9, 10 and 18 of the Capital Adequacy Directive.

(3) [deleted]

2.1.8A

Monitoring requirements

2.1.9 A firm must at all times monitor whether it is complying with the main BIPRU firm Pillar 1 rules and be able to demonstrate that it knows at all times whether it is complying with those rules.

2.1.10 For the purposes of GENPRU 2.1.9 R, a firm should have systems in place to enable it to be certain whether it has adequate capital resources to comply with the main BIPRU firm Pillar 1 rules at all times. This does not necessarily mean that a firm needs to measure the precise amount of its capital resources and its CRR on a daily basis. A firm should, however, be able to demonstrate the adequacy of its capital resources at any particular time if asked to do so by the FCA.

2.1.11 A firm must notify the FCA immediately of any breach, or expected breach, of the main BIPRU firm Pillar 1 rules.

Additional capital requirements

2.1.12 The FCA may impose a higher capital requirement than the minimum requirement set out in this section as part of the firm's Part 4A permission (see GENPRU 1.2 (Adequacy of financial resources) and BIPRU 2.2 (Internal capital adequacy standards)).
Main requirement: BIPRU firms

2.1.40  A BIPRU firm must maintain at all times capital resources equal to or in excess of the amount specified in the table in GENPRU 2.1.45 R (Calculation of the variable capital requirement for a BIPRU firm).

2.1.41  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 2.1.48 R).

2.1.42  At the time that it first becomes a BIPRU firm, a firm must hold initial capital of not less than the base capital resources requirement applicable to that firm.

2.1.43  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 2.2.60 R 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.

2.1.44  The base capital resources requirement and the variable capital requirement in GENPRU 2.1.40 R are together called the capital resources requirement (CRR) in the case of a BIPRU firm.

Calculation of the variable capital requirement for a BIPRU firm

2.1.45  This table belongs to GENPRU 2.1.40 R

<table>
<thead>
<tr>
<th>Firm category</th>
<th>Capital requirement</th>
</tr>
</thead>
</table>
| BIPRU firm (including collective portfolio management 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. |
Adjustment of the variable capital requirement calculation for collective portfolio management investment firms

When a collective portfolio management investment firm calculates the credit risk capital requirement and the market risk capital requirement for the purpose of calculating the variable capital requirement under GENPRU 2.1.40 R it must do so only in respect of designated investment business. For this purpose managing an AlF or managing a UK UCITS is excluded from designated investment business.

Calculation of the base capital resources requirement for a BIPRU firm

The amount of a BIPRU firm’s base capital resources requirement is set out in the table in GENPRU 2.1.48 R.

Table: Base capital resources requirement for a BIPRU firm

<table>
<thead>
<tr>
<th>Firm category</th>
<th>Amount: Currency equivalent of</th>
</tr>
</thead>
<tbody>
<tr>
<td>BIPRU firm (but not a collective portfolio management investment firm)</td>
<td>€50,000</td>
</tr>
</tbody>
</table>

A collective portfolio management investment firm is required to maintain base own funds requirement of €125,000 (in line with IPRU-INV -link- 11.3.1R(1)).

Definition of BIPRU firm

In summary, a BIPRU firm:

1) does not provide the ancillary service of safekeeping and administration of financial instruments for the account of clients, including custodianship and related services such as cash/collateral management, and is not authorised to do so;

2) is not authorised to provide the following investment services:
   a) to deal in any financial instruments for its own account;
   b) to underwrite issues of financial instruments on a firm commitment basis;
   c) to place financial instruments without a firm commitment basis; and
   d) to operate a multilateral trading facility;

3) is authorised to provide one or more of the following investment services:
   a) the execution of investors’ orders for financial instruments; or
   b) the management of individual portfolios of investments in financial instruments;

4) may be authorised to provide one or more of the following investment services:
(a) reception and transmission of investors’ orders for financial instruments; or
(b) investment advice; and

(5) does not hold clients’ money and/or securities and 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).

Calculation of the credit risk capital requirement (BIPRU firm only)

2.1.51 A BIPRU firm must calculate its credit risk capital requirement as the sum of:

(1) the credit risk capital component; and
(2) the counterparty risk capital component.
(3) [deleted]

Calculation of the market risk capital requirement (BIPRU firm only)

2.1.52 (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 7.1.9 R - BIPRU 7.1.13 R (Instruments for which no PRR treatment has been specified) must be allocated between the PRR charges in (1) in the most appropriate manner.

Calculation of the fixed overheads requirement

2.1.53 A BIPRU firm must calculate a fixed overheads requirement, an amount that is equal to one quarter of the firm’s relevant fixed expenditure calculated in accordance with GENPRU 2.1.54 R.

2.1.54 For the purpose of GENPRU 2.1.53 R, and subject to GENPRU 2.1.55 R to GENPRU 2.1.57 R, a BIPRU firm’s relevant fixed expenditure is the amount described as total expenditure in its most recent audited annual report and...
accounts, less the following items (if they are included within such expenditure):

1. staff bonuses, except to the extent that they are guaranteed;
2. employees' and directors' shares in profits, except to the extent that they are guaranteed;
3. other appropriations of profits;
4. shared commission and fees payable which are directly related to commission and fees receivable, which are included within total revenue;
5. interest charges in respect of borrowings made to finance the acquisition of the firm's readily realisable investments;
6. interest paid to customers on client money;
7. interest paid to counterparties;
8. fees, brokerage and other charges paid to clearing houses, exchanges and intermediate brokers for the purposes of executing, registering or clearing transactions;
9. foreign exchange losses; and
10. other variable expenditure.

2.155 The relevant fixed expenditure of a firm in the following circumstances is:

1. where its most recent audited annual report and accounts do not represent a twelve month period, an amount calculated in accordance with GENPRU 2.1.54 R, pro-rated so as to produce an equivalent annual amount; and
2. where it has not completed twelve months' trading, an amount based on forecast expenditure included in the budget for the first twelve months' trading, as submitted with its application for authorisation.

2.156 A firm must adjust its relevant fixed expenditure calculation so far as necessary if and to the extent that since the date covered by the most recent audited annual report and accounts or (if GENPRU 2.1.55R (2) applies) since the budget was prepared:

1. its level of fixed expenditure changes materially; or
2. its regulated activities comprised within its permission change.

2.157 If a firm has a material proportion of its expenditure incurred on its behalf by third parties and such expenditure is not fully recharged to that firm then the firm must adjust its relevant fixed expenditure calculation by adding back in the whole of the difference between the amount of the expenditure and the amount recharged.
For the purpose of GENPRU 2.1.57 R, the FCA would consider as material 10% of a firm’s expenditure incurred on its behalf by third parties.

For the purpose of GENPRU 2.1.54 R to 2.1.57 R, fixed expenditure is expenditure which is inelastic relative to fluctuations in a firm’s levels of business. Fixed expenditure is likely to include most salaries and staff costs, office rent, payment for the rent or lease of office equipment, and insurance premiums. It may be viewed as the amount of funds which a firm would require to enable it to cease business in an orderly manner, should the need arise. This is not an exhaustive list of such expenditure and a firm will itself need to identify (taking appropriate advice where necessary) which costs amount to fixed expenditure.

Calculation of base capital resources requirement for banks authorised before 1993

(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 2.1.62R (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.

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.
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 2.1.60R (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 2.1.60R (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.
2.2 Capital resources

Application

2.2.1 This section applies to a BIPRU firm.

Purpose

2.2.2 GENPRU 2.1 (Calculation of capital resources requirement) sets out minimum capital resources requirements for a firm. This section (GENPRU 2.2) sets out how, for the purpose of these requirements, capital resources are defined and measured.

2.2.4 This section also implements minimum standards for the composition of capital resources required to be held by a BIPRU firm. In particular pursuant to the third paragraph of article 95(2) of the UK CRR, it applies requirements that correspond to Articles 56 – 61, Articles 63 – 64, Article 66 and Articles 120 – 122 of the Banking Consolidation Directive 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.
Contents guide

2.2.5 The table in GENPRU 2.2.6 G sets out where the main topics in this section can be found.

Table: Arrangement of GENPRU 2.2

This table belongs to GENPRU 2.2.5 G

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<th>Location of text</th>
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<td>BIPRU firms that only have simple types of capital resources (simple capital issuers)</td>
<td>GENPRU 2.2.7 G</td>
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<td>Principles underlying the definition of capital resources</td>
<td>GENPRU 2.2.8 G</td>
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<td>Which method of calculating capital resources applies to which type of firm</td>
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<td>Use of higher tier capital in lower tiers</td>
<td>GENPRU 2.2.25 R to GENPRU 2.2.28 R</td>
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<td>Calculation of capital resources for BIPRU firms</td>
<td>GENPRU 2.2.20 R to GENPRU 2.2.21 G; GENPRU 2 Annex 4 to GENPRU 2 Annex 6</td>
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<td>Limits on the use of different forms of capital for BIPRU firms (certain types of capital resources cannot be used for certain purposes)</td>
<td>GENPRU 2.2.44 R to GENPRU 2.2.45 R; GENPRU 2.2.47 R to GENPRU 2.2.48 R</td>
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<td>GENPRU 2.2.29 R to GENPRU 2.2.31 G; GENPRU 2.2.46 R; GENPRU 2.2.50 R</td>
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<td>Example of how the capital resources calculation for BIPRU firms works</td>
<td>GENPRU 2.2.51 G to GENPRU 2.2.59 G</td>
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<td>GENPRU 2.2.61A R to GENPRU 2.2.61H G</td>
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<td>GENPRU 2.2.9 G to GENPRU 2.2.10 G; GENPRU 2.2.62 R to GENPRU 2.2.69 G; GENPRU 2.2.80 R to GENPRU 2.2.82 G</td>
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<tr>
<td>Tier one capital: payment of coupons (BIPRU firm only)</td>
<td>GENPRU 2.2.69A R to GENPRU 2.2.69F G</td>
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<td>General conditions for eligibility of capital instruments as core tier one capital (BIPRU firm only)</td>
<td>GENPRU 2.2.83A R to GENPRU 2.2.83D G; GENPRU 2.2.84A G</td>
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<td>Core tier one capital: exception to eligibility criteria (building societies only)</td>
<td>GENPRU 2.2.83E R to GENPRU 2.2.83H G</td>
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<tr>
<td>Topic</td>
<td>Location of text</td>
</tr>
<tr>
<td>-------</td>
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</tr>
<tr>
<td>Core tier one capital: profit and loss account and other reserves: material applicable to all firms</td>
<td>GENPRU 2.2.85 R; GENPRU 2.2.87 R to GENPRU 2.2.89 G; GENPRU 2.2.91 G</td>
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<tr>
<td>Core tier one capital: profit and loss account and other reserves: material specific to BIPRU firms</td>
<td>GENPRU 2.2.86 R; GENPRU 2.2.90 R; GENPRU 2.2.92 G</td>
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<td>Core tier one capital: provisions relating to partnerships and limited liability partnerships</td>
<td>GENPRU 2.2.93 R to GENPRU 2.2.100 R</td>
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<tr>
<td>Core tier one capital: share premium account</td>
<td>GENPRU 2.2.101 R</td>
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<td>Core tier one capital: externally verified interim net profits</td>
<td>GENPRU 2.2.102 R to GENPRU 2.2.103 G</td>
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<td>Hybrid capital (excluding issues through SPVs) (BIPRU firm only)</td>
<td>GENPRU 2.2.115A R to GENPRU 2.2.119 G</td>
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<td>Hybrid capital (issues through SPVs) (BIPRU firm only)</td>
<td>GENPRU 2.2.123 R to GENPRU 2.2.137 R</td>
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<td>Tier one capital: conversion ratio</td>
<td>GENPRU 2.2.138 R to GENPRU 2.2.144 G</td>
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<td>Tier one capital: requirement to have sufficient unissued stock</td>
<td>GENPRU 2.2.145 R</td>
</tr>
<tr>
<td>Deductions from tier one capital resources</td>
<td>GENPRU 2.2.155 R to GENPRU 2.2.156 G</td>
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<tr>
<td>Tier two capital</td>
<td>GENPRU 2.2.11 G; GENPRU 2.2.157 G to GENPRU 2.2.197 G</td>
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<tr>
<td>Deductions from tier one capital resources and tier two capital resources</td>
<td>GENPRU 2.2.208 R to GENPRU 2.2.216 G; GENPRU 2.2.217 R to GENPRU 2.2.220 R; GENPRU 2.2.236 R to GENPRU 2.2.240 G</td>
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<tr>
<td>Tier three capital</td>
<td>GENPRU 2.2.12 G; GENPRU 2.2.241 R to GENPRU 2.2.249 R</td>
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<tr>
<td>Deductions from total capital resources</td>
<td>GENPRU 2.2.14 G to GENPRU 2.2.16 G; GENPRU 2.2.259 R to GENPRU 2.2.62 R</td>
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<tr>
<td>The effect of swaps</td>
<td>GENPRU 2.2.198 R to GENPRU 2.2.201 R</td>
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<tr>
<td>Step-ups (tier one capital and tier two capital)</td>
<td>GENPRU 2.2.146 R to GENPRU 2.2.154 G</td>
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<td>Redemption of tier one instruments</td>
<td>GENPRU 2.2.64R (3); GENPRU 2.2.70 R to GENPRU 2.2.79 G</td>
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<tr>
<td>Purchases of tier one instruments: BIPRU firm only</td>
<td>GENPRU 2.2.79A R to GENPRU 2.2.79H G; GENPRU 2.2.79L G</td>
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<td>GENPRU 2.2.172 R to GENPRU 2.2.174 R; GENPRU 2.2.177 R to GENPRU 2.2.178 R (upper tier two instruments); GENPRU 2.2.194 R to GENPRU 2.2.197 G (lower tier two instruments)</td>
</tr>
<tr>
<td>Non-standard capital instruments</td>
<td>GENPRU 2.2.13 G</td>
</tr>
<tr>
<td>Standard form documentation for subordinated debt</td>
<td>GENPRU 2.2.164 G</td>
</tr>
<tr>
<td>Public sector guarantees</td>
<td>GENPRU 2.2.276 R</td>
</tr>
</tbody>
</table>
2.2 Simple capital issuers

Parts of this section are irrelevant to a BIPRU firm whose capital resources consist of straightforward capital instruments.

2.2.7

Principles underlying the definition of capital resources

The FCA has divided its definition of capital into categories, or tiers, reflecting differences in the extent to which the capital instruments concerned meet the purpose and conform to the characteristics of capital listed in GENPRU 2.2.9. The FCA generally prefers a firm to hold higher quality capital that meets the characteristics of permanency and loss absorbency that are features of tier one capital. Capital instruments falling into core tier one capital can be included in a firm’s regulatory capital without limit. Typically, other forms of capital are either subject to limits (see the capital resources gearing rules) or, in the case of some specialist types of capital, may only be included with the express consent of the FCA (which takes the form of a waiver under section 138A of the Act). Details of the individual components of capital are set out in the capital resources table.

2.2.8

Tier one capital

Tier one capital typically has the following characteristics:

1. it is able to absorb losses;
2. it is permanent or (in the case of a BIPRU firm) available when required;
3. it ranks for repayment upon winding up, administration or similar procedure after all other debts and liabilities; and
4. it has no fixed costs, that is, there is no inescapable obligation to pay dividends or interest.

2.2.9

The forms of capital that qualify for tier one capital are set out in the capital resources table and include, for example, share capital, reserves, partnership and sole trader capital, verified interim net profits and, for a mutual, the initial fund plus permanent members’ accounts. Tier one capital is divided into core tier one capital and hybrid capital. Hybrid capital is further divided into the different stages B1, B2 and C of the calculation in the capital resources table.

2.2.10

Upper and lower tier two capital

Tier two capital includes forms of capital that do not meet the requirements for permanency and absence of fixed servicing costs that apply to tier one capital. Tier two capital includes, for example:

1. capital which is perpetual (that is, has no fixed term) but cumulative (that is, servicing costs cannot be waived at the issuer’s option, although they may be deferred – for example, cumulative preference...
shares); only perpetual capital instruments may be included in upper tier two capital;

(2) capital which is not perpetual (that is, it has a fixed term) or which may have fixed servicing costs that cannot generally be either waived or deferred (for example, most subordinated debt); such capital should normally be of a medium to long-term maturity (that is, an original maturity of at least five years); dated capital instruments are included in lower tier two capital;

(3) (for BIPRU firms) certain revaluation reserves such as reserves arising from the revaluation of land and buildings, including any net unrealised gains for the fair valuation of equities held in the available-for-sale financial assets category; and

(4) (for BIPRU firms) general/collective provisions.

Tier three capital

Tier three capital consists of forms of capital conforming least well to the characteristics of capital listed in § GENPRU 2.2.9 G: either subordinated debt of short maturity (upper tier three capital) or net trading book profits that have not been externally verified (lower tier three capital).

Non-standard capital instruments

There may be examples of capital instruments that, although based on a standard form, contain structural features that make the rules in this section difficult to apply. In such circumstances, a firm may seek individual guidance on the application of those rules to the capital instrument in question. See SUP 9 (Individual guidance) for the process to be followed when seeking individual guidance.

Deductions from capital

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).

Deductions should also be made, in the case of certain BIPRU firms for illiquid assets (see § GENPRU 2.2.19 R).

A full list of deductions from capital resources is shown in the capital resources table applicable to the firm.
Which method of calculating capital resources applies to which type of firm

2.2.17 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 2.2.19 R.

2.2.18 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.

Table: Applicable capital resources calculation

2.2.19 This table belongs to ■ GENPRU 2.2.17 R

<table>
<thead>
<tr>
<th>Type of firm</th>
<th>Location of rules</th>
<th>Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td>BIPRU firm without an investment firm consolidation waiver</td>
<td>GENPRU 2 Annex 4 (Deducts material holdings)</td>
<td>Applies to a BIPRU firm not using GENPRU 2 Annex 5 or GENPRU 2 Annex 6</td>
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<tr>
<td>BIPRU firm without an investment firm consolidation waiver</td>
<td>GENPRU 2 Annex 5 (Deducts illiquid assets)</td>
<td>A BIPRU firm must give one Month’s prior notice to the FCA before starting to use or stopping using this method</td>
</tr>
<tr>
<td>BIPRU firm with an investment firm consolidation waiver</td>
<td>GENPRU 2 Annex 6 (Deducts illiquid assets and material holdings)</td>
<td>A firm with an investment firm consolidation waiver must use this method. No other BIPRU firm may use it.</td>
</tr>
</tbody>
</table>

Calculation of capital resources: Which rules apply to BIPRU firms

2.2.20 ■ GENPRU 2.2.19 R sets out three different methods of calculating capital resources for BIPRU 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 FCA, illiquid assets.

2.2.21 A consequence of a firm deducting all of its illiquid assets under ■ GENPRU 2 Annex 5 is that it is allowed a higher limit on short term subordinated debt under ■ GENPRU 2.2.49 R.

Limits on the use of different forms of capital: General

2.2.24 As the various components of capital differ in the degree of protection that they offer the firm and its customers and consumers, restrictions are placed on the extent to which certain types of capital are eligible for inclusion in a
A firm may include in a lower stage of capital, capital resources which are eligible for inclusion in a higher stage of capital if the capital resources gearing rules would prevent the use of that capital in that higher stage of capital. However:

1. The capital resources gearing rules applicable to that lower stage of capital apply to higher stage of capital included in that lower stage of capital; and

2. [subject to GENPRU 2.2.26 R and GENPRU 2.2.26A R] the rules in GENPRU governing the eligibility of capital in that lower stage of capital continue to apply.

An item of tier one capital which is included in a firm’s tier two capital resources under GENPRU 2.2.25 R is not subject to the requirement to obtain a legal opinion in GENPRU 2.2.159R (12).

A dated item of tier one capital which is included in a BIPRU firm’s tier two capital resources under GENPRU 2.2.25 R is not subject to the requirement to have no fixed maturity date in GENPRU 2.2.177R (1).

[deleted]

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 2.2.25 R but the requirements to obtain a legal opinion in GENPRU 2.2.118 R continue to apply.

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.
The purpose of the requirements in GENPRU 2.2.30AR (1) is to ensure that the firm’s tier one capital resources includes a minimum proportion of core tier one capital which provides the highest quality capital. Within the 50% limit on non-core tier one capital (1) [deleted]

(2) GENPRU 2.2.30AR (2) and GENPRU 2.2.30AR (3) place further sub-limits on the amounts of hybrid capital included at stages B2 and C of the calculation in the capital resources table that a BIPRU firm may include in its tier one capital resources.

