

IPRU-INV -link-



Interim Prudential sourcebook for Investment Businesses

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To view amending instruments for IPRU (INV) please see the relevant Instruments by module page

Interim Prudential Sourcebook for Investment Businesses

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Chapter 1

Application and General Provisions

1.1 PURPOSE

- 1.1.1 **R** [deleted]
- 1.1.2 **G** The *rules* and *guidance* in this sourcebook will assist the *appropriate regulator* to meet the statutory objectives. This sourcebook does so by setting minimal capital and other risk management standards thereby mitigating the possibility that firms will be unable to meet their liabilities and commitments to *consumers* and counterparties.
- 1.1.3 **R** The general scheme of this sourcebook is, wherever appropriate, to apply the financial and other prudential standards which applied to a *firm* immediately prior to it becoming authorised by the *appropriate regulator* under the *Act*. For convenience, the chapter numbers adopted in this sourcebook correspond with those of the rulebooks of *previous regulators*.
- 1.1.3A **R** This sourcebook does not apply to *BIPRU firms* except:
 - (1) it does apply to certain *exempt BIPRU commodities firms*; and
 - (2) [deleted]
- 1.1.3B **R** This sourcebook does not apply to *IFPRU investment firms* except it does apply to *exempt IFPRU commodities firms*.
- 1.1.4 **R** This sourcebook does not apply to *banks*, building societies, insurers, the *Society of Lloyd's* (except in relation to underwriting *agents*), friendly societies and certain other categories of *firm* and *members'* advisers.
- 1.1.5 **R** On becoming authorised by the *appropriate regulator* a *firm* will have to comply with the particular chapter of this sourcebook appropriate to its business. The *firm* will be able to seek guidance on this during the authorisation procedure. If subsequently, the business for which a *firm* has *permission* changes it may be necessary for it to comply with a different set of financial resources requirements. *Firms* will be able to discuss this aspect with the appropriate regulator during the application process.

1.1.6

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The *Supervision manual* sets out provisions relating to the periodic reporting and notification of financial information to the *appropriate regulator* or to the auditing of accounts. However, this sourcebook contains a few additional notification requirements (*notification rules*).

1

1.2 APPLICATION

- 1.2.1** **R** The *Glossary* applies to the transitional provisions, this chapter (■ IPRU-INV 1), ■ IPRU-INV 2, ■ IPRU-INV 4, ■ IPRU-INV 6, ■ IPRU-INV 11 and ■ IPRU-INV 13.
- 1.2.2** **R**
- (1) *IPRU-INV* applies to:
 - (a) a *members' adviser*;
 - (b) an *investment management firm*;
 - (c) a *personal investment firm*;
 - (d) an *authorised professional firm*;
 - (e) a *securities and futures firm*;
 - (f) a *service company*;
 - (g) the *Society of Lloyd's* (in relation to *underwriting agents*);
 - (h) [deleted]
 - (i) a *credit union* which is a *CTF provider*; and
 - (j) an *exempt CAD firm*; and
 - (k) a *collective portfolio management firm*; and
 - (l) a *collective portfolio management investment firm*.
 - (2) *IPRU-INV* does not apply to:
 - (a) a *lead regulated firm*; or
 - (b) a *media firm*; or
 - (c) a *BIPRU firm* (unless it is an *exempt BIPRU commodities firm*); or
 - (d) an *IFPRU investment firm* (unless it is an *exempt IFPRU commodities firm*).
 - (3) The definitions in the *Glossary* (which is applicable to the *Handbook* generally) apply to this chapter.
- 1.2.3** **G** For the avoidance of doubt, *IPRU-INV* does not apply to any of the following:
- (a) a *bank*; or
 - (b) a *building society*; or
 - (ba) a *designated investment firm*; or

- (c) a *friendly society*; or
- (d) an *ICVC*; or
- (e) an *incoming EEA firm* or an *incoming Treaty firm* which does not have a *top up permission*; or
- (f) an *insurer*; or
- (g) a *UCITS qualifier*.

Obligation to Comply

1.2.4 **R** A *firm* of a kind listed in the left-hand column of Table 1.2.4R must comply with the provisions of IPRU (INV) shown in the right hand column and, where relevant, the provisions of Chapter 14.

1.2.5 **R** Table

This table belongs to IPRU (INV) 1.2.4R

<i>Authorised professional firm</i>	Chapters 1 and 2
<i>Securities and futures firm</i> (which is not a <i>MiFID investment firm</i>)	Chapters 1 and 3
<i>Securities and futures firm</i> (which is an <i>exempt BIPRU commodities firm</i> or an <i>exempt IFPRU commodities firm</i>)	Chapters 1 and 3
The <i>Society of Lloyd's</i> (in relation to <i>underwriting agents</i>) and <i>members' advisers</i>	Chapters 1 and 4
<i>Investment management firm</i>	Chapters 1 and 5
An <i>exempt CAD firm</i> or a <i>local firm</i>	Chapters 1 and 9
<i>Service company</i>	Chapters 1 and 6
<i>Collective portfolio management firm</i>	Chapters 1 and 11
<i>Collective portfolio management investment firm</i>	Chapters 1 and 11
<i>Personal investment firm</i>	Chapters 1 and 13
<i>Credit union</i> which is a <i>CTF provider</i>	Chapters 1 and 8

CAPITAL SUBSTITUTES: TRANSITIONAL PROVISION

1.2.6 **G** The financial resource requirements of the Financial Services Act regulators permitted certain types of borrowings or facilities to be treated as part of a *firm's* capital resources. The most common example is that of a subordinated loan which met the relevant conditions. The following provisions permit *firms* to continue to use these borrowings or facilities in the same way as

under the relevant *previous regulator's* rules, provided that certain conditions are met.

1.2.7

R

- (1) If a *firm* was, immediately before *commencement* permitted to treat "relevant funds" as part of its capital resources under the financial resource rules of a *previous regulator* applicable to the *firm*, it may treat those funds in an equivalent manner under the corresponding provisions of *IPRU-INV*, provided that the conditions in (3) are met.
- (2) For the purposes of this *rule* "relevant funds" are funds provided to the *firm* under the terms of
 - (a) a subordinated loan agreement; or
 - (b) qualifying undertaking; or
 - (c) any other instrument treated in an equivalent manner under the financial resources *rules* applicable to the *firm*.
- (3) The conditions referred to in (1) are either:
 - (a) in the case of a subordinated loan agreement, qualifying undertaking or other relevant instrument to which the *firm's previous regulator* is not party:
 - (i) the parties to it treat all rights (including, without limitation, rights to notice) which the agreement, undertaking or instrument grants to the *firm's previous regulator* as having been granted to the *appropriate regulator*; and
 - (ii) if there is a variation of the commercial terms the parties include, in the terms of the instrument executed to effect the variation, provision to substitute reference to the *appropriate regulator* in place of any reference to the *firm's previous regulator*; or
 - (b) in the case of a subordinated loan agreement, qualifying undertaking or other relevant instrument to which the *firm's previous regulator* is party, the parties treat the rights accorded to the self regulating organisation under the relevant instrument as having been assigned to the *appropriate regulator* immediately before *commencement*.

1.2.8

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[deleted]

Chapter 2

Authorised professional firms

2.1 APPLICATION

- 2.1.1** **R** (1) This chapter applies to an *authorised professional firm* in accordance with ■ IPRU-INV 2.1.2R and ■ IPRU-INV 2.1.3R.
- (2) The definitions in the *Glossary* apply to this Chapter.
- 2.1.2** **G** (1) An *authorised professional firm* of a kind falling within (2) must comply with such of ■ IPRU-INV 3, ■ 5, ■ 9 or ■ 13 which in accordance with ■ IPRU-INV 2.1.4R, most appropriately correlates to the type and scale of the business which it conducts.
- (2) The type of *authorised professional firm* to which (1) applies is one:
- (a) which is also an *exempt CAD firm*;
 - (b) which acts as a *market maker*;
 - (c) which acts as a *stabilising manager*;
 - (da) which acts as a *small authorised UK AIFM* or a *residual CIS operator*;
 - (db) which acts as a *depository*;
 - () which acts as a *broker fund adviser* or otherwise participates in a *broker fund* arrangement;
 - () whose main business, having regard to (3), is not the practice of its profession or professions;
 - () whose *permission* includes a requirement that it acts in conformity with the financial resources *rules* applicable to another type of *firm*; or
 - () whose *permission* includes *establishing, operating or winding up a personal pension scheme*.
- (3) For the purposes of (2)(f), a *firm's* professional business practice is not the "main business" of the *firm* unless the proportion of income it derives from *professional fees* is, during its annual accounting period, at least 50% of the *firm's* total income (a temporary variation of not more than 5% may be disregarded for this purpose).
- (4) An *authorised professional firm* which, in accordance with (1), is required to comply with ■ IPRU-INV 3, ■ 5, ■ 9 or ■ 13 must immediately give notification of that fact to the *FCA* in accordance with ■ SUP 15.7 (Forms and method of notification).

2.1.3 **R** An authorised professional firm which does not fall within **■** IPRU-INV 2.1.2R must comply with sections 2.2, 2.3 and 2.4 of this chapter.

2.1.4 **G** This table belongs to **■** IPRU-INV 2.1.1R

TYPE OF BUSINESS ACTIVITY	CHAPTER OF SOURCEBOOK
(i) <i>managing investments</i> other than for <i>retail clients</i> ; or	<i>Investment management firm</i> - IPRU-INV 5
(ii) <i>OPS activity</i> ; or	<i>Investment management firm</i> (which is an exempt CAD firm) - IPRU-INV 5 and 9
(iii) [deleted]	
(iv) [deleted]	
(iva) <i>acting as trustee or depositary of a UCITS</i> ; or	
(ivb) <i>managing an AIF</i> ; or	
(ivc) <i>acting as trustee or depositary of an AIF</i> ; or	
(v) <i>acting as a residual CIS operator</i> ; or	
(va) <i>establishing, operating or winding up a personal pension scheme</i> ; or	
(vi) <i>safeguarding and administering investments</i> ;	
(i) <i>advising on, or arranging deals in, packaged products</i> ; or	
(ii) <i>managing investments for retail clients</i> ;	<i>Personal investment firm</i> - IPRU-INV 13
(i) <i>a regulated activity</i> carried on as a member of an exchange; or	<i>Securities and futures firm</i> (which is an exempt CAD firm) - IPRU-INV 9
(ii) <i>acting as a market maker in securities or derivatives</i> ; or	<i>Securities and futures firm</i> (which is not a MiFID investment firm) - IPRU-INV 3
(iii) <i>corporate finance business</i> ; or	
(iv) <i>dealing or arranging deals in securities or derivatives, other than interprofessional investments</i> ; or	
(v) <i>the provision of clearing services as a clearing firm</i> ; or	
(vi) <i>spread betting</i> ;	

- 2.1.5 **G** An *authorised professional firm* will be a *MiFID investment firm* if its business activities include the provision of *investment services and/or activities* for a third party. An *authorised professional firm* will not however be a *MiFID investment firm* if it falls within one of the exclusions contained in Article 2 of *MiFID*. Article 2(1)(c) provides an exclusion for an *authorised professional firm* which provides *investment services and/or activities* in an incidental manner in the course of a professional activity and that activity is regulated by the *firm's designated professional body*.
- 2.1.6 **G** The *FCA* considers the scope of this exclusion cannot be precisely defined. Ultimately questions of interpretation are for the Court to determine. The *FCA* considers that to satisfy the exclusion the services cannot be the major part of the practice of the *firm*. The *FCA* also considers the following factors to be among those that are relevant:
- (1) the scale of *regulated activity* in proportion to other professional services provided;
 - (2) whether and to what extent activities that are *regulated activities* are held out as separate services;
 - (3) the impression given as to how the *firm* provides *regulated activities*, for example through its advertising or other promotions of its service.
- 2.1.7 **G** The activities that a *full-scope UK AIFM* and a *UCITS management company* are allowed to perform are restricted by article 6 of *AIFMD* and article 6 of the *UCITS Directive* to the management of *AIFs* and/or *UCITS* and the additional investment activities permitted by article 6(4) of *AIFMD* and article 6(3) of the *UCITS Directive* (as applicable). As such, an *authorised professional firm* cannot be a *collective portfolio management firm* or a *collective portfolio management investment firm*.



2.2 FINANCIAL RESOURCES REQUIREMENTS

- 2.2.1** **G** (1) A *firm* must be able to meet its liabilities as they fall due.
- (2) In complying with (1) a *firm* may use any assets which are available to meet any of its liabilities.
- 2.2.2** **G** *Firms* are reminded that:
- (1) requirements relating to the systems and controls which *firms* must establish and maintain for ensuring compliance with financial resources and other requirements are set out in SYSC.
- (2) the financial reports that a *firm* is required to make to the FCA are set out in ■ SUP 16.

2.3 PROFESSIONAL INDEMNITY INSURANCE

- 2.3.1 **G** A *firm* must effect and maintain at all times adequate professional indemnity insurance cover for all the business activities which it carries on, or for which it is responsible.
- 2.3.2 **G** In assessing the adequacy of a *firms'* professional indemnity insurance cover for the purposes of ■ IPRU-INV 2.3.1R, the *FCA* may have regard to a *firm's* compliance with the professional indemnity insurance requirements of its *designated professional body* in force at the time.

2.4 BONDING REQUIREMENT FOR ACCOUNTANTS

- 2.4.1** **R** This section applies to a *firm* of accountants practising as such in the UK.
- 2.4.2** **R**
- (1) If the aggregate value of *client money* and *bonded investments* a *firm* holds for a *client* is over £50,000 then the *firm* must ensure that it holds a bond for the excess over £50,000.
 - (2) A *firm* must:
 - (a) ensure that the bond is in the form prescribed by the *FCA*;
 - (b) ensure that the *person* specified to act as trustee in the bond is a *designated professional body* or a solicitor practising as such in the UK;
 - (c) ensure that the bond is lodged with the trustee; and
 - (d) be able at all times to show that the amount of the bond is sufficient to meet the requirements of (1).
- 2.4.3** **R** A *firm* must notify the *FCA* immediately:
- (1) of any bond taken out specifying the amount and where it is lodged; and
 - (2) of the arrangements it has made to comply with **■ IPRU-INV 2.4.2R** if a bond is not renewed or is cancelled.
- 2.4.4** **G**
- (1) *Firms* which hold *client money* or bonded investments for more than one *client*, may hold one bond to cover all of the *clients* concerned. The bonding requirements may be complied with by taking out a global bond. In firms with numerous offices compliance may be achieved in practice by calculating the requirement based on figures supplied by offices which is likely to be at least quarterly. These figures would need to be supplied and assessed soon after the end of each quarter.
 - (2) To ensure the global cover is sufficient, this approach would require an estimated safety margin to be incorporated, to allow for changes in the amounts of *client money*, *investments* or assets held. An additional prudent measure would be to ensure that exceptional amounts of these assets are notified by branch offices so that the *firm* can check whether the safety margin can absorb them and reconsider whether the total global bond cover remains sufficient.

2.4.5

G

Firms which do not expect to hold *bonded investments* or *client money* in excess of the value limit need not hold a bond. However, *firms* may wish to make contingency arrangements with a surety whereby a bond facility is available and can be executed and delivered at short notice.

Chapter 3

Interim Prudential sourcebook for Investment Businesses



**3 Financial resources for Securities and
Futures Firms which are not MiFID
Investment Firms or which are Exempt
BIPRU Commodities Firms or Exempt
IFPRU Commodities Firms**

[Click here to view the provisions of IPRU \(INV\) 3](#)

Chapter 4

Lloyd's Firms



4.1 APPLICATION

- 4.1.1** **R** This chapter applies to the *Society* and *members' advisers*.
- 4.1.2** **R** This chapter does not apply to a *members' adviser* which is subject to another chapter of *IPRU-INV*.
- 4.1.3** **D** The directions in **■** IPRU-INV 4.4.1D to **■** IPRU-INV 4.4.5D and **■** IPRU-INV 4.5.1D are given to the *Council* and to the *Society* acting through the *Council*.

4.2 PURPOSE

- 4.2.1** **G** This chapter identifies the financial resource requirements and requirements as to accounts and statements to be met by certain *firms* conducting business at Lloyd's.
- 4.2.2** **G** The directions in ■ IPRU-INV 4.4.1D to ■ IPRU-INV 4.4.5D and ■ IPRU-INV 4.5.1D are given under section 318 of the *Act* (Exercise of powers through Council), for the purpose of achieving the objective specified, as required by section 318(2) of the *Act*, in ■ IPRU-INV 4.3.1D.
- 4.2.3** **G** *Underwriting agents* are subject to regulation by the *Society* as well as by the *appropriate regulator*. In particular, they are subject to requirements as to their financial resources and as to making and maintaining accounting records, set by the *Society*. The *appropriate regulator* is satisfied that *underwriting agents* will be subject to adequate financial resource and accounting requirements as long as they remain subject to and comply with requirements at least equivalent to Lloyd's Capital and Solvency Requirements 2001 and the relevant parts of, or requirements made under Lloyd's Underwriting Agents Byelaw (No. 4 of 1984), in each case as amended and in force immediately before *commencement*. Accordingly, instead of imposing an obligation directly on *members' agents*, the directions in ■ IPRU-INV 4.4.1D to ■ IPRU-INV 4.4.5D and ■ IPRU-INV 4.5.1D require the *Society* to require those firms to comply with the relevant requirements.
- 4.2.4** **G** A *members' adviser* is not regulated by the *Society* and accordingly this chapter specifies the financial resource and accounting requirements to be met. *Firms* which fall within the scope of this chapter will be *firms* with *permission* only to advise persons on *syndicate* participation at Lloyd's. The nature of that advisory business is akin to corporate finance advice and so the applicable requirements are those in ■ IPRU-INV 3 relevant to *firms* giving corporate finance advice. *Firms* with other *permissions* will fall within the scope of other chapters of *IPRU(INV)*, *GENPRU*, *BIPRU*, *IFPRU* (and the *EU CRR*) or *INSPRU*.



4.3 SPECIFICATION OF OBJECTIVE

4.3.1

- D** The directions in ■ IPRU-INV 4.4.1D to ■ IPRU-INV 4.4.5D and ■ IPRU-INV 4.5.1D are given in relation to the exercise of the powers of the *Society* and of the *Council* generally, with a view to achieving the objective that *members' agents* have adequate financial resources to support, and keep and preserve adequate accounting records in respect of their business at Lloyd's.

4.4 FINANCIAL RESOURCE REQUIREMENTS

- 4.4.1** **D** The *Society* must maintain appropriate and effective arrangements to require *members' agents* to meet and continue to meet financial resource requirements at least equivalent to the requirements set out in Lloyd's Capital and Solvency Requirements 2001, as they are in force immediately before *commencement*.
- 4.4.2** **D** The *Society* must give the *FCA* a report on each *members' agent's* compliance with the financial resource requirements referred to in ■ IPRU-INV 4.4.1D as at the end of each quarter (determined by reference to each underwriting agent's *accounting reference date*).
- 4.4.3** **D** The report referred to in ■ IPRU-INV 4.4.2D must reach the *FCA* within two months of the end of the relevant quarter and must state:
- (1) whether the *Society* has any information indicating or tending to indicate that, during the quarter to which the report relates, the *members' agents* failed to meet the financial resource requirements referred to in ■ IPRU-INV 4.4.1D;
 - (2) whether, at the end of the quarter to which the report relates, the *members' agents* failed to meet the financial resource requirements referred to in ■ IPRU-INV 4.4.1D; an
 - (3) the nature and extent of any failure to comply reported under (1) or (2) and the actions taken or to be taken by the *Society* in response to this.
- 4.4.4** **D** In addition to the reports required under ■ IPRU-INV 4.4.2D, the *Society* must give the *FCA* an annual report on each *members' agents* compliance or non-compliance with financial resource requirements as at the end of that *members' agent's* financial year.
- 4.4.5** **D** The report in ■ IPRU-INV 4.4.4D must reach the *FCA* within seven months of that *members' agent's* accounting reference date and must:
- (1) confirm that:
 - (a) the *Society* has received from that *members' agent* in respect of the financial year to which the report relates, all relevant attachments to the Annual Financial Return that the *members'*

agent is required to make to the *Society* under the requirements identified in ■ IPRU-INV 4.4.1D;

- (b) that *members' agent* met the applicable financial resource requirements at the end of the financial year to which the report relates; and
- (c) the *Society* is not aware of any matters likely to be of material concern to the *FCA* relating to that *members' agent's* compliance with financial resource requirements during the year to which the report relates, or arising from the attachments referred to in (a); or

- (2) if the *Society* is unable to give any of the confirmations required under ■ IPRU-INV 4.4.5D (1)(a), (b) or (c), set out in each case the reasons why it is unable to give that confirmation.

4.4.5A **D** The *Society* must submit the reports in ■ IPRU-INV 4.4.2D to ■ IPRU-INV 4.4.5D in accordance with the *rules* in ■ SUP 16.3 (General provision on reporting).

4.4.6 **R** A *members' adviser* must comply with the requirements of IPRU-INV 3-60(3) and IPRU-INV 3-62.



4.5 ACCOUNTING RECORDS

- 4.5.1** D The *Society* must maintain appropriate and effective arrangements to require *members' agents* to meet the obligation to keep and preserve accounting records, set out in Lloyd's Underwriting Agents Byelaw (No 4 of 1984), Section III, paragraph 53B, as it is in force immediately before *commencement*.

- 4.5.2** R A *members' adviser* must comply with the requirements of ■ IPRU-INV 3.10 to ■ IPRU-INV 3.14.

Chapter 5

Financial resources

5.1 Application

5.1.1

R

- (1) (a) This chapter applies to an *investment management firm*, other than:
- (i) an *incoming EEA firm* unless it has a *top-up permission* for acting as trustee or depositary of a UCITS; or
 - (ii) a *MiFID investment firm* (unless it is an *exempt CAD firm* for the purpose of calculating its own funds and if it carries on any *regulated activity* other than *MiFID business*).
- (aa) This chapter applies, as set out in ■ IPRU-INV 5.1.2R, to:
- (i) *exempt CAD firms*;
 - (ii) **OPS firms**;
 - (iii) non-OPS Life Offices and non-OPS Local Authorities; and
 - (iv) individuals admitted to membership collectively.

5.1.2

R

	Exempt CAD firms	OPS firms (see Note 1 below)	Non-OPS Life Offices and Non-OPS Local Authorities	Individuals admitted to membership collectively
Financial resources rules				
IPRU-INV 5.2.1R to 5.7.3R	No (see Note 3 below)	No	No	Yes
	Individuals whose sole investment business is giving investment advice to institutional or corporate investors		<i>Firms</i> subject to "lead regulator arrangements"	All other <i>firms</i>
Financial resources rules				
IPRU-INV 5.2.1R to 5.7.3R	No		No	Yes
			(see Note 2 below)	
Accounting records rules				

	Exempt CAD firms	OPS firms (see Note 1 below)	Non-OPS Life Offices and Non-OPS Local Authorities	Individuals admitted to membership collectively
IPRU-INV 5.3.1R (1) to 5.3.1R(6)	No		Yes	Yes

Note 1. *Firms* are referred to the specific compliance reports for **OPS firms** required by Chapter 16 of the Supervision Manual.

Note 2. A *firm* subject to "lead regulator arrangements" whereby a body other than the *FCA* is responsible for its financial regulation shall comply with the corresponding **financial resources rules** and **financial returns rules** of that body, and a breach of such rules shall be treated as a breach of the rules of the *FCA*.

Note 3. The financial and non-financial resources rules for an *exempt CAD firm* are set out in IPRU-INV chapter 9. However, IPRU-INV 5.2.1R to 5.7.3R apply to an *exempt CAD firm* for the purpose of calculating its **own funds** (see IPRU-INV 9.2.9R(2)(a)) (although the Category A items of Tier 1 capital as set out in IPRU-INV 5.8.1R are replaced by all the items in IPRU-INV 9.3.1R) and if it carries on any *regulated activity* other than *MiFID business* (see IPRU-INV 9.2.3R).

