CAPITAL REQUIREMENTS DIRECTIVE IV (CAPITAL BUFFERS) INSTRUMENT 2014

Powers exercised

A. The Financial Conduct Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137A (The FCA's general rules);
(2) section 137T (General supplementary powers);
(3) section 138D (Actions for damages); and
(4) section 139A (Power of the FCA to give guidance).

B. The rule-making powers listed above are specified for the purpose of section 138G(2) (Rule-making instruments) of the Act.

Commencement

C. This instrument comes into force as follows:

(1) Part 2 of Annex A comes into force on 1 January 2016.

(2) IFPRU 10.2 and IFPRU TP 7 in Annex B come into force on 1 January 2016.

(3) The remainder of this instrument comes into force on 1 May 2014.

Amendments to the FCA Handbook

D. The Glossary of definitions is amended in accordance with Annex A to this instrument.

E. The Prudential sourcebook for Investment Firms (IFPRU) is amended in accordance with Annex B to this instrument.

Citation

F. This instrument may be cited as the Capital Requirements Directive IV (Capital Buffers) Instrument 2014.

Notes

G. In the Annexes to this instrument, the "notes" (indicated by **"Note:"**) are included for the convenience of readers but do not form part of the legislative text.

By order of the Board of the Financial Conduct Authority
27 March 2014

Annex A

Amendments to the Glossary of definitions

Insert the following new definitions in the appropriate alphabetical position. The text is not underlined.

Part 1: Comes into force on 1 May 2014

countercyclical capital buffer	(in accordance with article 128(2) of *CRD* (Definitions)) the amount of *common equity tier 1 capital* a *firm* must calculate in line with *IFPRU* 10.3.
countercyclical buffer rate	(in accordance with article 128(7) of the *CRD* (Definitions)) the rate: (a) expressed as a percentage of *total risk exposure amount* set by the *UK countercyclical buffer authority* or an *EEA countercyclical buffer authority*; or (b) expressed in terms equivalent to a percentage of total risk exposure amount set by a *third country countercyclical buffer authority*, that a *firm* must apply in order to calculate its *countercyclical capital buffer*.
distribution in connection with common equity tier 1 capital	(in accordance with article 141(10) of CRD) includes: (a) a payment of cash dividends; (b) a distribution of fully or partly paid bonus *shares* or other capital instruments referred to in article 26(1)(a) of the *EU CRR* (Common equity tier 1 items); (c) a redemption or purchase by a *firm* of its own *shares* or other capital instruments referred to in article 26(1)(a) of the *EU CRR* (Common equity tier 1 items); (d) a repayment of amounts paid in connection with capital instruments referred to in article 26(1)(a) of the *EU CRR* (Common equity tier 1 items); and (e) a distribution of items referred to in article 26(1)(b) to (e) of the *EU CRR* (Common equity tier 1 items).
EEA countercyclical buffer authority	(1) the authority or body of a *EEA State*, other than the *UK*, designated for the purpose of article 136 of *CRD* with

	responsibility for setting the *countercyclical buffer rate* for that *EEA State*; or
	(2) the European Central Bank when it carries out the task of setting a countercyclical buffer rate for an *EEA State* conferred on it by article 5(2) of Council Regulation (EU) No. 1024/2013, conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions.
MDA	the maximum distributable amount calculated in line with *IFPRU* 10.4.3R.
relevant credit exposures	(in accordance with article 140(4) of CRD) exposures, other than those referred to in article 112(a) to (f) of the *EU CRR* (Exposure classes), that are subject to:
	(a) the *own funds requirements* for credit risk under Part Three, Title II of the *EU CRR*;
	(b) where the *exposure* is held in the *trading book*, *own funds requirements* for specific risk under Part Three, Title IV, Chapter 5 of the *EU CRR*; or
	(c) where the *exposure* is a *securitisation*, the *own funds requirements* under Part Three, Title II, Chapter 5 of the *EU CRR*.
third-country countercyclical buffer authority	the authority of a *third country* empowered by law or regulation with responsibility for setting the *countercyclical buffer rate* for that *third country*.
total risk exposure amount	the total risk exposure amount of a *firm* calculated in accordance with article 92(3) of the *EU CRR* (Own funds requirements).
UK countercyclical buffer authority	the Bank of England, designated for the purpose of article 136(1) of the *CRD* in article 7 of The Capital Requirements (Capital Buffers and Macro-prudential Measures) Regulations 2014.