These limits are necessary to ensure that most of a firm’s tier one capital comprises items of capital of the highest quality.

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) [deleted]

(3) the counterparty risk capital component; and

(4) the base capital resources requirement.

GENPRU 2.2.44 R (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 2.2.47 R and except as may otherwise be stated in the relevant part of the Handbook.

For the purpose of GENPRU 2.2.44 R:

(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.

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; and
(2) [deleted]
(3) the fixed overheads requirement;

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 2.2.44 R (GENPRU 2.2.48 R explains how to calculate how much tier one capital is required to meet the requirements in GENPRU 2.2.44 R);

(5) tier two capital to the extent that it:
   (a) comes within the limits in GENPRU 2.2.46 R (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 2.2.44 R;

   (GENPRU 2.2.48 R explains how to calculate how much tier two capital is required to meet the requirements in GENPRU 2.2.44 R);

(6) tier two capital that cannot be used for the purposes in GENPRU 2.2.44 R because it falls outside the limits in GENPRU 2.2.46 R; and

(7) tier three capital.

The amount of tier one capital and tier two capital that is not used to meet the requirements in GENPRU 2.2.44 R as referred to in GENPRU 2.2.47 R (1) to GENPRU 2.2.47 R (4) and (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).

Limits on the use of different kinds of capital: Combined tier two and tier three limits (BIPRU firm only)

2.2.48 R

For the purpose of meeting the requirements in GENPRU 2.2.47 R (1) to GENPRU 2.2.47 R (3) and subject to GENPRU 2.2.50 R, a BIPRU firm must not include any item in either:

(1) its tier two capital resources falling within GENPRU 2.2.47 R (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 2.2.48 R.

2.2.50 In relation to a BIPRU firm which calculates its capital resources under GENPRU 2 Annex 4 (Capital resources table for a BIPRU investment firm deducting material holdings), the figure of 200% replaces that of 250% in GENPRU 2.2.49 R.

Example of how the capital resources calculation for BIPRU firms works

2.2.51 GENPRU 2.2.52 G to GENPRU 2.2.59 G 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 2.2.52 G.

Table: Example of the calculation of the capital resources of a BIPRU firm

<table>
<thead>
<tr>
<th>Description of the stage of the capital resources calculation</th>
<th>Stage in the capital resources table</th>
<th>Amount (£)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total tier one capital after deductions</td>
<td>Stage F</td>
<td>80</td>
</tr>
<tr>
<td>Total tier two capital</td>
<td>Stage K</td>
<td>80</td>
</tr>
<tr>
<td>Deductions</td>
<td>Stage M</td>
<td>(20)</td>
</tr>
<tr>
<td>Total tier one capital and tier two capital after deductions</td>
<td>Stage N</td>
<td>140</td>
</tr>
<tr>
<td>Upper tier three capital (this example assumes the firm has no lower tier three capital (trading book profits))</td>
<td>Stage Q</td>
<td>50</td>
</tr>
<tr>
<td>Total capital resources</td>
<td>Stage T</td>
<td>190</td>
</tr>
</tbody>
</table>

2.2.53 [deleted]

2.2.54 In the example in the table in GENPRU 2.2.52 G the firm has total tier one capital after deductions of £80. Its tier two capital of £80 is therefore the maximum permitted under GENPRU 2.2.46 R (Tier two limits), that is 100% of tier one capital.
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 2.2.56 G.

Table: Example of how capital resources of a BIPRU firm are measured against its capital resources requirement

<table>
<thead>
<tr>
<th>Description of the stage of the capital resources calculation</th>
<th>Stage in the capital resources table</th>
<th>Amount (£)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total tier one capital and tier two capital after deductions</td>
<td>Stage N</td>
<td>140</td>
</tr>
<tr>
<td>Credit and counterparty risk requirement</td>
<td></td>
<td>(100)</td>
</tr>
<tr>
<td>Tier one capital and tier two capital available to meet market risk requirement</td>
<td>Stage Q</td>
<td>40</td>
</tr>
<tr>
<td>Tier three capital</td>
<td></td>
<td>50</td>
</tr>
<tr>
<td>Total capital available to meet market risk requirement</td>
<td></td>
<td>90</td>
</tr>
<tr>
<td>Market risk requirement</td>
<td></td>
<td>(90)</td>
</tr>
<tr>
<td>Market risk requirement met subject to meeting gearing limit set out in GENPRU 2.2.49 R – see GENPRU 2.2.57 G</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The gearing limit in § GENPRU 2.2.49 R (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.

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 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 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 2.2.49R (3) and § GENPRU 2.2.49R (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 risk requirement of £90 have been met by tier two capital in the first instance. However, the total sum of deductions and credit risk requirement 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 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.

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.

Capital used to meet the base capital resources requirement (BIPRU firm only)

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.

The explanation for GENPRU 2.2.60 R can be found in GENPRU 2.1.43 G (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.

Notification of issuance of capital instruments

This section applies to a firm intending to issue a capital instrument on or after 1 March 2012 for inclusion in its capital resources.

A firm must notify the FCA in writing of its intention to issue a capital instrument which it intends to include within its capital resources at least one month before the intended date of issue, 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:

1. provide details of the amount of capital the firm is seeking to raise through the intended issue and whether the capital is intended to be issued to external investors or within its group;
2. identify the stage of the capital resources table the capital instrument is intended to fall within;
3. include confirmation from a senior manager of the firm responsible for authorising the intended issue that the capital instrument complies with the rules applicable to instruments included in the stage of the capital resources table identified in (2); and
4. provide 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 or not specifically contemplated by GENPRU 2.2.

This rule does not apply to a firm which intends to issue a capital instrument listed in GENPRU 2.2.61E R.

2.2.61C R

A firm must provide a further notification to the FCA in writing including all the information required in GENPRU 2.2.61BR (1) to (4) as soon as it proposes any change to the intended date of issue, amount of issue, type of investors, stage of capital or any other feature of the capital instrument to that previously notified to the FCA.

2.2.61D R

If a firm proposes to establish a debt securities program for the issue of capital instruments for inclusion within its capital resources, it must:

(1) notify the FCA of the establishment of the program; and

(2) provide the information required by GENPRU 2.2.61BR (1) to (4) at least one month before the first proposed drawdown. Any changes must be notified to the FCA in accordance with GENPRU 2.2.61C R.

2.2.61E R

The capital instruments to which GENPRU 2.2.61B R does not apply are:

(1) ordinary shares which:

(a) are the most deeply subordinated capital instrument issued by the firm;

(b) meet the criteria set out in GENPRU 2.2.83R (2) and (3), and, for a BIPRU firm, GENPRU 2.2.83A R; and

(c) are the same as ordinary shares previously issued by the firm;

(2) debt instruments issued from a debt securities program, provided that program was notified to the FCA prior to its first drawdown, in accordance with GENPRU 2.2.61D R; and

(3) capital instruments which are not materially different in terms of their characteristics and eligibility for inclusion in a particular tier of capital to capital instruments previously issued by the firm.

2.2.61F R

A firm must notify the FCA in writing, no later than the date of issue, of its intention to issue a capital instrument listed in GENPRU 2.2.61E R which it intends to include within its capital resources. When giving notice, a firm must:

(1) provide the information set out at GENPRU 2.2.61BR (1) to (3); and

(2) confirm that the terms of the capital instrument have not changed since the previous issue by the firm of that type of capital instrument.
2.2.61G GENPRU 2.2.61B R provides that, in exceptional circumstances, a firm may provide less than one month’s notice of the intended issue. The FCA is unlikely to consider circumstances to be exceptional unless they are such that there is a risk of a firm’s capital resources falling below its capital resources requirement if a one-month notification period is observed. In such circumstances, a firm should notify the FCA as soon as it has resolved to issue further capital, and provide details of its circumstances and why it is not possible to provide one month’s notice of the intended issue.

2.2.61H Details of the notification to be provided by a BIPRU firm in relation to capital instruments issued by another undertaking in its group for inclusion in its capital resources or the consolidated capital resources of its UK consolidation group or non-UK sub-group are set out in BIPRU 8.6.1A R to BIPRU 8.6.1F R.

Tier one capital: General

2.2.62 A firm may not include a capital instrument in its tier one capital resources unless it complies with the following conditions:

(1) it is included in one of the categories in GENPRU 2.2.63 R;

(2) it complies with the conditions set out in GENPRU 2.2.64 R;

(3) it is not excluded under GENPRU 2.2.65 R (Connected transactions); and

(4) it is not excluded by any of the rules in GENPRU 2.2.

2.2.63 The categories referred to in GENPRU 2.2.62R (1) are:

(1) permanent share capital;

(2) eligible partnership capital;

(3) eligible LLP members’ capital;

(4) sole trader capital;

(5) [deleted]

(6) [deleted]

(7) [deleted]

(8) hybrid capital.

General conditions for eligibility as tier one capital

2.2.64 The conditions that an item of capital of a firm must comply with under GENPRU 2.2.62R (2) are as follows:

(1) it is issued by the firm;
(2) it is fully paid and the proceeds of issue are immediately and fully available to the firm;

(3) it:
   (a) cannot be redeemed at all or can only be redeemed on a winding up of the firm; or
   (b) complies with the conditions in § GENPRU 2.2.70 R (Basic requirements for redeemability);

(4) the item of capital meets the following conditions in relation to any coupon:
   (a) the firm is under no obligation to pay a coupon; or
   (b) (if the firm is obliged to pay the coupon) the coupon is payable in the form of an item of capital that is:
      (i) core tier one capital

(5) any coupon is either:
   (a) non-cumulative; or
   (b) (if it is cumulative) it must, if deferred, be paid by the firm in the form of tier one capital complying with (4)(b);

(6) it is able to absorb losses to allow the firm to continue trading and:
   (a) [deleted]
   (b) it does not, through appropriate mechanisms, hinder the recapitalisation of the firm, and in particular it complies with:
      (i) § GENPRU 2.2.80 R to § GENPRU 2.2.81 R (Loss absorption);
      (ii) in the case of core tier one capital, § GENPRU 2.2.83AR (9) to § GENPRU 2.2.83AR (10) (General conditions for eligibility of capital instruments as core tier one capital (BIPRU firm only)); and
      (iii) in the case of hybrid capital, § GENPRU 2.2.116 R to § GENPRU 2.2.118 R (Other tier one capital: loss absorption);

(7) the amount of the item included must be net of any foreseeable tax charge at the moment of its calculation or must be suitably adjusted in so far as such tax charges reduce the amount up to which that item may be applied to cover risks or losses;

(8) it is available to the firm for unrestricted and immediate use to cover risks and losses as soon as these occur;

(9) it ranks for repayment upon winding up, administration or any other similar process:
(a) [deleted]
(b) lower than any items of capital that are
   (i) eligible for inclusion within the firm’s tier two capital resources; and
   (ii) not eligible for inclusion within the firm’s tier one capital resources; and

(10) the description of its characteristics used in its marketing is consistent with the characteristics required to satisfy (1) to (9).

2.2.65 R  An item of capital does not qualify for inclusion as tier one capital if the issue of that item of capital by the firm is connected with one or more other transactions which, when taken together with the issue of that item, could result in that item of capital no longer displaying all of the characteristics set out in GENPRU 2.2.64R (1) to GENPRU 2.2.64R (9).

Guidance on certain of the general conditions for eligibility as tier one capital

2.2.66 G  GENPRU 2.2.65 R is an example of the general principle in GEN 2.2.1 R (purposive interpretation). Its purpose is to emphasise that an item of capital does not meet the conditions for inclusion in tier one capital if in isolation it does meet those requirements but it fails to meet those requirements when other transactions are taken into account. Examples of such connected transactions might include guarantees or any other side agreement provided to the holders of the capital instrument by the firm or a connected party or a related transaction designed, for example, to enhance their security or to achieve a tax benefit, but which may compromise the loss absorption capacity or permanence of the original capital item.

2.2.67 G  GENPRU 2.2.64R (2) is stricter than the Companies Act definition of fully paid, which only requires an undertaking to pay.

2.2.67A G  The purpose of GENPRU 2.2.64R (4) is to ensure that a firm retains flexibility over the payment of coupons and can preserve cash in times of financial stress. However, a firm may include, as part of the capital instrument terms, a right to make payments of a coupon mandatory if an item of capital becomes ineligible to form part of its capital resources (e.g. through a change in the relevant rules) and the firm has notified the FCA that the instrument is ineligible.

2.2.68 G  The FCA considers that dividend pushers diminish the quality of capital by breaching the principle of complete discretion over coupons set out in GENPRU 2.2.64R (4). A dividend pusher operates so that, in a given period of time, payments must be made on senior securities if payments have previously been made on junior securities or securities ranking pari passu. As such, dividend pushers may not be included in the terms of tier one capital, unless the firm has the option to fund the “pushed payment” in stock.

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.

2.2.68B  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 2.2.64R (6).

2.2.69  An item of capital does not comply with GENPRU 2.2.64R (10) if it is marketed as a capital instrument that would only qualify for a lower level of capital or on the basis that investing in it is like investing in an instrument in a lower tier of capital. For example, an undated capital instrument should not be marketed as a dated capital instrument if the terms of the capital instrument include an option by the issuer to redeem the capital instrument at a specified date in the future.

2.2.69A  A BIPRU firm must not make a payment of a coupon on an item of hybrid capital if the firm has no distributable reserves.

2.2.69B  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.

2.2.69C  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.

2.2.69D  The FCA 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.

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 2.2.69C R.

(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 FCA 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 FCA. If the FCA and the firm do not agree on the cancellation or deferral of the payment of a coupon, then the FCA may consider using its powers under 5SJ 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 FCA’s view of the financial and solvency situation of the firm.

(2) In considering a firm’s financial and solvency situation, the FCA 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 FCA, it may still be able to pay the coupon by way of newly issued core tier one capital in accordance with GENPRU 2.2.64R (4)(b) and GENPRU 2.2.69C R. The FCA may consider using its powers under 5SJ 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.

Redemption of tier one instruments

A firm may not include a capital instrument in its tier one capital resources, unless its contractual terms are such that:
(1) (if it is redeemable other than in circumstances set out in § GENPRU 2.2.64R (3)(a) (redemption on a winding up)) it is redeemable only at the option of the firm or, in the case of a BIPRU firm, on the date of maturity;

(2) the firm cannot exercise that redemption right:
   (a) before the fifth anniversary of its date of issue; and
   (b) unless it has given notice to the FCA in accordance with § GENPRU 2.2.74 R;
   (c) unless at the time of exercise of that right it complies with the main BIPRU firm Pillar 1 rules and will continue to do so after redemption;

(3) (in the case of a BIPRU firm and if it is undated) if it provides for a moderate incentive for the BIPRU firm to redeem it, that incentive does not occur before the tenth anniversary of its date of issue; and

(4) (in the case of a BIPRU firm and if it is dated):
   (a) it has an original maturity date of at least 30 years after its date of issue; and
   (b) it does not provide an incentive to redeem on any date other than its maturity date.

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 FCA 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 2.2.138 R and the rule on step-ups in § GENPRU 2.2.147 R.

A firm may include a term in a tier one instrument allowing the firm to redeem it before the date in § GENPRU 2.2.70R (2)(a) if the following conditions are satisfied:

(1) the other conditions in § GENPRU 2.2.70 R are met;

(2) the circumstance that entitles the firm to exercise that right is a change in the applicable tax treatment or regulatory classification of those instruments;

(3) the circumstance that entitles the firm to exercise that right was not reasonably foreseeable at the date of issue of the tier one instrument; and
(4) the firm's right is conditional on it obtaining the FCA's consent in the form of a waiver of GENPRU 2.2.72 R.

2.2.72 R A firm must not redeem a tier one instrument in accordance with a term included under GENPRU 2.2.71 R.

2.2.73 G The purpose of GENPRU 2.2.71 R to GENPRU 2.2.72 R is this. In general a tier one instrument should not be redeemable by the firm before its fifth anniversary. However there may be circumstances in which it would be reasonable for the firm to redeem it before then. GENPRU 2.2.71 R allows the firm to include a right to redeem the instrument before the fifth anniversary in certain circumstances. A tax call is an example of a term that may be allowed. GENPRU 2.2.71 R says that the terms of the tier one instrument should provide that the firm should not be able to exercise that right without the FCA's consent. Any such consent will be given in the form of a waiver allowing early repayment. Thus although a firm may include a right to redeem early in the terms of a tier one instrument without the need to apply for a waiver the actual exercise of that right will require a waiver.

2.2.74 R A firm must not redeem any tier one instrument that it has included in its tier one capital resources unless it has notified the FCA of its intention at least one month before it becomes committed to do so. When giving notice, the firm must provide details of its position after such redemption in order to show how it will:

(1) meet its capital resources requirement;

(2) have sufficient financial resources to meet the overall financial adequacy rule; and

(3) in the case of a BIPRU firm, not otherwise suffer any undue effects to its financial or solvency conditions.

2.2.74A G The FCA considers that, in order to comply with GENPRU 2.2.74 R, the firm should, at a minimum, provide the FCA with the following information:

(1) a comprehensive explanation of the rationale for the redemption;

(2) the firm's financial and solvency position before and after the redemption, in particular whether that redemption, or other foreseeable internal and external events or circumstances, may increase the risk of the firm breaching its capital resources requirement;

(3) an appropriately stressed capital plan covering 3-5 years, which includes the effect of the proposed redemption; and

(4) 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.
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.

If a firm gives notice of the redemption or repayment of any tier one instrument, the firm must no longer include that instrument in its tier one capital resources.

Meaning of redemption

(1) This rule applies to a tier one instrument, tier two instrument or tier three instrument (instrument A) that under its terms is exchanged for or converted into another instrument or is subject to a similar process.

(2) This rule also applies to instrument A if under its terms it is redeemed out of the proceeds of the issue of new securities.

(3) If the instrument with which instrument A is replaced is included in the same stage of capital or a higher stage of capital as instrument A, instrument A is treated as not having been redeemed or repaid for the purposes of GENPRU 2.2.

(4) (3) does not apply to Redeemable instrument likely to be repaid etc, Notice of redemption of tier one instruments, Notice of redemption of tier two instruments or so far as it relates to notice of redemption of tier three instruments.

(5) (3) only applies if it would be reasonable (taking into account the economic substance) to treat the original instruments as continuing in issue on the same or a more favourable basis. The question of whether that basis is more or less favourable must be judged from the point of view of the adequacy of the firm's capital resources.

A share is not redeemable for the purposes of this section merely because the Companies Act 1985, the Companies (Northern Ireland) Order 1986 or the Companies Act 2006 allows the firm that issued it to purchase it.

A capital instrument is not redeemable for the purposes of this section merely because the firm that issued it has a right to purchase it similar to the right in (1).

This section generally uses the term repay and redeem interchangeably.
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 FCA in accordance with GENPRU 2.2.79G R; and
4. (in the case of hybrid capital) it is on or after the fifth anniversary of the date of issue of the instrument.

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.

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.

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.

2.2.79E G

In the circumstances provided for in GENPRU 2.2.79D R, 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.

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.

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 FCA 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.

2.2.79H The FCA considers that:

(1) in order to comply with GENPRU 2.2.79G R, the firm should, at a minimum, provide the FCA 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.

2.2.79I 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 FCA in accordance with GENPRU 2.2.79G R and it has not, during the period of one month from the date of giving notice, received an objection from the FCA.

2.2.79J 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.

2.2.79K 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.

2.2.79L 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 2.2.79G R and for which the offer to purchase has been declined by the instrument holders unless the purchase offer period has expired.
Loss absorption

2.2.80 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) [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).

2.2.81 A firm may not include a capital instrument other than a share in its tier one capital resources unless it complies with GENPRU 2.2.80R (3).

2.2.82 There are additional loss absorption requirements for hybrid capital in GENPRU 2.2.116AR to GENPRU 2.2.118R (Other tier one capital: loss absorption) and for core tier one capital in GENPRU 2.2.83AR (9) to (10) (General conditions for eligibility of capital instruments as core tier one capital).