5.1.3

R

An incoming EEA firm with a top-up permission for acting as trustee or depositary of a UCITS must comply with:

- (a) ■ IPRU-INV 5.2.1R;
- (b) ■ IPRU-INV 5.2.2R;
- (c) ■ IPRU-INV 5.2.3R;
- (d) ■ IPRU-INV 5.3.2R;
- (e) ■ IPRU-INV 5.4.4R; and
- (f) ■ IPRU-INV 5.4.8R.

Interpretation

5.1.4

G

The definitions in the glossary at ■ IPRU-INV 5 Appendix 1 apply to terms shown in **bold** type in this chapter (other than headings and titles). Where the term is italicised, the *FCA Handbook Glossary* definition applies.

5.2 General requirement

Adequacy of financial resources

- 5.2.1 **R** A *firm* must at all times have available the amount and type of **financial resources** required by the rules in this chapter.

Basic requirement

- 5.2.2 **R** A *firm* must ensure that, at all times, its **financial resources** are not less than its **financial resources requirement**.

Financial resources

- 5.2.3 **R** A *firm's financial resources* means:
- (a) its **own funds**, if the *firm* is subject to an **own funds requirement** under ■ IPRU-INV 5.4.2R or ■ IPRU-INV 5.4.4R; or
 - (b) its **liquid capital**, if the *firm* is subject to a **liquid capital requirement** under ■ IPRU-INV 5.4.1R.

5.3 Financial resources

Own funds

- 5.3.1 **R** A *firm* must calculate its **own funds** in accordance with ■ IPRU-INV 5.8, unless the *firm* has a *Part 4A permission* for acting as trustee or depositary of a UCITS.
- 5.3.2 **R** For a *firm* that has a *Part 4A permission* for acting as trustee or depositary of a UCITS, own funds has the meaning in article 4(1)(118) of the EU CRR.

Liquid capital

- 5.3.3 **R**
- (a) A *firm* must calculate its **liquid capital** in accordance with ■ IPRU-INV 5.8.
 - (b) In addition to the above, a *firm* whose **permitted business** includes *establishing, operating or winding up a personal pension scheme* must comply with:
 - (i) the requirements in relation to the realisability of **liquid capital** found in Note 2 of ■ IPRU-INV 5.9.1R; and
 - (ii) the limitation in respect of Item 14 of ■ IPRU-INV 5.8.2R, not to include net **trading book** profits in the *firm's liquid capital* calculation.

5.4 Financial resources requirement

Determination of requirement

5.4.1 **R** The **financial resources requirement** for a *firm* is a **liquid capital requirement**, determined in accordance with ■ IPRU-INV 5.4.10R:

- (i) unless the *firm* falls within any of the exceptions in ■ IPRU-INV 5.4.2R; or
- (ii) the *firm* is an *incoming EEA firm* with a *top-up permission* of acting as trustee or depositary of a UCITS.

Exceptions from the liquid capital requirement

5.4.2 **R** The **financial resources requirement** is an **own funds requirement** determined in accordance with ■ IPRU-INV 5.4.3R for a *firm* if its **permitted business** does not include *establishing, operating or winding up a personal pension scheme* and which:

- (i) is an *exempt CAD firm* which is also a *residual CIS operator* or a *small authorised UK AIFM* and that scheme or AIF only invests in *venture capital investments* for **non-retail clients**; or
- (ii) is not an *exempt CAD firm* if:
 - (a) the *firm's permitted business* does not include the holding of customers' monies or assets and it neither executes transactions (or otherwise arranges deals) in **investments** nor has such transactions executed for itself or its customers; or
 - (b) the *firm's permitted business* includes the activities as in (a) above, but only in respect of *venture capital investments* for **non-retail clients**; or
 - (c) the *firm* is a trustee of an *authorised unit trust scheme* whose **permitted business** consists only of trustee activities and does not include any other activity constituting **specified trustee business** or the *firm* is a depositary of an ICVC or ACS or a *depositary* appointed in line with ■ FUND 3.11.12R (Eligible depositaries for UK AIFs) or a UK depositary of a *non-EEA AIF* whose **permitted business** consists only of depositary activities.
 - (d) the *firm's permitted business* limits it to *acting a residual CIS operator* or a *small authorised UK AIFM* where the main purpose of the *collective investment scheme* or *AIF* (as applicable) is to invest in *permitted immovables* whether in the UK or abroad.

Own funds requirement

- 5.4.3** **R** The **own funds requirement** for a *firm* subject to **■ IPRU-INV 5.4.2R** is the higher of:
- (i) £4 million for a *firm* which is a *depository* of an *authorised fund*, if the *authorised fund* is an *AIF*;
 - (ia) €125,000 for a *firm* which is a *depository* appointed in line with **■ FUND 3.11.12R** (Eligible depositories for UK AIFs) or a *UK depository* of a *non-EEA AIF*;
 - (ib) for a *firm* which is a *depository* of a *UCITS scheme*, the higher of:
 - (A) the requirement calculated depending on the selected approach in accordance with articles 315 or 317 of the *EU CRR*; and
 - (B) £4million; and
 - (ii) £5,000 for any other *firm*.
- 5.4.4** **R** The **financial resources requirement** for an *incoming EEA firm* with a *top-up permission* for acting as trustee or depository of a *UCITS* is the **own funds requirement** in **■ IPRU-INV 5.4.3R(ib)**.
- 5.4.5** **G** In accordance with **■ IPRU-INV 5.4.3R(ib)(A)** and **■ IPRU-INV 5.4.4R**, a *firm* which is a *depository* of a *UCITS scheme* has a choice between:
- (a) the basic indicator approach in article 315 of the *EU CRR*; and
 - (b) the standardised approach in article 317 of the *EU CRR*.
- 5.4.6** **G** If a *firm* that is the *depository* of a *UCITS scheme* is seeking to determine its **own funds requirement** on the basis of the standardised approach in article 317 *EU CRR*, it should notify the *FCA* in advance.
- 5.4.7** **G** The effect of **■ IPRU-INV 5.4.4R** is to apply the **financial resources requirement** to an *incoming EEA firm* with a *top-up permission* for acting as trustee or depository of a *UCITS* in relation to its activity in the *UK* of acting as trustee or depository of a *UCITS*.
- 5.4.8** **R** A *firm* which is the *depository* of a *UCITS scheme* must comply with the *rules* in **■ IFPRU 2** as if it were an *IFPRU investment firm* that is not a *significant IFPRU investment firm*.
- 5.4.9** **G** A *firm* to which **■ IPRU-INV 5.4.8R** applies is, in particular, reminded of the *rules* in **■ IFPRU 2** that determine whether a *firm* must apply the *ICAAP rules* on an individual basis or comply with them on a *consolidated basis* or *sub-consolidated basis* (see **■ IFPRU 2.2.45R** to **■ IFPRU 2.2.49R**).

Liquid capital requirement

5.4.10

R

The **liquid capital requirement** for a *firm* subject to ■ IPRU-INV 5.4.1R is:

- (i) for a *firm* whose **permitted business** includes *establishing, operating or winding up a personal pension scheme*, the higher of (A) £20,000, and (B) the calculation from ■ IPRU-INV 5.9.1R;
- (ii) for any other *firm*, the higher of (A) £5,000 and (B), its *total capital requirement* calculated in accordance with ■ IPRU-INV 5.4.12R.

5.4.11

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(1) This guidance applies to a *firm* whose **permitted business** includes *establishing, operating or winding up a personal pension scheme* for the purpose of ■ IPRU-INV 5.9.1R.

(2) A *firm* should:

- (a) value each asset in accordance with generally accepted standards used in the relevant sector for the asset, taking into account its individual characteristics and using all the information reasonably available;
- (b) on a consistent basis across all *clients* who hold the same type of assets, apply the following:
 - (i) a prudent valuation approach; and
 - (ii) a reasonable valuation methodology;
- (c) when determining whether an asset is capable of being readily realised within 30 days, consider whether:
 - (i) the transaction can be concluded within that time limit in the ordinary course of business. For example, if the transaction can be concluded within 30 days but, in practice, takes longer due to factors such as delays in receiving information or permissions from third parties, then the asset can be categorised as a Standard Asset;
 - (ii) a Standard Asset can be realised for a value close to the most recent valuation if no material change to the underlying economic conditions has occurred.

Total capital requirement

5.4.12

R

A *firm's total capital requirement* is the sum of its:

- (a) **expenditure based requirement** calculated in accordance with ■ IPRU-INV 5.10;
- (b) **position risk requirement** calculated in accordance with ■ IPRU-INV 5.11;
- (c) **counterparty risk requirement** calculated in accordance with ■ IPRU-INV 5.12 to ■ 5.15;
- (d) **foreign exchange requirement** calculated in accordance with ■ IPRU-INV 5.16; and

- (e) **other assets requirement** calculated in accordance with
■ IPRU-INV 5.17.

5.4.13

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A *firm* which discloses clients' money or assets on its balance sheet need not calculate the requirements under ■ IPRU-INV 5.11 to ■ 5.17 on such items where these do not represent assets or liabilities of the *firm* itself.

5.5 Annual expenditure

Determination

5.5.1

R

Annual expenditure is:

- (a) the sum of the amounts described as total expenditure in the four quarterly **financial returns** up to (and including) that prepared at the *firm's* most recent **accounting reference date**, less the following items (if they are included within such expenditure):
 - (i) staff bonuses, except to the extent that they are guaranteed;
 - (ii) employees' and directors' shares in profits, except to the extent that they are guaranteed;
 - (iii) other appropriations of profits;
 - (iv) shared commission and fees payable which are directly related to commission and fees receivable which are included within total revenue;
 - (v) interest charges in respect of borrowings made to finance the acquisition of the *firm's* **readily realisable investments**;
 - (vi) interest paid to customers on client money;
 - (vii) interest paid to *counterparties*;
 - (viii) fees, brokerage and other charges paid to clearing houses, exchanges and intermediate brokers for the purposes of executing, registering or clearing transactions;
 - (ix) foreign exchange losses; or
- (b) where the previous accounting period does not include twelve months' trading, an amount calculated in accordance with paragraph (a) above prorated to an equivalent annual amount; or
- (c) where a *firm* has not prepared four quarterly **financial returns** since the commencement of its **permitted business**, an amount based on forecast expenditure included in its budget for the first twelve months' trading, as submitted with its application for membership.

5.5.2

G

A *firm's* **financial resources requirement** will be recalculated annually when its fourth quarterly **financial return** is prepared. The *firm* must maintain **financial resources** sufficient to meet its new **financial resources requirement** from the date on which the fourth quarterly **financial return** is prepared and

no later than 80 business days after the *firm's accounting reference date*. The **expenditure based requirement** applicable at the **accounting reference date** will be based on the four quarterly **financial returns** prepared up to and on that date.

5.6 Qualifying subordinated loans

Characteristics of long term qualifying subordinated loans

- 5.6.1 **R** A long term **qualifying subordinated loan** (■ IPRU-INV 5.8.1R Item 11) must have the following characteristics:
- (a) the loan is repayable only on maturity or on the expiration of a period of notice in accordance with paragraph (c) below or on the winding up of the *firm*;
 - (b) in the event of the winding up of the *firm*, the loan ranks after the claims of all other creditors and is not to be repaid until all other debts outstanding at the time have been settled;
 - (c) either
 - (i) the minimum original maturity of the loan is 5 years; or
 - (ii) the loan does not have a minimum or fixed maturity but requires 5 years notice of repayment; and
 - (d) the loan is fully paid-up.

Amount allowable in the calculation of own funds

- 5.6.2 **R** A *firm* may only take into account the paid-up amount of a long term **qualifying subordinated loan** in the calculation of its **own funds**. This amount must be amortised on a straight-line basis over the five years prior to the date of repayment.

Requirements applicable to short-term qualifying subordinated loans

- 5.6.3 **R** A short term **qualifying subordinated loan** (■ IPRU-INV 5.8.1R item 15) must have the characteristics set out in ■ IPRU-INV 5.6.1R save that the minimum period set out in ■ IPRU-INV 5.6.1R(c) shall be two years.

- 5.6.4 **R** A *firm* must not make any payment of principal or interest which would result in a breach of ■ IPRU-INV 5.2.2R.

Form of qualifying subordinated loan agreement

- 5.6.5 **R** A **qualifying subordinated loan** must be in the form prescribed by the *FCA* for the purposes of this *rule*.

5.6.6 **G** *Firms* wishing to initiate a subordinated loan agreement other than in the prescribed form are advised to contact the *FCA*.

Conditions applicable to qualifying subordinated loans

5.6.7 **R** A *firm* wishing to include a **qualifying subordinated loan** in its calculation of **liquid capital** must:

- (a) provide the *FCA* with a copy of the agreement not less than 10 business days before the loan is to be made; and
- (b) certify to the *FCA* that the loan agreement complies with the *FCA*'s **prescribed subordinated loan agreement**.

Requirements on a firm in relation to qualifying subordinated loans

5.6.8 **R** A *firm* including a **qualifying subordinated loan** in its calculation of **liquid capital** must not:

- (a) secure all or any part of the loan;
- (b) redeem, purchase or otherwise acquire any of the liabilities of the borrower in respect of the loan;
- (c) amend or concur in amending the terms of the loan agreement;
- (d) repay all or any part of the loan otherwise than in accordance with the terms of the loan agreement; or
- (e) take or omit to take any action whereby the subordination of the loan or any part thereof might be terminated, impaired or adversely affected.

5.7 Qualifying property and qualifying undertakings

Qualifying property and qualifying amount defined

- 5.7.1** **R** **Qualifying property** is any freehold or leasehold (or the equivalent tenure in Scotland or other territories) land and buildings purchased or secured by way of a mortgage (or other form of secured long-term arrangement) where the security for the liability is the property (and does not include any other allowable assets). The qualifying amount is the lowest of:
- (a) 85 per cent of the current market value of the property (if known);
 - (b) 85 per cent of the net book value of the property;
 - (c) the amount of the liability outstanding under mortgage or other secured long term arrangement, excluding any part of the liability repayable within one year.

- 5.7.2** **G** ■ IPRU-INV 5.7.1R can be illustrated as follows:

Current market value	£200,000
Net book value	£100,000
Mortgage	£70,000, including £5,000 payable within one year
Qualifying amount is the lowest of:	
(a) 85% x £200,000 =	£170,000
(b) 85% x £100,000 =	£85,000
(c) £70,000 - £5,000 =	£65,000
i.e. £65,000	

Qualifying undertakings

- 5.7.3** **R** A **qualifying undertaking** is an arrangement between a *firm* and an approved bank which:
- (a) is in the form prescribed by the *FCA* for the purposes of this *rule*; and
 - (b) complies with the appropriate limitations set out in ■ IPRU-INV 5.8.2R(7).

5.8 Calculation of own funds and liquid capital

5.8.1

R A firm must calculate its **own funds** and **liquid capital** as shown below, subject to the detailed requirements set out in ■ IPRU-INV 5.8.2R.

	Financial resources	Category	IPRU-INV 5.8.2R paragraph
Tier 1			
	(1) Paid-up share capital (excluding preference shares)	A	
	(1A) Eligible LLP members' capital		
	(2) Share premium account		
	(3) Reserves		2A
	(4) Non-cumulative preference shares		
Less:	(5) Investments in own shares	B	
	(6) Intangible assets		
	(7) Material current year losses		4
	(8) Material holdings in credit and financial institutions and, for <i>exempt CAD firms</i> only, material insurance holdings.		5 and 5A
	(8A) Excess LLP members' drawings		
	Tier 1 capital = (A-B)	C	
	Plus: TIER 2		1
	(9) Revaluation reserves	D	
	(10) Fixed term cumulative preference share capital		1(a)
	(11) Long-term Qualifying Subordinated Loans		1(a); 6

Financial resources		Category	IPRU-INV 5.8.2R paragraph
(12)	Other cumulative preference share capital and debt capital but, for <i>exempt CAD firms</i> , only perpetual cumulative preference share capital and qualifying capital instruments		6A
(13)	Qualifying arrangements		7
"Own Funds" = (C+D)		E	
Plus: TIER 3			
(14)	Net trading book profits	F	1(b)(i); 8
(15)	Short-term Qualifying Subordinated Loans and excess Tier 2 capital		1(b)(ii); 1(c); 9
(16)	Illiquid assets	G	10
(17)	Qualifying Property		11
"Liquid Capital" = (E+F+G)			

5.8.2

R

1 Deductions and Ratios (Items 10, 11 and 15)	(a)	Notwithstanding IPRU-INV 5.8.1R and 5.8.2R for an <i>exempt CAD firm</i> , in calculating own funds , all of Item 8 must be deducted after the total of Tier 1 and Tier 2 capital and the following restrictions apply: <ul style="list-style-type: none"> (i) the total of fixed term cumulative preference shares (item 10) and long-term qualifying subordinated loans (item 11) that may be included in Tier 2 capital is limited to 50 per cent of Tier 1 capital; (ii) Tier 2 capital must not exceed 100 per cent of Tier 1 capital.
	(b)	A <i>firm</i> which is not an <i>exempt CAD firm</i> and which is subject to a liquid capital requirement under IPRU-INV 5.4.1R may take into account qualifying subordinated loans in the calculation of liquid capital up to a maximum of 400% of its Tier 1 capital.
2 Non corporate entities	(a)	In the case of <i>partnerships</i> or <i>sole traders</i> , the following terms should be substituted, as appropriate, for items 1 to 4 in Tier 1 capital: <ul style="list-style-type: none"> (i) partners' capital accounts (excluding loan capital);

- (ii) partners' current accounts (excluding unaudited profits and loan capital);
- (iii) proprietors' account (or other term used to signify the sole trader's capital but excluding unaudited profits).
- (b) Loans other than **qualifying subordinated loans** shown within partners' or proprietors' accounts must be classified as Tier 2 capital under item 12.
- (c) For the calculation of **own funds**, partners' current accounts figures are subject to the following adjustments in respect of a *defined benefit occupational pension scheme*:
 - (i) a *firm* must derecognise any *defined benefit asset*;
 - (ii) a *firm* may substitute for a *defined benefit liability* the *firm's deficit reduction amount*. The election must be applied consistently in respect of any one financial year.

Note 1

A *firm* should keep a record of and be ready to explain to its supervisory contacts in the *FCA* 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.

2A Reserves

For the calculation of **own funds** the following adjustments apply to the audited reserves figure:

- (a) a *firm* must deduct any unrealised gains or, where applicable, add back in any unrealised losses on cash flow hedges of financial instruments measured at cost or amortised cost;
- (b) in respect of a *defined benefit occupational pension scheme*, a *firm* must derecognise any *defined benefit asset*;
- (c) a *firm* may substitute for a *defined benefit liability* the *firm's deficit reduction amount*. The election must be applied consistently in respect of any one financial year.

Note 2

A *firm* should keep a record of and be ready to explain to its supervisory contacts in the *FCA* 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*.

- (d) a *firm* must not include any unrealised gains from investment property.

Note 3

Unrealised gains from investment property should be reported as part of revaluation reserves.

- (e) where applicable, a *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.

Note 4

Reserves must be audited unless the *firm* is exempt from the provisions of Part VII of the Companies Act 1985 (section 249A (Exemptions from audit)), or where applicable, Part 16 of the Companies Act 2006 (section 477 (Small companies: Conditions for exemption from audit)) relating to the audit of accounts.

3 Intangible assets (Item 6) Intangible assets comprise:

- (a) formation expenses to the extent that these are treated as an asset in the *firm's* accounts;
- (b) goodwill, to the extent that it is treated as an asset in the *firm's* accounts; and
- (c) other assets treated as intangibles in the *firm's* accounts.

Intangible assets do not include a deferred acquisition cost asset.

4 Material current year losses (Item 7) Losses in current year operating figures must be deducted when calculating Tier 1 capital if such losses are material. For this purpose profits and losses must be calculated quarterly or monthly, as appropriate. If this calculation reveals a net loss it shall only be deemed to be material for the purposes of this Table if it exceeds 10 per cent of the *firm's* Tier 1 capital.

5 Material holdings in credit and financial institutions (Item 8) Material holdings comprise:

- (a) where the *firm* holds more than 10 per cent of the equity share capital of the institution, the value of that holding and the amount of any subordinated loans to the institution and the value of holdings in **qualifying capital items** or **qualifying capital instruments** issued by the institution;
- (b) in the case of holdings other than those mentioned in (a) above, the value of holdings of equity share capital in, and the amount of subordinated loans made to, such institutions and the value of

	<p>holdings in qualifying capital items or qualifying capital instruments issued by such institutions to the extent that the total of such holdings and subordinated loans exceeds 10 per cent of the <i>firm's own funds</i> calculated before the deduction of item 8.</p>
<p>5A Material insurance holdings (Item 8)</p>	<p>(a) A material insurance holding means the holdings of an <i>exempt CAD firm</i> of items of the type set out in (b) in any:</p> <ul style="list-style-type: none"> (i) <i>insurance undertaking</i>; or (ii) <i>insurance holding company</i>; <p>that fulfils one of the following conditions:</p> <ul style="list-style-type: none"> (iii) it is a subsidiary undertaking of that <i>firm</i>; or (iv) that <i>firm</i> holds a participation in it. <p>(b) An item falls into this provision for the purpose of (a) if it is:</p> <ul style="list-style-type: none"> (i) an ownership share; or (ii) subordinated debt or another item of capital that forms part of the <i>tier two capital resources</i> that falls into GENPRU 2 or, as the case may be, INSPRU 7, or is an item of "basic own funds" defined in the <i>PRA Rulebook: Glossary</i>.
<p>6 Long term qualifying subordinated loans (Item 11)</p>	<p>Loans having the characteristics prescribed by IPRU-INV 5.6.1R may be included in item 11, subject to the limits set out in paragraph (1) above.</p>
<p>6A Perpetual cumulative preference share capital</p>	<p>Perpetual cumulative preference share capital may not be included in the calculation of own funds by an <i>exempt CAD firm</i> unless it meets the following requirements:</p> <ul style="list-style-type: none"> (a) it may not be reimbursed on the holder's initiative or without the prior agreement of the <i>FCA</i>; (b) the instrument must provide for the <i>firm</i> to have the option of deferring the dividend payment on the share capital; (c) the shareholder's claims on the <i>firm</i> must be wholly subordinated to those of all non-subordinated creditors; (d) the terms of the instrument must provide for the loss-absorption capacity of the share capital and unpaid dividends, whilst enabling the <i>firm</i> to continue its business; and (e) it must be fully paid-up.
<p>7 Qualifying arrangements (Item 13)</p>	<p>(a) An <i>exempt CAD firm</i> may only include a qualifying undertaking or other arrangement in item 13 if it is a qualifying capital instrument or a qualifying capital item.</p>

8 Net trading book profits (Item 14)

- (b) A *firm* which is not an *exempt CAD firm* may only include **qualifying undertakings** in its calculation of **liquid capital** if:
- (i) it maintains **liquid capital** equivalent to 6/52 of its **annual expenditure** in a form other than **qualifying undertakings**; and
 - (ii) the total amount of all **qualifying undertakings** plus **qualifying subordinated loans** does not exceed the limits set out in paragraph (1)(b) above.

For *firms* which are not *exempt CAD firms* unaudited profits can be included at item 14.

This Item must not be included in the *liquid capital calculation* of a *firm* whose *permitted business* includes *establishing, operating or winding up a personal pension scheme*.

Note 5

Non-trading book interim profits may only be included in Tier 1 of the calculation if they have been independently verified by the *firm's* external auditors, unless the *firm* is exempt from the provisions of Part VII of the Companies Act 1985 (section 249A (Exemptions from audit)), or where applicable, Part 16 of the Companies Act 2006 (section 477 (Small companies: Conditions for exemption from audit)) relating to the audit of accounts.

