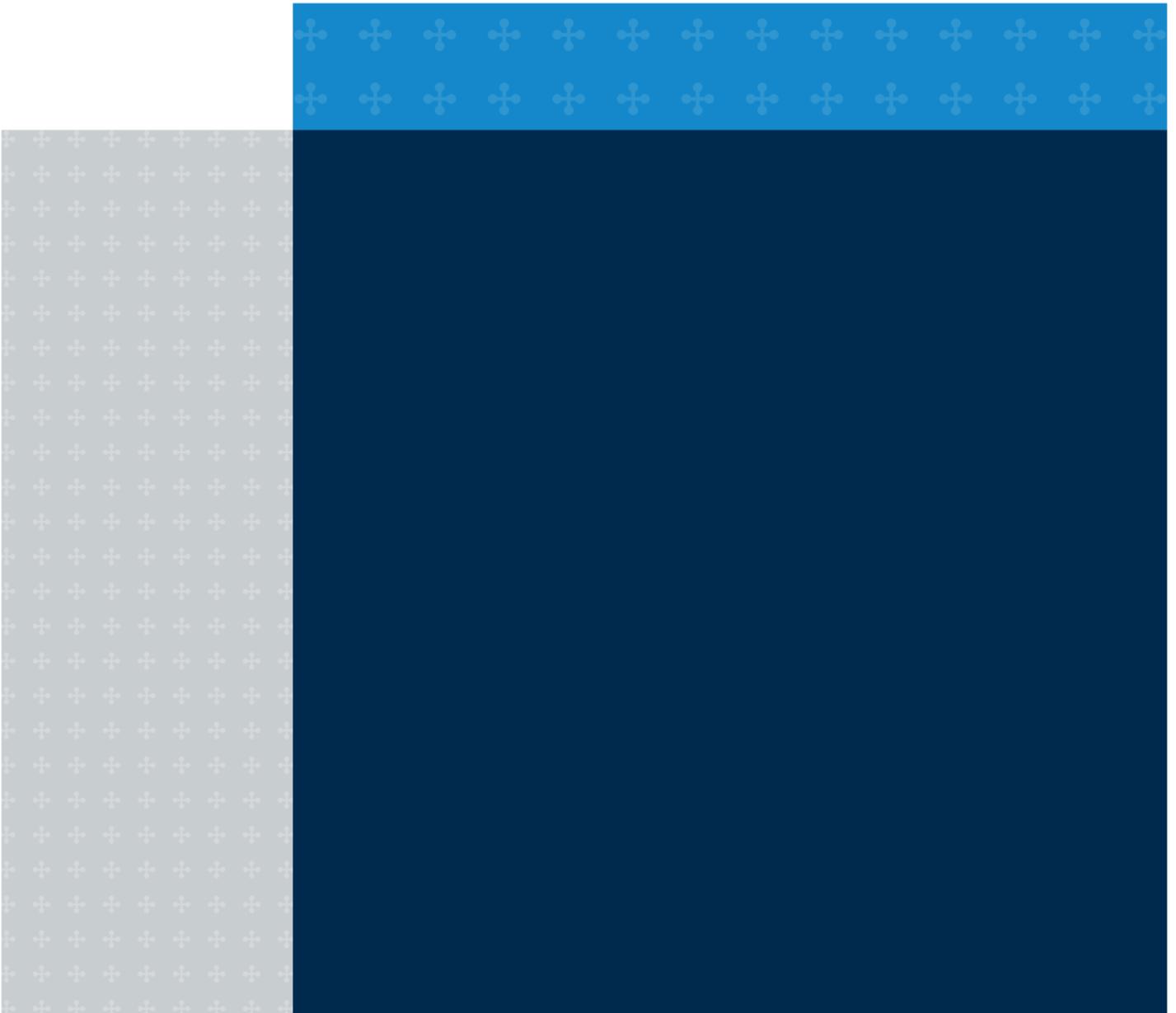




Policy Statement | PS17/21

Implementation of Basel standards

July 2021





BANK OF ENGLAND
PRUDENTIAL REGULATION
AUTHORITY

Policy Statement | PS17/21

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1 Overview

1.1 This Prudential Regulation Authority (PRA) Policy Statement (PS) provides feedback to responses to Consultation Paper (CP) 5/21 'Implementation of Basel standards'.¹ It also contains near-final rule instruments, Statements of Policy (SoP), Supervisory Statements (SS), and reporting templates and instructions.