Core tier one capital: permanent share capital

2.2.83 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) [deleted]

(2) any coupon on it is not cumulative, the firm is under no obligation to pay a coupon in any circumstances and the firm has the right to choose the amount of any coupon that it pays;

(3) the terms upon which it is issued do not permit redemption and it is otherwise incapable of being redeemed to at least the same degree as an ordinary share issued by a company incorporated under the Companies Act 2006 (whether or not it is such a share); and

(4) (in the case of a BIPRU firm) it meets the conditions set out in GENPRU 2.2.83A R (General conditions for eligibility of capital instruments as core tier one capital (BIPRU firm only)).
2.2.83A General conditions for eligibility of capital instruments as core tier one capital (BIPRU firm only)

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 2.2.95 R 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).

2.2.83B  
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 2.2.83 R and GENPRU 2.2.83A R but have differences in voting rights, unless it has notified the FCA 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.

2.2.83C  
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.

2.2.83D  
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.

Core tier one capital: exception to eligibility criteria (building societies only)

2.2.83E  
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 2.2.83R (2), GENPRU 2.2.83R (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 2.2.83AR (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).

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 2.2.83ER unless it has notified the PRA of its intention to do so at least one month before the intended date of issue.

2.2.83G G Under GENPRU 2.2.83ER (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).

2.2.83H G The purpose of GENPRU 2.2.83ER (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.

Core tier one capital: additional information

2.2.84 G [deleted]

2.2.84A G Under GENPRU 2.2.83AR (13) a tier one instrument does not meet the conditions for inclusion as core tier one capital if in isolation it does meet those requirements but fails to meet those requirements when other
transactions are taken into account. Examples of those transactions include guarantees, pledges of assets or other side agreements provided by the firm to the holder of a tier one instrument designed to enhance the legal or economic seniority of the tier one instrument.

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 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 firm must deduct the whole amount of those losses and not just the excess.

2.2.85A R

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 1.3.29 R to GENPRU 1.3.35A G (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 2.2.85 R.

(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 2.2.248 R (Net interim trading book profits) otherwise.

Core tier one capital: profit and loss account and other reserves: Dividends

2.2.87 R Dividends must be deducted from reserves as soon as they are foreseeable.

2.2.87A G Each firm must assess for itself when, in its particular circumstances, dividends are foreseeable. A dividend is foreseeable at the latest:

(1) in the case of an interim dividend, when it is declared by the directors; or

(2) in the case of a final dividend, when the directors approve the dividend to be proposed at the annual general meeting.
Core tier one capital: profit and loss account and other reserves: Capital contributions

2.2.88 R A firm must account for a capital contribution as an increase in reserves and may, notwithstanding § GENPRU 2.2.63 R, count that increase in reserves as core tier one capital.

2.2.89 G An item of capital qualifies as a capital contribution if it is a gift of capital (and, as such, is not repayable) and a coupon is not payable on it.

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.

Core tier one capital: profit and loss account and other reserves: Valuation

2.2.91 G Profit and loss account and other reserves should be valued in accordance with the rules in § GENPRU 1.3 (Valuation).

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.

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.

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.

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 2.2.83R (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 2.2.64R (3) (Redemption), GENPRU 2.2.83AR (5) (Capital repayment) and GENPRU 2.2.83AR (12) (Characteristics in contract) are replaced by GENPRU 2.2.93 R or GENPRU 2.2.94 R.

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 FCA 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.

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.

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.

### Core tier one capital: partnership and limited liability partnership excess drawings (BIPRU firm only)

2.2.100 A **BIPRU firm** which is a partnership or a **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.

### Core tier one capital: Share premium account

2.2.101

1. A **firm** must include share premium account relating to the issue of a share forming part of its **core tier one capital** in its **core tier one capital**.

2. A **firm** must include share premium account relating to the issue of a share forming part of another tier of capital in that other tier.

3. A **firm** that is incorporated under the Companies Act 2006 may include its share premium account as **core tier one capital** notwithstanding (2) to the extent that the terms of issue of the share concerned provide that any premium is not repayable on redemption.

4. Paragraph (3) applies to a **firm** that is not incorporated under the Companies Act 2006 if its share premium account is subject to substantially the same or greater restraints on use than a share premium account falling into (3).

### Core tier one capital: externally verified interim net profits

2.2.102 Externally verified interim net profits are interim profits which have been verified by a **firm's** external auditors after deduction of tax, foreseeable dividends and other appropriations.

2.2.103 A **firm** may include interim profits before a formal decision has been taken only if these profits have been verified, in accordance with the relevant guidance issued by the Financial Reporting Council, by persons responsible for the auditing of the accounts.

### Core tier one capital: deferred shares (building society only)

2.2.108A 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.

2.2.108B 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).

2.2.111 [deleted]

2.2.112 [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 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 FCA may require its conversion into core tier one capital when the FCA 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.
2.2.115B 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.

2.2.115C (1) In respect of GENPRU 2.2.115AR (4), the FCA may require the firm to convert the instrument into core tier one capital based on its financial and solvency situation. The FCA will take into account, among other things, the factors identified at GENPRU 2.2.69FG (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 FCA 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 FCA may require the firm to convert the instrument into core tier one capital.

2.2.115D 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.

2.2.115E (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.

2.2.115F 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.

2.2.115G 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 2.2.115FR (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.

Other tier one capital: loss absorption

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:
   - any such liability is not relevant for the purposes of deciding whether:
     - the firm is, or is likely to become, unable to pay its debts; or
     - its liabilities exceed its assets;
   - 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
   - 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).

The effect of GENPRU 2.2.116 R and GENPRU 2.2.116A R is that if a potential tier one instrument does constitute a liability, this should only be the case when the firm is able to pay that liability but chooses not to do so. The holder should agree that the firm has no liability (including any contingent or prospective liability) to pay any amount to the extent to which that liability would cause the firm to become insolvent if it made the payment or to the extent that its liabilities exceed its assets or would do if the payment were made. The terms of the capital instrument should be such that the directors can continue to trade in the best interests of the senior creditors even if this prejudices the interests of the holders of the instrument.

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).

The trigger points required by GENPRU 2.2.117AR (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.

The effects of the mechanisms described in GENPRU 2.2.117AR 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.

If a firm does not operate the loss absorption mechanism in a prudent and timely way, then the FCA 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.

(1) [deleted]

(2) A BIPRU firm may not include a capital instrument at stage B1, B2 or C of the calculation in the capital resources table unless it has obtained a properly reasoned independent legal opinion from an appropriately qualified individual confirming that the criteria in GENPRU 2.2.62 R (Tier one capital: General), GENPRU 2.2.64R (1) to GENPRU 2.2.64R (9) (General conditions for eligibility as tier one capital) and GENPRU 2.2.80 R to GENPRU 2.2.81 R (Loss absorption) are met.

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.

For the purpose of GENPRU 2.2.118 R, an independent legal opinion may be given by an employee of that firm, but if an employee does so he should not be part of the business unit responsible for the transaction (including the drafting of the issue documentation).

Other tier one capital: hybrid capital: indirectly issued tier one capital (BIPRU firm only)

(1) GENPRU 2.2.123 R to GENPRU 2.2.137 R apply to a BIPRU 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.

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.
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.

The SPV referred to in ▪ GENPRU 2.2.124R (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.

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.

▪ GENPRU 2.2.127R (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.

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).
2.2.129 R The SPV referred to in GENPRU 2.2.124R (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.

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.

2.2.131 R In relation to the obligation to substitute described in GENPRU 2.2.129R (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.

2.2.131A G GENPRU 2.2.129R (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.

2.2.132 R The capital which the firm seeks to include in its capital resources under GENPRU 2.2.124R (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.

(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 2.2.129R (1) and § GENPRU 2.2.129R (4), whether or not issued by an SPV.

(5) The obligations in § GENPRU 2.2.129R (2) and § GENPRU 2.2.129R (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).

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 2.2.129R (2).

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 FCA at least one Month in advance of the date on which the firm intends to include that capital in its capital resources.

The FCA 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 FCA would expect a firm to request individual guidance in such circumstances.
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.

Tier one capital: Conversion ratio

2.2.138 R (1) This rule applies to a potential tier one instrument if:

(a) it is redeemable by the firm (ignoring GENPRU 2.2.77 R (Meaning of redemption));

(b) it provides that if the issuer does not exercise that right or does not do so in specified circumstances the issuer must or may have to redeem it in whole or in part through the issue of shares eligible for inclusion in the firm’s tier one capital resources or the instrument converts or may convert into such shares; and

(c) GENPRU 2.2.77 R means that the obligation in (1)(b) is treated as not being inconsistent with GENPRU 2.2.70R (1) (Tier one capital should not be redeemable at the option of the holder).

(2) A firm must not include a potential tier one instrument to which this rule applies in its tier one capital resources if:

(a) the conversion ratio as at the date of redemption may be greater than the conversion ratio as at the time of issue by more than 150%; or

(b) the market price of the conversion instruments issued in relation to one unit of the original capital item (plus any cash element of the redemption) may be greater than the issue price of that original capital item.

(3) All determinations under this rule are made as at the date of issue of the original capital item.

2.2.139 R In GENPRU 2.2.138 R to GENPRU 2.2.142 R:

(1) the original capital item means the capital item that is being redeemed; and

(2) the conversion instrument means the tier one capital to be issued on its redemption.

2.2.140 R In GENPRU 2.2.138 R to GENPRU 2.2.142 R, the conversion ratio means the ratio of:

(1) the number of units of the conversion instrument that the firm must issue to satisfy its redemption obligation (so far as it is to be satisfied
by the issue of conversion instruments) in respect of one unit of the
original capital item; to

(2) one unit of the original capital item.

2.2.141 In GENPRU 2.2.138 R to GENPRU 2.2.142 R, the conversion ratio as at the date
of issue of the original capital item is calculated as if the original capital item
were redeemable at that time.

2.2.142 If the conversion instruments or the original capital item are subdivided or
consolidated or subject to any other occurrence that would otherwise result
in like not being compared with like, the conversion ratio calculation in
GENPRU 2.2.138 R must be adjusted accordingly.

2.2.143 (1) The significance of the limitations on conversion in
GENPRU 2.2.138R (2) can be seen in the example in this paragraph.

(2) A firm issues innovative notes with a par value of £100 each. The
terms of the instrument provide that if the instrument is not called at
par at the first call date the notes convert into a variable number of
ordinary shares.

(3) If the market price of the ordinary shares is 400 pence per share on
the day of issue of the innovative notes then the maximum number
of ordinary shares (M) that a single £100 par value innovative note
can be converted into is calculated as follows:

(a) $M = \text{Par value of innovative instrument} \times 150\% / \text{market value of}
\text{ordinary share}$;

(b) $M = £100 \times 1.5 / £4 = 37.5 \text{ shares}$.

(4) The practical effect is that conversion will result in the holder of an
innovative capital note receiving ordinary shares equal to the par
value of that note only when the market price of the ordinary shares
remains above half the market price of the shares at the date of issue
of the notes.

(5) If the market price of the ordinary shares fell by half to 200 pence,
the maximum permitted number of shares (37.5) would have to be
issued in order to give an investor in the innovative note ordinary
shares with a market value equal to £100. If the market price of the
ordinary shares fell below 200 pence, the issue of the maximum
permitted number of ordinary shares would have a market value
below £100.

2.2.144 (1) In addition to the maximum conversion ratio of 150%
GENPRU 2.2.138R (2)(b) does not permit a firm to issue shares that
would have a market value that exceeds the issue price of the
instrument being redeemed.
(2) In the example in §GENPRU 2.2.143 G, if the market value of the ordinary shares was 250 pence at the conversion date, the maximum number of ordinary shares that may be issued to satisfy the redemption of one of the £100 par value innovative notes would be 40 (= £100 / £2.5).

Tier one capital: Requirement to have sufficient unissued stock

(1) This rule applies to a potential tier one instrument of a firm where either:

(a) the redemption proceeds; or

(b) any coupon on that capital item;

can be satisfied by the issue of another capital instrument.

(2) A firm may only include an item of capital to which this rule applies in its tier one capital resources if the firm has authorised and unissued capital instruments of the kind in question (and the authority to issue them):

(a) that are sufficient to satisfy all such payments then due; and

(b) are of such amount as is prudent in respect of such payments that could become due in the future.

Step-ups: calculating the size of a step-up

(1) Where a rule in this section says that a particular treatment applies to an item of capital that is subject to a step-up of a specified amount, the question of whether that rule is satisfied must be judged by reference to the cumulative amount of all step-ups since the issue of that item of capital rather than just by reference to a particular step-up.

(2) Where a step-up arises through a change from paying a coupon on a debt instrument to paying a dividend on a share issued in settlement of the coupon, any net cost to the firm arising from the different tax treatment of the dividend compared to the tax treatment of interest may be ignored for the purpose of assessing the effect of that step-up.

Step-ups: Limits on the amount of step-ups on tier one and two capital

(1) A firm may not include in its tier one capital resources a tier one instrument that is or may be subject to a step-up that does not meet the definition of moderate in the press release of the Basle Committee on Banking Supervision of 27th October 1998 called "Instruments eligible for inclusion in Tier 1 capital".

(2) For the purpose of (1) the words in that press release "than, at national supervisory discretion, either" are replaced by "than the higher of the following two amounts".

(3) The calculations required by this rule and §GENPRU 2.2.151 R must be carried out as at the date of issue of the relevant instrument.
(4) **A BIPRU firm may not include a capital instrument in its tier one capital resources if it is redeemable and subject to more than one step-up.**

2.2.148 The effect of §GENPRU 2.2.147 R is that for inclusion in tier one capital resources, step-ups in instruments should be moderate. A moderate step-up for these purposes is one which results in an increase over the initial rate that is no greater than the higher of the following two amounts:

1. 100 basis points, less the swap spread between the initial index basis and the stepped-up index basis; or
2. 50% of the initial credit spread, less the swap spread between the initial index basis and the stepped-up index basis.

If a **coupon** paid on an item of capital is initially set at a specified spread above an index (the initial index basis), and the **coupon** moves to being set relative to another index (the stepped up index basis), there will be an implied step-up (positive or negative) even if the specified spread does not change. This is because each index may itself include a spread relative to the risk free rate and this spread may differ between the two indexes. The deduction of the swap spread in §GENPRU 2.2.148G (1) and §(2) above adjusts for this difference.

2.2.150 Where the step-up involves a conversion from fixed to floating (or vice versa), or a switch in basis index, the swap spread should be fixed at pricing date, reflecting the differential in pricing between indices at the time. The significance of deducting the swap spread can be seen by the following example:

1. the pricing date:
   - (a) 10 year gilts (G) = 5.5% (the initial index basis);
   - (b) 3 month LIBOR is the stepped up index basis and the 10 year mid swap rate (L) = 5.9%;
   - (c) initial fixed coupon rate = G + 200bp;
   - (d) swap spread = 0.4% (= 5.9% - 5.5%);
   - (e) initial fixed coupon rate = 7.5%;
   - (f) the swap spread shows that there is 40bps of spread in the stepped up index basis relative to the initial index basis; and
   - (g) the initial fixed coupon rate of 7.5% is equivalent to the mid swap rate + 160bp, or L + 200bp – the swap spread;

2. pricing of stepped-up rate at year 10 with step-up of 100bp without deducting swap spread:
   - (a) stepped-up floating rate = L + 200 + 100bp step-up = 8.9%; and
   - (b) effective step-up from initial fixed rate of 140bp (= 8.9% - 7.5%);
2. pricing of stepped-up rate at year 10 with step-up of 100bp with deduction of the swap spread:
(a) stepped-up floating coupon rate = \( L + 200 \) less 40bp swap spread (difference between 5.5% and 5.9%) + 100bp step-up = 8.5%

(b) effective step-up from initial rate of 100bp (= 8.5% - 7.5%).

2.2.151

(1) Subject to (2), if a tier two instrument is or may be subject to a step-up that does not meet the definition of moderate in the press release of the Basle Committee on Banking Supervision referred to in GENPRU 2.2.147R (1) as adjusted under GENPRU 2.2.147R (2), the first date that a step-up can take effect is deemed to be its final maturity date if that date is before its actual maturity date.

(2) If a tier two instrument:

(a) is or may be subject to a step-up during the period beginning on the fifth anniversary of the date of issue of that item and ending immediately before the tenth anniversary of the date of issue; and

(b) the step-up or possible step-up is one which may result in an increase over the initial rate that is greater than 50 basis points, less the swap spread between the initial index basis and the stepped-up index basis (all these terms must be interpreted in accordance with GENPRU 2.2.147R);

the first date that a step-up can take effect is deemed to be its final maturity date if that date is before its actual maturity date.

2.2.152

An instrument does not breach GENPRU 2.2.147R or as the case may be, is not subject to a deemed maturity date under GENPRU 2.2.151R, even though it is or may be subject to a step-up that exceeds the amount specified in those rules if:

(1) the instrument is fungible with other instruments (the “existing stock”) that are included in the firm’s tier one capital resources (in the case of GENPRU 2.2.147R) or tier two capital resources (in the case of GENPRU 2.2.151R);

(2) (if there has been no more than one previous issue of the existing stock) the existing stock complied with those limits on its date of issue;

(3) (if there has been more than one previous issue of the existing stock) the first such issue of the existing stock complied with those limits on its date of issue; and

(4) the result of the step-up on the instrument to which this rule applies is that the coupon on that instrument and the coupon on the existing stock is the same.

2.2.153

(1) A firm must not include in its tier one capital resources a potential tier one instrument that is or may become subject to a step-up if that step-up can arise earlier than the tenth anniversary of the date of issue of that item of capital.

(2) A firm must not include in its tier two capital resources a capital instrument that is or may become subject to a step-up if that step-up
Debt instruments containing embedded options, e.g. issues containing options for the interest rate after the step-up to be at a margin over the higher of two (or more) reference rates, or for the interest rate in the previous period to act as a floor, may affect the funding costs of the borrower and imply a step-up. In such circumstances, a firm may wish to seek individual guidance on the application of the rules relating to step-ups to the capital instrument in question. See SUP 9 (Individual guidance) for the process to be followed when seeking individual guidance.

**Deductions from tier one: Intangible assets**

A firm must deduct from its tier one capital resources the value of intangible assets.

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 firms is dealt with in GENPRU 1.3 (Valuation); they should not be deducted as an intangible asset.

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.

**Tier two capital: General**

Tier two capital resources are split into upper and lower tiers. A major distinction between upper and lower tier two capital is that, except as provided by GENPRU 2.2.26A R for BIPRU firms, only perpetual instruments may be included in upper tier two capital whereas dated instruments, such as fixed term preference shares and dated subordinated debt, may be included in lower tier two capital.

**General conditions for eligibility as tier two capital instruments**

A capital instrument must not form part of the tier two capital resources of a firm unless it meets the following conditions:

1. The claims of the creditors must rank behind those of all unsubordinated creditors;

2. The only events of default must be non-payment of any amount falling due under the terms of the capital instrument or the winding-up of the firm and any such event of default must not prejudice the subordination in (1);
(3) to the fullest extent permitted under the laws of the relevant jurisdictions, the remedies available to the subordinated creditor in the event of non-payment or other breach of the terms of the capital instrument must (subject to GENPRU 2.2.161 R) be limited to petitioning for the winding-up of the firm or proving for the debt in the liquidation or administration;

(4) any:
   (a) remedy permitted by (3);
   (b) remedy that cannot be excluded under the laws of the relevant jurisdictions as referred to in (3);
   (c) remedy permitted by GENPRU 2.2.161 R; and
   (d) terms about repayment as referred to in (5);

must not prejudice the matters in (1) and (2) and in particular any damages permitted by (b) or (c) and repayment obligation must be subordinated in accordance with (1);

(5) without prejudice to (1), the debt must not become due and payable before its stated final maturity date (if any) except on an event of default complying with (2) or as permitted by GENPRU 2.2.172 R (Repayment at the option of the issuer) or GENPRU 2.2.194R (2) (Repayment of lower tier two capital at the option of the holder) and any remedy described in (4)(a) to (c) must not prejudice this requirement;

(6) the debt agreement or terms of the capital instrument are governed by the law of England and Wales, or of Scotland or of Northern Ireland;

(7) to the fullest extent permitted under the laws of the relevant jurisdictions, creditors must waive their right to set off amounts they owe the firm against subordinated amounts included in the firm’s capital resources owed to them by the firm;

(8) the terms of the capital instrument must be set out in a written agreement that contains terms that provide for the conditions set out in (1) to (7);

(9) the debt must be unsecured and fully paid up;

(10) the description of its characteristics used in its marketing is consistent with the characteristics required to satisfy (1) to (9);

(11) the amount of the item included must be net of any foreseeable tax charge at the moment of its calculation or must be suitably adjusted in so far as such tax charges reduce the amount up to which that item may be applied to cover risks or losses; and

(12) the firm has obtained a properly reasoned independent legal opinion from an appropriately qualified individual stating that the requirements in (1) to (7) and (insofar as it relates to whether the capital instrument is unsecured) (9) have been met.
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.