For this purpose, the external auditor should normally undertake at least the following:

- (a) satisfy himself that the figures forming the basis of the interim profits have been properly extracted from the underlying accounting records;
- (b) review the accounting policies used in calculating the interim profits so as to obtain comfort that they are consistent with those normally adopted by the *firm* in drawing up its annual financial statements;
- (c) perform analytical review procedures on the results to date, including comparisons of actual performance to date with budget and with the results of prior periods;
- (d) discuss with management the overall performance and financial position of the *firm*;
- (e) obtain adequate comfort that the implications of current and prospective litigation, all known claims and commitments, changes in business activities and provisions for bad and doubtful debts have been properly taken into account in arriving at the interim profits; and

	<p>(f) follow up problem areas of which the auditors are already aware in the course of auditing the <i>firm's</i> financial statements.</p> <p>A <i>firm</i> wishing to include interim profits in Tier 1 capital in a financial return should submit to the FCA with the financial return a verification report signed by its external auditor which states whether the interim results are fairly stated, unless the <i>firm</i> is exempt from the provisions of Part VII of the Companies Act 198 (section 249A (Exemptions from audit)), or where applicable, Part 16 of the Companies Act 2006 (section 477 (Small companies: Conditions for exemption from audit)) relating to the audit of accounts.</p> <p>Profits on the sale of capital items or arising from other activities which are not directly related to the investment business of the <i>firm</i> may also be included within the calculation of liquid capital, but (unless the <i>firm</i> is exempt as above) only if they can be separately verified by the <i>firm's</i> auditors. In such a case, such profits can form part of the <i>firm's</i> Tier 1 capital as profits.</p>
9 Short term qualifying subordinated loans (Item 15)	Loans having the characteristics prescribed by IPRU-INV 5.6.3R may be included in item 15 subject to the limits set out in paragraph (1) above. Tier 2 capital which exceeds the ratios prescribed by paragraph (1)(a) and (b) may be included in item 15 subject to paragraph (1) above.
10 Illiquid assets (Item 16)	<p>Illiquid assets comprise:</p> <p>(a) tangible fixed assets.</p> <p>Note 6</p> <p>In respect of tangible fixed assets purchased under finance leases the amount to be deducted as an illiquid asset shall be limited to the excess of the asset over the amount of the related liability shown on the balance sheet.</p> <p>(b) holdings in, including subordinated loans to, credit or financial institutions which may be included in the own funds of such institutions unless they have been deducted under item 8;</p> <p>(c) any investment in undertakings other than credit institutions and other financial institutions where such investments are not readily realisable;</p> <p>(d) any deficiency in net assets of a subsidiary;</p> <p>(e) deposits not available for repayment within 90 days or less (except for payments in connection with margined futures or options contracts);</p> <p>Note 7</p> <p>Where cash is placed on deposit with a maturity of more than 90 days but is repayable on demand subject to the payment of a penalty, then</p>

this is not required to be deducted as an illiquid asset but a deduction is required for the amount of the penalty.

- (f) loans, other debtors and accruals not falling due to be repaid within 90 days or which are more than one month overdue by reference to the contractual payment date;
- (g) physical stocks (except where subject to the **position risk requirement** as set out in IPRU-INV 5.11; and
- (h) prepayments to the extent that the period of prepayment exceeds six weeks in the case of a *firm* subject to the 6/52 **expenditure based requirement** or thirteen weeks in the case of a firm subject to the 13/52 **expenditure based requirement**.
- (i) if not otherwise covered, any holding in eligible capital instruments of an insurance undertaking, insurance holding company, or reinsurance undertaking that is a subsidiary or participation. Eligible capital instruments include ordinary share capital, cumulative preference shares, perpetual securities and long-term subordinated loans that are eligible for insurance undertakings under INSPRU 1.

Illiquid assets do not include a defined benefit asset or a deferred acquisition cost asset.

11 Qualifying property (Item 17)

This item comprises the qualifying amount calculated in accordance with IPRU-INV 5.7.1R.

5.9 Liquid Capital Requirement for firms whose permitted business includes establishing, operating or winding up a personal pension scheme

5.9.1

R

Liquid Capital Requirement = Initial Capital Requirement + Capital Surcharge

Calculation of Initial Capital Requirement

$$\text{ICR} = (\sqrt{\text{AUA}}) \times \text{K1}$$

Where

ICR means Initial Capital Requirement

AUA means Assets Under Administration calculated as the sum of the most recent annual valuations over the preceding 12 months of the personal pension schemes administered by the *firm*, and adjusted to include any revaluation of assets that may occur between the date of the most recent annual valuation and the date when the *firm* must calculate its AUA.

A *firm* must calculate its AUA quarterly in line with the dates when it has to submit its regulatory capital reporting form in accordance with SUP 16.12 (Integrated Regulatory Reporting).

Where it is not possible to value an asset (for example because there is no readily available market price), the most recent market valuation should be used.

Where it would be reasonable to assume that the value of the asset has changed by more than 15% since the most recent market valuation, a *firm* should instead use a reasonable estimate. This is without prejudice to any requirement on a *firm* to provide a personal pension scheme member with accurate and timely valuations of their portfolios.

K1 is set subject to the *firm's* AUA as specified in the below table:

AUA	K1 constant to be applied
<£100m	10
£100-£200m	15
>£200m	20

When K1 changes due to an increase in AUA, in accordance with the thresholds in this table, the *firm* must apply the new K1 value within six months following the date on

which its AUA exceeded the threshold of its previous K1 value.

Calculation of Capital Surcharge

$$CS = (\sqrt{P}) \times K2 \times ICR$$

Where

CS

means Capital Surcharge

P

means the fraction of *personal pension schemes* administered by the *firm* which contain one or more asset types which do not appear in the list of Standard Assets below, at the most recent quarter end. For example, if a quarter of personal pensions contained non-Standard Assets, this would be inputted in to the formula as 0.25.

K2

is set at 2.5.

ICR

means the Initial Capital Requirement calculated as above.

Standard Assets

The List of Standard Assets is as follows (subject to Note 1):

Cash

Cash funds

Deposits

Exchange traded commodities

Government & local authority bonds and other fixed interest stocks

Investment notes (structured products)

Shares in *Investment trusts*

Managed pension funds

National Savings and Investment products

Permanent interest bearing shares (PIBs)

Physical gold bullion

Real estate investment trusts (REITs)

Securities admitted to trading on a regulated venue

UK commercial property

Units in *regulated collective investment schemes*

NOTE 1:

A Standard Asset must be capable of being accurately and fairly valued on an ongoing basis and readily realised within 30 days, whenever required.

NOTE 2:

In addition to complying with the provisions of IPRU-INV 5.8, in accordance with IPRU-INV 5.3.2R, a *firm* must hold its *liquid capital* in **financial resources** as follows:

ICR

realisable within 12 months; and

CS

realisable within 30 days

5.10 Expenditure based requirement

5.10.1 **R** A *firm's expenditure based requirement* is a fraction of its **annual expenditure** determined in accordance with ■ IPRU-INV 5.10.2 R.

5.10.2 **R**

1: The fraction is 6/52 where:

- (a) the *firm* is an *authorised unit trust manager*; or
- (aa) the *firm* is an *authorised contractual scheme manager*; or
- (b) the *firm* acts only as an *authorised corporate director* of an *ICVC*; or
- (c) the *firm* is an **investment manager** (including the operator of an unregulated collective investment scheme in relation to which the *firm* carries on the activity of an **investment manager**), unless paragraph 2 applies.

2: The fraction is 13/52 where the *firm* is an **investment manager** as in paragraph 1(c) above, or is a *custodian*, and the *firm* either:

- (a) itself holds customers' monies or assets; or
- (b) procures the appointment as custodian of its customers' monies or assets of an associate of the *firm* which is not an approved bank.

[**Note:** Paragraph 1(a) above includes a *firm* which acts as an authorised **unit trust manager** and, in addition, is both or either:

- (a) an *authorised corporate director* of an *ICVC*; or
- (b) an *authorised contractual scheme manager*]

5.11 Position risk requirement

5.11.1

R

A *firm's* **position risk requirement** is determined by calculating on a daily mark to market basis, the sum of the weighted value of each position held by the *firm*. The weighted value for each position must be calculated by multiplying its current market value by the appropriate factor set out in ■ IPRU-INV 5.11.2R.

[**Note:** this requirement does not attach to items deducted in full as illiquid assets]

5.11.2

R

Instrument		Requirement		
A Debt	Maturity	0-2 years	2-5 years	>5 years
Central Government		2%	5%	13%
Qualifying debt securities				
· fixed rate		8%	8%	15%
· floating rate		10%	10%	15%
Non-qualifying debt securities				
· fixed rate		10%	20%	30%
· floating rate		30%	30%	30%
B Equities				
· Traded on a recognised or designated investment exchange.	25%			
· other	100%			
C Stock position in physical commodities				
· Physical positions associated with <i>firm's</i> invest	30% of realisable value			

**ment
business****D Derivatives**

- Exchange traded futures and written options 4 x initial margin requirement.
- otc futures and written options Apply the appropriate percentage shown in Sections A, B, & C above to the market value of the underlying position.
- Purchased options Apply the appropriate percentage shown in Sections A, B & C above to the market value of the underlying position but the result may be limited to the market value of the option.
- Contracts for differences 20% of the market value of the contract.

E Other investments

- units in regulated collective investment schemes 25% of realisable value.
- with profit life policies 20% of surrender value.
- other 100% of the value of **investment** or underlying instrument.

5.12 Counterparty risk requirement (CRR)

5.12.1

R

1	Receivables	<p>In the case of receivables due to the <i>firm</i> in the form of fees, commission, interest, dividends and margin in exchange-traded futures or options contracts, which are directly related to items included in the trading book, the CRR is calculated as follows:</p> <p>$CRR = A \times RF$, where</p> <p>A = the amount of the sum due; and</p> <p>RF = the appropriate risk factor derived from IPRU-INV 5.14.1R.</p> <p>Note 1</p> <p>This requirement attaches only to balances arising from proprietary activity falling within the definition of the trading book.</p> <p>Note 2</p> <p>This requirement does not attach to items deducted in full as illiquid assets.</p>
2	Delivery of cash against documents	<p>Where a <i>firm</i> enters into a trading book transaction and the transaction is to be settled by delivery of cash against documents, the <i>firm's</i> CRR in respect of that transaction is calculated as follows:</p> <p>$CRR = (SP - MV) \times RF$, where</p> <p>SP = agreed settlement price;</p> <p>MV = current market value;</p> <p>RF = the appropriate risk factor derived from IPRU-INV 5.13.1R.</p> <p>The CRR should only be calculated where the difference between SP and MV would involve a loss if borne by the <i>firm</i>.</p>
3	Free deliveries	<p>Where a <i>firm</i> enters into a trading book transaction and the <i>firm</i> pays for the securities before it receives documents of title or delivers documents of title before receiving pay</p>

		<p>ment, the CRR in respect of that transaction is calculated as follows:</p> $CRR = \frac{V}{RF}, \quad \text{where}$ <p>V</p> <ul style="list-style-type: none"> (i) the full amount due to the <i>firm</i> (i.e. the contract value) where the <i>firm</i> has delivered securities to a counterparty and has not received payment; or (ii) the market value of the securities, where the <i>firm</i> has made payment to a counterparty for securities and has not received documents of title; and <p>RF = the appropriate risk factor derived from IPRU-INV 5.14.1R.</p>
4	Settlement outstanding 30 days or more	In the case of trading book transactions entered into by a <i>firm</i> where the <i>firm</i> pays for the securities before it receives documents of title or delivers documents of title before receiving payment and settlement has not been effected within 30 days of falling due, CRR = V.
5	Repos/Stock Lending and Reverse Repos/Stock Borrowing	<p>Where a <i>firm</i> enters into a transaction based on securities included in the trading book under the terms of a repurchase agreement or a securities lending agreement the <i>firm's</i> CRR in respect of that transaction is calculated as follows:</p> <p>CRR = V x RF, where</p> <p>RF = the appropriate risk factor derived from IPRU-INV 5.14.1R; and</p> <p>for repos/stock lending:</p> <p>V = the excess of the market value of the securities over the value of the collateral provided under the agreement, if the net figure is positive; or</p> <p>for reverse repos/stock borrowing:</p> <p>V = the excess of the amount paid or the collateral given for the securities received under the agreement, if the net figure is positive.</p>
6	otc derivatives	<p>In the case of a transaction entered into by a <i>firm</i> as principal in an otc derivative the CRR is calculated as follows:</p> <p>CRR = A x RF, where</p>

A = the appropriate credit equivalent amount derived from IPRU-INV 5.15.1R; and

RF = the appropriate risk factor derived from IPRU-INV 5.14.1R.

This calculation shall not apply to contracts for interest rate and foreign exchange which are traded on a recognised investment exchange or designated investment exchange where they are subject to a daily margin requirement and foreign exchange contracts with an original maturity of 14 calendar days or less.

A *firm* may net off contracts with the same **counterparty** in the same **otc derivative** contract for settlement on the same date in the same currency provided that the *firm* is legally entitled under the terms of the contracts with such a **counterparty** to net such contracts by novation.



5.13 Counterparty risk factor: cash settlements

5.13.1

R

Number of working days after due settle- ment date	Risk Factor
0-4	0%
5-15	8%
16-30	50%
31-45	75%
46 or more	100%

5.14.1

R

5.14 Counterparty risk requirement

Type of counterparty	Risk Weighting	Solvency Ratio	Risk Factor
(1) A counterparty which is, or the contract of which is, explicitly guaranteed by a category a body .	NIL	8%	NIL
(2) A counterparty which is, or the contract of which is, explicitly guaranteed by a category b body .	20%	8%	1.6%
(3) Any other counterparty	100%	8%	8%



5.15 OTC derivatives: calculation of credit equivalent amount

5.15.1

R

- A By attaching current market values to contracts (marking to market), obtain the current replacement cost of all contracts with positive values.
- B To obtain a figure for potential future credit exposure, the notional principal amounts or values underlying the *firm's* aggregate positions are multiplied by the following percentages:

Residual Maturity	Interest-Rate Contracts	Foreign-Exchange Contracts
One year or less	Nil	1%
- C The credit equivalent amount is the sum of current replacement cost and potential future credit exposure.
- Note Except in the case of single-currency "floating/floating interest rate" swaps in which only the current replacement cost will be calculated, bought OTC equity options and covered warrants shall be subject to the treatment accorded to exchange rate contracts.

5.16 Foreign exchange requirement

(1) A *firm's* **foreign exchange requirement** is determined by calculating the excess of its **foreign exchange position** (FEP) above 2 per cent of its own funds and multiplying this excess by 8 per cent.

(2) The FEP is the greater of:

(a) the total in the **reporting currency** of the net short positions in each currency other than the **reporting currency**; and

(b) the total in the **reporting currency** of the net long positions in each currency other than the **reporting currency**;

where the conversion to the **reporting currency** is performed using spot rates.

Note For this purpose, long and short positions in the same currency can be netted to produce the net position.

(3) In calculating the FEP, a *firm* must include relevant foreign exchange items.

EXCHANGE POSITION FOR HEDGING PURPOSES

Any positions which the *firm* has taken in order to hedge against the adverse effect of exchange rates on an item already deducted in the calculation of **liquid capital** may not be excluded from the calculation of net open currency positions.

5.17 Other assets requirement

- 5.17.1** **R** The requirement to be met in respect of the assets set out in IPRU-INV 5.17.2R, other than those to which position risk requirements and counterparty risk requirements apply or which have been deducted in full as illiquid assets, and in respect of off-balance sheet items set out in IPRU-INV 5.17.2R, must be calculated as follows:

A	= AV x RF where
A	= the amount of the requirement;
AV	= the current asset value; and
RF	= the appropriate risk factor derived from IPRU-INV 5.17.2R.

5.17.2 **R**

Assets and Off-Balance Sheet Items	Risk Factor
Assets	
Cash at bank and in hand and equivalent items	NIL
Assets secured by acceptable collateral including deposits and certificates of deposit with lending institutions	NIL
Amount due from trustees of authorised unit trusts or depositaries of authorised contractual schemes	NIL
Note 1	
This only applies to <i>firms</i> who are <i>authorised unit trust managers</i> in relation to <i>authorised unit trusts</i> or <i>authorised contractual scheme managers</i> in relation to authorised contractual schemes they manage.	
Amount due from depositaries of ICVCs	NIL
Note 2	
This only applies to <i>firms</i> who are <i>authorised corporate directors</i> in relation to ICVCs they operate	
Other receivables due from or explicitly guaranteed by or deposits with category a bodies	NIL
Other receivables due from or explicitly guaranteed by or deposits with category b bodies	1.6%
Pre-payments and accrued income (see paragraph 10 of IPRU-INV 5.8.2R)	8%
<i>Defined benefit asset</i>	NIL
Deferred acquisition cost asset	NIL
All other assets	8%
OFF-BALANCE SHEET ITEMS	

Full Risk Items e.g.		
	Charges granted against assets	8% x counterparty weight (see IPRU-INV 5.14.1R)
	Guarantees given	
Medium Risk Items e.g.		
	Undrawn credit facilities granted by the <i>firm</i> with an original maturity of more than one year	4% x counterparty weight (see IPRU-INV 5.14.1R)
Low Risk Items e.g.		
	Undrawn credit facilities granted by the <i>firm</i> with an original maturity of one year or less	NIL
Note		
(1)	In determining the appropriate other assets requirement (OAR) for guarantees given in a group context, a <i>firm</i> should follow the calculation below:	
	(a)	Categorise the guarantee agreements into:
		(i) those with the character of credit substitutes; or
		(ii) those not having the character of credit substitutes; or
		(iii) agreements to provide guarantees.
	(b)	Calculate the weighted value.
		(i) For guarantees falling under (1)(a)(i), the weighted value will be 100% of the estimated current year liability under the guarantee.
		(ii) For guarantees falling under (1)(a)(ii) the weighted value will be 50% of the estimated current year liability under the guarantee.
		(iii) For guarantees falling under (1)(a)(iii), the weighted value will be nil.
	(c)	The OAR is calculated as: Weighted value x 8% x counterparty weighting (IPRU-INV 5.14.1R)
(2)	For the purpose of this requirement, in assessing whether the guarantee has the characteristics of a credit substitute the following factors should be considered:	
	(a)	do the agreements allow for periodic or ad-hoc calling of funds;
	(b)	have the guarantees been drawn upon on a regular basis;
	(c)	do <i>firms</i> in the group rely on such guarantees to meet their working capital or regulatory capital requirements?

- (3) Where a *firm* is part of a group including other *FCA* regulated entities which together have entered into cross-group guarantee arrangements which give rise to an OAR, the estimate of the potential liability under the guarantee may be apportioned between the regulated entities for the purpose of calculating each *firm's* OAR.

5.18.1

G

Under the Financial Conglomerates and Other Financial Groups Instrument 2004, ■ IPRU-INV 14 shall (with respect to a particular firm, group or financial conglomerate) apply from the first day of its financial year beginning in 2005.

 5.18 Consolidated supervision

5 App 1

Appendix 5(1): Glossary of terms for IPRU-INV 5

App 1 Glossary of terms for IPRU-INV 5

5App 1.1 G The following words or terms throughout ■ IPRU-INV 5 appearing in bold (other than headings and titles) are to have the meanings given to them below if not inconsistent with the subject or context. If a defined term is italicised the definition appearing in the main Handbook Glossary applies.

Term	Meaning
accounting reference date	<p>means:</p> <p>(a) the date to which a <i>firm's</i> accounts are prepared in order to comply with the relevant Companies Act legislation. In the case of a <i>firm</i> not subject to Companies Act legislation, the equivalent date selected by the <i>firm</i>; and</p> <p>(b) in the case of an OPS firm which is not subject to the relevant Companies Act legislation, the date to which the accounts of the OPS in respect of which the firm acts are prepared.</p>
annual expenditure category a body	<p>has the meaning given in IPRU-INV 5.5.1 (Determination).</p> <p>means:</p> <p>(a) the government or central bank of a zone a country; or</p> <p>(b) EU or Euratom (the European Atomic Energy Community); or</p> <p>(c) the government or central bank of any other country, provided the receivable in question is denominated in that country's national currency.</p>
category b body	<p>means:</p> <p>(a) the European Investment Bank (EIB) or a multi-lateral development bank; or</p> <p>(b) the regional government or local authority of a zone a country; or</p>

Term	Meaning
	(c) an investment firm or credit institution authorised in a zone a country; or
	(d) a recognised clearing house or exchange; or
	(e) an investment firm or credit institution authorised in any other country, which applies a financial supervision regime at least equivalent to the Capital Adequacy Directive.
counterparty	means any person with or for whom a <i>firm</i> carries on regulated business or an ancillary activity.
counterparty risk requirement	has the meaning given in IPRU-INV 5.11.1R (Counterparty risk requirement).
expenditure based requirement	means the requirement calculated in accordance with IPRU-INV 5.9.1R (Expenditure based requirement).
financial resources	has the meaning given in IPRU-INV 5.2.3R (Financial resources).
financial resources requirement	has the meaning given in IPRU-INV 5.4.1R (Determination of requirement).
financial resources rules	has the meaning given in IPRU-INV 5.2.
financial return	means quarterly financial return or monthly financial return as the case may be.
foreign exchange position	has the meaning given in IPRU-INV 5.14.1R (Foreign exchange requirement).
investment	means a designated investment in the main <i>Glossary</i> .
investment business	means designated investment business in the main <i>Glossary</i> .
investment firm	has the meaning given to <i>investment firm</i> in the main <i>Glossary</i> except that it excludes persons to which <i>MiFID</i> does not apply as a result of articles 2 or 3 of <i>MiFID</i> . Note: An investment <i>firm</i> is not necessarily a firm for the purposes of the rules.
investment manager	means a person who, acting only on behalf of a customer, either: (a) manages an account or portfolio in the exercise of discretion; or (b) has accepted responsibility on a continuing basis for advising on the composition of the account or portfolio.
liquid capital	has the meaning given in IPRU-INV 5.3.1R (Calculation of own funds and liquid capital).
liquid capital requirement	has the meaning given in IPRU-INV 5.4.4R (Liquid capital requirement).
non-retail client	means a professional client or an eligible counterparty .
OPS or occupational pension scheme	means any scheme or arrangement which is comprised in one or more instruments or agreements and which has, or is capable of having, effect in relation to one or more descriptions or categories of employment so as to provide benefits, in the form of pensions or otherwise, payable on termination of service, or on death or retirement, to or respect of earners with qualifying service in an employment of any such description or category.

Term	Meaning
OPS firm	<p>means:</p> <p>(a) a <i>firm</i> which:</p> <p>(i) carries on OPS activity but not with a view to profit; and</p> <p>(ii) is one or more of the following:</p> <p>(A) a trustee of the occupational pension scheme in question;</p> <p>(B) a company owned by the trustees of the occupational pension scheme in question;</p> <p>(C) a company which is:</p> <p>(I) an employer in relation to the occupational pension scheme in question in respect of its employees or former employees or their dependants; or</p> <p>(II) a company within the group which includes an employer within (I); or</p> <p>(III) an administering authority subject to the Local Government Superannuation Regulations 1986; or</p> <p>(b) a <i>firm</i> which:</p> <p>(i) has satisfied the requirements set out in (a) at any time during the past 12 months; but</p> <p>(ii) is no longer able to comply with those requirements because of a change in the control or ownership of the employer referred to in (a)(ii) during that period.</p>
otc derivative	means interest rate and foreign exchange contracts covered by Annex III to the previous version of the Banking Consolidation Directive (i.e. Directive (2000/12/EC) and off balance sheet contracts based on equities which are not traded on a recognised or designated investment exchange or other exchange where they are subject to daily margin requirements, excluding any foreign exchange contract with an original maturity of 14 calendar days or less.
other assets requirement	has the meaning given in IPRU-INV 5.17.1R (Other assets requirement).
own funds	has the meaning given in IPRU-INV 5.3.1R and IPRU-INV 5.3.2R, as applicable.
own funds requirement	has the meaning given in IPRU-INV 5.4.3R and IPRU-INV 5.4.4R (Own funds requirement), as applicable.
permitted business	means regulated activity which a <i>firm</i> has permission to carry on.
position risk requirement	has the meaning given in IPRU-INV 5.11.1R (Position risk requirement).