Part 2: Comes into force on 1 January 2016

capital conservation buffer	(in accordance with article 128(1) of *CRD* (Definitions)) the amount of *common equity tier 1 capital* a *firm* must calculate in line with *IFPRU* 10.2.
combined buffer	the sum of:
	(1) the *capital conservation buffer*; and

(2) the *countercyclical capital buffer*.

Annex B

Prudential sourcebook for Investment Firms (IFPRU)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

1 Application

1.1 Application and Purpose

Application

1.1.1 G There is no overall application for *IFPRU*. Each chapter or section has its own application statement. However, *IFPRU* broadly applies in the following manner:

(1) only *IFPRU* 7 (Liquidity) and *IFPRU* 10 (Public disclosure) apply to an *exempt IFPRU commodities firm* and *IFPRU* 8.1 (Prudential consolidation) may apply subject to the conditions in that section; ~~and~~

(1A) *IFPRU* 10 (Capital buffers) applies to an *IFPRU investment firm*, unless it is an:

(a) *exempt IFPRU commodities firm*; or

(b) *IFPRU limited-licence firm*; and

(2) other than in (1) and (1A), the whole of *IFPRU* applies to an *IFPRU investment firm*.

Insert IFPRU 10 after IFPRU 9. The text is all new and is not underlined.

10 Capital buffers

10.1 Application

10.1.1 R *IFPRU* 10 applies to an *IFPRU investment firm*, unless it is one of the following:

(1) an *IFPRU limited-licence firm*; or

(2) an *exempt IFPRU commodities firm*.

Purpose

10.1.2 G This chapter implements articles 129 (part), 130 (part), 140 (part), 141, 142 (part) of *CRD*.

10.2 Capital conservation buffer

10.2.1 R A *firm* must calculate a *capital conservation buffer* of *common equity tier 1 capital* equal to 2.5% of its *total risk exposure amount*.

[**Note**: article 129(1) (part) of *CRD*]

10.3 Countercyclical capital buffer

Main requirement

10.3.1 R A *firm* must calculate a *countercyclical capital buffer* of *common equity tier 1 capital* equal to its *total risk exposure amount* multiplied by the weighted average of the *countercyclical buffer rates* that apply to exposures in the jurisdictions where the *firm's relevant credit exposures* are located.

[**Note**: article 130(1) (part) of *CRD*]

Calculation of countercyclical capital buffer rates

10.3.2 R (1) To calculate the weighted average in *IFPRU* 10.3.1R, a *firm* must apply to each applicable *countercyclical buffer rate* its total *own funds requirements* for credit risk, specific risk, incremental default and migration risk that relates to *the relevant credit exposures* in the jurisdiction in question, divided by its total *own funds requirements* for credit risk that relates to all of its *relevant credit exposures*.

(2) For the purposes of (1), a *firm* must calculate its total *own funds requiremen*t for credit risk, specific risk, incremental default and migration risk in accordance with Part Three, Titles II (Capital requirements for credit risk) and IV (Own funds requirements for market risk) of the *EU CRR.*

(3) The *countercyclical buffer rate* for an exposure located in the *UK* is the rate set by the *UK countercyclical buffer authority* for the *UK.*

(4) The *countercyclical buffer rate* for an exposure located in an *EEA State* other than the *UK* is:

(a) the rate set by the *EEA countercyclical buffer authority* for that jurisdiction; or

(b) if that rate exceeds 2.5% of *total risk exposure amount* and has not been recognised by the *UK countercyclical buffer authority*, 2.5%

(5) The *countercyclical buffer rate* for an exposure located in a *third country* is the rate set by the *UK countercyclical buffer authority* for that jurisdiction.