1.2 Before making any proposed rules, the PRA is required by the Financial Services and Markets Act 2000 (FSMA) to have regard to any representations made to it, and to publish an account, in general terms, of those representations and its feedback to them.²

1.3 The chapters in this PS follow the same chapter structure as the CP.

1.4 The policy material being updated in this PS is published as near-final. The PRA has not made the rule instruments at this stage because HM Treasury must first revoke the relevant parts of the CRR,³ as provided for in the Financial Services Act 2021 (FS Act), before the PRA can replace them in PRA rules.⁴

1.5 The appendices to this PS contain the near-final policy material, as set out in the table below.

Appendix	Near-final updated policy material	Relevant PS chapters
Appendix 1	CRR RULES INSTRUMENT 2021	All chapters
Appendix 2	CRR FIRMS: (CRR 2 REVOCATIONS AND OTHER AMENDMENTS) INSTRUMENT 2021	All chapters
Appendix 3	SS15/13 'Groups'	Levels of application (Chapter 5)
Appendix 4	SS12/13 'Counterparty credit risk'	Counterparty credit risk (Chapter 9)
Appendix 5	SoP 'The PRA's methodologies for setting Pillar 2 capital'	Counterparty credit risk (Chapter 9)
Appendix 6	SS16/13 'Large Exposures'	Large Exposures (Chapter 11)
Appendix 7	SoP 'Liquidity and funding permissions'	<ul style="list-style-type: none"> • Levels of application (Chapter 5) • Liquid Coverage Ratio (Chapter 12) • Net stable funding ratio (Chapter 13)
Appendix 8	SS24/15 'The PRA's approach to supervising liquidity and funding risks'	Net stable funding ratio (Chapter 13)
Appendix 9	SS34/15 'Guidelines for completing regulatory reports'	Reporting (Chapter 14)
Appendix 10	SS2/19 'PRA approach to interpreting reporting and disclosure requirements and regulatory transactions forms after the UK's	Disclosure (Chapter 15)

¹ February 2021: <https://www.bankofengland.co.uk/prudential-regulation/publication/2021/february/implementation-of-basel-standards>.

² Sections 138J(3) and 138J(4) of FSMA.

³ The onshored and amended UK version of Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 is referred to as the 'CRR' in this PS.

⁴ This is a result of HM Treasury using its powers under section 3(3) and 3(5) of the FS Act (see section 144A(4)(b) of FSMA).

Appendix	Near-final updated policy material	Relevant PS chapters
	withdrawal from the EU'	
Appendix 11	SoP 'Interpretation of EU Guidelines and Recommendations: Bank of England and PRA approach after the UK's withdrawal from the EU'	Disclosure (Chapter 15)
Appendix 12	Detailed analysis of objectives and have regards	All chapters
Appendix 13	Summary of the purpose of the rules	All chapters
Appendix 14	Corresponding provisions	All chapters
Appendix 15	Restatement provisions	All chapters
Appendix 16	Updated reporting data items and instructions: <ul style="list-style-type: none"> • PRA101–PRA108; • RFB001, RFB003, and RFB004; and • Annex I–XXIX: UK COREP and FINREP data items and instructions. 	Reporting (Chapter 14)
Appendix 17	Updated UK Pillar 3 disclosure data items and instructions	Disclosure (Chapter 15)
Appendix 18	SS6/17 'Compliance with the EBA's Guidelines on disclosure' - This SS would be repealed at the policy implementation date should policy become final.	Disclosure (Chapter 15)

1.6 This PS is relevant to UK banks, building societies, and PRA-designated investment firms (collectively 'firms'), as well as UK financial holding companies (FHCs) and UK mixed financial holding companies (MFHCs) of certain PRA-authorized firms.

Background

1.7 The Basel III framework is a central element of the Basel Committee on Banking Supervision's (BCBS) response to the financial crisis.⁵ In CP5/21, the PRA proposed new requirements to implement some of the remaining Basel III standards in the UK. The PRA also proposed to make rules that restate elements of the CRR and related onshored EU level 2 regulations made under the CRR (CRR Level 2 Regulations), that are being revoked by HM Treasury. The proposals in CP5/21 included:

- specification of the level and scope of application of the requirements for UK firms;
- revision to the definition of capital, in particular for the treatment of Common Equity Tier 1 (CET1) deductions for software assets and certain collective investment undertakings (CIUs);
- revised Basel standards for prudent valuation for market risk and amendments to market risk management requirements;
- revised Basel standards for calculating risk-weighted exposures to CIUs under the standardised approach, and application of a more prudent treatment of exposures to certain CIUs located and managed in third countries;

⁵ Basel III: international regulatory framework for banks: <https://www.bis.org/bcbs/basel3.htm>.