Term	Meaning
prescribed subordinated loan agreement	means the subordinated loan agreement prescribed by the appropriate regulator for the purposes of IPRU-INV 5.6.4R.
qualifying capital instrument	means that part of a <i>firm's</i> capital which is a security of indeterminate duration, or other instrument, that fulfils the following conditions: <ul style="list-style-type: none"> (a) it may not be reimbursed on the bearer's initiative or without the prior agreement of the appropriate regulator; (b) the debt agreement must provide for the <i>firm</i> to have the option of deferring the payment of interest on the debt; (c) the lender's claims on the <i>firm</i> must be wholly subordinated to those of all non-subordinated creditors; (d) the documents governing the issue of the securities must provide for debt and unpaid interest to be such as to absorb losses, whilst leaving the firm in a position to continue trading; and (e) only fully paid-up amounts shall be taken into account.
qualifying capital item	means that part of a <i>firm's</i> capital which has the following characteristics: <ul style="list-style-type: none"> (a) it is freely available to the <i>firm</i> to cover normal banking or other risks where revenue or capital losses have not yet been identified; (b) its existence is disclosed in internal accounting records; and (c) its amount is determined by the management of the <i>firm</i> and verified by independent auditors, and is made known to, and is monitored by, the FCA. <p>Note: Verification by internal auditors will suffice until such time as EU provisions making external auditing mandatory have been implemented.</p>
qualifying property	has the meaning given in IPRU-INV 5.7.1R (Qualifying property and qualifying amount defined).
qualifying subordinated loan	has the meaning given in IPRU-INV 5.6 (Qualifying subordinated loans).
qualifying undertaking	has the meaning given in IPRU-INV 5.7.3R (Qualifying undertakings).
readily realisable investment	means a unit in a regulated collective investment scheme, a life policy or any marketable investment other than one which is traded on or under the rules of a recognised or designated investment exchange so irregularly or infrequently: <ul style="list-style-type: none"> (a) that it cannot be certain that a price for that investment will be quoted at all times; or (b) that it may be difficult to effect transactions at any price which may be quoted.
regulated business	means designated investment business in the main <i>Glossary</i> .

Term	Meaning
relevant foreign exchange items	<p>means:</p> <ul style="list-style-type: none"> (a) all assets less liabilities, including accrued interest, denominated in the currency (all investments at market or realisable value); (b) any currency future, at the nominal value of the contract; (c) any forward contract for the purchase or sale of the currency, at the contract value, including any future exchange of principal associated with currency swaps; (d) any foreign currency options at the net delta (or delta-based) equivalent of the total book of such options; (e) any non-currency option, at market value; (f) any irrevocable guarantee; (g) any other off-balance sheet commitment to purchase or sell an asset denominated in that currency.
reporting currency	means the currency in which the <i>firm's</i> books of account are maintained.
specified trustee business	<p>1. means any investment business carried on in the UK by a trustee <i>firm</i>, but excluding each of the following activities:</p> <ul style="list-style-type: none"> (a) Dealing or arranging deals in investments <ul style="list-style-type: none"> (i) where the deal is transacted or arranged by a trustee firm with or through a PTP; or (ii) where the dealing or arranging is done in the course of, or is incidental to, an activity of management falling within paragraph (b) below; or (iii) where the trust is a unit trust scheme and the deal is or the arrangements are made with a view to either an issue or sale of units in such a scheme to, or a redemption or repurchase or conversion of such units or a dealing in investments for such a scheme carried out by with or through, the operator or on the instructions of the operator; or (iv) where the trustee <i>firm</i>, being a bare trustee (or, in Scotland, a nominee) holding investments for another person, is acting on that person's instructions; or (v) where any arrangements do not or would not bring about the transaction in question.

Term	Meaning
(b)	<p>Managing investments</p> <p>(i) where the trustee <i>firm</i> has no general authority to effect transactions in investments at discretion; or</p> <p>(ii) if and to the extent that all day-to-day decisions in relation to the management of the investments or any discrete part of the investments are or are to be taken by a PTP; or</p> <p>(iii) if and to the extent that investment decisions in relation to the investments or any discrete part of the investments are or are to be taken substantially in accordance with the advice given by a PTP; or</p> <p>(iv) where the trustee <i>firm</i> is a personal representative or executor and is acting in that capacity; or</p> <p>(v) where the trust is a unit trust scheme and all day-to-day investment decisions in the carrying on of that activity are or are to be taken by the operator of the scheme.</p>
(c)	<p>Investment advice</p> <p>(i) where the relevant advice:</p> <p>(A) does not recommend the entry into any investment transaction or the exercise of any right conferred by any investment to acquire, dispose of, underwrite or convert such an investment; and</p> <p>(ii) if and to the extent that the relevant advice is in substance the advice of a PTP; or</p> <p>(iii) where the relevant advice is given by the trustee <i>firm</i> acting in the capacity of personal representative or executor.</p>
(d)	<p>Establishing, operating or winding up a collective investment scheme including acting as trustee of an authorised unit trust scheme but only to the extent that such activities do not otherwise constitute specified trustee business.</p>
(e)	<p>Any trustee activity undertaken as trustee of an issue of debentures or government or public securities:</p>

Term	Meaning
	<ul style="list-style-type: none"> (i) where the issue is made by a company listed on a recognised investment exchange or on a designated investment exchange (or by a wholly-owned subsidiary of such a company); or (ii) where the issue is listed or traded either on a recognised investment exchange or on a designated investment exchange or on the Société de la Bourse de Luxembourg; or (iii) where the issue is made by a government, local authority or international organisation; or (iv) where the aggregate amounts issued (pursuant to the trust deed or any deed supplemental thereto and ignoring any amounts redeemed, repurchased or converted) exceed the sum of £10,000,000.
2.	<p>For the purpose of this definition of "specified trustee business":</p> <ul style="list-style-type: none"> (a) a transaction is entered into through a person if that person: <ul style="list-style-type: none"> (i) enters into it as agent; or (ii) arranges for it to be entered into as principal or agent by another person and the arrangements are such that they bring about the transaction in question; (b) investment transaction means a transaction to purchase, sell, subscribe for or underwrite a particular investment and "investment decision" means a decision relating to an investment transaction; (c) debentures means any securities falling within article 77 of the RAO; (d) government or public securities means any securities falling within article 78) of the RAO; (e) government, local authority or international organisation means: <ul style="list-style-type: none"> (i) the government of the United Kingdom, of Northern Ireland, or of any country or territory outside the United Kingdom; (ii) a local authority in the United Kingdom or Anywhere; or (iii) an international organisation the members of which include the United Kingdom or another EEA State.

Term	Meaning
	(f) in determining the size of an issue of debentures or government or public securities made in a currency other than sterling, the amount of the issue shall be converted into sterling at the exchange rate prevailing in London on the date of issue.
total capital requirement	has the meaning given in IPRU-INV 5.4.5R (Total capital requirement).
trading book	<p>in relation to a <i>firm's</i> business or exposures, means:</p> <p>(a) its proprietary positions in financial instruments:</p> <p>(i) which are held for resale and/or are taken on by the <i>firm</i> with the intention of benefiting in the short term from actual and/or expected differences between their buying and selling prices or from other price or interest-rate variations;</p> <p>(ii) arising from matched principal broking;</p> <p>(iii) taken in order to hedge other elements of the trading book;</p> <p>(b) exposures due to unsettled securities transactions, free deliveries, OTC derivative instruments, repurchase agreements and securities lending transactions based on securities included in (a)(i) to (iii) above, reverse repurchase agreements and securities borrowing transactions based on securities included in (a)(i) to (iii) above; and</p> <p>(c) fees, commission, interest and dividends, and margin on exchange-traded derivatives which are directly related to the items included in (a) and (b) above.</p>
trustee activity	means, in relation to a <i>firm</i> , any activity undertaken in the course of or incidental to the exercise of any of its powers, or the performance of any of its duties, when
unit trust manager	means the manager of a unit trust scheme.
zone b country	means a country which is not a Zone A country in the <i>Glossary</i> .

Chapter 6

Service Companies



6.1 APPLICATION

6.1.1 **G** This chapter applies to *service companies*.

FINANCIAL RESOURCES REQUIREMENTS

- 6.1.2 **G**
- (1) A *service company* must be able to meet its liabilities as they fall due.
 - (2) In complying with (1) a *firm* may use any assets which are available to meet any of its liabilities.

Chapter 9

Financial resources requirements for an exempt CAD firm

9.1 APPLICATION

9.1.1

R

- (1) This chapter applies to an *exempt CAD firm* which is:
- (a) an *investment management firm*; or
 - (b) a *securities and futures firm*.
- (2) This chapter also applies to a *local firm*.



9.2 GENERAL REQUIREMENTS

9.2.1 **G** For an *exempt CAD firm*, the *rules* contained within this chapter replace the *rules* in respect of financial resources, financial resources requirements and nonfinancial resources related requirements contained within Chapter 3 or 5, as applicable. However, an *exempt CAD firm* must continue to comply with the requirements of Chapter 3 or 5, to the extent it is referred to Chapter 3 or 5 by a *rule* in this chapter.

9.2.2 **R** A *firm* must be able to meet its liabilities as they fall due.

9.2.3 **R** An *exempt CAD firm* that carries on any *regulated activity* other than *MiFID business* must also have and maintain at all times financial resources calculated in accordance with the chapter of *IPRU(INV)* to which the *firm* is otherwise subject (Chapters 3 or 5) at least equal to the requirements set out in the relevant chapter (except that if the only *designated investment business* an *exempt CAD firm* is carrying on in addition to *investment services and activities* is *making arrangements with a view to transactions in investments* (article 25(2) *Regulated Activities Order*) or agreeing to carry on that *regulated activity* or both, it only needs to comply with requirements set out in this chapter and not chapters 3 or 5).

Initial capital and professional indemnity insurance requirements - exempt CAD firms that are not IMD insurance intermediaries

9.2.4 **R**

(1) An *exempt CAD firm* which is not an *IMD insurance intermediary* must have:

- (a) *initial capital* of EUR 50,000; or
- (b) professional indemnity insurance covering the whole territory of the *EEA* or some other comparable guarantee against liability arising from professional negligence, representing at least EUR 1,000,000 applying to each claim and in aggregate EUR 1,500,000 per year for all claims; or
- (c) a combination of *initial capital* and professional indemnity insurance in a form resulting in a level of coverage equivalent to (a) or (b).

[Note: article 31(1) of the *CRD*]

(2) If a *firm* chooses to meet the requirements of either (b) or (c) above, it must nevertheless have *initial capital* of at least £5,000.

Initial capital and professional indemnity insurance requirements - exempt CAD firms that are also IMD insurance intermediaries

- 9.2.5 **R** (1) An *exempt CAD firm* that is also an *IMD insurance intermediary* must comply with the professional indemnity insurance requirements at least equal to those set out in ■ IPRU-INV 9.2.4R(1)(b) (except that the minimum *limits of indemnity* are at least EUR 1,120,200 for a single claim and EUR 1,680,300 in aggregate) and in addition has to have:
- (a) *initial capital* of EUR 25,000; or
 - (b) professional indemnity insurance covering the whole territory of the *EEA* or some other comparable guarantee against liability arising from professional negligence, representing at least EUR 500,000 applying to each claim and in aggregate EUR 750,000 per year for all claims; or
 - (c) a combination of *initial capital* and professional indemnity insurance in a form resulting in a level of coverage equivalent to (a) or (b).
- [Note: article 31(2) of the *CRD*]
- (2) If a *firm* chooses to meet the requirements of either (b) or (c) above, it must nevertheless have *initial capital* of at least £5,000.

9.2.5A **G** Article 4(7) of the *Insurance Mediation Directive* requires the *limits of indemnity* to be reviewed every five years to take into account movements in European consumer prices. These *limits* will therefore be subject to further adjustments on the basis of index movements advised by the European Commission.

9.2.6 **G** A trade-off between *initial capital* and professional indemnity insurance is appropriate such that EUR 1 of *initial capital* is the equivalent of professional indemnity insurance cover of EUR 20 for a single claim against the *firm* and EUR 30 in aggregate.

Comparable guarantee

- 9.2.7 **R**
- (a) If another *authorised person* which has net tangible assets of more than £10 million provides a comparable guarantee, an *exempt CAD firm* can treat it as an alternative to effecting or maintaining professional indemnity insurance pursuant to the rules relating to professional indemnity insurance above.
 - (b) If the *exempt CAD firm* is a member of a *group* in which there is an *authorised person* with net tangible assets of more than £10 million, the comparable guarantee must be from that *person*.
 - (c) A comparable guarantee means a written agreement on terms at least equal to those required by the *initial capital* and professional indemnity insurance requirements above to finance the claims that might arise as a result of the breach by the *exempt CAD firm* of its duties under the *regulatory system* or civil law.

Initial capital and ongoing capital requirements for local firms

9.2.8

R

A *local firm* must:

- (a) have *initial capital* of EUR 50,000; and

[Note: article 30 of the *CRD*]

- (b) maintain *own funds* calculated in accordance with the *rules* relating to *own funds* in 9.5, at least to the requirement for *initial capital*.

Ongoing capital requirements

9.2.9

R

- (1) An *exempt CAD firm* must, at all times, maintain a combination of professional indemnity insurance and *own funds*, (*own funds* to be calculated in accordance with (2)), at least equal to the requirements in this chapter for professional indemnity insurance and *initial capital*.

- (2) (a) If the *exempt CAD firm* is an *investment management firm* its *own funds* must be calculated in accordance with the *rules* in ■ IPRU-INV 5.2 to ■ 5.7.
- (b) If the *exempt CAD firm* is a *securities and futures firm* its *own funds* must be calculated in accordance with the *rules* relating to *own funds* in 9.5.

9.3 CALCULATING INITIAL CAPITAL

Initial capital

9.3.1

R

A firm's *initial capital* consists of the sum of the following items:

- (1) ordinary *share* capital which is fully paid;
- (2) perpetual non-cumulative *preference share* capital which is fully paid;
- (3) *share* premium account;
- (4) reserves excluding revaluation reserves;
- (5) audited retained earnings;
- (6) externally *verified* interim net profits;
- (7) partners' capital;
- (8) *eligible LLP members' capital* (in accordance with the provisions of IPRU-INV Annex A); and
- (9) *sole trader* capital.

Perpetual noncumulative preference share capital

9.3.2

R

A firm may include *preference share* capital in *initial capital* only where any *coupon* on it is not cumulative, and the *firm* is under no obligation to pay a *coupon* in any circumstances.

Audited retained earnings

9.3.3

R

When calculating *initial capital*, a *firm* may include its audited retained earnings only after making the following adjustments:

- (1) a *firm* must not recognise the fair value reserves related to gains or losses on cash flow hedges of financial instruments measured at amortised cost;
- (2) in respect of a *defined benefit occupational pension scheme*, a *firm* must derecognise any *defined benefit asset*;
- (3) a *firm* must not include any unrealised gains from investment property (these should be reported as part of revaluation reserves);

- (4) where applicable, a *firm* must deduct any asset in respect of *deferred acquisition costs* and add back in any liability in respect of deferred income (but excluding from the deduction or addition any asset or liability which will give rise to future cash flows), together with any associated deferred tax.

Externally verified interim net profits or current account

9.3.4 **R** A *firm* may include interim net profits or current account when calculating *initial capital* to the extent that they have been *verified* by the *firm's* external auditor and are net of any foreseeable tax, dividend and other appropriations.

9.3.5 **R** When calculating *initial capital*, a *firm* may include its partners' capital only after making the following adjustments:

- (1) a *firm* must not recognise the fair value reserves related to gains or losses on cash flow hedges of financial instruments measured at amortised cost;
- (2) in respect of a *defined benefit occupational pension scheme*, a *firm* must derecognise any *defined benefit asset*;
- (3) where applicable, a *firm* must deduct any asset in respect of *deferred acquisition costs* and add back in any liability in respect of deferred income (but excluding from the deduction or addition any asset or liability which will give rise to future cash flows), together with any associated deferred tax.

Defined benefit pension scheme: defined benefit liability

9.3.6 **R** For the calculation of *initial capital*, a *firm* may substitute for a *defined benefit liability* the *firm's deficit reduction amount*. The election must be applied consistently in respect of any one financial year.

9.3.7 **G** A *firm* should keep a record of and be ready to explain to its supervisory contacts in the *FCA* 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*.

9.4 POLICY TERMS FOR PROFESSIONAL INDEMNITY INSURANCE

Insurers whose professional indemnity insurance policies can be used by an exempt CAD firm

9.4.1

R

An *exempt CAD firm* that has professional indemnity insurance in accordance with this chapter must take out and maintain professional indemnity insurance that is at least equal to the requirements of the rule below from:

- (1) an *insurance undertaking* which is authorised to transact professional indemnity insurance in the *EEA*; or
- (2) a person of equivalent status in:
 - (a) a *Zone A country*;
 - (b) the Channel Islands, Gibraltar, Bermuda or the Isle of Man.

Terms to be incorporated in the professional indemnity insurance policy

9.4.2

R

The policy of professional indemnity insurance must incorporate terms which make provision for:

- (1) cover in respect of claims for which an *exempt CAD firm* may be liable as a result of the conduct of itself, its *employees* and its *appointed representatives* or where applicable, its *tied agent* (acting within the scope of their appointment);
- (2) the minimum *levels of indemnity* per year as set out in the rules relating to professional indemnity insurance above;
- (3) appropriate cover in respect of legal defence costs; and
- (4) cover in respect of *Ombudsman* awards made against the *exempt CAD firm*.

Policies in other currencies

9.4.3

R

If a professional indemnity insurance policy is denominated in any currency other than euros, an *exempt CAD firm* must take reasonable *FCA* steps to ensure that the *limits of indemnity* are, when the policy is effected and at *renewal*, at least equivalent to those required for the purposes of the rules relating to professional indemnity insurance above.

Conditions and exclusions

9.4.4

R

A professional indemnity insurance policy must not be subject to conditions or exclusions which unreasonably limit the cover provided (whether by exclusion of cover, by policy excesses or otherwise).



9.5 CALCULATION OF OWN FUNDS

9.5.1 **R** *A firm's initial capital:*
minus the sum of the items set out against **B**
plus the sum of the items set out against **C**
minus *material holdings in credit and financial institutions and material insurance holdings*
 equals *own funds*.

9.5.2 **R** Table
 The table forms part of *rule 9.5.1R*

(1)	<i>Investments in own shares at book value</i>	B
(2)	<i>Intangible assets</i>	
(3)	<i>Material current year losses</i>	
(1)	Revaluation reserves	C
(2)	Perpetual cumulative preference <i>share</i> capital	
(3)	Long-term subordinated loans	
(4)	Perpetual long-term subordinated loans	
(5)	Fixed term preference <i>share</i> capital	

9.5.3 **R** **Perpetual long-term subordinated loans and perpetual cumulative preference share capital**

 Perpetual long-term subordinated loans and perpetual cumulative preference *share* capital may not be included in the calculation of *own funds* unless they meet the following requirements:

- (1) it may not be reimbursed on the holder's initiative or without the prior agreement of the *FCA*;
- (2) the instrument must provide for the *firm* to have the option of deferring the dividend payment on the *share* capital;
- (3) the shareholder's claims on the *firm* must be wholly subordinated to those of all non-subordinated creditors;

- (4) the terms of the instrument must provide for the loss-absorption capacity of the share capital and unpaid dividends, whilst enabling the *firm* to continue its business; and
- (5) it must be fully paid-up.

Subordinated loans

9.5.4 **R** A *firm* may include a subordinated loan in the calculation of its *own funds* only:

- (a) if it is drawn up in accordance with the standard forms obtained from the *FCA*;
- (b) if it is signed by authorised signatories of all the parties; and
- (c) to the extent that it is fully paid up.

Long-term subordinated loans

9.5.5 **R** A long-term subordinated loan may not be included in the calculation of *own funds* unless it meets the following requirements:

- (1) it must be fully paid-up;
- (2) it has an original maturity of at least five years;
- (3) the extent to which it may be used in the calculation of *own funds* shall be amortised on a straight line basis during at least the five years before repayment; and
- (4) it must not become repayable before the agreed repayment date other than in the winding-up of the *firm* or unless the *firm* has provided the *FCA* with at least five years' written notice.

9.5.6 **R** A *firm* must not (except in accordance with the terms of the loan) make any payment of interest if after such action the *firm's own funds* will fall below 120% of its *own funds requirement*.

Perpetual noncumulative and cumulative preference share capital

9.5.7 **R** A *firm* may include perpetual non-cumulative and cumulative preference share capital in its *initial capital* and its *own funds* only if there is an agreement between the *firm* and the shareholders which provides that redemption of the shares may not take place, if after such redemption the *firm* would be in breach of its *own funds requirement*

Own funds - Restrictions

9.5.8 **R** (1) In calculating *own funds*:

- (i) the total amount of revaluation reserves, perpetual cumulative preference *share capital*, long-term subordinated loans, perpetual

- long-term subordinated loans and fixed term preference *share* capital must not exceed 100% of *initial capital* minus B; and
- (ii) the total amount of fixed term preference *share* capital and long-term subordinated loans must not exceed 50% of *initial capital* minus B.

9.6 NON-FINANCIAL RESOURCE REQUIREMENTS

Reconciliation of balances

9.6.1

R

- (1) A *firm* must reconcile all balances and positions with:
- (i) *banks and building societies* (other than a client bank account subject to the *client money rules*), *exchanges, approved exchanges, clearing houses and intermediate brokers*; and
 - (ii) *eligible counterparties* which are *members* of an exchange or approved exchange

as recorded by the *firm* to the balance or position on a statement or circularisation obtained by the *firm* from those entities and must correct any differences by agreement on a timely basis, unless:

- (i) the balances and positions due to and from the *eligible counterparties* have been agreed by other means; or
 - (ii) it arises solely as a result of identified differences in timing between the records of the *firm* and the *bank or building society*.
- (2) A *firm* must perform reconciliations under (1) above as frequently as is appropriate for the volume of transactions on the accounts and in any event not less than once every five weeks or, in relation to positions with *eligible counterparties*, not less than once every year.
- (3) A *firm* must circularise or request statements from *banks, building societies, exchanges, approved exchanges, clearing houses, intermediate brokers and eligible counterparties* which are members of an *exchange or an approved exchange* in good time in order to be able to comply with (1) and (2) above.
- (4) A *firm* must use its best endeavours to respond within one month of receipt to any circularisation from another *firm* requesting confirmation of outstanding balances.

9.6.2

G

For *guidance* notes on the reconciliation of a *firm's* balance with market counterparties see Appendix 20 to Chapter 3.

Financial notification

9.6.3

R

A *firm* must notify the *FCA* in writing as soon as it has reason to believe that it is in breach of its *own funds requirement*.

9 App 1

Appendix 9(1): Interpretation

App 1 Interpretation

9App 1.1 G Glossary of defined terms for Chapter 9

Note: If a defined term does not appear in the glossary below, the definition appearing in the *Handbook Glossary* applies.

<i>approved exchange</i>	means an investment exchange listed as such in Appendix 33 to IPRU-INV 3.
<i>exchange</i>	means a <i>recognised investment exchange</i> or <i>designated investment exchange</i> .
<i>initial capital</i>	means the initial capital of a <i>firm</i> calculated in accordance with section 9.3.
<i>intangible assets</i>	the full balance sheet value of a <i>firm's</i> intangible assets including goodwill, capitalised development costs, licences, trademark and similar rights etc.
<i>intermediate broker</i>	in relation to a <i>marginised transaction</i> , means any person through whom the <i>firm</i> undertakes that transaction.
<i>material current year losses</i>	means losses of an amount equal to 10% or more of <i>initial capital</i> minus B (with B calculated in accordance with Table 9.5.2R).
<i>material holding</i>	means a <i>firm's</i> holdings of shares and any other interest in the capital of a <i>credit institution</i> or <i>financial institution</i> : (a) which exceeds 10% of the capital of the issuer, and, where this is the case, any holdings of subordinated debt of the same issuer, the full amount is a <i>material holding</i> ; or (b) holdings not deducted under (a) if the total amount of such holdings exceeds 10% of that <i>firm's own funds</i> , in which case only the excess amount is a <i>material holding</i> .
<i>material insurance holdings</i>	(a) means the holdings of an <i>exempt CAD firm</i> of items of the type set out in (b) in any: (i) <i>insurance undertaking</i> ; or (ii) <i>insurance holding company</i> that fulfils one of the following conditions:

	<p>(iii) it is a <i>subsidiary undertaking</i> of that <i>firm</i>; or</p> <p>(iv) that <i>firm</i> holds a participation in it.</p> <p>(b) An item falls into this provision for the purpose of (a) if it is:</p> <p>(i) an <i>ownership share</i>; or</p> <p>(ii) subordinated debt or another item of capital that forms part of the tier two capital resources that falls into GENPRU 2 or, as the case may be, INSPRU 7, or is an item of “basic own funds” defined in the PRA Rulebook: Glossary.</p>
<i>own funds</i>	means the own funds of a <i>firm</i> calculated in accordance with 9.2.9R(2) and The Interim Prudential Sourcebook for Investment Businesses Chapter 9: Financial resources requirements for an exempt CAD firm Page 2 of 2 Version: November 2007 9.2.8R(b).
<i>own funds requirement</i>	means the requirement set out in 9.2.9R(1) and 9.2.8R(b).
<i>verified</i>	<p>means checked by an external auditor who has undertaken at least to:</p> <p>(a) satisfy himself that the figures forming the basis of the interim profits have been properly extracted from the underlying accounting records;</p> <p>(b) review the accounting policies used in calculating the interim profits so as to obtain comfort that they are consistent with those normally adopted by the <i>firm</i> in drawing up its annual financial statements and are in accordance with the relevant accounting principles;</p> <p>(c) perform analytical procedures on the result to date, including comparisons of actual performance to date with budget and with the results of prior period(s);</p> <p>(d) discuss with management the overall performance and financial position of the <i>firm</i>;</p> <p>(e) obtain adequate comfort that the implications of current and prospective litigation, all known claims and commitments, changes in business activities and provisioning for bad and doubtful debts have been properly taken into account in arriving at the interim profits; and</p> <p>(f) follow up problem areas of which he is already aware in the course of auditing the <i>firm's</i> financial statements.</p>

Chapter 11

Collective Portfolio Management Firms and Collective Portfolio Management Investment Firms

11.1 INTRODUCTION

Application

11.1.1

R

This chapter applies to:

- (1) a collective portfolio management firm; and
- (2) a collective portfolio management investment firm.