General conditions for eligibility as tier two capital instruments: Additional remedies

A capital instrument may be included in a firm’s tier two capital resources even though the remedies available to the subordinated creditor go beyond those referred to in GENPRU 2.2.159R (3), if the following conditions are satisfied:

1. those remedies are not available for failure to pay any amount of principal, interest or expenses or in respect of any other payment obligation; and

2. those remedies do not in substance amount to remedies to recover payment of the amounts in (1).

If damages are a remedy that cannot be excluded as referred to in GENPRU 2.2.159R (3) those damages should be subordinated in accordance with GENPRU 2.2.159 R. Damages permitted by GENPRU 2.2.161 R should also be subordinated in accordance with GENPRU 2.2.159R (1).

General conditions for eligibility as tier two capital instruments: Alternative governing laws

GENPRU 2.2.159R (6) does not apply if the firm has obtained a properly reasoned independent legal opinion from an appropriately qualified individual confirming that the same degree of subordination has been achieved under the law that governs the debt and the agreement as that which would have been achieved under the laws of England and Wales, Scotland, or Northern Ireland.

General conditions for eligibility as tier two capital instruments: Standard form documentation

The FCA is more concerned that the subordination provisions listed in GENPRU 2.2.159 R should be effective than that they should follow a particular form. The FCA does not, therefore, prescribe that the loan agreement or capital instrument should be drawn up in a standard form.

Guidance on the general conditions for eligibility as tier two capital instruments

For the purposes of GENPRU 2.2.159R (5) the debt agreement or terms of the instrument should not contain any clause which might require early repayment of the debt (e.g. cross default clauses, negative pledges and restrictive covenants). A cross default clause is a clause which says that the loan goes into default if any of the borrower’s other loans go into default. It is intended to prevent one creditor being repaid before other creditors, e.g. obtaining full repayment through the courts. A negative pledge is a clause which puts the loan into default if the borrower gives any further charge over its assets. A restrictive covenant is a term of contract that directly, or
indirectly, could lead to early repayment of the debt. Some covenants, e.g. relating to the provision of management information or ownership restrictions, are likely to comply with GENPRU 2.2.159R (3) as long as monetary redress is ruled out, or any payments are covered by the subordination clauses.

2.2.166 GENPRU 2.2.159R (3) allows a capital instrument to form part of the tier two capital resources even though the laws of the relevant jurisdiction do not allow remedies to be limited in the way described there. For example it is not possible to limit certain remedies in the case of an issue in the United States that is SEC-registered and subject to the provisions of the Trust Indenture Act.

2.2.167 The purpose of GENPRU 2.2.159R (7) is to ensure that all of the firm's assets are available to consumers ahead of subordinated creditors. The waiver should apply both before and during liquidation or administration.

2.2.168 The guidance in GENPRU 2.2.119 G (Employee may give legal opinion) also applies for the purpose of GENPRU 2.2.159R (12) and GENPRU 2.2.163 R.

Tier two capital instruments: Connected transactions

2.2.169 An item of capital does not comply with GENPRU 2.2.159 R (General conditions for eligibility as tier two capital instruments) or GENPRU 2.2.177 R (Upper tier two capital: General) if the issue of that item of capital by the firm is connected with one or more other transactions which, when taken together with the issue of that item, could result in that item of capital no longer displaying all of the characteristics set out in whichever of those rules apply.

2.2.170 GENPRU 2.2.66 G (Guidance on GENPRU 2.2.65 R) applies to GENPRU 2.2.169 R in the same way as it does to GENPRU 2.2.65 R (The equivalent of GENPRU 2.2.169 R in relation to tier one capital).

Amendment of tier two instruments

2.2.171 A firm must not amend the terms of the capital or the documents referred to in GENPRU 2.2.159R (8) unless:

1. at least one Month before the amendment is due to take effect, the firm has given the FCA notice in writing of the proposed amendment and the FCA has not objected; and

2. that notice includes confirmation that the legal opinions referred to in GENPRU 2.2.159R (12) and, if applicable, GENPRU 2.2.163 R (General conditions for eligibility as tier two capital instruments: Alternative governing laws) and GENPRU 2.2.181 R (Legal opinions for upper tier two instruments), continue in full force and effect in relation to the terms of the debt and documents after any proposed amendment.
Redemption of tier two instruments

2.2.172 R

A tier two instrument may be redeemable at the option of the firm, but any term of the instrument providing for the firm to have the right to exercise such an option must not provide for that right to be exercisable earlier than the fifth anniversary of the date of issue of the instrument.

2.2.173 R

GENPRU 2.2.71 R to GENPRU 2.2.73 G (Tier one instruments may be redeemed by the issuer before the fifth anniversary in limited circumstances) apply to GENPRU 2.2.172 R in the same way as they do to GENPRU 2.2.70 R (The issuer should not redeem tier one capital before the fifth anniversary).

2.2.174 R

In relation to a tier two instrument, a firm must notify the:

(1) [deleted]

(2) [deleted]

FCA one month before it becomes committed to the proposed repayment (unless that firm intends to repay an instrument on its final maturity date). When giving notice, the firm must provide details of its position after such repayment in order to show how it will:

(3) meet its capital resources requirement; and

(4) have sufficient financial resources to meet the overall financial adequacy rule.

Tier two capital: step-ups

2.2.175 G

The rules and guidance in GENPRU 2.2.146 R to GENPRU 2.2.154 G on step-ups cover tier two capital as well as tier one capital.

Upper tier two capital: General

2.2.176 G

Examples of capital instruments which may be eligible to count in upper tier two capital resources include the following:

(1) perpetual cumulative preference shares;

(2) perpetual subordinated debt; and

(3) other instruments that have the same economic characteristics as (1) or (2).

2.2.177 R

A capital instrument must (in addition to meeting the requirements of the rules about eligibility for inclusion in tier two capital) meet the following conditions before it can be included in a firm's upper tier two capital resources:

(1) it must have no fixed maturity date;
(2) the terms of the instrument must provide for the firm to have the option to defer any coupon on the debt, except that the firm need not have that right in the case of a coupon payable in the form of an item of capital that is included in the same stage of capital or a higher stage of capital as that first item of capital;

(3) the terms of the instrument must provide for the loss-absorption capacity of the capital instrument and unpaid coupons, whilst enabling the firm to continue its business;

(4) it meets the conditions in GENPRU 2.2.169 R (Connected transactions) and GENPRU 2.2.180 R (Loss absorption); and

(5) the terms of the instrument are such that either the instrument or debt is not redeemable or repayable or it is repayable or redeemable only at the option of the firm.

If a firm gives notice of the redemption or repayment of an upper tier two instrument, the firm must no longer include it in its upper tier two capital resources.

Upper tier two capital: Loss absorption

A capital instrument may only be included in upper tier two capital resources if a 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).

Upper tier two capital: Legal opinions

A firm may not include an upper tier two instrument in its upper tier two capital resources unless it has obtained a properly reasoned independent legal opinion from an appropriately qualified individual confirming that the criteria in § GENPRU 2.2.177R (3) and § GENPRU 2.2.180 R (Loss absorption) are met. This rule does not apply to a perpetual cumulative preference share.

Upper tier two capital: Guidance

■ GENPRU 2.2.180 R is an example of the general principle in § GENPRU 2.2.177R (3).

The guidance in § GENPRU 2.2.117 G (There should be no liability to the extent that the firm would become insolvent, etc) also applies for the purpose of § GENPRU 2.2.180 R.

The guidance in § GENPRU 2.2.119 G (Employee may give legal opinion) also applies for the purpose of § GENPRU 2.2.181 R.

Upper tier two capital: Revaluation reserves (BIPRU firm only)

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.

2.2.186 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).

Upper tier two capital: General/collective provisions (BIPRU firm only)

2.2.187 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 FCA.

2.2.188 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 market risk capital requirement multiplied by a factor of 12.5; and
2. the sum of risk weighted assets under the standardised approach for credit risk.

2.2.189 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.

Upper tier two capital: Surplus provisions (BIPRU firm only)

2.2.190 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.

2.2.191 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.

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%.

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.

Lower tier two capital

2.2.194  ＊R
A firm may include a capital instrument in its lower tier two capital resources if (in addition to meeting the requirements of the rules about eligibility for inclusion in tier two capital) either the holder has no right to repayment or it satisfies either of the following conditions:

(1) it has an original maturity of at least five years; or

(2) it is redeemable on notice from the holder, but the period of notice of repayment required to be given by the holder is five years or more.

A firm may include perpetual capital instruments that do not meet the conditions in ＊GENPRU 2.2.177 R (Eligibility conditions for upper tier two capital) in lower tier two capital resources if they meet the general conditions described in ＊GENPRU 2.2.159 R (General conditions for eligibility as tier two capital instruments).

2.2.195  ＊G
(1) For the purposes of calculating the amount of a lower tier two instrument which may be included in a firm’s capital resources:

(a) in the case of an instrument with a fixed maturity date, in the final five years to maturity; and

(b) in the case of an instrument with or without a fixed maturity date but where five years’ or more notice of redemption or repayment has been given, in the final five years to the date of redemption or repayment;

the principal amount must be amortised on a straight line basis.

(2) If a firm gives notice of the redemption or repayment of a lower tier two instrument and (1) does not apply, the firm must no longer include it in its lower tier two capital resources.

2.2.196  ＊R
If a firm wishes to include in lower tier two capital resources an instrument with or without a fixed maturity date but where less than five years’ notice of redemption or repayment has been given, it should seek individual guidance from the FCA.
The effect of swaps on debt capital

2.2.198 A firm must recognise for the purpose of this section any effect that changes in exchange rates or interest rates have on a debt instrument (as defined in GENPRU 2.2.198) under the accounting framework to which the firm is subject as referred to in GENPRU 1.3.4 (General requirements: accounting principles to be applied). A firm must recognise, in accordance with GENPRU 2.2.201, the effect of a foreign currency hedge on a debt instrument (as defined in GENPRU 2.2.198) denominated in a foreign currency or of an interest rate hedge on a fixed rate coupon debt instrument if:

1. the accounting framework to which the firm is subject as referred to in GENPRU 1.3.4 (General requirements: accounting principles to be applied) provides for a fair value hedge accounting relationship between a liability and its related hedge;

2. such a relationship exists under that accounting framework between that debt instrument and that hedge;

3. (if the debt instrument is a tier one instrument) the firm’s obligations under that hedge comply with the conditions in GENPRU 2.2.64 to GENPRU 2.2.65 (General conditions for eligibility as tier one capital);

4. (if the debt instrument is a tier two instrument or an upper tier three instrument) the firm’s obligations under that hedge comply with the conditions in GENPRU 2.2.159 to GENPRU 2.2.169 (General conditions for eligibility as tier two capital instruments) as modified, in the case of an upper tier three instrument, by GENPRU 2.2.244 (Application of tier two capital rules to tier three capital debt) except as follows:
   a. GENPRU 2.2.159R (9) only applies to the extent that it requires that hedge to be unsecured; and
   b. GENPRU 2.2.159R (12) (legal opinion) does not apply.

2.2.200 A firm must recognise the effect of a hedge as referred to in GENPRU 2.2.200 by including the net accounting fair value of the hedging instrument in the valuation of the debt instrument (as defined in GENPRU 2.2.198).

Deductions from tiers one and two: Qualifying holdings (bank or building society only)

2.2.201 A firm must recognise the effect of a hedge as referred to in GENPRU 2.2.200 by including the net accounting fair value of the hedging instrument in the valuation of the debt instrument (as defined in GENPRU 2.2.198).

2.2.202 GENPRU 2.2.202 to GENPRU 2.2.207 only apply to a bank or building society.
2.2.203  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.

2.2.204  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.

2.2.205  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.

2.2.206  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).

2.2.207  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.

Deductions from tiers one and two: Material holdings (BIPRU firm only)

2.2.208 GENPRU 2.2.208 R to GENPRU 2.2.216 G only apply to a BIPRU firm.

2.2.209 (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.

**2.2.210** 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.

**2.2.211** 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.
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 fulfil(s) one of the following conditions:

3. it is a *subsidiary undertaking* of that *firm*; or

4. that *firm* holds a *participation* in it.

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. an item of “basic own funds” as defined in the PRA Rulebook: Glossary.

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:

   a. for an *insurer* that is a *Solvency II firm*, the PRA Rulebook: Solvency II Firms; and

   b. for an *insurer* other than in (a), the PRA Rulebook: Non-Solvency II Firms.

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.

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.

(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 (Capital resources table for a bank) and GENPRU 2 Annex 3 (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 2.2.204R (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.

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.
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).

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.

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 FCA or any other regulator, territory or country.

Deductions from tiers one and two: Connected lending of a capital nature (bank only)

(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.

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.
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*.

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*.

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.

■ BIPRU 10.3.13 G (*Guidance on exposures to trustees*) applies to ■ GENPRU 2.2.225 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 2.2.227 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.
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.

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.

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 2.2.228R (2).

A guarantee is also connected lending of a capital nature if it is a guarantee by the bank of a loan falling into GENPRU 2.2.229R (1); and

1. the loan meets the conditions in GENPRU 2.2.228 R; or

2. the guarantee meets the conditions in GENPRU 2.2.231R (2).

The amount of a guarantee that constitutes connected lending of a capital nature that a firm must deduct is the amount guaranteed.

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.

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.

### Deductions from tiers one and two: Expected losses and other negative amounts (BIPRU firm only)

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*).

### Deductions from tiers one and two: Securitisation positions (BIPRU firm only)

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*.

### Deductions from tiers one and two: Special treatment of material holdings and other items (BIPRU firm only)

[BIPRU 2.2.238 R](#) to [BIPRU 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 [BIPRU 2.2.236 R](#); and

3. *securitisation positions* referred to in [BIPRU 2.2.237 R](#).

1. The treatment in the *capital resources table* of the deductions in [BIPRU 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.

The alternative calculation in GENPRU 2.2.239R (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 firm with an investment firm consolidation waiver has effect for all purposes.

### Tier three capital: upper tier three capital resources (BIPRU firm only)

2.2.240 The alternative calculation in GENPRU 2.2.239R (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 firm with an investment firm consolidation waiver has effect for all purposes.

2.2.241 GENPRU 2.2.241 R to GENPRU 2.2.245 R only apply to a BIPRU firm.

2.2.242 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.

2.2.243 A BIPRU firm which includes subordinated debt in its tier three capital resources must notify the FCA 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.

2.2.244 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.

2.2.245 Table: Application of tier two capital rules to tier three debt

This table belongs to GENPRU 2.2.244 R
<table>
<thead>
<tr>
<th>Tier two capital rule</th>
<th>Adjustment</th>
</tr>
</thead>
<tbody>
<tr>
<td>GENPRU 2.2.159 R (General conditions for eligibility as tier two capital)</td>
<td>The references in GENPRU 2.2.159R (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 2.2.242R (1) <em>(Upper tier three capital should have maturity or notice period of at least two years)</em></td>
</tr>
<tr>
<td></td>
<td>The reference in GENPRU 2.2.159R (10) <em>(Description of tier two capital in marketing documents)</em> to GENPRU 2.2.265R</td>
</tr>
<tr>
<td>GENPRU 2.2.161 R (Additional remedies)</td>
<td></td>
</tr>
<tr>
<td>GENPRU 2.2.163 R (Legal opinion where debt subject to a law of a country outside the United Kingdom)</td>
<td></td>
</tr>
<tr>
<td>GENPRU 2.2.168 R (Ineligibility as tier two capital owing to connected transactions)</td>
<td>The reference to GENPRU 2.2.177 R <em>(General eligibility conditions for upper tier two capital)</em> does not apply</td>
</tr>
<tr>
<td>GENPRU 2.2.171 R (Amendments to terms of the capital instrument)</td>
<td></td>
</tr>
<tr>
<td>GENPRU 2.2.172 R to GENPRU 2.2.173 R (Redeemability at the option of the issuer)</td>
<td></td>
</tr>
<tr>
<td>GENPRU 2.2.174 R (Notification of redemption)</td>
<td>References in the rules in the first column to the fifth anniversary are amended so as to refer to the second anniversary.</td>
</tr>
</tbody>
</table>

**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.*

**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:
   - interim net profits (see stage (A) of the capital resources table); or
   - interim net losses or material interim net losses (see stage (A) of the capital resources table); or
   - profit and loss and other reserves (see stage (A) of the capital resources table).
Trading book profits and losses, other than those losses to which GENPRU 2.2.86R (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.

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 2.2.86R (2).

Deductions from total capital: Illiquid assets (BIPRU investment firm only)

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.

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 2.2.260R (6) where through the passage of time the remaining time to the contractual repayment date falls below 90 days.
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.

**Deductions from total capital: Excess trading book position (bank or building society only)**

(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.

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.

A BIPRU firm may not include a guarantee from a state or public authority in its capital resources.
Capital resources table for an insurer
Capital resources table for a bank
Capital resources table for a building society
## Capital resources table for a BIPRU firm deducting material holdings

| The capital resources calculation for an investment firm deducting material holdings |
| --- | --- | --- |
| **Type of capital** | **Related text** | **Stage** |
| **Core tier one capital** |  |  |
| Permanent share capital | GENPRU 2.2.83 R | (A) |
| Profit and loss account and other reserves (taking into account material interim net losses) | GENPRU 2.2.85 R to 2.2.90 |  |
| Eligible partnership capital | GENPRU 2.2.93 R; GENPRU 2.2.95 R |  |
| Eligible LLP members’ capital | GENPRU 2.2.94 R; GENPRU 2.2.95 R |  |
| Sole trader capital | None |  |
| Share premium account | GENPRU 2.2.101 R |  |
| Externally verified interim net profits | GENPRU 2.2.102 R |  |
| **Hybrid capital** |  |  |
| Stage B1 | GENPRU 2.2.115A R to GENPRU 2.2.117B R | (B1) |
| Stage B2 | GENPRU 2.2.115D R to GENPRU 2.2.117B R | (B2) |
| Stage C | GENPRU 2.2.115F R to GENPRU 2.2.117B R | (C) |
| **Total tier one capital before deductions = A + B1 + B2 + C** |  | (D) |
| **Deductions from tier one capital** |  | (E) |
| Investments in own shares | None |  |
| Intangible assets | GENPRU 2.2.155 R |  |
| Excess of drawings over profits for partnerships, limited liability partnerships and sole traders | GENPRU 2.2.100 R; there is no related text for sole traders |  |
| Net losses on equities held in the available-for-sale financial asset category | GENPRU 2.2.185 R |  |
| (For certain limited purposes only certain additional deductions are made here) | GENPRU 2.2.239R (2) to GENPRU 2.2.239R (4) |  |
| **Total tier one capital after deductions = D-E** |  | (F) |
| **Upper tier two capital** |  | (G) |
| Perpetual cumulative preference shares | GENPRU 2.2.159 R to GENPRU 2.2.181 R |  |
| Perpetual subordinated debt | See previous entry |  |
The capital resources calculation for an investment firm deducting material holdings

<table>
<thead>
<tr>
<th>Type of capital</th>
<th>Related text</th>
<th>Stage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Perpetual subordinated securities</td>
<td>See previous entry</td>
<td></td>
</tr>
<tr>
<td>Revaluation reserves</td>
<td>GENPRU 2.2.185 R</td>
<td></td>
</tr>
<tr>
<td>General/collective provisions</td>
<td>GENPRU 2.2.187 R to GENPRU 2.2.189 R</td>
<td></td>
</tr>
<tr>
<td>Surplus provisions</td>
<td>GENPRU 2.2.190 R to GENPRU 2.2.193 R</td>
<td></td>
</tr>
</tbody>
</table>

**Lower tier two capital**

- Fixed term preference shares
  - GENPRU 2.2.159 R to GENPRU 2.2.174 R; GENPRU 2.2.194 R to GENPRU 2.2.196 R
- Long term subordinated debt
  - See previous entry
- Fixed term subordinated securities
  - See previous entry

**Total tier two capital** = $G+H$ (H)

**Deductions from tier two capital**

- (For certain limited purposes only certain additional deductions are made here)
  - GENPRU 2.2.239R (2) to GENPRU 2.2.239R (4)

**Total tier two capital after deductions** = $I-J$ (K)

**Total tier one capital plus tier two capital** = $F+K$ (L)

**Deductions from the totals of tier one and two**

<table>
<thead>
<tr>
<th>Items</th>
<th>Related text</th>
<th>Stage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Material holdings</td>
<td>GENPRU 2.2.208 R to GENPRU 2.2.215 R</td>
<td></td>
</tr>
<tr>
<td>Expected loss amounts and other negative amounts</td>
<td>GENPRU 2.2.236 R</td>
<td>(Part 1 of stage M)</td>
</tr>
<tr>
<td>Securitisation positions</td>
<td>GENPRU 2.2.237 R</td>
<td></td>
</tr>
<tr>
<td>Reciprocal cross-holdings</td>
<td>GENPRU 2.2.217 R to GENPRU 2.2.220 R</td>
<td>(Part 2 of stage M)</td>
</tr>
</tbody>
</table>

**Total tier one capital plus tier two capital after deductions** = $L-M$ (N)

In calculating whether a firm’s capital resources exceed its capital resources requirement:
1. the credit risk capital component and the counterparty risk capital component; or
2. the base capital resources requirement; as the case may be, must be deducted here.