- a new Basel standardised approach to counterparty credit risk (SA-CCR) and the revised Basel framework for exposures to central counterparties (CCPs);
- clarification of the treatment of operating leases under the basic indicator approach (BIA) for operational risk;
- implementation of the Basel III standards revised large exposures framework;
- implementation of Basel III standards liquidity coverage ratio (LCR);
- Basel III standards for the net stable funding ratio (NSFR), which would help ensure stable funding structures over a longer-term horizon;
- an update to supervisory reporting;
- revised Basel disclosure standards, which would help enhance the comparability, quality, and consistency of institutions' regulatory disclosures;
- the currency in which requirements would be set;
- the interaction between the temporary transitional power (TTP) and CRR rules; and
- enhanced proportionality for smaller firms, including:
 - revised counterparty credit risk requirements, including a simpler, more conservative SA-CCR approach (the simplified SA-CCR or sSA-CCR) for certain smaller firms, and amendments to the original exposures method (OEM);
 - a simpler, more conservative NSFR (the simplified NSFR, or sNSFR) that certain smaller firms could choose to use;
 - updates to the simplified capital requirements calculation for credit valuation adjustment risk;
 - increasing the scope of more proportionate market risk capital requirements and exemptions from new market risk reporting requirements; and
 - tailored disclosure requirements.

1.8 The near-final policy material broadly corresponds with the set of issues covered by the EU's Capital Requirements Regulation 2 (EU CRR II),⁶ which implements the same set of remaining Basel III standards.

Summary of responses

1.9 The PRA received 20 written responses to CP5/21, in addition to comments received in a number of meetings with interested stakeholders. Respondents generally welcomed the PRA's proposals to implement the remaining parts of the Basel III standards. However, respondents also

⁶ Regulation (EU) 2019/876 of the European Parliament and of the Council of 20 May 2019 amending CRR as regards the leverage ratio, the NSFR, requirements for own funds and eligible liabilities, counterparty credit risk, market risk, exposures to central counterparties, exposures to CIU, large exposures, reporting and disclosure requirements, and Regulation (EU) No 648/2012. The EU CRR II entered into force on the 28 June 2019, but the majority of its provisions apply in the EU from 28 June 2021.

sought additional clarification on the PRA's general approach, provided general comments on the proposals, and raised concerns over the nature and impact of certain proposals, as discussed in the chapters below. Most responses focused in particular on the PRA's proposals on the definition of capital, the NSFR, and SA-CCR.

Changes to draft policy

1.10 Where the rules that the PRA makes differ from the drafts in the CP in a way that the PRA considers is significant, FSMA⁷ requires the PRA to publish:

- (a) details of the difference together with a cost benefit analysis; and
- (b) a statement setting out the PRA's opinion on whether or not the impact of the rule on mutuals is significantly different to the impact that the draft rule would have had on mutuals, or the impact that the rule will have on other PRA-authorised firms.

1.11 The PRA has considered the responses to CP5/21 and identified other minor corrections that are appropriate to make to the policy that was proposed. The PRA has also further considered the proposed policy in light of its statutory objectives, the matters to which it must have regard, and additional evidence provided by firms. As a result, the PRA has:

- changed a number of Required Stable Funding (RSF) factors under the NSFR, including those applicable to certain centrally cleared derivatives transactions;
- postponed the application of the mandatory substitution approach to large exposures that are secured by collateral issued to a third party, pending further consultation and impact assessment;
- decided to consider, on a case-by-case basis, applications from firms to increase their non-core large exposures group limits to offset the impact of applying SA-CCR instead of the internal model method;
- introduced a notification requirement that applies if firms' exposures to CIUs are material. This will allow the PRA to address any risks to firms' safety and soundness through Pillar 2, while also having regard to proportionality, the UK's relative standing, growth, competitiveness, and trade;
- assessed that further consideration is needed of the conditions under which a domestic liquidity subgroup (DoLSub) may be granted;
- not implemented new reporting templates for the Fundamental Review of the Trading Book (FRTB) Alternative Standardised Approach (SA) in light of changes to HM Treasury's approach to Basel III implementation; and
- made consequential changes to update the SoP 'Interpretation of EU Guidelines and Recommendations: Bank of England and PRA approach after the UK's withdrawal from the EU'. This reflects the discontinued relevance of the EBA Guidelines on disclosure requirements under Part Eight of CRR and the EBA Guidelines on LCR disclosure, once the Disclosure Part of the PRA Rulebook comes into effect.

⁷ Section 138J(5) and 138K(4) of FSMA.