11.1.2

G

A *collective portfolio management firm* that manages an *AIF* is an *internally managed AIF* or an *external AIFM*. If the *firm* is a *full-scope UK AIFM* this affects the *firm's base capital resources requirement* (see ■ IPRU-INV 11.3.1R). An *internally managed AIF* that is a *full-scope UK AIFM* is not permitted to engage in activities other than the management of that *AIF*, whereas an *external AIFM* that is a *full-scope UK AIFM* may manage *AIFs* and/or *UCITS*, provided it has *permission* to do so. A *full-scope UK AIFM* that is an *external AIFM* and/or a *UCITS management company* may undertake any of the additional investment activities permitted by article 6(4) of *AIFMD* or article 6(3) of the *UCITS Directive* (as applicable), provided it has *permission* to do so, but if so it is classified as a *collective portfolio management investment firm*, as opposed to a *collective portfolio management firm*.

A *collective portfolio management investment firm* is also subject to the requirements of either (i) *GENPRU* and *BIPRU* or (ii) *IFPRU* in addition to the requirements of ■ IPRU-INV 11, as explained in ■ IPRU-INV 11.6.2G.

11.1.2A

G

A *small authorised UK AIFM* that is not also a *UCITS management company* is not a *collective portfolio management firm* or a *collective portfolio management investment firm* and is therefore not subject to ■ IPRU-INV 11. This type of *firm* is subject to ■ IPRU-INV 5 if it is an *investment management firm*, *GENPRU* and *BIPRU* if it is a *BIPRU firm* or *IFPRU* if it is an *IFPRU investment firm*.

Relevant accounting principles

11.1.3

R

- (1) Except where a *rule* makes a different provision, terms in this chapter must have the meaning given to them in the *Companies Act 2006* or the *firm's* accounting framework (usually *UK* generally accepted accounting principles or *IFRS*) where defined in that Act or framework.
- (2) Accounting policies must be the same as those adopted in the *firm's annual report and accounts* and must be consistently applied.

Purpose

11.1.4

G

- (1) This chapter amplifies *threshold condition 2D* (Appropriate resources) by providing that a *firm* must meet, on a continuing basis, a minimum capital resources requirement. This chapter also amplifies *Principles 3 and 4* which require a *firm* to take reasonable care to organise and control its affairs responsibly and effectively with adequate risk management systems, and to maintain adequate financial resources by setting out a capital resources requirement for a *firm* according to the *regulated activity* or activities it carries on.
- (2) This chapter also implements relevant requirements of *AIFMD* and the *UCITS Directive*, which includes imposing capital and professional indemnity insurance requirements on a *full-scope UK AIFM* and a *UCITS management company*. *AIFMD* and the *UCITS Directive* incorporate references to provisions of the *Banking Consolidation Directive* and the *Capital Adequacy Directive* in relation to initial capital, own funds and fixed overheads. However, in line with article 163 of the *CRD*, the *Banking Consolidation Directive* and the *Capital Adequacy Directive* are repealed from 1 January 2014 and references to these directives are replaced with references to the *CRD* and the *EU CRR* in line with the correlation table set out in Annex II to the *CRD* and in Annex IV to the *EU CRR*.

11.2 MAIN REQUIREMENTS

Collective portfolio management firm

11.2.1

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A firm must:

- (1) when it first becomes a *collective portfolio management firm* or a *collective portfolio management investment firm*, hold *initial capital* of not less than the applicable *base own funds requirement* (in line with ■ IPRU-INV 11.3.1R);
- (2) at all times, maintain *own funds* which equal or exceed:
 - (a) the higher of:
 - (i) the *funds under management requirement* (in line with ■ IPRU-INV 11.3.2R); and
 - (ii) the amount specified in article 97 of the *EU CRR* (Own funds based on fixed overheads) (as replicated in ■ IPRU-INV 11.3.3AEU)); plus
 - (b) whichever is applicable of:
 - (i) the *professional negligence capital requirement* (in line with ■ IPRU-INV 11.3.11G(1)(a)); or
 - (ii) the *PII capital requirement* (in line with ■ IPRU-INV 11.3.11G(1)(b)); and
- (3) at all times, hold liquid assets (in line with ■ IPRU-INV 11.3.17R) which equal or exceed:
 - (a) the higher of:
 - (i) the *funds under management requirement* (in line with ■ IPRU-INV 11.3.2R) less the *base own funds requirement* (in line with ■ IPRU-INV 11.3.1R); and
 - (ii) the amount specified in article 97 of the *EU CRR* (Own funds based on fixed overheads); plus
 - (b) whichever is applicable of:
 - (i) the *professional negligence capital requirement* (in line with ■ IPRU-INV 11.3.11G(1)(a)); or
 - (ii) the *PII capital requirement* (in line with ■ IPRU-INV 11.3.11G(1)(b)).

[Note: article 9(5) and 9(7) of *AIFMD* and article 7(1)(a)(iii) of the *UCITS Directive*]

Professional negligence

11.2.2

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- (1) The *professional negligence capital requirement* applies to a *full-scope UK AIFM* which, in line with ■ IPRU-INV 11.3.11G(1)(a), covers professional liability risks by way of *own funds*.
- (2) The *PII capital requirement* applies to a *full-scope UK AIFM* which, in line with ■ IPRU-INV 11.3.11G(1)(b), decides to cover professional liability risks by professional indemnity insurance.

11.3 DETAIL OF MAIN REQUIREMENTS

Base own funds requirement

11.3.1 **R** The *base own funds requirement* is:

- (1) EUR 125,000 for a *firm* that is a *UCITS management company* or a *full-scope UK AIFM* that is an *external AIFM*; and
- (2) EUR 300,000 for a full-scope UK AIFM that is an *internally managed AIF*.

[Note: article 9(1), (2) and (10) of *AIFMD* and article 7(1)(a) of the *UCITS Directive*]

Funds under management requirement

11.3.2 **R** The *funds under management requirement* is (subject to a maximum of EUR 10,000,000) the sum of:

- (1) the *base own funds requirement*; plus
- (2) 0.02% of the amount by which the *funds under management* exceed EUR 250,000,000,

[Note: article 9(3) of *AIFMD* and article 7(1)(a)(i) of the *UCITS Directive*]

Fixed overheads requirement

11.3.3 **R** [deleted]

Own Funds based on Fixed Overheads

- 11.3.3A **EU**
- (1) In accordance with Articles 95 and 96, an investment firm and firms referred to in point (2)(c) of Article 4(1) that provide the investment services and activities listed in points (2) and (4) of Section A of Annex I to Directive 2004/39/EC shall hold eligible capital of at least one quarter of the fixed overheads of the preceding year.
 - (2) Where there is a change in the business of an investment firm since the preceding year that the competent authority considers to be material, the competent authority may adjust the requirement laid down in paragraph 1.
 - (3) Where an investment firm has not completed business for one year, starting from the day it starts up, an investment firm shall hold

eligible capital of at least one quarter of the fixed overheads projected in its business plan, except where the competent authority requires the business plan to be adjusted.

[Note: article 97(1) to (3) of the *EU CRR*]

11.3.4 **R** [deleted]

11.3.5 **G** [deleted]

11.3.6 **R** [deleted]

11.3.7 **R** [deleted]

11.3.8 **G** [deleted]

11.3.9 **R** [deleted]

11.3.10 **G** [deleted]

Professional negligence

11.3.11 **G** A full-scope UK AIFM should:

- (1) cover the professional liability risks set out in article 12 of the *AIFMD level 2 regulation* (professional liability risks) (as replicated in ■ IPRU-INV 11.3.12EU) by either:
 - (a) maintaining an amount of *own funds* in line with article 14 of the *AIFMD level 2 regulation* (additional own funds) (as replicated in ■ IPRU-INV 11.3.14EU) (the *professional negligence capital requirement*); or
 - (b) holding professional indemnity insurance and maintaining an amount of *own funds* to meet the *PII capital requirement* under article 15 of the *AIFMD level 2 regulation* (professional indemnity insurance) (as replicated in ■ IPRU-INV 11.3.15EU) and ■ IPRU-INV 11.3.16R; and
- (2) comply with the qualitative requirements addressing professional liability risks in article 13 of the *AIFMD level 2 regulation* (qualitative requirements addressing professional liability risks) (as replicated in ■ IPRU-INV 11.3.13EU).

Professional liability risks

11.3.12 **EU** (1) The professional liability risks to be covered pursuant to Article 9(7) of Directive 2011/61/EU shall be risks of loss or damage caused by a relevant person through the negligent performance of activities for which the AIFM has legal responsibility.

- (2) Professional liability risks as defined in paragraph 1 shall include, without being limited to, risks of:
 - (a) loss of documents evidencing title of assets of the AIF;
 - (b) misrepresentations or misleading statements made to the AIF or its investors;
 - (c) acts, errors or omissions resulting in a breach of:
 - (i) legal and regulatory obligations;
 - (ii) duty of skill and care towards the AIF and its investors;
 - (iii) fiduciary duties;
 - (iv) obligations of confidentiality;
 - (v) AIF rules or instruments of incorporation;
 - (vi) terms of appointment of the AIFM by the AIF;
 - (d) failure to establish, implement and maintain appropriate procedures to prevent dishonest, fraudulent or malicious acts;
 - (e) improperly carried out valuation of assets or calculation of unit/ share prices;
 - (f) losses arising from business disruption, system failures, failure of transaction processing or process management.
- (3) Professional liability risks shall be covered at all times either through appropriate additional own funds determined in accordance with Article 14 or through appropriate coverage of professional indemnity insurance determined in accordance with Article 15.

[Note: article 12 of the *AIFMD level 2 regulation*]

Qualitative requirements addressing professional liability risks

11.3.13 EU

- (1) An AIFM shall implement effective internal operational risk management policies and procedures in order to identify, measure, manage and monitor appropriately operational risks including professional liability risks to which the AIFM is or could be reasonably exposed. The operational risk management activities shall be performed independently as part of the risk management policy.
- (2) An AIFM shall set up a historical loss database, in which any operational failures, loss and damage experience shall be recorded. This database shall record, without being limited to, any professional liability risks as referred to in Article 12(2) that have materialised.
- (3) Within the risk management framework the AIFM shall make use of its internal historical loss data and where appropriate of external data, scenario analysis and factors reflecting the business environment and internal control systems.
- (4) Operational risk exposures and loss experience shall be monitored on an ongoing basis and shall be subject to regular internal reporting.
- (5) An AIFM's operational risk management policies and procedures shall be well documented. An AIFM shall have arrangements in place for ensuring compliance with its operational risk management policies

and effective measures for the treatment of non-compliance with these policies. An AIFM shall have procedures in place for taking appropriate corrective action.

- (6) The operational risk management policies and procedures and measurement systems shall be subject to regular review, at least on an annual basis.
- (7) An AIFM shall maintain financial resources adequate to its assessed risk profile.

[Note: article 13 of the *AIFMD level 2 regulation*]

Additional own funds

11.3.14 EU

- (1) This Article shall apply to AIFMs that choose to cover professional liability risks through additional own funds.
- (2) The AIFM shall provide additional own funds for covering liability risks arising from professional negligence at least equal to 0,01 % of the value of the portfolios of AIFs managed.

The value of the portfolios of AIFs managed shall be the sum of the absolute value of all assets of all AIFs managed by the AIFM, including assets acquired through use of leverage, whereby derivative instruments shall be valued at their market value.

- (3) The additional own funds requirement referred to in paragraph 2 shall be recalculated at the end of each financial year and the amount of additional own funds shall be adjusted accordingly.

The AIFM shall establish, implement and apply procedures to monitor on an ongoing basis the value of the portfolios of AIFs managed, calculated in accordance with the second subparagraph of paragraph 2. Where, before the annual recalculation referred to in the first subparagraph, the value of the portfolios of AIFs managed increases significantly, the AIFM shall without undue delay recalculate the additional own funds requirement and shall adjust the additional own *funds* accordingly.

- (4) The competent authority of the home Member State of the AIFM may authorise the AIFM to provide additional own funds lower than the amount referred to in paragraph 2 only if it is satisfied - on the basis of the historical loss data of the AIFM as recorded over an observation period of at least three years prior to the assessment - that the AIFM provides sufficient additional own funds to appropriately cover professional liability risks. The authorised lower amount of additional own funds shall be not less than 0,008 % of the value of the portfolios of AIFs managed by the AIFM.
- (5) The competent authority of the home Member State of the AIFM may request the AIFM to provide additional own funds higher than the amount referred to in paragraph 2 if it is not satisfied that the AIFM has sufficient additional own funds to appropriately cover professional liability risks. The competent authority shall give reasons why it considers that the AIFM's additional own funds are insufficient.

[Note: article 14 of the *AIFMD level 2 regulation*]

Professional indemnity insurance

11.3.15 **EU**

- (1) This Article shall apply to AIFMs that choose to cover professional liability risks through professional indemnity insurance.
- (2) The *AIFM* shall take out and maintain at all times professional indemnity insurance that:
 - (a) shall have an initial term of no less than one year;
 - (b) shall have a notice period for cancellation of at least 90 days;
 - (c) shall cover professional liability risks as defined in Article 12(1) and (2);
 - (d) is taken out from an EU or non-EU undertaking authorised to provide professional indemnity insurance, in accordance with Union law or national law;
 - (e) is provided by a third party entity

Any agreed defined excess shall be fully covered by own funds which are in addition to the own funds to be provided in accordance with Article 9(1) and (3) of Directive 2011/61/EU.
- (3) The coverage of the insurance for an individual claim shall be equal to at least 0,7 % of the value of the portfolios of AIFs managed by the AIFM calculated as set out in the second subparagraph of Article 14(2).
- (4) The coverage of the insurance for claims in aggregate per year shall be equal to at least 0,9 % of the value of the portfolios of AIFs managed by the AIFM calculated as set out in the second subparagraph of Article 14(2).
- (5) The AIFM shall review the professional indemnity insurance policy and its compliance with the requirements laid down in this Article at least once a year and in the event of any change which affects the policy's compliance with the requirements in this Article

[Note: article 15 of the *AIFMD level 2 regulation*]

11.3.16 **R**

If a *firm* satisfies the requirement referred to in ■ IPRU-INV 11.3.11G with professional indemnity insurance it must, in addition to maintaining an amount of *own funds* to cover any defined excess, hold adequate *own funds* to cover any exclusions in the insurance policy that would otherwise result in the *firm* having insufficient resources to cover liabilities arising. A *firm* may satisfy its requirements for professional indemnity insurance with a policy that also provides cover to one or more entities other than the *firm*, provided that the policy satisfies the conditions of the *AIFMD level 2 regulation*, exclusive of the cover provided to other entities.

Liquid assets

11.3.17 **R**

- For the purposes of this chapter, liquid assets are assets which:
- (1) are readily convertible to cash within one month; and
 - (2) have not been invested in speculative positions.

11.3.18 **G** Examples of liquid assets that are acceptable under **■ IPRU-INV 11.3.17R** include cash, *readily realisable investments* that are not held for short-term resale, and debtors.

[Note: article 9(8) of *AIFMD*]



11.4 [DELETED]

11.4.1

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			11.5	[DELETED]
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11.6 ADDITIONAL REQUIREMENTS FOR COLLECTIVE PORTFOLIO MANAGEMENT INVESTMENT FIRMS

- 11.6.1** **G** A *collective portfolio management investment firm* is required to comply with the applicable requirements of either of the following sourcebooks in addition to complying with ■ IPRU-INV 11:
- (1) *GENPRU* and *BIPRU* if it is a *BIPRU firm*; or
 - (2) *IFPRU* if it is *IFPRU investment firm*.
- 11.6.2** **G**
- (1) A *collective portfolio management investment firm* may undertake the following *MiFID business: portfolio management; investment advice; safekeeping and administration in relation to shares or units of collective investment undertakings; and (if it is an AIFM investment firm) reception and transmission of orders in relation to financial instruments*.
 - (2) Subject to the conditions that the *firm* is not authorised to provide safekeeping and administration in relation to *shares* or *units* of collective investment undertakings and is not permitted to hold client money or client assets in relation to its *MiFID business* (and for that reason may not place itself in debt with those clients) competent authorities may allow the *firm* to stay on the capital requirements that would be binding on that *firm* as at 31 December 2013 under the *Banking Consolidation Directive* and the *Capital Adequacy Directive* (in line with article 95(2) of the *EU CRR*). The *FCA* has exercised this derogation and, as such, a *firm* meeting those conditions is a *BIPRU firm*. If the above conditions are not met, a *collective portfolio management investment firm* is an *IFPRU investment firm*.
- 11.6.3** **G** A *collective portfolio management investment firm* is required to comply with the applicable requirements of the sourcebooks set out in ■ IPRU-INV 11.6.1G, in parallel with its requirements under ■ IPRU-INV 11. This means that a capital instrument may be used to meet either or both sets of requirements provided it meets the conditions set out in the relevant sourcebook.
- 11.6.4** **G**
- (1) When a *collective portfolio management investment firm* that is a *BIPRU firm* calculates the *credit risk capital requirement* and the

market risk capital requirement for the purpose of calculating the variable capital requirement under ■ GENPRU 2.1.40R it must do so only in respect of *designated investment business*. For this purpose, *managing an AIF* or *managing a UCITS* is excluded from *designated investment business*.

- (2) Generally, *BIPRU* only applies to a *collective portfolio management investment firm* that is a *BIPRU firm* in respect of its *designated investment business* (excluding *managing an AIF* and *managing a UCITS*). However, ■ BIPRU 2.2 (Internal capital adequacy standards), ■ BIPRU 2.3 (Interest rate risk in the non-trading book), ■ BIPRU 8 (Group risk - consolidation) and ■ BIPRU 11 (Disclosure) apply to the whole of its business.

11.6.5

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- (1) When a *collective portfolio management investment firm* that is an *IFPRU investment firm* calculates the total risk exposure amount in article 92(3) of the *EU CRR*, the *own funds requirements* referred to in article 92(3)(a) (Risk weighted exposure amount for credit risk and dilution risk) and article 92(3)(b) (Risk weighted exposure amount for position risk) should include only those arising from its *designated investment business*. For this purpose, *managing an AIF* or *managing a UCITS* is excluded from *designated investment business*.
- (2) Generally, *IFPRU* only applies to the *designated investment business* (excluding *managing an AIF* and *managing a UCITS*) of a *collective portfolio management investment firm* that is an *IFPRU investment firm*. However, ■ IFPRU 2.2 (Internal capital adequacy standards) and ■ IFPRU 2.3 (Supervisory review and evaluation process: Internal capital adequacy standards) apply to the whole of its business.

11.7 CAPITAL REPORTING

11.7.1

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The reporting requirements of capital adequacy for a *collective portfolio management firm* and a *collective portfolio management investment firm* are set out in ■ SUP 16.12 (Integrated regulatory reporting). In summary, the relevant capital adequacy forms for its business of *managing an AIF* or *managing a UCITS* are as follows:

- (1) a *collective portfolio management firm* is required to submit FIN066 (and FSA042 if it is a *UCITS firm*);
- (2) a *collective portfolio management investment firm* that is an *IFPRU investment firm* is required to submit FIN067 (and FSA042 if it is a *UCITS investment firm*) and report using COREP; and
- (3) a *collective portfolio management investment firm* that is a *BIPRU firm* is required to submit FIN068 (and FSA042 if it is a *UCITS investment firm*) and FSA003.

Chapter 12

Financial resources requirements for operators of electronic systems in relation to lending.



12.1 APPLICATION AND PURPOSE

Application

- 12.1.1 **R** This chapter applies to an *operator of an electronic system in relation to lending*.
- 12.1.2 **G** This chapter amplifies the *threshold condition 2D* (Appropriate resources) by providing that a *firm* must meet, on a continuing basis, a basic solvency requirement. This chapter also builds on *Principle 4* which requires a *firm* to maintain adequate **financial resources** by setting out appropriate requirements for a *firm* according to what type of *firm* it is.
- 12.1.3 **G** Prudential standards have an important role in minimising the risk of harm to consumers by requiring a *firm* to behave prudently in monitoring and managing business and financial risks.
- 12.1.4 **G** More generally, having adequate **financial resources** gives the *firm* a degree of resilience and some indication to consumers of creditworthiness, substance and the commitment of its owners. The *rules* in this chapter aim to ensure that a *firm* has **financial resources** which can provide cover for operational and compliance failures and pay redress, as well as reducing the possibility of a shortfall in funds and providing a cushion against disruption if the *firm* ceases to trade.

Relevant accounting principles

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

Actions for damages

- 12.1.6 **R** A contravention of the *rules* in this chapter 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).

Interpretation

- 12.1.7 **R** The definitions in the glossary at **IPRU-INV 12 Appendix 1** apply to terms shown in **bold** type this chapter. Where the term is italicised, the *FCA Handbook Glossary* definition applies.



12.2 FINANCIAL RESOURCES REQUIREMENTS

General solvency requirement

12.2.1 **R** A *firm* must at all times be able to meet its liabilities as they fall due.

General financial resource requirement

12.2.2 **R** A *firm* must ensure that at all times its **financial resources** are not less than its **financial resources requirement**.

Financial resources requirement: firms carrying on other regulated activities

12.2.3 **R** The **financial resources requirement** for a *firm* carrying on one or more regulated activities in addition to operating an electronic system in relation to lending, is the higher of:

- (1) the **financial resources requirement** which is applied by this chapter; and
- (2) the financial resources or own funds requirement which is applied by another *rule* or by directly applicable legislation of the *EU* to the *firm*.

Financial resources requirement

12.2.4 **R** On its *accounting reference date* in each year, a *firm* must calculate:

- (1) the total value of *loaned funds* outstanding on that date; and
- (2) the sum of:
 - (a) 0.2% of the first £50 million of that total value;
 - (b) 0.15% of the next £200 million of that total value;
 - (c) 0.1% of the next £250 million of that total value; and
 - (d) 0.05% of any remaining total value.

12.2.5 **R** The total value of *loaned funds* outstanding is the total amount of funds that are currently being provided to borrowers under *P2P agreements* through an *operator of an electronic system in relation to lending*.

12.2.6 **R** The **financial resources requirement** for a *firm* to which this chapter applies is the higher of:

- (1) £50,000; and
- (2) the sum calculated in accordance with **■ IPRU-INV 12.2.4R(2)** for the period until (subject to **■ IPRU-INV 12.2.9R**) its next *accounting reference date*.

12.2.7 **R** To determine a *firm's financial resources requirement* for the period beginning on the date on which it obtains a *Part 4A permission* and ending on the *day* before its next *accounting reference date*, the *firm* must carry out the calculation in **■ IPRU-INV 12.2.4R(2)** on the basis of the total value of *loaned funds* the *firm* projects will be outstanding on the *day* before its next *accounting reference date*.