**Upper tier three**

- Short term subordinated debt
  - GENPRU 2.2.241 R to GENPRU 2.2.245 R

**Lower tier three**

- Net interim trading book profit and loss
  - GENPRU 2.2.246 R to GENPRU 2.2.249 R

**Total tier three capital** = $O+P$ (O)

**Total capital before deductions** = $N+Q$ (R)

**Deductions from total capital** (S)
The capital resources calculation for an investment firm deducting material holdings

<table>
<thead>
<tr>
<th>Type of capital</th>
<th>Related text</th>
<th>Stage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Free deliveries</td>
<td>BIPRU 14.4</td>
<td></td>
</tr>
</tbody>
</table>

Total capital after deductions \((R - S)\) (T)

In calculating whether a firm's capital resources exceed its capital resources requirement, the market risk capital requirement and the fixed overheads requirement must be deducted here.

Note (1): Where the table refers to related text, it is necessary to refer to that text in order to understand fully what is included in the descriptions of capital items and deductions set out in the table.

Note (2): If the amount calculated at:
(a) stage N less the deductions in respect of the capital resources requirement made immediately following stage N; or
(b) stage T less the deductions in respect of the capital resources requirement made immediately following stages N and T;

is a negative number the firm's capital resources are less than its capital resources requirement.
### Capital resources table for a BIPRU firm deducting illiquid assets

The capital resources calculation for an investment firm that deducts illiquid assets

<table>
<thead>
<tr>
<th>Type of capital</th>
<th>Related text</th>
<th>Stage</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Core tier one capital</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Permanent share capital</td>
<td>GENPRU 2.2.83 R</td>
<td>(A)</td>
</tr>
<tr>
<td>Profit and loss account and other reserves (taking into account material interim net losses)</td>
<td>GENPRU 2.2.85 R to GENPRU 2.2.90 R</td>
<td></td>
</tr>
<tr>
<td>Eligible partnership capital</td>
<td>GENPRU 2.2.93 R; GENPRU 2.2.95 R</td>
<td></td>
</tr>
<tr>
<td>Eligible LLP members’ capital</td>
<td>GENPRU 2.2.94 R; GENPRU 2.2.95 R</td>
<td></td>
</tr>
<tr>
<td>Sole trader capital</td>
<td>None</td>
<td></td>
</tr>
<tr>
<td>Share premium account</td>
<td>GENPRU 2.2.101 R</td>
<td></td>
</tr>
<tr>
<td>Externally verified interim net profits</td>
<td>GENPRU 2.2.102 R</td>
<td></td>
</tr>
<tr>
<td><strong>Hybrid capital</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Stage B1</td>
<td>GENPRU 2.2.115A R to GENPRU 2.2.117B R</td>
<td>(B1)</td>
</tr>
<tr>
<td>Stage B2</td>
<td>GENPRU 2.2.115D R to GENPRU 2.2.117B R</td>
<td>(B2)</td>
</tr>
<tr>
<td>Stage C</td>
<td>GENPRU 2.2.115F R to GENPRU 2.2.117B R</td>
<td>(C)</td>
</tr>
<tr>
<td><strong>Total tier one capital before deductions = A + B1 + B2 + C</strong></td>
<td></td>
<td>(D)</td>
</tr>
<tr>
<td><strong>Deductions from tier one capital</strong></td>
<td></td>
<td>(E)</td>
</tr>
<tr>
<td>Investments in own shares</td>
<td>None</td>
<td></td>
</tr>
<tr>
<td>Intangible assets</td>
<td>GENPRU 2.2.155 R</td>
<td></td>
</tr>
<tr>
<td>Excess of drawings over profits for partnerships, limited liability partnerships and sole traders</td>
<td>GENPRU 2.2.100 R; there is no related text for sole traders</td>
<td></td>
</tr>
<tr>
<td>Net losses on equities held in the available-for-sale financial asset category</td>
<td>GENPRU 2.2.185 R</td>
<td></td>
</tr>
<tr>
<td>(For certain limited purposes only certain additional deductions are made here)</td>
<td>GENPRU 2.2.239R (2) to GENPRU 2.2.239R (4)</td>
<td></td>
</tr>
<tr>
<td><strong>Total tier one capital after deductions = D-E</strong></td>
<td></td>
<td>(F)</td>
</tr>
<tr>
<td><strong>Upper tier two capital</strong></td>
<td></td>
<td>(G)</td>
</tr>
<tr>
<td>Perpetual cumulative preference shares</td>
<td>GENPRU 2.2.159 R to GENPRU 2.2.181 R</td>
<td></td>
</tr>
<tr>
<td>Perpetual subordinated debt</td>
<td>See previous entry</td>
<td></td>
</tr>
</tbody>
</table>
### The capital resources calculation for an investment firm that deducts illiquid assets

<table>
<thead>
<tr>
<th>Type of capital</th>
<th>Related text</th>
<th>Stage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Perpetual subordinated securities</td>
<td>See previous entry</td>
<td></td>
</tr>
<tr>
<td>Revaluation reserves</td>
<td>GENPRU 2.2.185 R</td>
<td></td>
</tr>
<tr>
<td>General/collectional provisions</td>
<td>GENPRU 2.2.187 R to GENPRU 2.2.189 R</td>
<td></td>
</tr>
<tr>
<td>Surplus provisions</td>
<td>GENPRU 2.2.190 R to GENPRU 2.2.193 R</td>
<td></td>
</tr>
</tbody>
</table>

#### Lower tier two capital

- Fixed term *preference shares*  
  - See previous entry
- Long term subordinated debt  
  - See previous entry
- Fixed term subordinated securities  
  - See previous entry

**Total tier two capital** = G+H

**Deductions from tier two capital**

(For certain limited purposes only certain additional deductions are made here)  
- GENPRU 2.2.239R (2) to GENPRU 2.2.239R (4)

**Total tier two capital after deductions** = I - J

**Total tier one capital plus tier two capital** = F+K

**Deductions from the totals of tier one and two**

- **Expected loss amounts and other negative amounts**  
  - GENPRU 2.2.236 R  
  - (Part 1 of stage M)
- **Securitisation positions**  
  - GENPRU 2.2.237 R  
  - (Part 2 of stage M)

**Total tier one capital plus tier two capital after deductions** = L-M

In calculating whether a firm’s capital resources exceed its capital resources requirement:

1. the credit risk capital component and the counterparty risk capital component; or
2. the base capital resources requirement; as the case may be, must be deducted here.

#### Upper tier three

- Short term subordinated debt  
  - GENPRU 2.2.241 R to GENPRU 2.2.245 R

#### Lower tier three

- Net interim *trading book profit and loss*  
  - GENPRU 2.2.246 R to GENPRU 2.2.249 R

**Total tier three capital** = O+P

**Total capital before deductions** = N+Q

**Deductions from total capital**

(S)
The capital resources calculation for an investment firm that deducts illiquid assets

<table>
<thead>
<tr>
<th>Type of capital</th>
<th>Related text</th>
<th>Stage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Illiquid assets</td>
<td>GENPRU 2.2.259 R to GENPRU 2.2.260 R</td>
<td></td>
</tr>
<tr>
<td>Free deliveries</td>
<td>BIPRU 14.4</td>
<td></td>
</tr>
</tbody>
</table>

Total capital after deductions = R - S

In calculating whether a firm's capital resources exceed its capital resources requirement, the market risk capital requirement and the fixed overheads requirement must be deducted here.

Note (1): Where the table refers to related text, it is necessary to refer to that text in order to understand fully what is included in the descriptions of capital items and deductions set out in the table.

Note (2): If the amount calculated at:
(a) stage N less the deductions in respect of the capital resources requirement made immediately following stage N; or
(b) stage T less the deductions in respect of the capital resources requirement made immediately following stages N and T;

is a negative number the firm's capital resources are less than its capital resources requirement.
## Capital resources table for a BIPRU firm with a waiver from consolidated supervision

### Part 1 of the capital resources calculation for an investment firm with a waiver from consolidated supervision

<table>
<thead>
<tr>
<th>Type of capital</th>
<th>Related text</th>
<th>Stage</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Core tier one capital</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Permanent share capital</td>
<td>GENPRU 2.2.83 R</td>
<td>(A)</td>
</tr>
<tr>
<td>Profit and loss account and other reserves (taking into account material interim net losses)</td>
<td>GENPRU 2.2.85 R to 2.2.90</td>
<td></td>
</tr>
<tr>
<td>Eligible partnership capital</td>
<td>GENPRU 2.2.93 R; GENPRU 2.2.95 R</td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Sole trader capital</td>
<td>None</td>
<td></td>
</tr>
<tr>
<td>share premium account</td>
<td>GENPRU 2.2.101 R</td>
<td></td>
</tr>
<tr>
<td>Externally verified interim net profits</td>
<td>GENPRU 2.2.102 R</td>
<td></td>
</tr>
<tr>
<td><strong>Hybrid capital</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Stage B1</td>
<td>GENPRU 2.2.115A R to GENPRU 2.2.117B R</td>
<td>(B1)</td>
</tr>
<tr>
<td>Stage B2</td>
<td>GENPRU 2.2.115D R to GENPRU 2.2.117B R</td>
<td>(B2)</td>
</tr>
<tr>
<td>Stage C</td>
<td>GENPRU 2.2.115F R to GENPRU 2.2.117B R</td>
<td>(C)</td>
</tr>
<tr>
<td><strong>Total tier one capital before deductions = A + B1 + B2 + C</strong></td>
<td></td>
<td>(D)</td>
</tr>
<tr>
<td><strong>Deductions from tier one capital</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Investments in own shares</td>
<td>None</td>
<td>(Part 1 of stage E)</td>
</tr>
<tr>
<td>Intangible assets</td>
<td>GENPRU 2.2.155 R</td>
<td></td>
</tr>
<tr>
<td>Excess of drawings over profits for partnerships, limited liability partnerships and sole traders</td>
<td>GENPRU 2.2.100 R; there is no related text for sole traders</td>
<td>(Part 1 of stage E)</td>
</tr>
<tr>
<td>Net losses on equities held in the available-for-sale financial asset category</td>
<td>GENPRU 2.2.185 R</td>
<td></td>
</tr>
<tr>
<td>(For certain limited purposes only certain additional deductions are made here. This line does not include material holdings.)</td>
<td>GENPRU 2.2.239R (2) to GENPRU 2.2.239R (4)</td>
<td></td>
</tr>
<tr>
<td>Material holdings falling into Note (4)</td>
<td>Note (4) of Part 2 of this table; GENPRU 2.2.208 R to GENPRU 2.2.215 R</td>
<td>(Part 2 of stage E)</td>
</tr>
</tbody>
</table>
### Part 1 of the capital resources calculation for an investment firm with a waiver from consolidated supervision

<table>
<thead>
<tr>
<th>Type of capital</th>
<th>Related text</th>
<th>Stage</th>
</tr>
</thead>
<tbody>
<tr>
<td>(For certain limited purposes only certain additional deductions of material holdings are made here)</td>
<td>Note (5) of Part 2 of this table; GENPRU 2.2.239R (2) to GENPRU 2.2.239R (4)</td>
<td>(Part 3 of stage E)</td>
</tr>
<tr>
<td>Total tier one capital after deductions = D-E</td>
<td>(F)</td>
<td></td>
</tr>
<tr>
<td>Upper tier two capital</td>
<td></td>
<td>(G)</td>
</tr>
<tr>
<td>Perpetual cumulative preference shares</td>
<td>GENPRU 2.2.159 R to GENPRU 2.2.181 R</td>
<td></td>
</tr>
<tr>
<td>Perpetual subordinated debt</td>
<td>See previous entry</td>
<td></td>
</tr>
<tr>
<td>Perpetual subordinated securities</td>
<td>See previous entry</td>
<td></td>
</tr>
<tr>
<td>Revaluation reserves</td>
<td>GENPRU 2.2.185 R</td>
<td></td>
</tr>
<tr>
<td>General/collective provisions</td>
<td>GENPRU 2.2.187 R to GENPRU 2.2.189 R</td>
<td></td>
</tr>
<tr>
<td>Surplus provisions</td>
<td>GENPRU 2.2.190 R to GENPRU 2.2.193 R</td>
<td></td>
</tr>
<tr>
<td>Lower tier two capital</td>
<td></td>
<td>(H)</td>
</tr>
<tr>
<td>Fixed term preference shares</td>
<td>GENPRU 2.2.159 R to GENPRU 2.2.174 R; GENPRU 2.2.194 R to GENPRU 2.2.196 R</td>
<td></td>
</tr>
<tr>
<td>Long term subordinated debt</td>
<td>See previous entry</td>
<td></td>
</tr>
<tr>
<td>Fixed term subordinated securities</td>
<td>See previous entry</td>
<td></td>
</tr>
<tr>
<td>Total tier two capital = G+H</td>
<td>(I)</td>
<td></td>
</tr>
<tr>
<td>Deductions from tier two capital</td>
<td></td>
<td>(J)</td>
</tr>
<tr>
<td>(For certain limited purposes only certain additional deductions are made here)</td>
<td>Note (5) of Part 2 of this table; GENPRU 2.2.239R (2) to GENPRU 2.2.239R (4)</td>
<td></td>
</tr>
<tr>
<td>Total tier two capital after deductions = I - J</td>
<td>(K)</td>
<td></td>
</tr>
<tr>
<td>Total tier one capital plus tier two capital = F+K</td>
<td>(L)</td>
<td></td>
</tr>
<tr>
<td>Deductions from the totals of tier one and two</td>
<td></td>
<td>(M)</td>
</tr>
<tr>
<td>Material holdings falling into Note (5)</td>
<td>Note (5) of Part 2 of this table; GENPRU 2.2.208 R to GENPRU 2.2.215 R</td>
<td>(Part 1 of stage M)</td>
</tr>
<tr>
<td>Contingent liabilities</td>
<td>Note (6) of Part 2 of this table</td>
<td></td>
</tr>
<tr>
<td>Expected loss amounts and other negative amounts</td>
<td>GENPRU 2.2.236 R</td>
<td></td>
</tr>
<tr>
<td>Securitisation positions</td>
<td>GENPRU 2.2.237 R</td>
<td></td>
</tr>
<tr>
<td>Reciprocal cross-holdings</td>
<td>GENPRU 2.2.217 R to GENPRU 2.2.220 R</td>
<td>(Part 2 of stage M)</td>
</tr>
<tr>
<td>Total tier one capital plus tier two capital after deductions = L-M</td>
<td>(N)</td>
<td></td>
</tr>
</tbody>
</table>

In calculating whether a firm’s capital resources exceed its capital resources requirement: (1) the credit risk capital component and the counterparty risk capital component; or
Part 1 of the capital resources calculation for an investment firm with a waiver from consolidated supervision

<table>
<thead>
<tr>
<th>Type of capital</th>
<th>Related text</th>
<th>Stage</th>
</tr>
</thead>
<tbody>
<tr>
<td>(2)the base capital resources requirement; as the case may be, must be deducted here.</td>
<td>GENPRU 2.2.241 R to GENPRU 2.2.245 R</td>
<td>(O)</td>
</tr>
<tr>
<td>Upper tier three</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Short term subordinated debt</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lower tier three</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net interim trading book profit and loss</td>
<td>GENPRU 2.2.246 R to GENPRU 2.2.249 R</td>
<td>(P)</td>
</tr>
<tr>
<td>Total tier three capital = O + P</td>
<td></td>
<td>(Q)</td>
</tr>
<tr>
<td>Total capital before deductions = N + Q</td>
<td></td>
<td>(R)</td>
</tr>
<tr>
<td>Deductions from total capital</td>
<td></td>
<td>(S)</td>
</tr>
<tr>
<td>Illiquid assets</td>
<td>GENPRU 2.2.259 R to GENPRU 2.2.260 R</td>
<td></td>
</tr>
<tr>
<td>Free deliveries</td>
<td>BIPRU 14.4</td>
<td></td>
</tr>
<tr>
<td>Total capital after deductions = R - S</td>
<td></td>
<td>(T)</td>
</tr>
</tbody>
</table>

In calculating whether a firm's capital resources exceed its capital resources requirement, the market risk capital requirement, and the fixed overheads requirement must be deducted here.

Part 2 of the capital resources calculation for an investment firm with a waiver from consolidated supervision

Note (1): Where the table refers to related text, it is necessary to refer to that text in order to understand fully what is included in the descriptions of capital items and deductions set out in the table.

Note (2): If the amount calculated at:
(a) stage N less the deductions in respect of the capital resources requirement made immediately following stage N; or
(b) stage T less the deductions in respect of the capital resources requirement made immediately following stages N and T;

is a negative number the firm's capital resources are less than its capital resources requirement.

Note (4): The material holdings that must be deducted at part 2 of stage E are material holdings issued by undertakings which would have been members of the firm's UK consolidation group or non-UK sub-group if the firm did not have an investment firm consolidation waiver if:

(1) in relation to a BIPRU firm, the holding forms part of the undertaking's tier one capital resources; or

(2) (subject to (3)) in relation to any other undertaking, the holding would form part of the undertaking's tier one capital resources if:
(a) that undertaking were a BIPRU firm with a Part 4A permission; and
(b) it had carried on all its business in the United Kingdom and had obtained whatever permissions for doing so are required under the Act; or

(3) in relation to any undertaking not falling within (1) and for which the methodology in (2) does not give an answer, the holding would form part of its tier one capital resources if the undertak-
Part 2 of the capital resources calculation for an investment firm with a waiver from consolidated supervision

| Note (5): The material holdings that must be deducted by a firm at part 3 of stage E and at stage J or at Part 1 of stage M are material holdings issued by undertakings which would have been members of that firm's UK consolidation group or non-UK sub-group if the firm did not have an investment firm consolidation waiver and which do not fall into Note (4). |

| Note (6): The contingent liabilities that must be deducted by a firm at Part 1 of stage M are any contingent liabilities which the firm has in favour of BIPRU firms, financial institutions, asset management companies and ancillary services undertakings which would have been members of the firm's UK consolidation group or non-UK sub-group if the firm did not have an investment firm consolidation waiver. |
Admissible assets in insurance
Guidance on applications for waivers relating to Implicit items
Chapter 3

Cross sector groups
3.1 Application

3.1.1 Unless otherwise stated, GENPRU 3.1 applies to every firm that is a member of a financial conglomerate other than:

(a) [deleted]
(b) [deleted]
(c) [deleted]
(d) an ICVC;
(e) a bank;
(f) a designated investment firm; and
(g) an insurer.

(1A) GENPRU 3.1 (except GENPRU 3.1.5R to GENPRU 3.1.12G) applies to each of the following firms that is a member of a financial conglomerate:

(a) a bank;
(b) a designated investment firm; and
(c) an insurer that is a “UK Solvency II firm” as defined in the PRA Rulebook: Glossary.