1.12 The PRA has decided to implement the proposed SA-CRR framework as set out in the CP. The PRA will undertake a holistic review of SA-CRR and other elements of the counterparty credit risk framework as part of the implementation of Basel 3.1 standards.

1.13 Further details on less material changes to the policy are set out in each chapter, including minor corrections that the PRA has identified.

1.14 The PRA considers that these changes will reduce overall costs to firms while maintaining the prudential benefits of implementing Basel III. This supports the PRA's judgement that the burden imposed on firms is proportionate to the benefits. The PRA also does not consider that the impact of the changes will have a significantly different impact on mutuals.

1.15 As noted in the new accountability framework section below, where changes to policy have affected the PRA's consideration of the matters to which it must have regard, these are noted in the updated detailed analysis of objectives and have regards in Appendix 12.

Financial Services Act 2021

1.16 The PRA's proposals in CP5/21 were determined in accordance with the provisions in the Financial Services Bill as introduced into Parliament on Wednesday 21 October 2020. This Bill received Royal Assent on 29 April 2021, becoming law as the Financial Services Act 2021 (the FS Act). There were no material changes to the Bill as introduced that affected the proposals in CP5/21.

1.17 HM Treasury can therefore use the powers in the FS Act to revoke provisions from the CRR and related CRR Level 2 Regulations. In turn, the PRA can make the rules set out in this PS as near-final. The PRA can use the powers in FSMA (introduced by the FS Act) to make certain types of rules applying to holding companies that are approved or designated by the PRA, and to include permissions in its CRR rules, as explained in the CP.

1.18 HM Treasury plans to use its powers under the FS Act to make savings provisions in relation to CRR permissions that are replicated in PRA rules. Firms therefore do not need to apply for a new permission to retain their existing capital treatment in relation to these rules.

1.19 The FS Act requires the PRA to publish a document setting out whether and, if so, how CRR rules correspond to the provision revoked by HM Treasury.⁸ Any pre-revocation references to the revoked provision in UK legislation are treated as a reference to the corresponding PRA rule identified in this publication. The PRA has satisfied this obligation in Appendix 14.

1.20 The FS Act allows the PRA to satisfy its FSMA consultation requirements in advance of the (then) Bill becoming an Act, including in relation to the new accountability framework.⁹

The new accountability framework

1.21 The FS Act has applied a new accountability framework to the making of CRR rules by making amendments to FSMA. This requires the PRA to consider certain matters and include certain explanations in addition to the normal requirements for PRA rulemaking.

1.22 When making CRR rules on or before Saturday 1 January 2022, the PRA must have regard to the following additional matters:

⁸ Section 5(4) of the FS Act.

⁹ Paragraph 23 of Schedule 3 to the FS Act.

- (a) relevant standards recommended by the BCBS from time to time;
- (b) the likely effect of the rules on the relative standing of the United Kingdom as a place for internationally active credit institutions and investment firms to be based or to carry on; and
- (c) the likely effect of the rules on the ability of CRR firms to continue to provide finance to businesses and consumers in the United Kingdom on a sustainable basis in the medium and long term.

1.23 The PRA must also publish an explanation of the ways in which the PRA has had regard to the above additional matters when making the CRR rules.¹⁰ In CP5/21, the PRA set out this explanation in Chapter 17: Statutory Obligations, and Appendix 12. In Appendix 12 of this PS, the PRA has updated the explanation of the have regards to take into account consultation responses.

1.24 The PRA must also have regard to the target in section 1 of the Climate Change Act 2008 (carbon target for 2050) for rules made after Saturday 1 January 2022.¹¹ As these rules will be final before that date, they are out of the scope of that requirement. In addition, during the consultation period for CP5/21, the Prudential Regulation Committee's (PRC) remit letter was revised to recommend that the PRC should, where relevant and practical, have regard to the Government's commitment to achieve a net-zero economy by 2050.¹² As consultation was underway at the point the PRC's remit letter was revised, the PRA could not consider this new have regard for these particular rules, as to do so would have caused an impractical delay to their implementation.

1.25 When making CRR rules, the PRA must consider, and consult HM Treasury about, the likely effect of the rules on 'relevant' equivalence decisions.

1.26 The PRA must also publish a summary of the purpose of the proposed rules. This summary is set out in Appendix 13.

1.27 There is an exception from the FSMA consultation requirements (except the requirement to consult the Financial Conduct Authority (FCA)), including the new accountability framework, for PRA rules that reproduce an existing provision of the CRR or a CRR Level 2 Regulation unaltered.¹³ These provisions are referred to as 'CRR restatement provisions'. The PRA must publish a statement identifying CRR restatement provisions.¹⁴ This statement is set out in Appendix 15.