Determining the financial resources requirement

12.2.8 **G** If the *firm* has 30,000 individuals each lending £100,000, the total value of the *firm's loaned funds* outstanding is £3,000,000,000. If the *firm* does not carry on any other *regulated activity* to which another higher financial resources or own funds requirement applies, its **financial resources requirement** is £1,900,000. This is calculated as follows:

- (1) $0.2\% \times £50,000,000 = £100,000$;
- (2) $0.15\% \times £200,000,000 = £300,000$;
- (3) $0.1\% \times £250,000,000 = £250,000$;
- (4) $0.05\% \times £2,500,000,000 = £1,250,000$.

Recalculating the financial resources requirement

12.2.9 **R** If the *firm* experiences a greater than 25% increase in the total value of loaned funds outstanding compared to the value used in its last **financial resources requirement** calculation, it must recalculate its **financial resources requirement** using the higher total value of loaned funds outstanding.

12.2.10 **R** A *firm* must notify the FCA of any change, or any likely change, in its **financial resources requirement** within 14 days of that change, or it becoming aware that the change is likely, whichever is the earlier.



12.3 CALCULATION OF FINANCIAL RESOURCES

- 12.3.1 **R** (1) A firm must at all times have available the amount and type of **financial resources** required by this chapter (see ■ IPRU-INV 12.3.2R).
 (2) In arriving at its calculation of its **financial resources**, a firm must deduct certain items (see ■ IPRU-INV 12.3.3R).

12.3.2 **R** Table: Items which are eligible to contribute to the financial resources of a firm

Item	Additional explanation
1. <i>Share capital</i>	This must be fully paid and may include: (1) ordinary <i>share capital</i> ; or (2) preference <i>share capital</i> (excluding preference <i>shares</i> redeemable by shareholders within two years).
2. Capital other than <i>share capital</i> (for example, the capital of a <i>sole trader, partnership or limited liability partnership</i>)	The capital of a <i>sole trader</i> is the net balance on the <i>firm's</i> capital account and current account. The capital of a <i>partnership</i> is the capital made up of the <i>partners'</i> : (1) capital account, that is the account: (a) into which capital contributed by the <i>partners</i> is paid; and (b) from which, under the terms of the <i>partnership</i> agreement, an amount representing capital may be withdrawn by a <i>partner</i> only if: (i) he ceases to be a <i>partner</i> and an equal amount is transferred to another such account by his former <i>partners</i> or any <i>person</i> replacing him as their <i>partner</i> ; or

Item	Additional explanation
	<p>(ii) the <i>partnership</i> is otherwise dissolved or wound up; and</p> <p>(2) current accounts according to the most recent financial statement.</p> <p>For the purpose of the calculation of financial resources, in respect of a <i>defined benefit occupational pension scheme</i>:</p> <p>(1) a <i>firm</i> must derecognise any <i>defined benefit asset</i>;</p> <p>(2) a <i>firm</i> may substitute for a <i>defined benefit liability</i> the <i>firm's deficit reduction amount</i>, provided that the election is applied consistently in respect of any one financial year.</p>
<p>3. Reserves (Note 1)</p>	<p>These are, subject to Note 1, the audited accumulated profits retained by the <i>firm</i> (after deduction of tax, dividends and proprietors' or <i>partners</i>' drawings) and other reserves created by appropriations of share premiums and similar realised appropriations. Reserves also include gifts of capital, for example, from a <i>parent undertaking</i>.</p> <p>For the purposes of calculating financial resources, a <i>firm</i> must make the following adjustments to its reserves, where appropriate:</p> <p>(1) a <i>firm</i> must deduct any unrealised gains or, where applicable, add back in any unrealised losses on debt instruments held, or formerly held, in the available-for-sale financial assets category;</p> <p>(2) a <i>firm</i> must deduct any unrealised gains or, where applicable, add back in any unrealised losses on cash flow hedges of financial instruments measured at cost or amortised cost;</p> <p>(3) in respect of a <i>defined benefit occupational pension scheme</i>:</p> <p>(a) a <i>firm</i> must derecognise any <i>defined benefit asset</i>;</p> <p>(b) a <i>firm</i> may substitute for a <i>defined benefit liability</i> the <i>firm's deficit reduction amount</i>, provided that the election is applied consistently in respect of any one financial year.</p>

Item	Additional explanation
4. Interim net profits (Note 1)	If a <i>firm</i> seeks to include interim net profits in the calculation of its financial resources , the profits have, subject to Note 1, to be verified by the <i>firm's</i> external auditor, net of tax, anticipated dividends or proprietors' drawings and other appropriations.
5. Revaluation reserves	
6. Subordinated loans/debt	Subordinated loans/debt must be included in financial resources on the basis of the provisions in this chapter that apply to subordinated loans/debt.
Note	
1	Reserves must be audited and interim net profits, general and collective provisions must be verified by the <i>firm's</i> external auditor unless the <i>firm</i> is exempt from the provisions of Part VII of the Companies Act 1985 (section 249A (Exemptions from audit)) or, where applicable, Part 16 of the Companies Act 2006 (section 477 (Small companies: Conditions for exemption from audit)) relating to the audit of accounts.

12.3.3

R Table: Items which must be deducted in arriving at financial resources

1	<i>Investments in own shares</i>
2	<i>Investments in subsidiaries</i> (Note 1)
3	Intangible assets (Note 2)
4	Interim net losses (Note 3)
5	Excess of drawings over profits for a <i>sole trader</i> or a <i>partnership</i> (Note 3)
Notes	<p>1. <i>Investments in subsidiaries</i> are the full balance sheet value.</p> <p>2. Intangible assets are the full balance sheet value of goodwill, capitalised development costs, brand names, trademarks and similar rights and licences.</p> <p>3. The interim net losses in row 4, and the excess of drawings in row 5, are in relation to the period following the date as at which the capital resources are being computed.</p>

Subordinated loans/debt

12.3.4

R A subordinated loan/debt must not form part of the **financial resources** of the *firm* unless it meets the following conditions:

- (1) it has an original maturity of:
 - (a) at least five years; or
 - (b) it is subject to five years' notice of repayment;

- (2) the claims of the subordinated creditors must rank behind those of all unsubordinated creditors;
- (3) the only events of default must be non-payment of any interest or principal under the debt agreement or the winding up of the *firm* and such event of default must not prejudice the subordination in (2);
- (4) the remedies available to the subordinated creditor in the event of non-payment or other default in respect of the subordinated loan/ debt must be limited to petitioning for the winding up of the *firm* or proving the debt and claiming in the liquidation of the *firm*;
- (5) the subordinated loan/debt must not become due and payable before its stated final maturity date except on an event of default complying with (3);
- (6) the agreement and the debt are governed by the law of England and Wales, or of Scotland or of Northern Ireland;
- (7) to the fullest extent permitted under the rules of the relevant jurisdiction, creditors must waive their right to set off amounts they owe the *firm* against subordinated amounts owed to them by the *firm*;
- (8) the terms of the subordinated loan/debt must be set out in a written agreement that contains terms that provide for the conditions set out in this *rule*; and
- (9) the loan/debt must be unsecured and fully paid up.

12.3.5

G

When calculating its **financial resources**, the *firm* must exclude any amount by which the aggregate amount of its subordinated loans/debts exceeds the amount calculated as follows:

a – b

where:

- a = Items 1 -5 in the table of items which are eligible to contribute to a *firm's financial resources* (see IPRU-INV 12.3.2R)
- b = Items 1- 5 in the table of items which must be deducted from a *firm's financial resources* (see IPRU-INV 12.3.3R)

12.3.6

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■ IPRU-INV 12.3.5R can be illustrated as follows:

Share Capital	£20,000
Reserves	£30,000
Subordinated loans/debts	£10,000
Intangible Assets	£10,000

As subordinated loans/debts (£10,000) are less than the total of share capital + reserves – intangible assets (£40,000) the *firm* need not exclude any

of its subordinated loans/debts pursuant to IPRU-INV 12.3.5R. Therefore, total **financial resources** will be £50,000.

Share Capital	£20,000
Reserves	£30,000
Subordinated loans/debts	£60,000
Intangible Assets	£10,000

As subordinated loans/debts (£60,000) exceed the total of share capital + reserves – intangible assets (£40,000) by £20,000, the *firm* should exclude £20,000 of its subordinated loans/debts when calculating its **financial resources**. Therefore, total **financial resources** will be £80,000.

12.4 NOTIFICATION REQUIREMENTS

12.4.1

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Handbook reference	Matter to be notified	Contents of notification	Trigger event	Time allowed
IPRU-INV 12.2.10R	A change or likely change, in a <i>firm's financial resources requirement</i>	The financial resources requirement as re-calculated	A greater than 25% increase in the <i>firm's</i> total value of the amount of <i>loaned funds</i> outstanding compared to the value used in its last financial resources requirement calculation	Within 14 <i>days</i> of the trigger event

12 App 1 Appendix 1: Glossary of terms for IPRU(INV) 12

App 1 Terms

12App1.1 G If a defined term does not appear in the *IPRU(INV)* glossary below, the definition appearing in the main *Handbook Glossary* applies.

financial resources	a <i>firm's</i> financial resources as calculated in accordance with <i>IPRU(INV)</i> 12.3 (Calculation of financial resources).
financial resources requirement	an amount of financial resources that a <i>firm</i> must hold as set out in <i>IPRU(INV)</i> 12.2 (Financial resources requirements).

Chapter 13

Financial Resources Requirements for Personal Investment Firms



13.1 APPLICATION, GENERAL REQUIREMENTS AND PROFESSIONAL INDEMNITY INSURANCE REQUIREMENTS

Application

13.1.1

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This chapter applies to a *firm* which is a *personal investment firm* as set out in the table below.

Type of personal investment firm	Application of this Chapter
A <i>personal investment firm</i> which is an exempt CAD firm	13.1, 13.1A, 13.13 and 13.14
A <i>personal investment firm</i> which is a category B firm	13.1 and 13.13 to 13.15

(2) [deleted]

(3) [deleted]

Purpose

13.1.2

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This chapter amplifies *threshold condition* 2D (Appropriate resources) by providing that a *firm* must meet, on a continuing basis, a basic solvency requirement and a minimum capital resources requirement. This chapter also amplifies *Principles* 3 and 4 which require a *firm* to take reasonable care to organise and control its affairs responsibly and effectively with adequate risk management systems and to maintain adequate financial resources by setting out capital resources for a *firm* according to the *regulated activity* or activities it carries on.

13.1.3

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Although financial resources and appropriate systems and controls can generally mitigate operational risk, professional indemnity insurance has a role in mitigating the risks a *firm* faces in its day-to-day operations, including those arising from not meeting the legally required standard of care when *advising on investments*. The purpose of the *rules* in this section is also to ensure that a *firm* has in place the type, and level, of professional indemnity insurance necessary to mitigate these risks. This includes, in the case of a *UK firm* exercising an *EEA right*, cover for breaches of obligations imposed by or under laws, or provisions having the force of law, in each *EEA State* in which the *firm* carries on business.

General capital resources and solvency requirements

- 13.1.4 **R** A *firm* must at all times:
- (1) have and maintain capital resources at least equal to its relevant capital resources requirement; and
 - (2) be able to meet its liabilities as they fall due.

Capital resources: general accounting principles

- 13.1.4A **R** Unless a *rule* provides otherwise, a *firm* must:
- (a) recognise an asset or liability; and
 - (b) measure the amount of that asset or liability, by using the accounting principles it applies in preparing the *firm's* reporting form in (2).
- (2) The accounting principles are referred to in:
- (a) the Notes for completion of the Retail Mediation Activities Return (*RMAR*) (under the heading "Accounting Principles") in ■ SUP 16 Annex 18BG for a *category B firm*; and
 - (b) the Guidance notes for data items in FSA032 (under the heading "Defined terms") in ■ SUP 16 Annex 25AG for an *exempt CAD firm*.

Requirement to hold professional indemnity insurance

- 13.1.5 **R** A *firm* must take out and maintain at all times professional indemnity insurance that is at least equal to the requirements in this section from:
- (1) an *insurance undertaking* which is authorised to transact professional indemnity insurance in the *EEA*; or
 - (2) a *person of equivalent status* in:
 - (a) a Zone A country;
 - (b) the Channel Islands, Gibraltar, Bermuda or the Isle of Man.

[Note: Article 4(3) of the *Insurance Mediation Directive*]

- 13.1.6 **R** An *exempt CAD firm* is not required to effect and maintain professional indemnity insurance unless it chooses this *option* (see 13.1A).

Comparable guarantee

- 13.1.7 **R**
- (1) A *firm* is not required to effect or maintain professional indemnity insurance if a *bank*, *building society* or an *insurer* provides the *firm* with a comparable guarantee.
 - (2) If the *firm* is a member of a *group* in which there is a *bank*, *building society* or an *insurer*, the *firm's* comparable guarantee must be from that *bank*, *building society* or *insurer*.

- (3) A comparable guarantee means an enforceable, written agreement on terms at least equal to those required by ■ IPRU-INV 13.1.9R to ■ 13.1.13R, as appropriate.

Relevant income

- 13.1.8** **R** The term "relevant income" in this section refers to all income received or receivable which is commission, brokerage, fees or other related income, whether arising from the *firm's permitted activities* or not, for the last accounting year prior to inception or renewal of the professional indemnity insurance policy ("the policy").

Policy terms

- 13.1.9** **R** The policy must incorporate terms which are appropriate and must make provision for cover in respect of any claim for loss or damage, for which the *firm* may be liable as a result of an act or omission by:
- (1) the *firm*; or
 - (2) any *person* acting on behalf of the *firm* including *employees*, appointed representatives or its other *agents*.

Limits of indemnity

- 13.1.10** **R** If the *firm* is an *IMD insurance intermediary*, whether or not it is also an *exempt CAD firm*, the appropriate minimum *limits of indemnity* per year are no lower than:

- (1) EUR 1,120,200 for a single claim against the *firm*; and
- (2) EUR 1,680,300 in the aggregate.

[Note: Article 4(3) of the *Insurance Mediation Directive*]

- 13.1.11** **R** If the *firm* is an *exempt CAD firm* that maintains professional indemnity insurance under 13.1A.3(1)(b), the appropriate minimum *limits of indemnity* per year are no lower than:

- (1) EUR 1,000,000 for a single claim against the *firm*; and
- (2) EUR 1,500,000 in the aggregate.

[Note: article 31(1) of the *CRD* (see also ■ IPRU-INV 13.1A.3R)]

- 13.1.12** **R** If the *firm* is both an *IMD insurance intermediary* and an *exempt CAD firm* that maintains professional indemnity insurance under 13.1A.4(1)(b), the appropriate additional *limits of indemnity* to 13.1.10R per year are no lower than:

- (1) EUR 500,000 for a single claim against the *firm*; and
- (2) EUR 750,000 in the aggregate.

[Note: article 31(2) of the *CRD* (see also ■ IPRU-INV 13.1A.4R)]

- 13.1.13** **R** If the *firm* is not an *IMD insurance intermediary* or an *exempt CAD firm*, then the following *limits of indemnity* apply:
- (1) if the *firm* has relevant income of up to £3,000,000, no lower than £500,000 for a single *claim* against the *firm* and £500,000 in the aggregate; or
 - (2) if the *firm* has relevant income of more than £3,000,000, no lower than £650,000 for a single claim against the *firm* and £1,000,000 in the aggregate.
- 13.1.14** **G** Article 4(7) of the *Insurance Mediation Directive* requires the *limits of indemnity* to be reviewed every five years to take into account movements in European consumer prices. These *limits* will therefore be subject to further adjustments on the basis of index movements advised by the European Commission.
- 13.1.15** **R** If a policy is denominated in any currency other than euros, a *firm* must take reasonable steps to ensure that the *limits of indemnity* are, when the policy is effected (i.e. agreed) and at renewal, at least equivalent to those denominated in euros.
- 13.1.16** **G** A *firm* should consider whether the overall cover is adequate taking account of 13.1.22G(2) and whether the *firm* should seek additional cover or legal expenses insurance. (Legal defence costs are costs of defence against claims that fall under the terms of the policy.)
- 13.1.17** **G** The cover provided by the policy should be wide enough to include the liability of the *firm*, its *appointed representatives*, its *tied agents*, *employees* and its agents for breaches under the *regulatory systems* or civil law. If the *firm* operates outside the *United Kingdom* then the policy should cover other regulatory requirements imposed under the laws of other countries in which the *firm* operates.

Policies providing for more than one firm.....

- 13.1.18** **R** If the *policy* provides cover to more than one *firm* then:
- (1) The relevant income for calculating the limits of indemnity is that of all the *firms* named in the policy combined;
 - (2) each *firm* named in the policy must have the benefit of the minimum *limits of indemnity* as required in this section; and
 - (3) each *firm* named in the policy must notify the *FCA* if the aggregate cover in the policy falls below the minimum *limits of indemnity*.

Limits of indemnity – additional requirements

13.1.19

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In addition to the specific requirements in ■ 13.1.9R to ■ 13.1.13R, the policy must make provision for the following:

- (1) for a *firm* with relevant income of more than £6,000,000, the aggregate limit identified in the table below:

Relevant income is (£)		Minimum aggregate <i>limit of indemnity</i>
more than	up to	(£)
6,000,000	7,000,000	1,150,000
7,000,000	8,000,000	1,300,000
8,000,000	9,000,000	1,450,000
9,000,000	10,000,000	1,600,000
10,000,000	12,500,000	2,000,000
12,500,000	15,000,000	2,400,000
15,000,000	17,500,000	2,800,000
17,500,000	20,000,000	3,150,000
20,000,000	25,000,000	3,800,000
25,000,000	30,000,000	4,250,000
30,000,000	35,000,000	4,500,000
35,000,000	40,000,000	4,750,000
40,000,000	50,000,000	5,500,000
50,000,000	60,000,000	6,000,000
60,000,000	70,000,000	6,750,000
70,000,000	80,000,000	7,250,000
80,000,000	90,000,000	7,750,000
90,000,000	100,000,000	8,500,000
100,000,000	150,000,000	11,250,000
150,000,000	200,000,000	14,000,000
200,000,000	250,000,000	17,000,000
250,000,000	300,000,000	19,750,000
300,000,000	n/a	22,500,000

- (2) full retroactive cover in respect of the kinds of liabilities described in ■ 13.1.9R for claims arising from work carried out by the *firm*, or on its behalf, in the past; and
- (3) cover in respect of *Ombudsman* awards made against the *firm*.

Limitations

13.1.20 **R** The policy must not be subject to conditions or exclusions which unreasonably limit its cover (whether by exclusion of cover, by policy excesses or otherwise).

Exclusions

13.1.21 **R** The policy must not:

- (1) exclude any type of business or activity that has been carried out by the *firm* in the past or will be carried out by the *firm* during the time for which the policy is in force; or
- (2) exclude liabilities which are identified or crystallised as a result of regulatory action against the *firm* (either individually or as a member of a *class of authorised persons*);

unless the *firm* holds additional capital resources, in accordance with ■ 13.1.23R.

13.1.22 **G**

- (1) The *FCA* considers it reasonable for a *firm's* policy to exclude cover for:
 - (a) specific business lines if that type of business has not been carried out by the *firm* in the past and will not be carried out by the *firm* during the life of the policy; or
 - (b) specific *claims* that have been previously notified to the *firm's insurer* and claimed for under another policy.
- (2) The *FCA* does not consider it reasonable for a *firm's* policy to treat legal defence costs cover as part of the *limits of indemnity* if this reduces the cover available for any individual substantive claim.

Additional capital resources - exclusions

13.1.23 **R** The amount of additional capital resources that a *firm* must hold as a result of an exclusion under ■ IPRU-INV 13.1.21R must be calculated by referring to the *firm's* relevant income in the following table:

Relevant income £000s		Minimum additional capital resources
more than	up to	£000s
		(Notes 1 and 2)
0	100	5
100	200	12

200	300	18
300	400	21
400	500	23
500	600	25
600	700	27
700	800	28
800	900	30
900	1,000	31
1,000	1,500	37
1,500	2,000	42
2,000	2,500	46
2,500	3,000	51
3,000	3,500	55
3,500	4,000	59
4,000	4,500	63
4,500	5,000	67
5,000	6,000	73
6,000	7,000	79
7,000	8,000	85
8,000	9,000	90
9,000	10,000	95
10,000	100,000	95y
100,000	n/a	950

Note 1 - For *firms* with relevant income of more than £10m but up to £100m value y is calculated by relevant income/ £10m.

Note 2 - The calculation of a *firm's* capital resources is set out in sections 13.1A to 13.15 (see IPRU-INV 13.1.1R for application of these sections to an exempt CAD *firm* or a category B *firm*).

13.1.24

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The *firm* should hold additional capital resources in excess of those minimum amounts set out in the table in 13.1.23R where the required amounts of additional capital resources provide insufficient cover, taking into account the *firm's* individual circumstances.

Excess level

13.1.25 **R** The policy must not make provision for payment by the *firm* of an excess on any claim of more than £5,000, unless the *firm* holds additional capital resources, in accordance with 13.1.27R.

13.1.26 **R** The reference to "excess" is to the highest excess level required to be paid under the policy unless that excess relates to a type of business that has not been carried out by the *firm* in the past. In those circumstances, the reference is to the next highest excess level required by the policy applicable to a type of business that has been carried out by the *firm* in the past.

Additional capital resources - excess

13.1.27 **R** The amount of additional capital resources that a *firm* must hold where the policy's excess on any claim is more than £5,000 must be calculated by referring to the *firm's* relevant income and excess obtained in the following table:

All amounts are shown in £000s (Notes 1 and 2)

Relevant income is		Excess obtained, up to and including												
more than	up to	5	10	15	20	25	30	40	50	75	100	150	200+	
0	100	0	4	7	9	12	14	18	21	28	34	45	54	
100	200	0	7	11	14	17	20	25	29	38	46	59	70	
200	300	0	9	14	18	21	24	30	35	45	54	69	82	
300	400	0	11	16	21	24	28	34	39	50	60	77	91	
400	500	0	13	18	23	27	30	37	43	55	66	83	98	
500	600	0	14	20	25	29	33	40	46	59	70	89	105	
600	700	0	16	22	27	31	35	42	49	63	74	94	111	
700	800	0	17	23	28	33	37	45	52	66	78	99	117	
800	900	0	18	24	30	35	39	47	54	69	82	103	122	
900	1,000	0	19	26	31	36	41	49	56	72	85	107	126	
1,000	1,500	0	23	31	37	43	48	57	66	83	99	124	146	
1,500	2,000	0	26	35	42	48	54	64	73	93	109	138	161	
2,000	2,500	0	29	38	46	53	59	71	81	102	121	152	179	
2,500	3,000	0	32	42	51	58	65	78	89	112	132	166	195	
3,000	3,500	0	35	46	55	63	71	84	96	121	142	179	210	
3,500	4,000	0	38	50	59	68	76	90	102	129	152	191	223	
4,000	4,500	0	41	53	63	72	80	95	108	137	161	202	236	

4,500	5,000	0	43	56	67	76	85	100	114	144	169	212	248
5,000	6,000	0	48	62	73	84	93	110	125	157	185	231	271
6,000	7,000	0	52	67	79	90	101	119	135	169	199	249	291
7,000	8,000	0	56	72	85	97	107	127	144	181	212	265	310
8,000	9,000	0	59	76	90	103	114	134	152	191	224	280	328
9,000	10,000	0	63	80	95	108	120	141	160	201	236	294	344
10,000	100,000	0	63y	80y	95y	108y	120y	141y	160y	201y	236y	294y	344y
100,000	n/a	0	630	800	950	1080	1200	1410	1600	2010	2360	2940	3440

Note 1 - For *firms* with relevant income more of £10m but up to £100m value *y* is calculated by relevant income/ £10m.

Note 2 - The calculation of a *firm's* capital resources is set out in sections 13.1A to 13.15 (see IPRU-INV 13.1.1R for application of these sections to an exempt CAD *firm* or a category B *firm*).