(2) GENPRU 3.1 does not apply to a firm with respect to a financial conglomerate of which it is a member if the interest of the financial conglomerate in that firm is no more than a participation.

(3) GENPRU 3.1.25 R (Capital adequacy requirements: high level requirement), and GENPRU 3.1.35 R (Risk concentration and intra group transactions: the main rule) do not apply with respect to a third-country financial conglomerate.

Purpose

3.1.2 GENPRU 3.1 implements requirements that correspond to the Financial Groups Directive. However, material on the following topics is to be found elsewhere in the Handbook as follows:

(1) further material on third-country financial conglomerates can be found in GENPRU 3.2;

(2) SUP 15.9 contains notification rules for members of financial conglomerates;
Section 3.1: Application

(3) material on reporting obligations can be found in SUP 16.12.32 R and SUP 16.12.33 R; and

(4) material on systems and controls in financial conglomerates can be found in SYSC 12.

Introduction: identifying a financial conglomerate

(1) In general the process in (2) to (8) applies for identifying financial conglomerates.

(2) The relevant competent authority that has authorised regulated entities should try to identify any consolidation group that is a financial conglomerate. If a competent authority is of the opinion that a regulated entity authorised by that competent authority is a member of a consolidation group which may be a financial conglomerate it should communicate its view to the other competent authority.

(3) A competent authority may start (as described in (2)) the process of deciding whether a group is a financial conglomerate even if it would not be the coordinator.

(4) A member of a group may also start that process by notifying one of the competent authorities that have authorised group members that its group may be a financial conglomerate, for example by notification under SUP 15.9.

(5) If a group member gives a notification in accordance with (4), that does not automatically mean that the group should be treated as a financial conglomerate. The process described in (6) to (9) still applies.

(6) The competent authority that would be coordinator will take the lead in establishing whether a group is a financial conglomerate once the process has been started as described in (2) and (3).

(7) The process of establishing whether a group is a financial conglomerate will normally involve discussions between the financial conglomerate and the competent authorities concerned.

(8) A financial conglomerate should be notified by its coordinator that it has been identified as a financial conglomerate and of the appointment of the coordinator. The notification should be given to the parent undertaking at the head of the group or, in the absence of a parent undertaking, the regulated entity with the largest balance sheet total in the most important financial sector. That notification does not of itself make a group into a financial conglomerate; whether or not a group is a financial conglomerate is governed by the definition of financial conglomerate as set out in GENPRU 3.1.

(9) GENPRU 3 Annex 3 is a questionnaire (together with its explanatory notes) that the FCA asks groups that may be financial conglomerates to fill out in order to decide whether or not they are.

(10) If a mixed financial holding company is subject to equivalent provisions under the UK prudential sectoral legislation in relation to
If a mixed financial holding company is subject to equivalent provisions under this Chapter and under UK prudential sectoral legislation in relation to the insurance sector as and the FCA is the coordinator, the FCA may, on application by the firm, disapply such provisions of the UK prudential sectoral legislation with regard to that undertaking which are considered by the FCA as equivalent to those applying to the firm under GENPRU 3.1.

[Note: article 120(2) of CRD]

Introduction: The role of other competent authorities

A lead supervisor (called the coordinator) is appointed for each financial conglomerate. The definition of coordinator in the Financial Groups Directive Regulations describes the criteria for deciding which competent authority is appointed as coordinator.

[Note: Article 10 and 11 of the Financial Groups Directive]

Definition of financial conglomerate: basic definition

A financial conglomerate means a consolidation group that is identified as a financial conglomerate in accordance with the decision tree in GENPRU 3 Annex 4.

Definition of financial conglomerate: sub-groups

A consolidation group is not prevented from being a financial conglomerate because it is part of a wider:

(1) consolidation group; or

(2) financial conglomerate; or

(3) group of persons linked in some other way.

Definition of financial conglomerate: the financial sectors: general

For the purpose of the definition of financial conglomerate, there are two financial sectors as follows:

(1) the banking sector and the investment services sector, taken together; and

(2) the insurance sector.
(1) This rule applies for the purpose of the definition of financial conglomerate and the financial conglomerate definition decision tree.

(1A) In determining the investment services sector for the purpose of identifying a financial conglomerate in the boxes entitled Threshold Test 1, Threshold Test 2 and Threshold Test 3 in the financial conglomerate definition decision tree, any investment firm that does not fall within the definition of article 4(1)(2) of the UK CRR is excluded.

(2) Any mixed financial holding company is considered to be outside the overall financial sector for the purpose of the tests set out in the boxes titled Threshold Test 1, Threshold Test 2 and Threshold Test 3 in the financial conglomerate definition decision tree.

(3) Determining whether the tests set out in the boxes titled Threshold Test 2 and Threshold Test 3 in the financial conglomerate definition decision tree are passed is based on considering the consolidated and/or aggregated activities of the members of the consolidation group within the insurance sector and the consolidated and/or aggregated activities of the members of the consolidation group within the banking sector and the investment services sector.

Definition of financial conglomerate: adjustment of the percentages

Once a financial conglomerate has become a financial conglomerate and subject to supervision in accordance with this chapter, the figures in the financial conglomerate definition decision tree are altered as follows:

(1) the figure of 40% in the box titled Threshold Test 1 is replaced by 35%;

(2) the figure of 10% in the box titled Threshold Test 2 is replaced by 8%; and

(3) the figure of six billion Euro in the box titled Threshold Test 3 is replaced by five billion Euro.

The alteration in GENPRU 3.1.9 R only applies to a financial conglomerate during the period that:

(1) begins when the financial conglomerate would otherwise have stopped being a financial conglomerate because it does not meet one of the unaltered thresholds referred to in GENPRU 3.1.9 R; and

(2) covers the three years following that date.

Definition of financial conglomerate: balance sheet totals

The calculations referred to in the financial conglomerate definition decision tree regarding the balance sheet must be made on the basis of the aggregated balance sheet total of the members of the consolidation group, according to their annual accounts. For the purposes of this calculation, undertakings in which a participation is held must be taken into account as regards the amount of their balance sheet total corresponding to the
aggregated proportional share held by the consolidation group. However, where consolidated accounts are available, they must be used instead of aggregated accounts.

**Definition of financial conglomerate: solvency requirement**

3.1.12 R

The solvency and capital adequacy requirements referred to in the financial conglomerate definition decision tree must be calculated in accordance with the provisions of the relevant sectoral rules.

**Definition of financial conglomerate: discretionary changes to the definition**

3.1.13 G

Regulation 16 to 20, 21 and 24 of the financial groups directive regulations allow competent authorities, on a case by case basis, to:

1. change the definition of financial conglomerate and the obligations applying with respect to a financial conglomerate (which would include, where the appropriate regulator would be the coordinator under GENPRU 3.1.3G (6), permitting firms to apply, on an annual basis and subject to publication and notification to the competent authority, for a group of which it is a member not to be regarded as a financial conglomerate on the basis of regulation 16 of the financial groups directive regulations (for a group that, in terms of the tests in GENPRU 3 Annex 4, does not meet Threshold Test 2 but meets Threshold Test 3) or regulation 17 of the financial groups directive regulations (for a group that, in terms of the tests in GENPRU 3 Annex 4, meets Threshold Test 2 but not Threshold Test 3);

2. apply the scheme in the financial groups directive regulations to UK regulated entities in specified kinds of group structures that do not come within the definition of financial conglomerate; and

3. exclude a particular entity in the scope of capital adequacy requirements that apply with respect to a financial conglomerate.

**Capital adequacy requirements: introduction**

3.1.14 G

The capital adequacy provisions of GENPRU 3.1 are designed to be applied to EEA-based financial conglomerates.

3.1.15 G

GENPRU 3.1.25 R is a high level capital adequacy rule. It applies whether or not the FCA is the coordinator of the financial conglomerate concerned.

3.1.16 G

GENPRU 3.1.29 R to GENPRU 3.1.31 R and GENPRU 3 Annex 1 apply the detailed capital adequacy requirements that correspond with the Financial Groups Directive. They only deal with a financial conglomerate for which the FCA is the coordinator. If another competent authority is coordinator of a financial conglomerate, those rules do not apply with respect to that financial conglomerate and instead that coordinator will be responsible for implementing those detailed requirements.
Annex I of the *Financial Groups Directive* laid down three methods for calculating capital adequacy at the level of a *financial conglomerate*. Those three methods are implemented as follows:

1. Method 1 calculates capital adequacy using accounting consolidation. It is implemented by GENPRU 3.1.29 R to GENPRU 3.1.31 R and Part 1 of GENPRU 3 Annex 1.

2. Method 2 calculates capital adequacy using a deduction and aggregation approach. It is implemented by GENPRU 3.1.29 R to GENPRU 3.1.31 R and Part 2 of GENPRU 3 Annex 1.

3. [deleted]

4. Method 3 consists of a combination of Methods 1 and 2 and would be implemented by means of a requirement.

Paragraph 5.7 of GENPRU 3 Annex 1 (Capital adequacy calculations for financial conglomerates) deals with a case in which there are no capital ties between entities in a *financial conglomerate*. In particular, the *FCA*, after consultation with the other *competent authority* and in accordance with this chapter, will determine which proportional share of a solvency deficit in such an entity will have to be taken into account, bearing in mind the liability to which the existing relationship gives rise.

The method to be applied may be decided by the *coordinator* after consultation with the other *competent authority* and the *financial conglomerate* itself. Where the *FCA* acts as coordinator, the *financial conglomerate* itself may choose which of Method 1 or Method 2 it will apply, unless the *firm* is subject to a requirement obliging the *firm* to apply a particular method.

A *firm* that is a member of a *financial conglomerate* must at all times have capital resources of such an amount and type that results in the capital resources of the *financial conglomerate* taken as a whole being adequate.
(2) This rule does not apply with respect to any financial conglomerate until notification has been made that it has been identified as a financial conglomerate as contemplated by regulation 2 of the Financial Groups Directive Regulations.

3.1.26 [deleted]

3.1.27 [deleted]

3.1.28 (1) [deleted]

(2) [deleted]

Capital adequacy requirements: application of Method 1 or 2

3.1.29 If, with respect to a firm and a financial conglomerate of which it is a member, this rule applies under GENPRU 3.1.29A R to the firm with respect to that financial conglomerate as described in GENPRU 3.1.30 R, the firm must at all times have capital resources of an amount and type that ensures that the conglomerate capital resources of that financial conglomerate at all times equal or exceed its conglomerate capital resources requirement.

3.1.29A GENPRU 3.1.29 R applies to a firm with respect to the financial conglomerate of which it is a member if notification has been made in accordance with regulation 2 of the Financial Groups Directive Regulations that the financial conglomerate is a financial conglomerate and that the FCA is coordinator of that financial conglomerate.

Capital adequacy requirements: use of requirement to apply Method 1 or 2 for calculating capital adequacy

3.1.30 If GENPRU 3.1.29 R (application of Method 1 or 2) applies to a firm with respect to the financial conglomerate of which it is a member, then with respect to the firm and the financial conglomerate:

(1) the definitions of conglomerate capital resources and conglomerate capital resources requirement that apply for the purposes of that rule are the ones from whichever of Part 1 or Part 2 of GENPRU 3 Annex 1 the firm has indicated to the FCA it will apply, unless the firm is subject to a requirement obliging the firm to apply a specific part of GENPRU 3 Annex 1, in which case GENPRU 3.1.31 R will apply; and

(2) the firm must indicate to the FCA in advance which Part of GENPRU 3 Annex 1 the firm intends to apply.
If GENPRU 3.1.29 R (application of Method 1 or 2) applies to a firm with respect to a financial conglomerate of which it is a member, and the firm is subject to a requirement obliging the firm to apply a specific part of GENPRU 3 Annex 1, the definitions of conglomerate capital resources and conglomerate capital resources requirement that apply for the purposes of that rule are the ones from whichever of Part 1 or Part 2 of GENPRU 3 Annex 1 is specified in the requirement.

**Risk concentration and intra-group transactions: introduction**

GENPRU 3.1.35 R implements requirements that correspond to Article 7(4) and Article 8(4) of the Financial Groups Directive that where a financial conglomerate is headed by a mixed financial holding company, the sectoral rules regarding risk concentration and intra-group transactions of the most important financial sector in the financial conglomerate, if any, shall apply to that sector as a whole, including the mixed financial holding company.

The FCA may, on a case by case basis, require the application at the level of the financial conglomerate of the provisions of the sectoral rules on risk concentrations and intra-group transactions.

(Note: Article 7(3), Article 8(3) and Annex II of the Financial Groups Directive)

**Risk concentration and intra-group transactions: application**

GENPRU 3.1.35 R applies to a firm with respect to a financial conglomerate of which it is a member if the financial conglomerate is headed by a mixed financial holding company.

**Risk concentration and intra group transactions: the main rule**

A firm must ensure that the sectoral rules regarding risk concentration and intra-group transactions of the most important financial sector in the financial conglomerate referred to in GENPRU 3.1.34 R are complied with with respect to that financial sector as a whole, including the mixed financial holding company. The sectoral rules for these purposes are those identified in the table in GENPRU 3.1.36 R.

**Risk concentration and intra-group transactions: Table of applicable sectoral rules**

Table: application of sectoral rules

This table belongs to GENPRU 3.1.35 R

<table>
<thead>
<tr>
<th>The most important financial sector</th>
<th>Applicable sectoral rules</th>
</tr>
</thead>
<tbody>
<tr>
<td>Risk concentration</td>
<td>Intra-group transactions</td>
</tr>
<tr>
<td>Banking and investment services sector</td>
<td>the UK CRR</td>
</tr>
<tr>
<td>Insurance sector</td>
<td>PRA Rulebook: Solvency II Firms Group Supervision 16.1</td>
</tr>
</tbody>
</table>
**The financial sectors: asset management companies and alternative investment fund managers**

1. This rule deals with the inclusion of an asset management company or an alternative investment fund manager that is a member of a financial conglomerate in the scope of regulation of financial conglomerates.

   [Note: Articles 30 and 30a of the Financial Groups Directive]

2. An asset management company or an alternative investment fund manager is in the overall financial sector and is a regulated entity for the purpose of:
   (a) GENPRU 3.1.29 R to GENPRU 3.1.36 R;
   (b) GENPRU 3 Annex 1 (Capital adequacy calculations for financial conglomerates) and GENPRU 3 Annex 2 (Prudential rules for third country groups); and
   (c) any other provision of the Handbook relating to the supervision of financial conglomerates.

3. In the case of a financial conglomerate for which the FCA is the coordinator, all asset management companies and all alternative investment fund managers must be allocated to one financial sector to which they belong for the purposes in (2), being either the investment services sector or the insurance sector. But if that choice...
has not been made in accordance with (4) and notified to the FCA in accordance with (4)(d), an asset management company or an alternative investment fund manager must be allocated to the smallest financial sector.

(4) The choice in (3):
   (a) must be made by the undertaking in the financial conglomerate that is:
       (i) the parent undertaking at the head of the group or,
       (ii) in the absence of a parent undertaking, the regulated entity with the largest balance sheet total in the most important financial sector;
   (b) applies to all asset management companies and all alternative investment fund managers that are members of the financial conglomerate from time to time;
   (c) cannot be changed; and
   (d) must be notified to the FCA as soon as reasonably practicable after the notification in (4)(a).

   [Note: Article 4(2) of the Financial Groups Directive]

(5) This rule applies even if:
   (a) a UCITS management company is an IFPRU investment firm; or
   (b) an asset management company or alternative investment fund manager is an investment firm.
3.2 Third-country groups

Application

3.2.1 GENPRU 3.2 applies to every firm that is a member of a third-country group. But it does not apply to:

(1) [deleted]
(2) [deleted]
(3) [deleted]
(4) an ICVC; or
(5) a bank; or
(6) a designated investment firm; or
(7) an insurer.

3.2.1A GENPRU 3.2.9R (Supervision by analogy: rules for third-country banking and investment groups) applies in relation to the following:

(1) a CAD investment firm; and
(2) an investment firm that falls within the definition of “investment firm” in article 4(1)(2) of the UK CRR.

Purpose

3.2.2 GENPRU 3.2 implements requirements that correspond in part to article 18 of the Financial Groups Directive, article 127 of the CRD and (in relation to BIPRU firms) article 143 of the BCD.

Equivalence

3.2.3 The first question that must be asked about a third-country group is whether the UK regulated entities in that third-country group are subject to supervision by a third-country competent authority, which is equivalent to that provided for in GENPRU 3 (in the case of a financial conglomerate) or the UK prudential sectoral legislation for the banking sector or the investment services sector (in the case of a banking and investment group).
Other methods: General

3.2.4 **G** If the supervision of a third-country group by a third-country competent authority does not meet the equivalence test referred to in ■ GENPRU 3.2.3 G, the methods set out in the UK provisions which implemented the CRD and UK CRR will apply or the FCA may apply other methods that ensure appropriate supervision of the UK regulated entities in that third-country group in accordance with the aims of supplementary supervision in ■ GENPRU 3 or consolidated supervision under the applicable UK prudential sectoral legislation.

Supervision by analogy: introduction

3.2.5 **G** If the supervision of a third-country group by a third-country competent authority does not meet the equivalence test referred to in ■ GENPRU 3.2.3 G, the FCA may, rather than take the measures described in ■ GENPRU 3.2.4 G, apply, by analogy, the provisions concerning supplementary supervision in ■ GENPRU 3 or, as applicable, consolidated supervision under the applicable UK prudential sectoral legislation, to the UK regulated entities in the banking sector, investment services sector and (in the case of a financial conglomerate) insurance sector.

3.2.6 **G** The FCA believes that it will only be right to adopt the option in ■ GENPRU 3.2.5 G in response to very unusual group structures.

3.2.7 **G** ■ GENPRU 3.2.8 R and ■ GENPRU 3.2.9 R and ■ GENPRU 3 Annex 2 set out rules to deal with the situation covered in ■ GENPRU 3.2.5 G. Those rules do not apply automatically. Instead, they can only be applied with respect to a particular third-country group through the Part 4A permission of a in that third-country group.

Supervision by analogy: rules for third-country conglomerates

3.2.8 **R** If the Part 4A permission of a firm contains a requirement obliging it to comply with this rule with respect to a third-country financial conglomerate of which it is a member, it must comply, with respect to that third-country financial conglomerate, with the rules in Part 1 of ■ GENPRU 3 Annex 2, as adjusted by Part 3 of that annex.

