

Chapter 8

Prudential consolidation and large exposures

8.2 Large Exposures

Application

- 8.2.1 **R** This section applies to an *IFPRU investment firm*, unless it is an *exempt IFPRU commodities firm* to which article 493 of the *EU CRR* applies.
- 8.2.2 **R** This section does not apply to a *FCA consolidation group* on the basis of its *consolidated situation* if the *group* only contains *limited activity firms* or *limited licence firms*.

Purpose

- 8.2.3 **G** This section contains the *rules* that exercise the discretion afforded to the *FCA* as *competent authority* under article 400(2)(c) and (3) of the *EU CRR* (Large exposures: exemptions). The *FCA* does not intend to exercise its discretion for any of the other exemptions in article 400(2).

Intra-group exposures: non-core large exposures group

- 8.2.4 **G** Article 400(2) of the *EU CRR* permits the *FCA* to fully or partially exempt *exposures* incurred by a *firm* to intra-group *undertakings* that meet the specified criteria from the limit stipulated in article 395(1) of the *EU CRR* in relation to a *firm's group of connected clients* that represent its wider group. The *FCA* will consider exempting *non-trading book* and *trading book exposures* to intra-group *undertakings* if specified conditions throughout **IFPRU 8.2** are met.
- 8.2.5 **G** The *FCA* expects that applications for exemptions under article 400(2)(c) of the *EU CRR* will be for *firms* established in the *UK* where the intra-group *undertakings* to which they have *exposures* meet the criteria for the *core UK group* in article 113(6) of the *EU CRR*, except for article 113(6)(d) (established in the same *EEA State* as the *firm*).
- 8.2.6 **R** A *firm* with a *non-core large exposures group permission* may (in line with that permission) exempt, from the application of article 395(1) of the *EU CRR* (Limits to large exposures), *exposures*, including *participations* or other kinds of holdings, incurred by a *firm* to:
- (1) its *parent undertaking*; or
 - (2) other *subsidiary undertakings* of that *parent undertaking*; or

- (3) its own *subsidiary undertakings*;

in so far as those *undertakings* are covered by the supervision on a *consolidated basis* to which the *firm* itself is subject, in accordance with the *EU CRR*, Directive 2002/87/EC regarding the supplementary supervision of financial entities in a *financial conglomerate* or with equivalent standards in force in a *third country*; *exposures* that do not meet these criteria, whether or not exempted from article 395(1), shall be treated as *exposures* to a third party.

[Note: article 400(2) of the *EU CRR*]

8.2.7

R

A *firm* may only make use of the non-core large exposure group exemption where the following conditions are met:

- (1) the total amount of the non-trading book exposures from the *firm* to its *non-core large exposures group* does not exceed 100% of the *firm's eligible capital*; or

(if the *firm* has a *core UK group permission*) the total amount of non-trading book exposures from its *core UK group* (including the *firm*) to its *non-core large exposures group* does not exceed 100% of the *core UK group eligible capital*;

- (2) the total amount of trading book exposures from the *firm* to its *non-core large exposures group* does not exceed 500% of the *firm's eligible capital*; or

(if the *firm* has a *core UK group permission*) the total amount of *trading book exposures* from its *core UK group* (including the *firm*) to its *non-core large exposures group* does not exceed 500% of the *core UK group eligible capital*;

- (3) (if the *firm* has a *core UK group permission*) it gives the *FCA* prior written notice if it intends to concentrate its intra-group exposure to a particular member of its *non-core large exposures group* in excess of 25% of *core UK group eligible capital*.

The written notice must contain the following:

- (a) an explanation of how the *firm* will ensure that it will still meet the condition in (1) on a continuing basis;
 - (b) details of the counterparty, the size of the *exposure* and the expected duration of the *exposure*; and
 - (c) an explanation of the reason for the *exposure*;
- (4) if the *firm* stops concentrating its intra-group *exposure* to a particular member of its *non-core large exposures group* in excess of 25% of *core UK group eligible capital*, it gives the *FCA* prior written notice as set out in (3) if it intends to start to do so again; and
- (5) the *firm* submits FSA018 under SUP 16.12 (Integrated regulatory reporting) as applicable to it.