Notification requirements

13.1.28

R

A *firm* must notify the FCA immediately if it becomes aware, or has information which reasonably suggests, that any of the following matters in relation to its professional indemnity insurance has occurred, may have occurred or may occur in the foreseeable future:

- (1) professional indemnity insurance cannot be obtained within 28 days of the inception or renewal date;
- (2) professional indemnity insurance is cancelled;
- (3) the amount of aggregate cover is exhausted;
- (4) the *firm* commences business lines for which it had not obtained cover;
- (5) the *firm* is relying on a policy cover for more than one *firm*; or
- (6) the *firm* is relying on a comparable guarantee provided in accordance with the *rules* in this chapter.

13.1.29

G

- (1) For the purposes of the provisions relating to professional indemnity insurance, "additional capital resources" means readily realisable *own funds* or capital resources under ■ IPRU-INV 13.15.3R, depending on the type of *firm*.
- (2) The FCA expects items included in *own funds* or capital resources under ■ IPRU-INV 13.15.3R, depending on the type of *firm*, to be regarded as "readily realisable" only if they can be realised, at any given time, within 90 days.



13.1A Capital resources and professional indemnity insurance requirements for an exempt CAD firm

Application

- R** This section applies to a *personal investment firm* which is an *exempt CAD firm*.

Requirement to hold initial capital and professional indemnity insurance

- R** The financial resources requirement for a *personal investment firm* which is an *exempt CAD firm* is the higher of:

- (1) the requirement that is applied by section 13.1A; and
- (2) the requirement that is applied by sections 13.13 to 13.14.

13.1A.3

- R** (1) A *firm* which is not an *IMD insurance intermediary* must have:
- (a) *initial capital* of EUR 50,000; or
 - (b) professional indemnity insurance at least equal to the requirements of ■ IPRU-INV 13.1.11R and ■ IPRU-INV 13.1.15R to ■ IPRU-INV 13.1.27R; or
 - (c) a combination of *initial capital* and professional indemnity insurance in a form resulting in a level of coverage equivalent to (a) or (b).
- [**Note:** Article 67(3) of *MiFID* and article 31(1) of the *CRD* (see also rule ■ IPRU-INV 13.1.11R)]
- (2) A *firm* applying (b) or (c) above, must have *initial capital* of at least £20,000.

13.1A.4

- R** (1) A *firm* that is also an *IMD insurance intermediary* must have professional indemnity insurance at least equal to the limits set out in ■ IPRU-INV 13.1.10R and in addition must have:
- (a) *initial capital* of EUR 25,000; or
 - (b) professional indemnity insurance at least equal to the requirements of ■ IPRU-INV 13.1.12R and ■ IPRU-INV 13.1.15R to ■ IPRU-INV 13.1.27R; or

- (c) a combination of *initial capital* and professional indemnity insurance in a form resulting in a level of coverage equivalent to (a) or (b).

[Note: Article 67(3) of *MiFID* and article 31(2) of the *CRD* (see also ■ IPRU-INV 13.1.12R)]

- (2) A *firm* applying (b) or (c) above must have initial capital of at least £20,000.

13.1A.5

G

A trade-off between *initial capital* and professional indemnity insurance is appropriate such that EUR 1 of *initial capital* is the equivalent of professional indemnity insurance cover of EUR 20 for a single claim against the *firm* and EUR 30 in aggregate.

Initial capital

R

A *firm's initial capital* consists of the sum of the following items:

- (1) ordinary *share capital* which is fully paid;
- (2) perpetual non-cumulative *preference share capital* which is fully paid;
- (3) *share premium account*;
- (4) reserves excluding revaluation reserves;
- (5) audited retained earnings;
- (6) externally *verified* interim net profits;
- (7) partners' capital;
- (8) *eligible LLP members' capital* (in accordance with the provisions of ■ IPRU-INV Annex A); and
- (9) *sole trader* capital.

Perpetual non-cumulative preference share capital

13.1A.7

R

A *firm* may include *preference share capital* in *initial capital* only where any *coupon* on it is not cumulative, and the *firm* is under no obligation to pay a *coupon* in any circumstances.

Audited retained earnings

13.1A.8

R

When calculating *initial capital*, a *firm* may include its audited retained earnings only after making the following adjustments:

- (1) a *firm* must not recognise the fair value reserves related to gains or losses on cash flow hedges of financial instruments measured at amortised cost;
- (2) in respect of a *defined benefit occupational pension scheme*, a *firm* must derecognise any *defined benefit asset*;
- (3) a *firm* must not include any unrealised gains from investment property (these should be reported as part of revaluation reserves);

- (4) where applicable, a *firm* must deduct any asset in respect of deferred acquisition costs and add back in any liability in respect of deferred income (but excluding from the deduction or addition any asset or liability which will give rise to future cash flows), together with any associated deferred tax.

Externally verified interim net profits or current account

13.1A.9 **R** A *firm* may include interim net profits or current account when calculating *initial capital* to the extent that they have been *verified* by the *firm's* external auditor and are net of any foreseeable tax, dividend and other appropriations.

13.1A.10 **R** When calculating *initial capital*, a *firm* may include its partners' capital only after making the following adjustments:

- (1) a *firm* must not recognise the fair value reserves related to gains or losses on cash flow hedges of financial instruments measured at amortised cost;
- (2) in respect of a *defined benefit occupational pension scheme*, a *firm* must derecognise any *defined benefit asset*;
- (3) where applicable, a *firm* must deduct any asset in respect of *deferred acquisition costs* and add back in any liability in respect of deferred income (but excluding from the deduction or addition any asset or liability which will give rise to future cash flows), together with any associated deferred tax.

Defined benefit pension scheme: defined benefit liability

13.1A.11 **R** For the calculation of *initial capital*, a *firm* may substitute for a *defined benefit liability* the *firm's deficit reduction amount*. The election must be applied consistently in respect of any one financial year.

13.1A.12 **G** A *firm* should keep a record of and be ready to explain to its supervisory contacts in the *FCA* 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*.

Ongoing capital requirements

13.1A.13 **R** A *firm* must, at all times, maintain a combination of professional indemnity insurance and *own funds*, at least equal to the requirements in this chapter for professional indemnity insurance and *initial capital*.

13.1A.14 **R** A *firm's initial capital*:
minus the sum of the items set out against **B**
plus the sum of the items set out against **C**

minus material holdings in *credit* and *financial institutions* and *material insurance holdings*
equals *own funds*.

13.1A.15 **R** This table forms part of *rule* 13.1A.14 ■ IPRU-INV 13.1A.14R.

- | | | |
|-----|-----------------------------------------------------------------------------------------------|----------|
| (1) | <i>Investments</i> in own <i>shares</i> at book value | B |
| (2) | Intangible assets | |
| (3) | <i>Material current year losses</i> | |
| (4) | Excess of current year drawings over current year profits | |
| (1) | Revaluation reserves | C |
| (2) | Perpetual cumulative preference <i>share capital</i> and <i>debt capital</i> | |
| (3) | Long-term subordinated loans (in accordance with IPRU-INV 13.1A.18R) | |
| (4) | Fixed term preference <i>share capital</i> (if not redeemable by shareholders within 5 years) | |

Perpetual cumulative preference share capital

13.1A.16 **R** Perpetual cumulative preference *share capital* may not be included in the calculation of *own funds* unless it meets the following requirements:

it may not be reimbursed on the holder's initiative or without the prior agreement of the *FCA*

;

- (2) the instrument must provide for the *firm* to have the option of deferring the dividend payment on the share capital;
- (3) the shareholder's claims on the *firm* must be wholly subordinated to those of all non-subordinated creditors;
- (4) the terms of the instrument must provided for the loss-absorption capacity of the share capital and unpaid dividends, whilst enabling the *firm* to continue its business; and
- (5) it must be fully paid-up.

Own funds - Restrictions

- 13.1A.17** **R**
- (1) In calculating own funds:
 - (i) the total amount of revaluation reserves, perpetual cumulative preference *share capital*, long-term subordinated loans and fixed term preference *share capital* must not exceed 100% of *initial capital* minus the sum of the items set out against B; and

- (ii) the total amount of fixed term preference *share* capital and long-term subordinated loans must not exceed 50% of *initial capital* minus the sum of the items set out against B.

Subordinated Loans – Exempt CAD firm

- 13.1A.18** **R** ■ IPRU-INV 13.1A.19R to ■ IPRU-INV 13.1A.20R apply to an *exempt CAD firm*.
- 13.1A.19** **R** A *firm* may include a long-term subordinated loan as *own funds* (see item C(3) table 13.1A.15R) if all the conditions in ■ IPRU-INV 13.1A.20R are satisfied.
- 13.1A.20** **R** The conditions referred to in ■ IPRU-INV 13.1A.19R are:
- (1) the subordinated loan must be fully paid up;
 - (2) the subordinated loan must have an original maturity of at least five years or, where there is no fixed term, the subordinated loan must be subject to not less than five years' notice of repayment;
 - (3) the agreement governing the subordinated loan must only permit repayment, prepayment or termination on:
 - (a) maturity, or on expiration of the period of notice, if a *firm* has at least 120% of its financial resources requirement after that payment or termination; or
 - (b) winding up after the claims of all other creditors and all outstanding debts have been settled;
 - (4) the amount of the subordinated loan used in the calculation of a *firm's own funds* must be reduced on a straight-line basis over the last five years of the term of the subordinated loan;
 - (5) the subordinated loan is in the standard form prescribed by the *FCA* for long-term subordinated loans (see form 13.1 Form of subordinated loan agreement for *personal investment firms*).



**13.3 FINANCIAL RESOURCES TEST 1 -
OWN FUNDS**

13.3.1 **R** [deleted]

13.3.1A **G** [deleted]

13.3.2 **R** [deleted]

13.3.2A **R** [deleted]

13.3.2B **G** [deleted]
[deleted]

Alternative to Financial Resources Test 1

13.3.3 **R** [deleted]

13.3.3A **R** [deleted]

13.3.3B **R** [deleted]



13.6 Large exposures [deleted]

13.6.1 **R** [deleted]

Requirements [deleted]

13.6.2 **R** [deleted]

13.6.2A **R** [deleted]

13.6.2B **R** [deleted]

13.6.2C **R** [deleted]

13.6.2D **R** [deleted]

Table 13.6.2(1) [deleted]

Calculation of financial resources to meet tests 1, 1A OR 2 [deleted]

13.6.2D **R** Table 13.6.2(2) [deleted]



13.8 Trading Book [deleted]

13.8.2 **G** [deleted]

13.8.2 **R** [deleted]

13.8.3 **G** [deleted]



13.13 CAPITAL RESOURCES REQUIREMENT FOR AN EXEMPT CAD FIRM AND A CATEGORY B FIRM

Application

13.13.1 **R** This section applies to a *personal investment firm* which is either:

- (1) an *exempt CAD firm*; or
- (2) a *category B firm*.

Requirement

13.13.2 **R**

- (1) A *firm* to which *MIPRU* does not apply must calculate its capital resources requirement as in (2).
- (2) The *firm* must calculate its capital resources requirement as the higher of:
 - (a) £20,000; and
 - (b) the amount equivalent to the applicable percentage of its *annual income* specified in table 13.13.2(2)(b), depending on the type of *firm*.

Table 13.13.2(2)(b)

This table forms part of ■ IPRU-INV 13.13.2R.

(A)	(B) Type of firm	(C) Applicable percentage of annual income
(1)	<i>Exempt CAD firm</i>	5%
(2)	<i>Category B1 firm</i>	10%
(3)	<i>Category B2 firm</i>	10%
(4)	<i>Category B3 firm</i> which is permitted to carry on the activity of <i>managing investments</i> in respect of portfolios containing only <i>life policies</i> or to delegate such activity to an <i>investment firm</i>	10%
(5)	<i>Category B3 firm</i> not in (4)	5%

13.13.3 R

- (1) A *firm* to which *MIPRU* also applies must calculate its capital resources requirement as in (2).
- (2) The *firm* must calculate its capital resources requirement as the higher of:
 - (a) £20,000; and
 - (b) the sum of:
 - (i) the amount that would have applied to it under ■ IPRU-INV 13.13.2R(2)(b) if it were a *firm* of the type in column (B) of table 13.13.2(2)(b); and
 - (ii) the capital resources requirement in ■ MIPRU 4.2. (Capital resources requirements), after excluding the fixed amounts specified in table 13.13.3(2)(b)(ii).

Table 13.13.3(2)(b)(ii)

This table forms part of ■ IPRU-INV 13.13.3R.

Activity	Provision	Fixed amount
<i>Insurance mediation activity or home finance mediation activity</i>	MIPRU 4.2.11R(1)(a) (<i>firm not holding client money or assets</i>)	£5,000
	MIPRU 4.2.11R(2)(a) (<i>firm holding client money or assets</i>)	£10,000
<i>Home financing and home finance administration (not connected to regulated mortgage contracts)</i>	MIPRU 4.2.12R(1)(a)	£100,000
<i>Home finance administration (with all assets off balance sheet)</i>	MIPRU 4.2.19R(1)	£100,000
<i>Home financing and home finance administration (connected to regulated mortgage contracts)</i>	MIPRU 4.2.23R(1)	£100,000

13.13.4 G

- (1) ■ IPRU-INV 13.13.4G(2) illustrates how a *firm* that is subject to this section and *MIPRU* calculates its capital resources requirement under ■ IPRU-INV 13.13.3R.
- (2) Example: A *category B3 firm* with *annual income* of £300,000 under this section and £100,000 from its *home finance mediation activity* (without holding *client money*) should calculate capital resources requirement as specified in table 13.13.4G(2).

Table 13.13.4G(2)

This table forms part of ■ IPRU-INV 13.13.4G.

Requirement	Calculation	Amount
The capital resources requirement is the higher of:		

Requirement	Calculation	Amount
(1) £20,000; and	£20,000	£20,000
(2) The sum of:		
(a) the amount that would have applied to it under IPRU-INV 13.13.2R(2)(b) if it were a firm of the type in column (B) of table 13.13.2(2)(b); and	As this is a <i>category B3 firm</i> , the applicable calculation is 5% of £300,000.	£15,000
(b) the capital resources requirement in MIPRU 4.2. (Capital resources requirements), after excluding the fixed amounts specified in table 13.13.3(2)(b)(ii).	For a <i>firm</i> carrying on <i>home finance mediation activity</i> without holding <i>client money</i> , MIPRU 4.2.11R(1) specifies a requirement of 2.5% of £100,000 (excluding the amount of £5,000 in MIPRU 4.2.11R(1)(a)).	£2,500
	Total of part (2) of the capital resources requirement, which is £15,000 plus £2,500.	£17,500
	The capital resources requirement is the higher of part (1), which is £20,000, and part (2), which is £17,500.	£20,000

13.13.5 **R** A firm whose permission includes *establishing, operating or winding up a personal pension scheme* must calculate its capital resources requirement as the sum of:

- (1) the capital resources requirement that is applied under
 - IPRU-INV 13.13.2R(2) or ■ IPRU-INV 13.13.3R(2); and
- (2) the financial resources requirement calculated in accordance with
 - IPRU-INV 5 (Investment Management Firms).

13.14 CALCULATION OF ANNUAL INCOME FOR AN EXEMPT CAD FIRM AND A CATEGORY B FIRM

Application

13.14.1 **R** This section applies to a personal investment firm which is either:

- (1) an *exempt CAD firm*;
- (2) a *category B firm*.

Annual income

13.14.2 **R** This section applies to a *firm* when it calculates *annual income* for its capital resources requirement.

- 13.14.3 **R**
- (1) "*Annual income*" is the *annual income* from the *firm's designated investment business* as given in its reporting form in (3) drawn up at its most recent *accounting reference date*.
 - (2) In (1), the most recent *accounting reference date* is the last one for which the *firm* reported *annual income*.
 - (3) The relevant reporting form under ■ SUP 16.12 is:
 - (a) the Retail Mediation Activities Return (*RMAR*) (Section B: Profit and Loss Account) for a *category B firm*; and
 - (b) FSA030 (Income Statement) for an *exempt CAD firm*.
 - (4) If the *firm's* most recent reporting form does not cover a 12-month period, the *annual income* is derived by converting the amount reported, proportionally, to a 12-month period.
 - (5) If the *firm* does not yet have a reporting form under (1), the *annual income* is taken from the forecast or other appropriate accounts which the *firm* has submitted to the *FCA*.

13.14.4 **R** *Annual income* must include the following amounts due to the *firm* in respect of its *designated investment business*:

- (1) brokerage;
- (2) *fees*;

(3) *commissions*; and

(4) other related income (for example, administration charges or profit shares).

13.14.5 **G** A *firm* should include in its *annual income* those amounts it may have agreed to pay to other *persons* involved in a *transaction*, such as other intermediaries or self-employed *advisers*.

13.14.6 **G** A *firm* should not include in its *annual income* those amounts due to it that are used in the calculation of its capital resources requirement under ■ MIPRU 4.2.11R (Capital resources requirement: mediation activity only) or ■ MIPRU 4.2.19R (Capital resources requirement: insurance mediation activity and home financing, or home finance administration).

13.14.7 **G** For the purpose of ■ IPRU-INV 13.14.3R, a *firm* should ensure that the amount of *annual income* adequately reflects the level of its *designated investment business* when deciding whether to add any income not included under any of the reporting forms in IPRU-INV 13.4.3R(3). In doing so, the *firm* should have regard to its circumstances, for example, where such income is being accounted for by a third party.

13.14.8 **R** If a *firm* is a *principal*, its *annual income* includes amounts due to its *appointed representative* for activities related to *designated investment business* for which the *firm* has accepted responsibility.

13.14.9 **G** If a *firm* is a *network*, its *annual income* should include the relevant income due to all of its *appointed representatives* for *designated investment business*.



13.15 CALCULATION OF OWN FUNDS TO MEET THE CAPITAL RESOURCES REQUIREMENT FOR A CATEGORY B FIRM

Application

13.15.1 **R** This section applies to a *personal investment firm* which is a *category B firm*.

13.15.2 **G** The calculation of *own funds* by an *exempt CAD firm* is in **■ IPRU-INV 13.1A.14R.**

13.15.3 **R** A *firm* must calculate its capital resources in accordance with table 13.15.3(1).

Table 13.15.3(1)

This table forms part of **■ IPRU-INV 13.15.3R.**

Capital resources	
Companies	Sole traders: Partnerships
Paid-up <i>share</i> capital (excluding preference shares redeemable by shareholders within two years)	Balances on proprietor's or partners' <ul style="list-style-type: none"> - capital accounts - current accounts (see IPRU-INV 13.15.4R)
<i>Eligible LLP members' capital</i>	Revaluation reserves
<i>Share premium account</i>	Subordinated loans (see IPRU-INV 13.15.7R)
Retained profits (see IPRU-INV 13.15.4R) and interim net profits (Note 1)	
Revaluation reserves	
Subordinated loans (see IPRU-INV 13.15.7R)	
<i>Debt capital</i>	
less	less
- Intangible assets	- Intangible assets
- <i>Material current year losses</i>	- <i>Material current year losses</i>
- <i>Excess LLP members' drawings</i>	- Excess of current year drawings over current year profits
Note 1	
Retained profits must be audited and interim net profits must be verified by the <i>firm's</i> external auditor, unless the <i>firm</i> is exempt from the provi-	

Capital resources

sions of Part 16 of the Companies Act 2006 (section 477 (Small companies: Conditions for exemption from audit)) relating to the audit of accounts.

13.15.4 **R** When calculating a *firm's* capital resources, the following adjustments apply to retained profits or (for *sole traders* or *partnerships*) current accounts figures:

- (1) a *firm* must deduct any unrealised gains or, where applicable, add back in any unrealised losses on cash flow hedges of financial instruments measured at cost or amortised cost;
- (2) a *firm* must de-recognise any *defined benefit asset*;
- (3) a *firm* may substitute for a *defined benefit liability* its *deficit reduction amount* and that election must be applied consistently in respect of any one financial year;
- (4) a *firm* must deduct any unrealised gains on investment property and include these within revaluation reserves; and
- (5) where applicable, a *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.

13.15.5 **G** A *firm* should keep a record of, and be ready to explain to its supervisory contacts in the *FCA*, 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*.

Personal assets

13.15.6 **G** Where a *firm* is a *sole trader* or a *partnership*:

- (1) it can use (to the extent necessary to make up any shortfall in the required resources) any of its personal assets (not being needed to meet liabilities arising from its personal activities and any business activities not regulated by the *FCA*);
- (2) the *firm's* total financial resources, from whatever source, must at all times be sufficient to cover its total liabilities.

Subordinated loans – Category B firm

13.15.7 **R** A *category B firm* may include a short-term subordinated loan as capital resources (see table in **IPRU-INV 13.15.3R**), if all the conditions in **IPRU-INV 13.15.8R** are satisfied.

13.15.8 **R** The conditions referred to in **■ IPRU-INV 13.15.7R** are:

- (1) the subordinated loan must have an original maturity of at least two years or, if it has no fixed term, it is subject to not less than two years' notice of repayment;
- (2) the agreement governing the subordinated loan must not permit payment of interest unless a *firm* has at least 120% of its capital resources requirement after that payment;
- (3) the agreement governing the subordinated loan must only permit *repayment*, prepayment or termination on:
 - (a) maturity, or on expiration of the period of notice, if a *firm* has at least 120% of its capital resources requirement after that payment or termination; or
 - (b) winding up after the claims of all other creditors and all outstanding debts have been settled;
- (4) the agreement governing the subordinated loan is in the standard form for short term subordinated loans prescribed by the *FCA* (see form 13.1 Form of subordinated loan agreement for *personal investment firms*); and
- (5) the restrictions in **■ IPRU-INV 13.15.9R** and **■ IPRU-INV 13.15.10R** are complied with.

Restrictions

13.15.9 **R** A *Category B firm* must calculate:

- (1) the aggregate amount of its short-term subordinated loans and its preference *shares* which are not redeemable within two years;
- (2) the amount of the *firm's* total capital and reserves excluding preference *share* capital, less the amount of its intangible assets, multiplied by 400%.

13.15.10 **R** A *category B firm* must treat as a liability in the calculation of its capital resources any amount by which the sum of **■ IPRU-INV 13.15.9R(1)** exceeds the product of **■ IPRU-INV 13.15.9R(2)**.

13 App 1

App

Chapter 14

Chapter 14 Consolidated Supervision for Investment Businesses

14.1 APPLICATION

14.1.1 **R** Subject to rule 14.1.2, *consolidated supervision* and this chapter apply to a *firm* which is a member of a group if:

(1) It is:

- (i) a *securities and futures firm*, subject to the financial rules in Chapter 3, which is a *broad scope firm* but not a *venture capital firm*; and
- (ii) [deleted]
- (iii) [deleted]

(2) It is neither a *BIPRU firm* nor an *IFPRU investment firm*.

(3) [Deleted]

(4) [Deleted]

(5) [Deleted]

Cases where consolidated supervision under this chapter will not apply

14.1.2 **R** A *firm* is not subject to *consolidated supervision* under the rules in this Chapter where any of the following conditions are fulfilled:

- (1) the *firm* is included in the supervision on a consolidated basis of the group of which it is a member by a *competent authority* other than the *FCA*; or
- (2) the *firm* is a member of a *UK consolidation group* already included in the supervision on a consolidated basis of the group of which it is a member by the *FCA* under ■ BIPRU 8; or
- (3) the *firm* is a member of a group already included in the supervision on a consolidated basis of the group of which it is a member by the appropriate regulator under Part One, Title II, Chapter 2 of the *EU CRR*.

14.1.3 **G** (1) [Deleted]

(2) [Deleted]

- (3) Where there is more than one authorised *firm* in the group, subject to the rules of this chapter, one consolidated supervision return may be submitted on behalf of all the *firms* in the group in accordance with ■ SUP 16.3.25G.

Exemption from consolidated supervision

14.1.4

R

A *firm* need not meet the requirements in rules 14.3.1 and 14.3.2 if:

- (1) there is no *credit institution* in the group;
- (2) no *firm* in the group *deals in investments as principal*, except where it is dealing solely as a result of its activity of operating a *collective investment scheme*, or where the *firm's* positions fulfil the *CAD Article 5* exempting criteria;
- (3) [Deleted]
- (4) the *firm* notifies the *FCA* of any serious risk that could undermine the financial stability of the group as soon as it becomes aware of that risk;
- (5) the *firm* reports to the *FCA* all group *large exposures* as at the end of each quarter, and within the period specified in ■ SUP 16;
- (6) the *firm* meets the conditions in rule 14.1.5; and
- (7) the *firm* has first notified the *FCA* in writing that it intends to rely on this rule.