Supervision by analogy: rules for third-country banking and investment groups

3.2.9 **R** If the Part 4A permission of a firm contains a requirement obliging it to comply with this rule with respect to a third-country banking and investment group of which it is a member, it must comply, with respect to that third-country banking and investment group, with the rules in Part 2 of ■ GENPRU 3 Annex 2, as adjusted by Part 3 of that annex.
# Capital adequacy calculations for financial conglomerates (GENPRU 3.1.29R)

1 Table: PART 1: Method 1 (Accounting Consolidation Method)

<table>
<thead>
<tr>
<th>Capital resources</th>
<th>1.1</th>
<th>The conglomerate capital resources of a financial conglomerate calculated in accordance with this Part are the capital of that financial conglomerate, calculated on an accounting consolidation basis, that qualifies under paragraph 1.2.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1.2</td>
<td>The elements of capital that qualify for the purposes of paragraph 1.1 are those that qualify in accordance with the applicable sectoral rules, in accordance with the following:</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(1) the conglomerate capital resources requirement is divided up in accordance with the contribution of each financial sector to it; and</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(2) the portion of the conglomerate capital resources requirement attributable to a particular financial sector must be met by capital resources that are eligible in accordance with the applicable sectoral rules for that financial sector.</td>
</tr>
<tr>
<td>Capital resources requirement</td>
<td>1.3</td>
<td>The conglomerate capital resources requirement of a financial conglomerate calculated in accordance with this Part is equal to the sum of the capital adequacy and solvency requirements for each financial sector calculated in accordance with the applicable sectoral rules for that financial sector.</td>
</tr>
<tr>
<td>Consolidation</td>
<td>1.4</td>
<td>The information required for the purpose of establishing whether or not a firm is complying with GENPRU 3.1.29R (insofar as the definitions in this Part are applied for the purpose of that rule) must be based on the consolidated accounts of the financial conglomerate, together with such other sources of information as appropriate.</td>
</tr>
<tr>
<td></td>
<td>1.5</td>
<td>The applicable sectoral rules that are applied under this Part are the applicable sectoral consolidation rules. Other applicable sectoral rules must be applied if required.</td>
</tr>
</tbody>
</table>

2 Table: PART 2: Method 2 (Deduction and aggregation Method)

<table>
<thead>
<tr>
<th>Capital resources</th>
<th>2.1</th>
<th>The conglomerate capital resources of a financial conglomerate calculated in accordance with this Part are equal to the sum of the following amounts (so far as they qualify under paragraph 2.3) for each member of the overall financial sector:</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>(1) (for the person at the head of the financial conglomerate) its solo capital resources;</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(2) (for any other member):</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(a) its solo capital resources; less</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(b) the book value of the financial conglomerate’s investment in that member, to the extent not already deducted in the calculation of the solo capital resources for:</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(i) the person at the head of the financial conglomerate; or</td>
</tr>
<tr>
<td>Section</td>
<td>Description</td>
<td></td>
</tr>
<tr>
<td>---------</td>
<td>-------------</td>
<td></td>
</tr>
<tr>
<td>2.2</td>
<td>The deduction in paragraph 2.1(2) must be carried out separately for each type of capital represented by the <em>financial conglomerate’s</em> investment in the member concerned.</td>
<td></td>
</tr>
<tr>
<td>2.3</td>
<td>The elements of capital that qualify for the purposes of paragraph 2.1 are those that qualify in accordance with the applicable sectoral rules. In particular, the portion of the conglomerate capital resources requirement attributable to a particular member of a financial sector must be met by capital resources that would be eligible under the sectoral rules that apply to the calculation of its solo capital resources.</td>
<td></td>
</tr>
<tr>
<td>Capital resources requirement</td>
<td>2.4</td>
<td>The conglomerate capital resources requirement of a financial conglomerate calculated in accordance with this Part is equal to the sum of the solo capital resources requirement for each member of the financial conglomerate that is in the overall financial sector.</td>
</tr>
<tr>
<td>Partial inclusion</td>
<td>2.5</td>
<td>The capital resources and capital resources requirements of a member of the financial conglomerate in the overall financial sector must be included proportionally. If however the member is a subsidiary undertaking and it has a solvency deficit, they must be included in full.</td>
</tr>
<tr>
<td>Accounts</td>
<td>2.6</td>
<td>The information required for the purpose of establishing whether or not a firm is complying with GENPRU 3.1.29 R (insofar as the definitions in this Part are applied for the purpose of that rule) must be based on the individual accounts of members of the financial conglomerate, together with such other sources of information as appropriate.</td>
</tr>
</tbody>
</table>

---

(1) This paragraph sets out how to determine the category of financial conglomerate.

(2) If there is a UK regulated entity at the head of the financial conglomerate, then:

(a) if that entity is in the banking sector or the investment services sector, the financial conglomerate is a banking and investment services conglomerate; or

(b) if that entity is in the insurance sector, the financial conglomerate is an insurance conglomerate.

(3) If (2) does not apply and the most important financial sector is the banking and investment services sector, it is a banking and investment services conglomerate.

(4) If (2) and (3) does not apply, it is an insurance conglomerate.
A mixed financial holding company must be treated in the same way as:

1. a financial holding company (if Part One, Title II, Chapter 2 of the UK CRR and the PRA Rulebook : Groups Part) are applied; or
2. an insurance holding company (if the rules in PRA Rulebook: Solvency II Firms: Group Supervision are applied).

Capital may not be included in a firm’s conglomerate capital resources under GENPRU 3.1.29 R if the effectiveness of the transferability and availability of the capital across the different members of the financial conglomerate is insufficient, given the objectives of the capital adequacy rules for financial conglomerates.

(Note: third unnumbered sub-paragraph of paragraph 2(ii) of Annex I of the Financial Groups Directive (Technical principles))

Capital must not be included in a firm’s conglomerate capital resources under GENPRU 3.1.29 R if:

1. it would involve double counting or multiple use of the same capital; or
2. it results from any inappropriate intra-group creation of capital.

The solvency requirements for each different financial sector represented in a financial conglomerate required by GENPRU 3.1.29 R must be covered by own funds elements in accordance with the corresponding applicable sectoral rules.

If there is a deficit of own funds at the financial conglomerate level, only cross sectoral capital (as referred to in that sub-paragraph) shall qualify for verification of compliance with the additional solvency requirement required by GENPRU 3.1.29 R.

(Note: second sub-paragraph of paragraph 2(ii) of Section I of Annex I of the Financial Groups Directive)

The following adjustments apply to the applicable sectoral rules as they are applied by the rules in this annex.

1. (deleted)
2. If any of those rules would otherwise not apply to a situation in which they are applied by GENPRU 3 Annex 1, those rules nevertheless still apply (and in particular, any of those rules that would otherwise have the effect of disapplying consolidated supervision do not apply).
3. (If it would not otherwise have been included) an ancillary insurance services undertaking is included in the insurance sector.
4. The scope of those rules is amended so as to remove restrictions relating to where members of the financial conglomerate are incorporated or have their head office, so that the scope covers every member of the financial conglomerate that would have been included in the scope of...
those rules if those members had their head offices in the UK.

(5) (For the purposes of Parts 1 and 2) those rules must be adjusted, if necessary, when calculating the capital resources, capital resources requirements or solvency requirements for a particular financial sector to exclude those for a member of another financial sector.

(6) Any waiver, approval or permission granted to a member of the financial conglomerate under those rules does not apply for the purposes of this annex.

| Application of sectoral rules: Insurance sector | 5.5 |
| Application of sectoral rules: Banking sector and investment services sector | 5.6 |

In relation to a BIPRU firm that is a member of a financial conglomerate where there are no credit institutions or investment firms, the following adjustments apply to the applicable sectoral rules for the banking sector and the investment services sector as they are applied by the rules in this annex.

(1) References in those rules to non-UK sub-groups – if applicable – do not apply.

(3) Any investment firm consolidation waivers granted to members of the financial conglomerate do not apply.

(4) (For the purposes of Parts 1 and 2), without prejudice to the application of requirements in BIPRU 8 preventing the use of an advanced prudential calculation approach on a consolidated basis, any advanced prudential calculation approach permission that applies for the purpose of BIPRU 8 does not apply.

(5) (For the purposes of Parts 1 and 2), BIPRU 8.5.9 R and BIPRU 8.5.10 R do not apply.

(6) (For the purposes of Part 3), where the financial conglomerate does not include a credit institution, the method in GENPRU 2 Annex 4 must be used for calculating the capital resources and BIPRU 8.6.8 R does not apply.
(Other than as above) the UK CRR and the provisions which implemented the CRD apply for the banking sector and the investment services sector.

(1) This rule deals with a financial conglomerate in which some of the members are not linked by capital ties at the time of the notification referred to in GENPRU 3.1.29A R (Capital adequacy requirements: Application of Method 1 or 2).

[deleted]

[deleted]

(4) If:

[deleted]

(b) GENPRU 3.1.29 R (Capital adequacy requirements: Application of Method 1 or 2) applies with respect to a financial conglomerate falling into (1);

then:

(c) the treatment of the links in (1) (including the treatment of any solvency deficit) is as provided for in whichever of Part 1 or Part 2 of GENPRU 3 Annex 1 the firm has, under GENPRU 3.1.30 R, indicated to the FCA it will apply or, if applicable, in the requirement referred to in GENPRU 3.1.31 R; and

(d) GENPRU 3.1.29 R applies even if the applicable sectoral rules do not deal with how undertakings not linked by capital ties are to be dealt with for the purposes of consolidated supervision.

[deleted]

9 Table: PART 6: Definitions used in this Annex

<table>
<thead>
<tr>
<th>Defining the financial sectors</th>
<th>6.1</th>
</tr>
</thead>
<tbody>
<tr>
<td>For the purposes of Parts 1 and 2 of this annex:</td>
<td></td>
</tr>
<tr>
<td>(1) an asset management company is allocated in accordance with GENPRU 3.1.39 R; an alternative investment fund manager is allocated in accordance with GENPRU 3.1.39 R; and</td>
<td></td>
</tr>
<tr>
<td>(3) a mixed financial holding company must be treated as being a member of the most important financial sector.</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Solo capital resources requirement: Banking sector and investment service sector</th>
<th>6.2</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) The solo capital resources requirement of an undertaking in the banking sector or the investment services sector must be calculated in accordance with this rule, subject to paragraph 6.6.</td>
<td></td>
</tr>
<tr>
<td>(2) The solo capital resources requirement of a building society is its own funds requirements.</td>
<td></td>
</tr>
<tr>
<td>(3) The solo capital resources requirement of an electronic money institution is the capital resources requirement that applies to it under the Electronic Money Regulations.</td>
<td></td>
</tr>
<tr>
<td>(4) If there is a credit institution in the financial conglomerate, the solo capital resources requirement for any undertaking in the banking sector or the investment services sector is, subject to (2) and (3), calculated in accordance with the UK CRR for calculating the own funds requirements of a bank.</td>
<td></td>
</tr>
<tr>
<td>(5) If:</td>
<td></td>
</tr>
<tr>
<td>(a) the financial conglomerate does not include a credit institution;</td>
<td></td>
</tr>
<tr>
<td>(b) there is at least one investment firm in the financial conglomerate; and</td>
<td></td>
</tr>
<tr>
<td>(c) all the investment firms in the financial conglomerate...</td>
<td></td>
</tr>
</tbody>
</table>
conglomerate are limited licence firms or limited activity firms; the solo capital resources requirement for any undertaking in the banking sector or the investment services sector is calculated in accordance with the UK CRR for calculating the own funds requirements of:

(i) (if there is a limited activity firm in the financial conglomerate), an IFPRU limited activity firm; or

(ii) (in any other case), an IFPRU limited licence firm.

(6) If:

(a) the financial conglomerate does not include a credit institution; and

(b) (5) does not apply;

the solo capital resources requirement for any undertaking in the banking sector or the investment services sector is calculated in accordance with the UK CRR for calculating the own funds requirements of a full-scope IFPRU investment firm.

(7) In relation to a BIPRU firm that is a member of a financial conglomerate where there are no credit institutions or investment firms, any capital resources requirements calculated under a BIPRU TP may be used for the purposes of the solo capital resources requirement in this rule in the same way that the capital resources requirements can be used under BIPRU 8.

Solo capital resources requirement: application of rules

6.3 Any exemption that would otherwise apply under any rules applied by paragraph 6.2 do not apply for the purposes of this Annex.

Solo capital resources requirement: Insurance sector

6.4 (1) The solo capital resources requirement of an undertaking in the insurance sector must be calculated in accordance with this rule. The solo capital resources requirement of an undertaking in the insurance sector is:

(a) in respect of a UK Solvency II firm, the SCR;

(b) [deleted]

(c) in respect of a third country insurance undertaking or third country reinsurance undertaking to which the PRA Rulebook: Solvency II Firms: Group Supervision, 10.4(2) applies, the equivalent of the SCR as calculated in accordance with the applicable requirements in that third country; and

(d) in respect of any undertaking which is not within (a) to (c), the capital resources requirement calculated according to the rules for the calculation of the solo capital resources requirement applicable to that undertaking for the purposes of the calculation referred to in the PRA Rulebook: Solvency II Firms: Group Supervision and Chapter 1 of Title II of the delegated acts, or if no rules are applicable for that calculation under Group Supervision and Chapter 1 of Title II of the delegated acts, in accordance with the SCR Rules.
For the purpose of this Part as it applies in relation to GENPRU 3.1, the following expressions bear the same meaning as defined in the PRA Rulebook: Glossary:

(i) “UK Solvency II firm”;
(ii) [deleted]
(iii) “delegated acts”;
(iv) “third country insurance undertaking”;
(v) “third country reinsurance undertaking”; and
(vi) “SCR Rules”.

Solo capital resources requirement: EEA firms in the banking sector or investment services sector

6.5 [deleted]

Solo capital resources requirement: non-UK firms subject to equivalent regimes in the banking sector or investment services sector

6.6 The solo capital resources requirement for a recognised third country credit institution or a recognised third country investment firm is the amount of capital resources that it is obliged to hold under the sectoral rules for its financial sector that apply to it in the state or territory in which it has its head office provided that:

(1) there is no reason for the firm applying the rules in this annex to believe that the use of those sectoral rules would produce a lower figure than would be produced under paragraph 6.2; and

(2) paragraph 6.3 applies to the entity and those sectoral rules.

Solo capital resources requirement: mixed financial holding company

6.7 The solo capital resources requirement of a mixed financial holding company is a notional capital requirement. It is the capital adequacy requirement that applies to regulated entities in the most important financial sector under the table in paragraph 6.10.

Reference to “rules”

6.7A A reference to “rules” in this annex includes any onshored regulations that are relevant to the purpose of which “rules” as used refers to.

10 Table

<table>
<thead>
<tr>
<th>Solo capital resources requirement: the insurance sector</th>
<th>6.8 References to capital requirements in the provisions of GENPRU 3 Annex 1 defining solo capital resources requirement must be interpreted in accordance with paragraph 5.4.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Applicable sectoral consolidation rules</td>
<td>6.9 The applicable sectoral consolidation rules for a financial sector are the sectoral rules about capital adequacy and solvency on a consolidated basis that are applied in the table in paragraph 6.10.</td>
</tr>
</tbody>
</table>

11 Table: Paragraph 6.10: Application of sectoral consolidation rules

<table>
<thead>
<tr>
<th>Financial sector</th>
<th>Sectoral rules</th>
</tr>
</thead>
<tbody>
<tr>
<td>Banking sector</td>
<td>Part One, Title II, Chapter 2 of the UK CRR and IFPRU 8.1.</td>
</tr>
<tr>
<td>Insurance sector</td>
<td>PRA Rulebook: Solvency II Firms: Group Supervision.</td>
</tr>
<tr>
<td>Investment services sector</td>
<td>(in relation to an IFPRU investment firm which is a member of a financial conglomerate for which the PRA is the co-ordinator) Part One, Title II, Chapter 2 of the UK CRR and the PRA Rulebook;</td>
</tr>
<tr>
<td></td>
<td>(in relation to a designated investment firm or an IFPRU investment firm which is a member of a financial conglomerate)</td>
</tr>
<tr>
<td>Financial sector</td>
<td>Sectoral rules</td>
</tr>
<tr>
<td>------------------</td>
<td>----------------</td>
</tr>
<tr>
<td></td>
<td>for which the FCA is the coordinator) Part One, Title II, Chapter 2 of the UK CRR and IFPRU 8.1;</td>
</tr>
<tr>
<td></td>
<td>(in relation to a BIPRU firm that is a member of a financial conglomerate where there are no credit institutions or investment firms for which the FCA is the coordinator) BIPRU 8 and BIPRU TP.</td>
</tr>
</tbody>
</table>

12 Table:

| Part 5 | 1 | This Part 6 is subject to Part 5 of this Annex. |
Prudential rules for third country groups (GENPRU 3.2.8R to GENPRU 3.2.9R)

1 Table: PART 1: Third-country financial conglomerates

1.1 This Part of this annex sets out the rules with which a firm must comply under GENPRU 3.2.8 R with respect to a financial conglomerate of which it is a member.

1.2 A firm must comply, with respect to the financial conglomerate referred to in paragraph 1.1, with GENPRU 3.1.29 R as applied under paragraph 1.3.

1.3 For the purposes of paragraph 1.2:

(1) [deleted]

(2) the definitions of conglomerate capital resources and conglomerate capital resources requirement that apply for the purposes of that rule are the ones from whichever of Part 1 or Part 2 of GENPRU 3 Annex 1 is specified in the requirement referred to in GENPRU 3.2.8 R; and

(3) the rules so applied (including those in GENPRU 3 Annex 1) are adjusted in accordance with paragraph 3.1.

1.4 If the condition in Articles 7(4) and 8(4) of the Financial Groups Directive is satisfied (the financial conglomerate is headed by a mixed financial holding company) with respect to the financial conglomerate referred to in paragraph 1.1 the firm must also comply with GENPRU 3.1.35 R (as adjusted in accordance with paragraph 3.1) with respect to that financial conglomerate.

1.5 A firm must comply with the following with respect to the financial conglomerate referred to in paragraph 1.1:

(1) SYSC 12 (as it applies to financial conglomerates and as adjusted under paragraph 3.1); and

(2) GENPRU 3.1.25 R.

2 Table: PART 2: Third-country banking and investment groups

2.1 This Part of this annex sets out the rules with which a firm must comply under GENPRU 3.2.9 R with respect to a third-country banking and investment group of which it is a member.

2.2 A firm must comply with one of the sets of rules specified in paragraph 2.3 as adjusted under paragraph 3.1 with respect to the third-country banking and investment group referred to in paragraph 2.1.

2.3 The rules referred to in paragraph 2.2 are:

(1) the applicable sectoral consolidation rules in paragraph 6.10 of GENPRU 3 Annex 1.

2.4 The set of rules from paragraph 2.3 that apply with respect to a particular third-country banking and investment group (as referred to in paragraph 2.1) are those that would apply if they were adjusted in accordance with paragraph 3.1.
2.5 The sectoral rules applied by Part 2 of this annex cover all prudential rules applying on a consolidated basis including those relating to large exposures.

2.6 A firm must comply with SYSC 12 (as it applies to banking and investment groups and as adjusted under paragraph 3.1) with respect to the third-country banking and investment group referred to in paragraph 2.1.

3 Table: PART 3: Adjustment of scope

3.1 The adjustments that must be carried out under this paragraph are that the scope of the rules referred in Part 1 or Part 2 of this annex, as the case may be, are amended:

(1) so as to remove any provisions disapplying those rules for third-country groups;
(2) so as to remove all limitations relating to where a member of the third-country group is incorporated or has its head office; and
(3) so that the scope covers every member of the third-country group that would have been included in the scope of those rules if those members had their head offices in, and were incorporated in, the UK.

4Table: PART 4: Definition used in this Annex

4.1 This Part sets out the definition which a firm must apply for the purposes of this annex as it applies in relation to GENPRU 3.2.

4.2 A reference to “rules” in this annex includes any onshored regulations that are relevant to the purpose of which “rules” as used refers to.
Guidance Notes for Classification of Groups

Classification of Groups (GENPRU 3.1.3 G) - This annex consists only of one or more forms. Forms are to be found through the following address. [genpru_ch3_annex3G.pdf]

Purpose and scope

The form is designed to identify groups and sub-groups that are likely to be financial conglomerates under the Financial Groups Directive. A group may be a financial conglomerate if it contains both insurance and banking/investment businesses and meets certain threshold tests. The FCA needs to identify conglomerates with their head offices in the EEA and those with their head offices outside the EEA, although this does not necessarily mean that the latter will be subject to EEA conglomerate supervision.

This form’s purpose is to enable the FCA to obtain sufficient information so as to be able to determine how likely a group/sub-group is to be a financial conglomerate. In certain cases this can only be determined after consultation with the other EU relevant competent authorities. A second purpose of the form is therefore to identify any groups and sub-groups that may need such consultation so that this can be made as soon as possible. This should allow firms time to prepare to comply.

The third purpose of the form is to gain information from firms on the most efficient way to implement the threshold calculations in detail (consistently with the directive). We have, therefore, asked for some additional information in part 4 of the form.

A copy of this form can be found on the FCA’s Financial Groups Website with current contact details.

Please include workings showing the method employed to determine the percentages in part 2 (for the threshold conditions) and giving details of all important assumptions / approximations made in doing the calculations.

The definition of financial conglomerate includes not only conventional groups made up of parent-subsidiary relationships but groups linked by control and “consolidation Article 12(1) relationships”. If this is the case for your group, please submit along with this form a statement that this is the case. Please include in that statement an explanation of how you have included group members not linked by capital ties in the questionnaire calculations.

A consolidation Article 12(1) relationship arises between undertakings in the circumstances set out in Article 12(1) of the Seventh Company Law Directive. These are set out in the Handbook Glossary (in the definition of consolidation Article 12(1) relationship). Broadly speaking, undertakings come within this definition if they do not form a conventional group but:

(a) are managed on a unified basis; or
(b) have common management.