(6) If the *UK countercyclical buffer authority* has not set a rate for a *third country*, *the countercyclical buffer rate* for an exposure located in that jurisdiction is:

(a) the rate set by the *third country countercyclical buffer authority* for that jurisdiction; or

(b) if that rate exceeds 2.5% and has not been recognised by the *UK countercyclical buffer authority*, 2.5%.

(7) If the *UK countercyclical buffer authority* has not set a rate for a *third country* and either there is no *third-country countercyclical buffer authorit*y for that country or the authority has not set a rate for that jurisdiction, the *countercyclical buffer rate* for an exposure located in that jurisdiction is zero.

(8) If the *countercyclical buffer rate* for the *UK* is increased, that increase takes effect from the date specified by the *UK countercyclical buffer authority*.

(9) If the *countercyclical buffer rate* for an *EEA State* other than the *UK* is increased, subject to (4)(b), that increase takes effect from:

(a) the date specified by the *EEA countercyclical buffer authority* for that jurisdiction, if the rate applied under this chapter does not exceed 2.5%; or

(b) the date specified by the *UK countercyclical buffer authority* if the rate applied under this chapter exceeds 2.5%.

(10) If the *countercyclical buffer rate* for a *third country* is increased by the *UK countercyclical buffer authority*, that increase takes effect from the date specified by the *UK countercyclical buffer authority*.

(11) If the *UK countercyclical buffer authority* does not set a *countercyclical buffer rate* for a *third country* and that rate is increased by the *third-country countercyclical buffer authority* for that jurisdiction, subject to 6(b), that increase takes effect from:

(a) the date 12 months after the date on which the increase was published by the *third-country countercyclical buffer authority* in accordance with the relevant law of the *third country*, if the rate applied under this chapter does not exceed 2.5%; or

(b) the date specified by the *UK countercyclical buffer authority* if the rate applied under this chapter exceeds 2.5%.

(12) If a *countercyclical buffer rate* is reduced, that reduction takes effect immediately.

[**Note**: articles 136(4) (part) , 139(2) to (5) (part) and 140(1) to (4) and (6) (part) of *CRD*]

Location of exposures

10.3.3 G A *firm* must identify the geographical location of a *relevant credit exposure* in accordance with the regulatory technical standards adopted under article 140(7) of *CRD*.

[**Note**: article 140(5) of *CRD*]

10.4 Capital conservation measures

Combined buffer

10.4.1 R A *firm* does not meet the *combined buffer* if the *common equity tier 1 capital* maintained by the *firm* which is not used to meet the *own funds requirement* under article 92(1)(c) of the *EU CRR* (Total capital ratio) does not meet the *combined buffer*.

[**Note:** articles 129(1) (part) and 130(5) (part) of *CRD*]

Restrictions on distributions

10.4.2 R A *firm* that meets the *combined buffer* must not make a *distribution in connection with common equity tier 1 capital* to an extent that would decrease its *common equity tier 1 capital* to a level where the *combined buffer* is no longer met.

[**Note:** article 141(1) of *CRD*]

10.4.3 R (1) A *firm* that does not meet the *combined buffer* must:

(a) calculate the *MDA* in accordance with (4); and

(b) report the *MDA* to the *FCA* in writing no later than five *business days* after the *firm* identified that it did not meet the *combined buffer*.

(2) A *firm* that does not meet the *combined buffer* must not undertake any of the following actions before it has calculated the *MDA*:

(a) make a *distribution in connection with common equity tier 1 capital*;

(b) create an obligation to pay variable remuneration or *discretionary pension benefits* or pay variable remuneration or *discretionary pension benefits* if the obligation to pay was created at a time when the *firm* did not meet the *combined buffer*; and

(c) make payments on *additional tier 1 instruments*.