[Note: article 400(2)(c) of the *EU CRR*]

8.2.8 **R** A *firm* may calculate limits in ■ IFPRU 8.2.7 R after taking into account the effect of *credit risk mitigation* in line with articles 399 to 403 of the *EU CRR*.

Core UK group eligible capital

8.2.9 **R** For the purposes of the conditions in ■ IFPRU 8.2.7 R, a *firm* must calculate *core UK group eligible capital* in line with the deduction and aggregation method in ■ IFPRU 8.2.10 R.

8.2.10 **R** (1) *Core UK group eligible capital* is equal to the sum of the following amounts for each member of the *core UK group* and the *firm* (the sub-group):

- (a) for ultimate *parent undertaking* of the sub-group, the amount calculated in line with article 6 of the *EU CRR* (or other prudential requirements that apply);
- (b) for any other member of the sub-group, the amount calculated in line with article 6 of the *EU CRR* (or other prudential requirements that apply) less the book value of the sub-group's holdings of capital instruments in that member, to the extent not already deducted in calculations in line with article 6 of the *EU CRR* (or other prudential requirements that apply) for:
 - (i) the ultimate *parent undertaking* of the sub-group; or
 - (ii) any other member of the sub-group.
- (c) The deduction in (1)(b) must be carried out separately for each type of capital instrument eligible as *own funds*.

8.2.11 **G** The *FCA* will assess *core UK group* and non-core large exposure group applications against article 400(2)(c) on a case-by-case basis. The *FCA* will only approve this treatment for non-core large exposure group undertakings where the conditions in article 400(2)(c) are met. A *firm* should note that the *FCA* will still make a wider judgement whether it is appropriate to grant this treatment even where the conditions in article 400(2)(c) are met.

Notification

8.2.12 **R** A *firm* must immediately notify the *FCA* in writing if it becomes aware that any *exposure* that it has treated as exempt under ■ IFPRU 8.2.6 R or any counterparty that it has been treating as a member of its *non-core large exposures group* has ceased to meet the conditions for application of the treatment in this section.

Conditions for exemptions

8.2.13 **R** A *firm* may only make use of the exemptions provided in this section where the following conditions are met:

- (1) the specific nature of the *exposure*, the counterparty or the relationship between the *firm* and the counterparty eliminate or reduce the risk of the *exposure*; and

- (2) any remaining concentration risk can be addressed by other equally effective means, such as the arrangements, processes and mechanisms in article 81 of *CRD* (Concentration risk).

[Note: article 400(3) of the *EU CRR*]

Exposures to trustees

8.2.14 G If a *firm* has an *exposure* to a person ('A') when A is acting on his own behalf, and also an *exposure* to A when A acts in his capacity as trustee, custodian or general partner of an investment trust, unit trust, venture capital or other investment fund, pension fund or a similar fund (a "fund"), the *firm* may treat the latter *exposure* as if it was to the fund, unless such a treatment would be misleading.

8.2.15 G When considering whether the treatment described is misleading, factors a *firm* should consider include:

- (1) the degree of independence of control of the fund, including the relation of the fund's board and senior management to the *firm* or to other funds or to both;
- (2) the terms on which the counterparty, when acting as trustee, is able to satisfy its obligation to the *firm* out of the fund of which it is trustee;
- (3) whether the beneficial owners of the fund are connected to the *firm*, or related to other funds managed within the *firm's group*, or both; and
- (4) for a counterparty that is connected to the *firm* itself, whether the *exposure* arises from a transaction entered into on an arm's length basis.

8.2.16 G In deciding whether a transaction is at arm's length, the following factors should be taken into account:

- (1) the extent to which the person to whom the *firm* has an *exposure* ('A') can influence the *firm's* operations through, for example, the exercise of voting rights;
- (2) the management role of A where A is also a director of the *firm*; and
- (3) whether the *exposure* would be subject to the *firm's* usual monitoring and recovery procedures if repayment difficulties emerged.