14.1.5

R

If the *firm* notifies the *FCA* under rule 14.1.4 that it will not apply the rules in this section, it must:

- (1) submit to *FCA* a consolidated supervision return within the time period specified by ■ SUP 16, together with a consolidated profit and loss account;
- (2) ensure that each *firm* in the group deducts from its solo financial resources any quantifiable *contingent liability* in respect of other group entities;
- (3) ensure that the solo financial resources requirement of each *firm* in the group incorporates the full value of the expenditures of the *firm* wherever they are incurred on behalf of the *firm*; and
- (4) make a note in its audited financial statements that it is not subject to regulatory consolidated capital requirements.

14.1.6

G

- (1) [Deleted]
- (2) The conditions in rule 14.1.5 aim to ensure that the *firm* is protected from weaknesses in other group entities.
- (3) In rule 14.1.5(2), *contingent liabilities* includes direct and indirect guarantees.

- (4) 14.1.5(3) aims to ensure that the expenditure-based requirement incorporates the *firm's* actual ongoing annual expenditures (including any share of depreciation on fixed assets) where these have been met by another group entity.
- (5) The *FCA* may require further information from the *firm* if it considers that the *firm's* consolidated financial position raises undue risks to consumers. It may also seek reassurance that the *firm* has sufficiently robust *client money* and *asset controls* - for example, it may require a *skilled person's* report. The *FCA* may also use its own initiative power to impose conditions on the *firm*. This could include raising additional capital or further limitations on the *firm's* intra-group exposures.
- (6) *Rule 14.1.4(5)* refers to *large exposures*, which should be measured against group consolidated own funds or (if this would result in all *exposures* being classified as *large exposures*) by aggregating all the *exposures* of the individual entities in the group and measuring them against the own funds of the individual *firm* giving rise to the consolidated supervision requirement. If there is more than one *firm* in the group giving rise to the consolidated supervision requirement, the group *large exposures* should be measured against the *firm* with the smallest own funds.

14.2 SCOPE OF CONSOLIDATION

- 14.2.1** **R** For the purposes of the rules in this chapter, a *firm's* group means the *firm* and:
- (1) any *EEA parent* in the group which is a *financial holding company*, a *credit institution*, or an *investment firm*;
 - (2) any *credit institution*, *investment firm* or *financial institution* which is a *subsidiary* either of the *firm* or of the *firm's EEA parent* as defined in (1); and
 - (3) any *credit institution*, *investment firm* or *financial institution* in which the *firm* or one of the entities in (1) or (2) holds a *participation*.
- 14.2.2** **R** If a group exists under rule 14.2.1, the *firm* must also include in the scope of consolidation any *ancillary services undertaking* and *asset management company* in the group.
- 14.2.3** **G** Rule 14.1.1 states what type of *firm* may be subject to consolidated supervision (trigger firm). Rule 14.2.1 states what type of relationship triggers the existence of a group for consolidated supervision purposes. Rules 14.2.1 and 14.2.2 specify what entities should be included in the scope of consolidated supervision.
- 14.2.4** **G** (1) A *firm's parent* is a *financial holding company* if it is either a *financial institution* or a *securities and futures firm* that is subject to the financial rules in Chapter 3 and that is a *broad scope firm* (but not a *venture capital firm*) and if its *subsidiary undertakings* carry out mainly *listed activities*, activities of a *credit institution* or activities undertaken by a Chapter 3 *broad scope firm*. For this purpose the *FCA* interprets the phrases 'mainly' or 'main business' to mean where the balance of business is over 40% of the relevant group or sub-group's balance sheet (measured on the basis of total assets) or profit and loss statement (measured on the basis of gross income). In addition, if the *firm's parent* has significant holdings in *insurance undertakings* or *reinsurance undertakings*, it is a *mixed financial holding company*, and the *firm* is subject to the rules in GENPRU 3.1 instead of the rules in this chapter. This is because a *parent* cannot be a *financial holding company* and a *mixed financial holding company* at the same time. GENPRU 3.1 sets out what constitutes significant insurance holdings (broadly more than 10% of the financial sector activities of the group). A *firm's parent* is a *financial holding company* and not regarded as a *mixed financial holding company* unless:

- (a) the parent has been notified by its *coordinator* that the *group* it heads is a financial conglomerate (in accordance with Article 4(2) of the *Financial Groups Directive*); and
 - (b) it has not been notified that the *coordinator* and the relevant competent authorities have agreed not to treat the group as a *financial conglomerate* in accordance with Article 3(3) of the *Financial Groups Directive*.
- (2) A *firm* with an ultimate non-EEA parent may also be subject to the provisions in GENPRU 3.2.
- (3) In the case where undertakings are linked to the domain of consolidation by a relationship within the meaning of article 12(1) of Directive (83/349/EEC), the *FCA* will determine how consolidation is to be carried out.

Exclusions

14.2.5

R

A *firm* may, having first notified the *FCA* in writing, exclude from its group the following:

- (1) any entity the total assets of which are less than the smaller of the following two amounts:
 - (a) 10 million euros; or
 - (b) 1% of the total assets of the group's parent or the undertaking that holds the *participation*;provided that the total assets of such entities do not collectively *breach* these limits.
- (2) any entity the inclusion of which within the group would be misleading or inappropriate for the purposes of *consolidated supervision*.

14.2.6

G

- (1) The *FCA* may require a *firm* to provide information about the position in the group of any undertaking excluded from the consolidation under rule 14.2.5.
- (2) An exclusion under rule 14.2.5(2) would normally be appropriate when an entity would be excluded from the scope of consolidation under the relevant *UK* generally accepted accounting principles.



14.3 CONSOLIDATED SUPERVISION REQUIREMENT

- 14.3.1 **R** A *firm* must at all times ensure that its group maintains *group financial resources* in excess of its *group financial resources requirement*.
- 14.3.2 **R** A *firm*, other than one which is defined in rule 14.1.1(1), must at all times comply with *large exposures* limits applied on a group basis.

14.4 GROUP FINANCIAL RESOURCES

- 14.4.1** **R** A *firm* must calculate its *group financial resources* on the basis of the consolidated accounts of the relevant group, subject to the adjustments in rule 14.4.2 and on the basis specified in rule 14.4.3.
- 14.4.2** **R**
- (1) If more than one *firm* in the group is subject to the rules of this chapter, *group financial resources* are defined according to the relevant rules applicable to the main *firm* in the group to which this chapter applies, with Tier 1 minority interests being allowed as Group Tier 1 capital and Tier 2 minority interests being allowed as Group Tier 2 capital.
 - (2) In calculating the *group financial resources*, deductions should be made for intangible assets, material unaudited losses incurred since the balance sheet date and investments in own shares.
 - (3) *Material holdings* and *material insurance holdings* must be recalculated on a group basis and deducted in arriving at the *group financial resources*.
- 14.4.3** **R** Financial resources will be defined based upon the main *firm* in the group to which this chapter applies as follows:
- (1) if a *broad scope securities and futures firm* (excluding a *venture capital firm*), Table 3-61R;
 - (2) [Deleted]
 - (3) [Deleted]
 - (4) [deleted]
 - (5) [deleted]
- 14.4.4** **G**
- (1) The *FCA* interprets 'main' by reference to the share of the *firm's* business in the group, its contribution to the group's balance sheet (measured on the basis of total assets) or profit and loss statement (measured on the basis of gross income).

- (2) The form in SUP 16 Ann 19 R, together with the guidance in
 - SUP 16 Ann 20 G, shows the mechanics of the calculation.

14.4.5

G

A firm may apply for a *waiver of rule 14.4.1* to permit an aggregation approach to determine *group financial resources*. Any *waiver* application should guarantee future compliance with any relevant own funds limit.

14.5 GROUP FINANCIAL RESOURCES REQUIREMENT

14.5.1 **R** A *firm* must calculate its *group financial resources requirement* as the aggregate of:

- (1) the sum of the financial resources requirements of all group entities within the scope of consolidation calculated in accordance with rule 14.5.2, except that:
 - (a) requirements in respect of intra-group balances with other entities within the scope of consolidation should be excluded; and
 - (b) [deleted]
- (2) the sum of any adjustments that are made to each *firm's* financial resources, calculated on a solo basis in accordance with rule 14.4.3, in order to arrive at the amount of financial resources used to meet its solo financial resources requirement. These adjustments must exclude deductions in respect of the investment in and other relationships with other entities that are included within the scope of consolidation.
- (3) [deleted]

The financial resources requirements of entities in which the group holds a *participation* must be included proportionately.

14.5.2 **R** Financial resources requirements for individual entities in the group are:

- (1) for *firms* regulated by the *FCA*, their regulatory capital requirement under *FCA* rules;
- (2) for entities regulated by an *EEA regulator* and which is subject to the local regulatory capital requirement of that regulator, that local regulatory capital requirement;
- (2A) for entities that are *recognised third country credit institutions* or *recognised third country investment firms* and which is subject to the local regulatory capital requirement of that regulator, that local regulatory capital requirement;
- (2B) for entities not in (2A) that are regulated by a third country competent authority named in the table in BIPRU 8 Annex 3R and which is subject to the local regulatory capital requirement of that regulator, that local regulatory capital requirement; and

- 14.5.3 **G** (3) for other entities in the group, a notional financial resources requirement calculated as if the entity were regulated by the *FCA*.
- 14.5.3 **G** (1) For the purposes of rule 14.5.2(3) the notional financial resources requirements of group entities should normally be calculated as if the entities were subject to the financial rules in IPRU-INV relevant to the main *firm* in the group. The interpretation of 'main' given in 14.4.4 G applies here.
- (2) For the purposes of calculating an expenditure-based requirement, no account should be taken of expenses that have been recharged to another entity included in the scope of consolidation. For example, in calculating the notional requirement for a service company, the expenditure-based requirement should be calculated net of recharged expenses. This is to avoid double counting of the expenses.
- (3) [deleted]
- 14.5.4 **G** A *firm* may apply for a *waiver* of rule 14.5.1R, to permit a line-by-line approach to determine its *group financial resources requirement*. A *firm* should also demonstrate that calculating its *requirement* in this way does not result in a distortion of the *group financial resources requirement*.

14 App 1

Appendix 14(1): Interpretation

App 1 Interpretation

14App1.1 **G** Glossary of defined terms for Chapter 14

If a defined term does not appear in the IPRU(INV) 14 glossary below, the definition appearing in the main Handbook *Glossary* applies.

<i>ancillary services undertaking</i>	an undertaking the principal activity of which consists of owning or managing property, managing data-processing services, or any other similar activity which is ancillary to the principal activity of one or more of the <i>firms</i> subject to this chapter.
<i>broad scope firm</i>	as in the Glossary in IPRU(INV) chapter 3.
<i>CAD Article 5 exempting criteria</i>	the following criteria in respect of the <i>firm's</i> dealing positions: <ul style="list-style-type: none"> - such positions arise only as a result of the <i>firm's</i> failure to match investors orders precisely; - the total market value of all such positions is subject to a ceiling of 15% of the <i>firm's</i> initial capital; and - such positions are incidental and provisional in nature and strictly limited to the time required to carry out the transaction in question.
<i>contingent liability</i>	the meaning in FRS 12 which states that it is: <ul style="list-style-type: none"> (a) a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence of one or more uncertain future events not wholly within the entity's control or (b) a present obligation that arises from past events but is not recognised because: <ul style="list-style-type: none"> (i) it is not probable that a transfer of economic benefits will be required to settle the obligation; or (ii) the amount of the obligation cannot be measured with sufficient reliability.

<i>consolidated supervision</i>	the application of the financial rules in the Interim Prudential sourcebook for investment businesses in accordance with rules and guidance in 14.1.1 to 14.5.4.
<i>EEA parent</i>	a <i>firm's</i> direct or indirect <i>parent</i> which has its head office in the <i>EEA</i> .
<i>financial holding company</i>	an undertaking that satisfies the following conditions: (a) it is: (i) a <i>financial institution</i> ; or (ii) a <i>firm</i> falling within IPRU-INV rule 14.1.1(1); (b) <i>subsidiary undertakings</i> are either exclusively or mainly: (i) <i>credit institutions</i> ;; (ii) <i>investment firms</i> ; (iii) <i>broad scope firms</i> or <i>undertakings</i> carrying on activities which (if they were <i>firms</i> doing those activities in the <i>United Kingdom</i>) would make them <i>broad scope firms</i> ; and (iv) <i>financial institutions</i> , one of which at least is a <i>credit institution</i> , a <i>firm</i> falling within IPRU-INV rule 14.1.1(1) or an investment firm; and (c) it is not a <i>mixed financial holding company</i> .
<i>financial institution</i>	an undertaking other than a <i>credit institution</i> , the principal activity of which is to acquire holdings or to carry on a <i>listed activity</i> .
<i>group financial resources</i>	the resources of a <i>firm's</i> group calculated in accordance with rules 14.4 (Group financial resources).
<i>group financial resources requirement</i>	the requirement that a <i>firm's</i> group maintains financial resources calculated in accordance with the rules in 14.5 (Group financial resources requirement).
<i>investment firm</i>	<i>investment firm</i> as in the main <i>Glossary</i> except that it excludes persons to which the <i>MiFID</i> does not apply as a result of article 2 or 3 of the <i>MiFID</i> .
<i>Material holding</i>	a holding of – (a) ordinary share capital and non cumulative preference share capital; or (b) subordinated loan and non fixed-term cumulative preference share capital, in a <i>credit institution</i> or a <i>financial institution</i> where – (i) (a) or (b) above exceeds 10% of the share capital plus share premium of the issuer; or (ii) the aggregate of (a) and (b) above exceeds 10% of the <i>firm's own funds</i> , before deducting the holding.
<i>Material insurance holding</i>	the higher of – (1) the book value of an <i>investment</i> held in an insurance undertaking, reinsurance undertaking, or insurance holding company (<i>investment</i> for this purpose is either a <i>participation</i> or the <i>investment</i> in a subsidiary undertaking); or (2) the group's proportionate share of that undertaking's local or notional regulatory capital requirement."

<i>Non-trading book</i>	in relation to a <i>firm's</i> business or exposures, means any position, counterparty exposure or balance sheet item not falling within the definition of <i>trading book</i> .
<i>parent</i>	any parent undertaking as defined in section 1162 of the Companies Act 2006 and any undertaking which effectively exercises a dominant influence over another undertaking.
<i>participation</i>	a participation within the meaning of Article 17 of Directive 78/660/EEC or the ownership either direct or indirect of 20% or more of the voting rights or capital of another undertaking which is not a <i>subsidiary</i> .
<i>subsidiary</i>	as in section 1159(1) of the Companies Act 2006.
<i>trading book</i>	as in the Glossary in IPRU(INV) chapter 5.

Chapter Annex

LIMITED LIABILITY PARTNERSHIPS: ELIGIBLE MEMBERS' CAPITAL



Annex A 1 INTRODUCTION

Application

R This annex applies to any *firm* :

- (1) that is a *limited liability partnership*; and
- (2) that is a kind of *firm* to whom the provisions of this sourcebook apply.

Annex **R** In this annex, an expression in italics has the meaning given in the *Handbook Glossary*.

Annex **G**

- (1) *Firms* are reminded that a *limited liability partnership* incorporated under the Limited Liability Partnership Act 2000 is a *body corporate* with legal personality separate to that of its members and is not therefore a form of *partnership* for the purposes of this sourcebook.
- (2) A *limited liability partnership* is not a separate prudential categorisation under this sourcebook but a kind of *firm* for whom the appropriate provisions of this sourcebook are modified to the extent indicated in this annex.

Purpose

Annex **G** The purpose of this annex is to amplify *Principle 8* (Financial resources) which requires a *firm* to maintain adequate financial resources to meet its investment business commitments and to withstand the risks to which its business is subject. This annex imposes various conditions that must be satisfied for members' capital to count as "Tier 1" or equivalent grade capital in meeting the *limited liability partnership's* financial resources requirement. These conditions are made up of conditions specific to *limited liability partnerships* and general conditions based for the most part on those set out in article 57 of the *Banking Consolidation Directive*. This assists in the achievement of the *statutory objective* of consumer protection.

Annex **G** The following *rules* allow inclusion of members' capital within a *firm's* capital if it meets the conditions in this annex:

Chapter	IPRU(INV) rule	How eligible LLP members' capital should be treated for the purposes of the IPRU(-INV) rule
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3	Table 3-61	<i>Eligible LLP members' capital</i> may be counted as Tier 1 capital under item "A" within Table 3-61.
5	Table 5.2.2 (1): Item (1A)	<i>Eligible LLP members' capital</i> may be counted as Tier 1 capital within Category A of Table 5.2.2(1).
9	9.3.1	<i>Eligible LLP members' capital</i> may be counted as initial capital with IPRU-INV 9.3.1
11	Table 11.4	<i>Eligible LLP members' capital</i> may be counted as Item (5) in Table 11.4.
13	Table 13.15.3(1)13.1A.6	<i>Eligible LLP members' capital</i> may be counted as capital resources relating to companies in IPRU-INV 13.15.3(1). <i>Eligible LLP members' capital</i> may be counted as initial capital within IPRU-INV 13.1A.6.



Annex A 2 CONDITIONS FOR USE OF MEMBERS' CAPITAL

Annex	R	Members' capital of a limited liability partnership In this sourcebook, members' capital of a <i>limited liability partnership</i> may be included within a <i>firm's</i> resources if it complies with: (1) the specific conditions; and (2) the general conditions.
Annex	R	Specific conditions for eligibility The specific conditions are that: (1) members' capital is made up of the members' capital account; and (2) the members' capital account is an account: (a) into which capital contributed by the members is paid; and (b) from which under the terms of the <i>limited liability partnership</i> agreement an amount representing capital may be withdrawn by a member only if: (i) 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; (ii) the <i>limited liability partnership</i> is wound up or otherwise dissolved; or (iii) the <i>firm</i> has ceased to be <i>authorised</i> or no longer has a <i>Part 4A permission</i> .
Annex	R	General conditions for eligibility The general conditions in respect of the <i>members'</i> capital are that: (1) it is fully paid and the proceeds are immediately and fully available to the <i>firm</i> ; (2) it is not capable of being redeemed at all (otherwise than in the circumstances set out in the specific conditions) or can only be redeemed on a winding up of the <i>firm</i> ; (3) any <i>coupon</i> is non-cumulative;

- (4) it is able to absorb losses to allow the *firm* to continue trading;
- (5) the amount of the item included is net of any foreseeable tax *charge*;
- (6) it is available to the *firm* for unrestricted and immediate use to cover risks and losses as soon as they occur;
- (7) it ranks for repayment on a winding up of the *firm* no higher than a *share* of a company incorporated under the Companies Act 2006 (whether or not it is such a share); and
- (8) the *firm* is under no obligation to pay a *coupon* on it at any time.

Surplus eligible LLP members' capital

Annex

G

If a *firm* has surplus *eligible LLP members' capital* that it wishes to repay in circumstances otherwise than those in the specific conditions, 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 to support the application might include:

- (1) a demonstration that the *firm* would have sufficient financial resources to meet its financial resources requirement immediately after the repayment; and
- (2) 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.

Limited liability partnership excess drawings

Annex

R

A *firm* which is a *limited liability partnership* must in calculating its Tier 1 or equivalent grade capital in accordance with the requirements of any chapter of this sourcebook deduct the amount by which the aggregate of the amounts withdrawn by its members exceeds the profits of that *firm* ("*excess LLP members' drawings*"). Amounts of *eligible LLP members' capital* repaid in accordance with the specific conditions are not to be included in this calculation.

IPRU-INV Annex D



Annex D Required Forms

[Click here to view the provisions of IPRU-INV Annex D](#)

Interim Prudential sourcebook for Investment Businesses

IPRU-INV TP 1

Table: Transitional provisions applying to IPRU(INV)

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
1			[Deleted:	[Deleted:	[Deleted:
2			[Deleted]	[Deleted]	[Deleted]
3	IPRU-INV 9.2.5R and IPRU-INV 13.1.4(2)R (b)	R	The new limits of indemnity apply to a professional indemnity policy or a comparable guarantee commenced, renewed or extended with effect from or after 1 March 2009. Any other existing non-annual arrangements must be aligned with the new limits of indemnity before 1 March 2010	1 March 2009 to 28 February 2010	1 March 2009
4	13.1.21 and 13.1.23	R	The requirement to hold additional capital resources where a policy excludes business or activities that have been carried out by the <i>firm</i> in the past or will be carried out by the <i>firm</i> only apply to a <i>professional indemnity policy</i> taken out, renewed or extended with effect from 31 December 2009.	31 December 2009 to 31 December 2010	31 December 2009
5	IPRU-INV 11	R	[Deleted] [expired]		
6	The changes to <i>IPRU-INV</i> in Annex J of the Alternative Investment Fund Managers Directive Instrument 2013 and An-	R	[Deleted] [expired]		

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
7	Annex C of the Capital Requirements Directive IV (AIFMD and UCITS Consequential Amendments) Instrument 2013 IPRU-INV 11	R	Where a <i>firm</i> falls within regulation 74(1) or 75(1) of the <i>AIFMD UK regulation</i> it need not include <i>AIFs</i> managed by it that fall within those regulations in the calculation of its <i>funds under management requirement</i> , <i>professional negligence capital requirement</i> or <i>PII excess capital requirement</i> .	From 22 July 2013	22 July 2013
8	[spent]	[spent]	[spent]	[spent]	[spent]
9	[spent]	[spent]	[spent]	[spent]	[spent]
10	IPRU(INV) 12	R	IPRU(INV) 12 does not apply to a <i>firm</i> with an <i>interim permission</i>	Indefinitely	1 April 2014
11	IPRU(INV) 12.2.6R(1)	R	The amount is replaced with £20,000	From 1 April 2014 to 31 March 2017 From	1 April 2014
12	IPRU(INV) 12.3.5R	R	b = items 1,4 and 5 in the Table of items which must be deducted in arriving at a <i>firm's financial resources</i> (see IPRU(INV) 12.3.3R)	1 April 2014 to 31 March 2017	1 April 2014
13	IPRU-INV 13.1A.3R(2)	R	A <i>firm</i> applying (b) or (c) above must have <i>initial capital</i> of at least £15,000.	From 30 June 2016 to 29 June 2017	30 June 2016
14	IPRU-INV 13.1A.4R(2)	R	A <i>firm</i> applying (b) or (c) above must have <i>initial capital</i> of at least £15,000.	From 30 June 2016 to 29 June 2017	30 June 2016

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
15	IPRU-INV 13.13.2R(2)(a)	R	The <i>firm</i> must calculate its capital resources requirement as the higher of: (a) £15,000.	From 30 June 2016 to 29 June 2017	30 June 2016
16	IPRU-INV 13.13.3R(2)(a)	R	The <i>firm</i> must calculate its capital resources requirement as the higher of: (a) £15,000.	From 30 June 2016 to 29 June 2017	30 June 2016
17	IPRU-INV 13.15.9R and IPRU-INV 13.15.10R	R	These <i>rules</i> do not apply to a <i>category B3 firm</i> which is not a <i>network</i> , has fewer than 26 <i>financial advisers</i> or <i>representatives</i> and is not permitted to: (a) carry on discretionary portfolio management; (b) <i>establish, operate or wind up a personal pension scheme</i> ; or (c) delegate the activities in (a) or (b) to an <i>investment firm</i> .	From 30 June 2016 to 29 June 2017	30 June 2016
18	IPRU(INV) 5.4.3R(i)(ib)	R	A <i>depository</i> of a <i>UCITS scheme</i> appointed before 18 March 2016 need not calculate its <i>own funds requirement</i> under articles 315 or 317 of the <i>EU CRR</i> .	From 18 March 2016 until 18 March 2018	18 March 2016
19	IPRU(INV) 5.4.8R	R	A <i>depository</i> of a <i>UCITS scheme</i> appointed before 18 March 2016 need not comply with IPRU(INV) 5.4.8R.	From 18 March 2016 to 18 March 2018	18 March 2016