(3) If a *firm* does not meet the *combined buffer*, it must not distribute more than the *MDA*, calculated in (4), through any action in (2)(a) to (c).

(4) (a) A *firm* must calculate the *MDA* by multiplying the sum calculated in (5) by the factor determined in (6).

(b) Any of the actions in (2)(a), (b) or (c) shall have the effect of reducing the *MDA.*

(5) The sum to be multiplied in (4) shall consist of:

(a) interim profits not included in *common equity tier 1 capital* under article 26(2) of the *EU CRR* (Common equity tier 1 items) that have been generated since the most recent decision on the distribution of profits or any of the actions in 2(a), (b) or (c);

Plus

(b) year-end profits not included in *common equity tier 1 capital* under article 26(2) of the *EU CRR* that have been generated since the most recent decision on the distribution of profits or any of the actions in (2) (a), (b) or (c);

Minus

(c) amounts which would be payable by tax if the items specified in (a) and (b) were to be retained.

(6) The factor in (4) shall be determined as follows:

(a) if the *common equity tier 1 capital* maintained by the *firm* which is not used to meet the *own funds requirement* under article 92(1)(c) of the *EU CRR* expressed as a percentage of the *firm's total risk exposure amount* is within the first (ie, the lowest) quartile of the *combined buffer*, the factor shall be 0;

(b) if the *common equity tier 1 capital* maintained by the *firm* which is not used to meet the *own funds* requirement under article 92(1)(c) of the *EU CRR*, expressed as a percentage of the *firm's total risk exposure amount* is within the second quartile of the *combined buffer*, the factor shall be 0.2;

(c) if the *common equity tier 1 capital* maintained by the *firm* which is not used to meet the *own funds* requirement under article 92(1)(c) of the *EU CRR* expressed as a percentage of the *firm's total risk exposure amount* is within the third quartile of the *combined buffer*, the factor shall be 0.4;

(d) if the *common equity tier 1 capital* maintained by the *firm* which is not used to meet the *own funds* requirement under article 92(1)(c) of the *EU CRR* expressed as a percentage of the *firm's total risk exposure amount* is within the fourth (ie, the highest) quartile of the *combined buffer*, the factor shall be 0.6.

(7) A *firm* must calculate the lower and upper bounds of each quartile of the *combined buffer* as follows:

$$\text{Lower bound of quartile} = \frac{\textit{Combined buffer}}{4} \times (Q_n - 1)$$

$$\text{Upper bound of quartile} = \frac{\textit{Combined buffer}}{4} \times Q_n$$

"Q_n" indicates the ordinal number of the quartile concerned.

(8) The restrictions imposed by this *rule* only apply to payments that result in a reduction of *common equity tier 1 capital* or in a reduction of profits, and where a suspension of payment or failure to pay does not constitute an event of default or a condition for the commencement of proceedings for an order for the appointment of a liquidator or administrator of the *firm*.

(9) If a *firm* does not meet the *combined buffer* and intends to distribute any of its distributable profits or undertake an action in (2)(a), (b) and (c), it must give the *FCA* not less than one *month's* notice before the intended date of distribution or action. When giving notice a *firm* must provide the following information:

(a) the amount of *own funds* maintained by the *firm*, subdivided as follows:

(i) *common equity tier 1 capital*;

(ii) *additional tier 1 capital*; and

(iii) *tier 2 capital*;

(b) the amount of its interim and year-end profits;

(c) the *MDA* calculated in (4);

(d) the amount of distributable profits it intends to allocate between the following:

(i) dividend payments;

(ii) share buybacks;

(iii) payments on *additional tier 1 instruments*; and

(iv) the payment of variable remuneration or *discretionary pension benefits*, whether by creation of a new obligation to pay, or payment pursuant to an obligation to pay created at a time when the *firm* did not meet its *combined buffer*.