General guidance

We would like this to be completed based on the most senior parent in the group, and, if applicable, for the company heading the most senior conglomerate group in the EEA. If appropriate, please also attach a list of all other likely conglomerate sub-groups.

Please use the most recent accounts for the top level company in the group together with the corresponding accounts for all subsidiaries and participations that are included in the consolidated accounts. Please indicate the names of any significant subsidiaries with a different year-end from the group’s year-end.

Please note the following:

(a) Branches should be included as part of the parent entity.
(b) Include in the calculations overseas entities owned by the relevant group or sub-group.
(c) There are only two sectors for this purpose: banking/investment and insurance.
(d) You will need to assign non-regulated financial entities to one of these sectors:
   • banking/investment activities are listed in – Annex 1 to the Capital Requirements Directive 2013/36/EU
   • insurance activities are listed in - schedule 1 to, and contracts of insurance defined in article 3(1) of, the Regulated Activities Order .
   • Any operator of a UCITS scheme, insurance intermediary, mortgage broker and mixed financial holding company does not fall into the directive definitions of either financial sector or insurance sector and should be treated for these purposes as being outside the financial sector. They should therefore be ignored for the purposes of these calculations.

Threshold tests
For the purpose of completing section 2 of the form relating to the threshold tests, the following guidance should be used. However, if you consider that for your group there is a more appropriate calculation then you may use this calculation so long as the method of computation is submitted with the form.

Calculating balance sheet totals
Generally, use total (gross) assets for the balance sheet total of a group/entity. However, investments in other entities that are part of the group will need to be deducted from the sector that has made the investment and the balance sheet total of the entity is added to the sector in which it operates.

Our expectation of how this may be achieved efficiently is as follows:
(i) Off-balance-sheet items should be excluded.
(ii) Where off-balance sheet treatment of funds under management and on-balance sheet treatment of policy holders’ funds may distort the threshold calculation, groups should consult the FCA on the appropriateness of using other measures under article 3.5 of the Financial Groups Directive.
(iii) If consolidated accounts exist for a sub-group consisting of financial entities from only one of the two sectors, these consolidated accounts should be used to measure the balance-sheet total of the sub-group (i.e. total assets less investments in entities in the other sector). If consolidated accounts do not exist, intra-group balances should be netted out when calculating the balance sheet total of a single sector (but cross-sector intra-group balances should not be netted out).
(iv) Where consolidated accounts are used, minority interests should be excluded and goodwill should be included.
(v) Where accounting standards differ between entities, groups should consult the FCA if they believe this is likely materially to affect the threshold calculation.
(vi) Where there is a subsidiary or participation in the opposite sector from its parent (i.e. insurance sector for a banking/investment firm parent and vice versa), the balance sheet amount of the subsidiary or participation should be allocated to its sector using its individual accounts.
(vii) The balance-sheet total of the parent entity/sub-group is measured as total assets of the parent/sub-group less the book value of its subsidiaries or participations in the other sector (i.e. the value of the subsidiary or participation in the parent’s consolidated accounts is deducted from the parent’s consolidated assets).
(viii) The cross-sector subsidiaries or participations referred to above, valued according to their own accounts, are allocated pro-rata, according to the aggregated share owned by the parent/sub-group, to their own sector.
(ix) If the cross-sector entities above themselves own group entities in the first sector (i.e. that of the top parent/sub-group) these should (in accordance with the methods above) be excluded from the second sector and added to the first sector using individual accounts.

Solvency (capital adequacy) requirements
Generally, the solvency requirements should be according to sectoral rules of the FCA that would apply to the type of entity. However, you can use EEA rules or local rules in the circumstances set out in Part 6 of GENPRU 3 Annex 1. But if this choice makes a significant difference,
either with respect to whether the group is a financial conglomerate or with respect to which sector is the biggest, you should consult with the FCA. Non-regulated financial entities should have proxy requirements calculated on the basis of the most appropriate sector. If sub-groups submit single sector consolidated returns then the solvency requirement may be taken from those returns.

Our expectation of how this may be achieved efficiently is as follows:

(i) If you complete a solvency return for a sub-group consisting of financial entities from only one of the two sectors, the total solvency requirement for the sub-group should be used.
(ii) Solvency requirements taken must include any deductions from available capital so as to allow the appropriate aggregation of requirements.
(iii) Where there is a regulated subsidiary or participation in the opposite sector from its parent/sub-group, the solvency requirement of the subsidiary or participation should be from its individual regulatory return. If there is an identifiable contribution to the parent’s solvency requirement in respect of the cross-sector subsidiary or participation, the parent’s solvency requirement may be adjusted to exclude this.
(iv) Where there is an unregulated financial undertaking in the opposite sector from its parent/sub-group, the solvency requirement of the subsidiary or participation should be one of the following:
   (a) as if the entity were regulated by the FCA under the appropriate sectoral rules;
   (b) using EU minimum requirements for the appropriate sector; or
   (c) using non-EU local requirements* for the appropriate sector.
   Please note on the form which of these options you have used, according to the country and sector, and whether this is the same treatment as in your latest overall group solvency calculation.
(v) For banking/investment requirements, use the total amount of capital required.
(vi) For insurance requirements, use the total amount of capital required.

Market share measures

These are not defined by the directive. The aim is to identify any standard industry approaches to measuring market share in individual EU countries by sector, or any data sources which are commonly used as a proxy.

Article I.

Article II. Threshold tests

Test F2
B/S of banking/investment + insurance sector = result %
B/S total
Test F3/F4/F5
B/S of insurance sector
B/S of banking/investment sector + insurance sector = A%
B/S of banking/investment sector
B/S of banking/investment sector + insurance sector = B%
Solvency requirement of insurance sector
Solvency requirement of banking/investment sector +insurance sector = C%
Solvency requirement of banking/investment sector
Solvency requirement of banking/investment sector +insurance sector = D%
The relevant percentage for the insurance sector is:
(A% + C%)/2 = I %
The relevant percentage for the banking/investment sector is:
(B% + D%)/2 = BI %
The smallest sector is the sector with the smallest relevant percentage.
Article III. If $I\% < B_1\%$ then $F_3$ is insurance, $F_4 = A\%$, and $F_5 = C\%$

Article IV. If $B_1\% < I\%$ then $F_3$ is banking/investment, $F_4 = B\%$ and $F_5 = D\%$
(see GENPRU 3.1.5R)

Footnote: The conditions are that the *UK regulated entity* at the head of the *consolidation group*: (1) is a *parent undertaking* of a member of the *consolidation group* in the *overall financial sector*; (2) has a *participation* in a member of the *consolidation group* that is in the *overall financial sector*; or (3) has a *consolidation Article 12(1) relationship* with a member of the *consolidation group* that is in the *overall financial sector*. 

---

**Key**

- **Yes**
- **No**

---

**Is at least one of the members in the consolidation group within the insurance sector and at least one within the banking sector or investment services sector?**

Article 2(14)(d)

---

**Is an EEA regulated entity at the head of the consolidation group?**

Article 2(14)(a)

---

**Does the EEA regulated entity satisfy at least one of the conditions on the footnotes below (lexim 2010/08)?**

---

**THRESHOLD TEST 1**

Does the ratio of the balance sheet total of the members of the consolidation group in the overall financial sector to the balance sheet total of the consolidation group as a whole exceed 40%?  

Article 2(14)(b), Article 3(1)

---

**THRESHOLD TEST 2**

Does for each financial sector, the average of: (1) the ratio of the balance sheet total of that financial sector to the balance sheet total of the overall financial sector, and (2) the ratio of the solvency and capital adequacy requirements of the same financial sector to the total solvency and capital adequacy requirements of members in the overall financial sector, exceed 10%?  

Article 2(14)(a), Article 3(2)

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**THRESHOLD TEST 3**

Does the balance sheet total of the smallest financial sector exceed EUR 6 billion?  

Article 3(3)

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**FINANCIAL CONGLOMERATE**

---

**NOT A FINANCIAL CONGLOMERATE**

---
General Prudential sourcebook

GENPRU TP 1
Application of GENPRU TP 1 to GENPRU TP 6 and other general provisions for insurers
Table: IPRU(INS) waivers
Table: IPRU(INS) waivers
General Prudential sourcebook

GENPRU TP 5
Calls for supplementary contributions
General Prudential sourcebook

GENPRU TP 6
Implicit items waivers
General Prudential sourcebook

GENPRU TP 8
Miscellaneous capital resources definitions for BIPRU firms

<table>
<thead>
<tr>
<th>Section</th>
<th>Requirement</th>
<th>Explanation</th>
</tr>
</thead>
<tbody>
<tr>
<td>8.1</td>
<td>R</td>
<td>This section applies to a BIPRU firm.</td>
</tr>
<tr>
<td>8.2</td>
<td>R</td>
<td>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.</td>
</tr>
<tr>
<td>8.3</td>
<td>R</td>
<td>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.</td>
</tr>
<tr>
<td>8.7</td>
<td>R</td>
<td>A BIPRU 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:</td>
</tr>
<tr>
<td>(1)</td>
<td></td>
<td>on 31 December 2006 the firm was subject to IPRU(INV);</td>
</tr>
<tr>
<td>(2)</td>
<td></td>
<td>the firm issued it on or before 31 December 2006;</td>
</tr>
<tr>
<td>(3)</td>
<td></td>
<td>as at 31 December 2006 the firm included it, and was entitled to include it, in the calculation of its capital resources under IPRU(INV) as capital of a type that corresponded to tier one capital resources;</td>
</tr>
<tr>
<td>(4)</td>
<td></td>
<td>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;</td>
</tr>
<tr>
<td>(5)</td>
<td></td>
<td>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;</td>
</tr>
<tr>
<td>(6)</td>
<td></td>
<td>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...</td>
</tr>
</tbody>
</table>
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

A BIPRU 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(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(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.

Conversion ratio

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(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) [deleted]
   (b) IPRU(INV) as capital of a type that corresponded to tier one capital.

Legal opinions

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(INV);
8.13 R The following rules:

<table>
<thead>
<tr>
<th>Rule</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1)</td>
<td>GENPRU 2.2.159 R (12) (Legal opinions for tier two capital);</td>
</tr>
<tr>
<td>(2)</td>
<td>GENPRU 2.2.163 R (Legal opinions for tier two capital governed by a foreign law);</td>
</tr>
<tr>
<td>(3)</td>
<td>GENPRU 2.2.181 R (Legal opinions for upper tier two capital); and</td>
</tr>
<tr>
<td>(4)</td>
<td>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);</td>
</tr>
</tbody>
</table>

The rules do not apply to a capital instrument issued by a firm if:

<table>
<thead>
<tr>
<th>Rule</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>(5)</td>
<td>on 31 December 2006 the firm was subject to IPRU(INV);</td>
</tr>
<tr>
<td>(6)</td>
<td>the firm issued the capital instrument on or before 31 December 2006; and</td>
</tr>
<tr>
<td>(7)</td>
<td>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(INV) as capital of a type that corresponds to:</td>
</tr>
<tr>
<td></td>
<td>(a) (where the firm disapplies the rule in (1) or (2)) tier two capital; or</td>
</tr>
<tr>
<td></td>
<td>(b) (where the firm disapplies the rule in (3)) upper tier two capital; or</td>
</tr>
<tr>
<td></td>
<td>(c) (where the firm disapplies the rule in (4)) tier three capital.</td>
</tr>
</tbody>
</table>

Version of IPRU

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

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 [FCA]

| G | A reference to a *firm* being entitled to include *capital instruments* in the calculation of its capital resources under **IP-RU(INV)** at a particular level includes the *firm* being able to do this under a *waiver*. |

**Combinations of provisions**

| 8.17 [FCA] | G | A *firm* may combine the use of two or more of the provisions in this section. |
### 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   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. must apply the limit in GENPRU 2.2.30AR (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. [deleted]
4. [deleted]
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 2.2.30AR (2)
   (a) **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;
   (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 2.2.30AR (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 2.2.30AR (1):
Further miscellaneous capital resources definitions for BIPRU firms

(a) capital instruments included at stage C in the capital resources table under (1) and GENPRU 2.2; and

(b) 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 2.2.30AR (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) [deleted]

(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 2.2.30AR (3) must develop strategies and processes on the necessary measures to resolve this situation before the dates set out in GENPRU TP8A.6R.
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### GENPRU TP 8B

**Miscellaneous capital resources definitions for BIPRU firms: Core tier one capital**

<table>
<thead>
<tr>
<th>Application</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>8B.1 R</strong></td>
</tr>
<tr>
<td><strong>8B.2 R</strong></td>
</tr>
<tr>
<td><strong>8B.5 R</strong></td>
</tr>
</tbody>
</table>
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GENPRU TP 10
Assets of former underwriting members
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GENPRU TP 11
PRU waivers
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GENPRU TP 12
Table: PRU waivers
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GENPRU TP 16
[deleted]
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Schedule 1
Record keeping requirements

Sch 1 G

1 The aim of the guidance in the following table is to give the reader a quick overall view of the relevant record keeping requirements.
2 It is not a complete statement of those requirements and should not be relied on as if it were.
3 Table

<table>
<thead>
<tr>
<th>Handbook reference</th>
<th>Subject of Record</th>
<th>Contents of record</th>
<th>When record must be made</th>
<th>Retention Period</th>
</tr>
</thead>
<tbody>
<tr>
<td>GENPRU 1.2.60 R - GENPRU 1.2.61 R</td>
<td>Firm's assessment of its financial resources</td>
<td>(1) The major sources of risk the firm has identified (2) How the firm intends to deal with those risks (3) Details of the stress and scenario analyses carried out and the resulting financial resources estimated to be required</td>
<td>Not specified</td>
<td>At least three years</td>
</tr>
<tr>
<td>GENPRU 1.3.22 R</td>
<td>Valuation models for marking to model</td>
<td>Secure copy of firm's own valuation model</td>
<td>When model is in use</td>
<td>Not specified</td>
</tr>
</tbody>
</table>
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## Schedule 2
### Notification and reporting requirements

### Sch 2 G

1. The aim of the *guidance* in the following table is to give the reader a quick overall view of the relevant notification requirements.
2. It is not a complete statement of those requirements and should not be relied on as if it were.

<table>
<thead>
<tr>
<th>Handbook reference</th>
<th>Matter to be notified</th>
<th>Contents of notification</th>
<th>Trigger events</th>
<th>Time allowed</th>
</tr>
</thead>
<tbody>
<tr>
<td>GENPRU 1.5.19 R</td>
<td>Intention to change maximum amount of callable contribution</td>
<td>Fact of intention and details of the change</td>
<td>Intention to change the maximum amount</td>
<td>Adequate advance notice, normally not less than 6 months</td>
</tr>
<tr>
<td>GENPRU 2.1.11 R</td>
<td>Breach or expected breach of GENPRU 2.1.13 R or main BIPRU firm Pillar 1 rules</td>
<td>Fact of breach or expectation of breach</td>
<td>Breach or expectation of breach</td>
<td>Immediately</td>
</tr>
<tr>
<td></td>
<td>[deleted]</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>GENPRU 2.2.61B R</td>
<td>Intention to issue a capital instrument for inclusion in capital resources</td>
<td>Fact of intention and details of intended amount, issue date, type of investor, stage of capital, features of instrument and confirmation of compliance with rules</td>
<td>Intention to issue</td>
<td>One month prior to issue, unless exceptional circumstances prevent a <em>firm</em> adhering to a one-month period</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>GENPRU 2.2.61C R</td>
<td>Proposed changes to details of the issue of a capital instrument notified under GENPRU 2.2.61B R (1) to GENPRU 2.2.61B R (4)</td>
<td>Proposed change and all information required under GENPRU 2.2.61B R (1) to GENPRU 2.2.61B R (4)</td>
<td>Intention to change any details of the issue previously notified to the appropriate regulator</td>
<td>As soon as the changes are proposed</td>
</tr>
<tr>
<td>GENPRU 2.2.61D R</td>
<td>Proposed establishment of a debt securities program</td>
<td>All information required under GENPRU 2.2.61B R (1) to GENPRU 2.2.61B R (4)</td>
<td>Intention to establish</td>
<td>One month prior to first drawdown</td>
</tr>
<tr>
<td>Handbook reference</td>
<td>Matter to be notified</td>
<td>Contents of notification</td>
<td>Trigger events</td>
<td>Time allowed</td>
</tr>
<tr>
<td>--------------------</td>
<td>-----------------------</td>
<td>-------------------------</td>
<td>----------------</td>
<td>--------------</td>
</tr>
<tr>
<td>GENPRU 2.2.61F R [FCA] [PRA]</td>
<td>Issue of capital instruments for inclusion in capital resources where instrument or facility previously notified to the appropriate regulator</td>
<td>All information required under GENPRU 2.2.61B R (1) to GENPRU 2.2.61B R (3) and confirmation no changes have been made to the terms of the instrument since a previous similar issue</td>
<td>Intention to issue</td>
<td>No later than date of issue</td>
</tr>
<tr>
<td>GENPRU 2.2.74 R [FCA] [PRA]</td>
<td>Intention to redeem tier one instrument included in tier one capital resources</td>
<td>Fact of intention and details of the firm’s position after such redemption in order to show how it will meet the capital resources requirement, how it will have sufficient financial resources to meet the overall financial adequacy rule and, in the case of a BIPRU firm, how it will not otherwise suffer any undue effects to its financial or solvency conditions</td>
<td>Intention to redeem</td>
<td>At least one month prior to becoming committed to redeem</td>
</tr>
<tr>
<td>[deleted]</td>
<td>Proposal to amend a tier two instrument</td>
<td>Details of the proposed amendment</td>
<td>Proposal to amend</td>
<td>One month before amendment is due to take effect</td>
</tr>
<tr>
<td>[deleted]</td>
<td>Intention to repay (other than on contractual repayment date) tier two instrument</td>
<td>Fact of intention and details of the firm’s position after such repayment in order to show how it will meet the capital resources requirement and how it will have sufficient financial resources</td>
<td>Intention to repay</td>
<td>Six Months (in the case of an insurer) or one Month (in the case of a BIPRU firm) prior to becoming committed to repayment</td>
</tr>
<tr>
<td>Handbook reference</td>
<td>Matter to be notified</td>
<td>Contents of notification</td>
<td>Trigger events</td>
<td>Time allowed</td>
</tr>
<tr>
<td>--------------------</td>
<td>-----------------------</td>
<td>-------------------------</td>
<td>----------------</td>
<td>--------------</td>
</tr>
<tr>
<td>[deleted]</td>
<td>[deleted]</td>
<td>to meet the overall financial adequacy rule</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Schedule 2**

Notification and reporting requirements
There are no requirements for fees or other payments in GENPRU.
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Schedule 4
Powers exercised

Sch 4.1 G
[deleted]

Sch 4.2 G
[deleted]
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### Schedule 5

#### Rights of action for damages

**Sch 5 G**

1. The table below sets out the rules in *GENPRU* contravention of which by an *authorised person* may be actionable under section 138D of the Act (Actions for damages) by a person who suffers loss as a result of the contravention.

2. If a "Yes" appears in the column headed "For private person", the rule may be actionable by a private person under section 138D (or, in certain circumstances, his fiduciary or representative; see article 6(2) and (3)(c) of the Financial Services and Markets Act 2000 (Rights of Action) Regulations 2001 (SI 2001/2256)). A "Yes" in the column headed "Removed" indicates that the FCA has removed the right of action under section 138D(3) of the Act. If so, a reference to the rule in which it is removed is also given.

3. The column headed "For other person" indicates whether the rule may be actionable by a person other than a private person (or his fiduciary or representative) under article 6(2) and (3) of those Regulations. If so, an indication of the type of person by whom the rule may be actionable is given.

<table>
<thead>
<tr>
<th>Chapter/Appendix</th>
<th>Section/Annex</th>
<th>Right of action under section 138D</th>
<th>For private person</th>
<th>Removed</th>
<th>For other person</th>
</tr>
</thead>
<tbody>
<tr>
<td>All rules in GENPRU</td>
<td></td>
<td></td>
<td>No</td>
<td>Yes - GENPRU 1.4.1 R</td>
<td>No</td>
</tr>
</tbody>
</table>
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Schedule 6
Rules that can be waived

Sch 6 G
The rules in GENPRU may be waived by the appropriate regulator under section 138A of the Act (Modification or waiver of rules).