[**Note**: article 141(2) to (9) of *CRD*]

10.5 Capital conservation plan

10.5.1 R When a *firm* does not meet the *combined buffer*, it must prepare a capital conservation plan and submit it to *FCA* no later than five *business days* after the *firm* identified that it did not meet the *combined buffer*.

[**Note**: article 142(1) of *CRD*]

10.5.2 R The capital conservation plan must include the following

(1) the *MDA*;

(2) estimates of income and expenditure and a forecast balance sheet;

(3) measures to increase the capital ratios of the *firm*; and

(4) a plan and timeframe for the increase of *own funds* with the objective of meeting the *combined buffer*.

[**Note**: article 142(2) of *CRD*].

10.6 Application on an individual and consolidated basis

Application on an individual basis

10.6.1 R This chapter applies to a *firm* on an individual basis, whether or not it also applies to the *firm* on a *consolidated basis* or *sub-consolidated basis*.

Application on a consolidated basis

10.6.2 R A *firm* that is a *parent institution in a Member State* must comply with this chapter on the basis of its *consolidated situation*.

10.6.3 R A *firm* controlled by a *parent financial holding company in a Member State* or a *parent mixed financial holding company in a Member State* must comply with this chapter on the basis of the *consolidated situation* of that holding company in the *FCA consolidation group*.

Sub-consolidation of entities in third countries

10.6.4 R A *firm* that is a *subsidiary* must apply this chapter on a *sub-consolidated basis* if the *firm*, or the *parent undertaking* where it is a *financial holding company* or *mixed financial holding company*, have an *institution* or *financial institution* as a *subsidiary* in a *third country* or hold a *participation* in such an *institution* or *financial institution*.

[**Note**: articles 129(1) (part) and 130(1) (part) of *CRD*]

Extent and manner of prudential consolidation

10.6.5 G If this chapter applies to a *firm* on a *consolidated basis* on a *sub-consolidated basis*, the *firm* must carry out consolidation to the extent and in the manner prescribed in Part One, Title II, Chapter 2, Section 2 (Methods for prudential consolidation) and Section 3 (Scope of prudential consolidation) of the *EU CRR* and *IFPRU* 8.1 (Prudential consolidation).

10.7 Exemption

10.7.1 R This chapter does not apply to a *firm* that meets the condition in *IFPRU* 10.7.2R.

[**Note**: articles 129(2) (part) and 130(2) (part) of *CRD*]

10.7.2 R (1) The condition referred to in *IFPRU* 10.7.1R is that the *firm* is a small and medium-sized *investment firm.*

(2) For this purpose, a *firm* is categorised as small and medium-sized in accordance with the European Commission Recommendation 2003/361/EC concerning the definition of micro, small and medium-sized enterprises.

[**Note**: articles 129(4) and 130(4) of *CRD*]

Insert IFPRU TP 7 and IFPRU TP 8 after IFPRU TP 6. The text is all new and is not underlined.

TP 7 Capital conservation buffer: transitional

	Application			
7.1	R	*IFPRU* TP 7 applies to an *IFPRU investment firm*, unless it is an *IFPRU limited-licence firm* or *exempt IFPRU commodities firm*.		
	Purpose			
7.2	G	This section implements article 160 of *CRD* in relation to the *capital conservation buffer*. The amounts of the *capital conservation buffer* in *IFPRU* TP 7 apply instead of the amount of the *capital conservation buffer* in *IFPRU* 10.2.1R (Main requirement) for the duration of the transitional.		
	Duration of transitional			
7.3	R	*IFPRU* TP 7 applies with effect from 1 January 2016 (which is the date that *IFPRU* 10.2 (Capital conservation buffer) comes into effect) until 31 December 2018.		
	Modified main requirement			
7.4	R	This *rule* modifies *IFPRU* 10.2.1R (Main requirement) in the following manner:		
		(1)	from 1 January 2016 until 31 December 2016, the *capital conservation buffer* is the amount of *common equity tier 1 capital* equal to 0.625% of a *firm's total risk exposure amount*;	
		(2)	from 1 January 2017 until 31 December 2017, the *capital conservation buffer* is the amount of *common equity tier 1 capital* equal to 1.25% of a *firm's total risk exposure amount*; and	
		(3)	from 1 January 2018 until 31 December 2018, the *capital conservation buffer* is the amount of *common equity tier 1 capital* equal to 1.875% of a *firm's total risk exposure amount*.	

TP 8 Countercyclical capital buffer: transitional

	Application	
8.1	R	*IFPRU* TP 8 applies to an *IFPRU investment firm*, unless it is an *IFPRU limited-licence firm* or *exempt IFPRU commodities firm*.
	Purpose	

8.2	G	This section implements article 160(6) of *CRD* in relation to the *countercyclical capital buffer*. *IFPRU* TP 8 applies instead of *IFPRU* 10.3 and modifies *IFPRU* 10.4 and *IFPRU* 10.5 for the duration of the transitional.
	Duration of transitional	
8.3	R	*IFPRU* TP 8 applies until 31 December 2015.
	Modified main requirement	
8.4	R	A *firm* must calculate a *countercyclical capital buffer* of *common equity tier 1 capital* equal to its *total risk exposure amount* multiplied by the weighted average of the *countercyclical buffer rates* that apply in the jurisdictions where the *firm's relevant credit exposures* are located.
8.5	R	To calculate the weighted average referred to in *IFPRU* TP 8.4R, a *firm* must apply to each applicable *countercyclical buffer rate* its total *own funds requirements* for credit risk, specific risk, incremental default and migration risk that relates to the *relevant credit exposures* in the jurisdiction in question, divided by its total *own funds requirements* for credit risk that relates to all its *relevant credit exposures*.
8.6	R	For the purpose of *IFPRU* TP 8.5R, a *firm* must calculate its total *own funds requirements* for credit risk, specific risk, the incremental default and migration risk in line with Part Three, Titles II (Capital requirements for credit risk) and IV (Own funds requirements for market risk) of the *EU CRR*.
	Modified calculation of countercyclical buffer rates	
8.7	R	The *countercyclical buffer rate* for an exposure is the rate set by the *UK countercyclical buffer authority* for the jurisdiction in which that exposure is located.
8.8	R	If the *UK countercyclical buffer authority* does not set a rate for the jurisdiction in which an exposure is located, the *countercyclical buffer rate* for that exposure is zero.
8.9	R	If the rate for a jurisdiction is increased by the *UK countercyclical buffer authority*, that increase takes effect from the date specified by the *UK countercyclical buffer authority*.
8.10	R	If a rate is reduced, that reduction takes place immediately.
	Modified combined buffer requirement	
8.11	R	For the purposes of the following provisions, the expression "*combined buffer*" means the *countercyclical capital buffer*:

		(1)	*IFPRU* 10.4 (Capital conservation measures); and
		(2)	*IFPRU* 10.5 (Capital conservation plan).

…

Sch 2G Notification and reporting requirements

Handbook reference	Matter to be notified	Contents of notification	Trigger event	Time allowed
…	…	…	…	…
IFPRU 8.2.5R(6)	…	…	…	…
IFPRU 10.4.3R(2)	Failure to meet the *combined buffer*	Failure to meet the *combined buffer*	Failure to meet the *combined buffer*	No later than five *business days* from when it identified its failure
IFPRU 10.4.3R(9)	Intention to distribute any distributable profits or undertake any action under *IFPRU* 10.4.3R(2)	Matters described in *IFPRU* 10.4.3R(9)(a) to (d)	Intention to distribute any distributable profits or undertake any of the specified action	Not less than one *month* before intended date of distribution or action
IFPRU 10.5.2R	Capital conservation plan	Capital conservation plan	Failure to meet the *combined buffer*	No later than five *business days* from when it identified its failure