Implementation and next steps

1.28 The policy material in this PS is published as near-final. The PRA does not intend to change the policy or make significant alterations to the text of the instruments before the making of the final policy material.

1.29 The PRA expects to publish the final rule instruments in a subsequent PS, after HM Treasury has laid the Statutory Instrument (SI), to delete the relevant parts of the CRR that these near-final rules will replace.

¹⁰ Section 144D of FSMA.

¹¹ Section 144C(1)(d) of FSMA and paragraph 25 of Schedule 3 to the FS Act.

¹² March 2021:

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/972443/CX_Letter_-_PRC_Remit_230321.pdf.

¹³ This includes any changes to the rules which, in the PRA's opinion, are not material (Section 144E(2) and (3)).

¹⁴ Section 144E(3) of FSMA.

1.30 This policy is intended to take effect at the same time as HM Treasury’s revocation of the relevant parts of the CRR, which will be on Saturday 1 January 2022.

1.31 Aspects of the near-final rules are linked to existing publications, such as Discussion Paper (DP) 1/21 ‘A strong and simple prudential framework for non-systemic banks and building societies’,¹⁵ the leverage ratio,¹⁶ and forthcoming PRA consultations, such as Basel 3.1. For further information on these aspects, please refer to the Regulatory Initiatives Grid (RIG).¹⁷

¹⁵ April 2021: <https://www.bankofengland.co.uk/prudential-regulation/publication/2021/april/strong-and-simple-framework-banks>.

¹⁶ CP14/21 ‘Consultations by the FPC and PRA on changes to the UK leverage ratio framework FPC Consultation Paper’: <https://www.bankofengland.co.uk/prudential-regulation/publication/2021/june/changes-to-the-uk-leverage-ratio-framework>.

¹⁷ Regulatory Initiatives Grid: <https://www.bankofengland.co.uk/report/2021/third-edition-of-the-regulatory-initiatives-grid>.

2 General responses to the consultation

2.1 This chapter covers the PRA's feedback to responses that addressed CP5/21 as a whole, as opposed to any of the individual proposals contained in the CP.

General approach, have regards, and PRA objectives

2.2 Three respondents commented in support of the PRA's general approach to the implementation of Basel III standards. One respondent supported the introduction of the new have regards in the FS Act, suggesting these principles will enable UK authorities to strike the right balance between prudent rulemaking, international regulatory alignment, and the future attractiveness of the UK as a financial centre.

2.3 Another respondent suggested that the new have regards, together with the proportionality measures, should help unlock economic growth and investment in the UK. Two respondents supported the PRA's approach to implementing the Basel III standards using the CRR II legislation as the initial basis. Those respondents supported the FS Act requirements, particularly the requirement to have regard to Basel standards and the competitiveness of the UK.

2.4 One respondent recognised the PRA's primary and secondary objectives, but suggested the PRA should give greater consideration to the have regard on competitiveness.

2.5 Two respondents stated that, in determining how to implement prudential standards, the PRA had adopted standards higher than the international minimum and the EU standards. Both respondents raised concerns about the impact of this approach on international competitiveness, suggesting that taking this approach could disadvantage UK banks and their customers internationally.

2.6 The PRA's approach strikes an appropriate balance between its statutory objectives, and the factors to which it must have regard. These include the implementation of international standards and the relative standing and competitiveness of the UK and equivalent standards applied in other jurisdictions.

2.7 In Appendix 12 of the CP, the PRA set out its assessment of its objectives and the factors to which it must have regard under the FS Act.

2.8 The PRA has made several changes to the near-final policy in response to new information provided by firms and in the consultation responses. The PRA has updated Appendix 12 to include the additional factors considered following consultation. After further consideration of the matters to which it must have regard, and in light of the responses received, the PRA changed its proposed policy on levels of application, CIUs, counterparty credit risk, large exposures, and the NSFR.

2.9 One example of an aspect of the proposed approach that was subject to significant change following consultation is the NSFR. Respondents raised a number of concerns about some of the proposed RSF factors proposed by the PRA. Further information is set out in Chapter 13. In considering its feedback to these concerns, the PRA weighed the potential effect on its statutory objectives and compliance with international standards against the other matters to which it must have regard, in particular the proportionality of the proposals and their potential impact on competitiveness and the standing of the UK, finance for the UK real economy, and growth.

2.10 A second example is the PRA's proposed approach to large exposures. Respondents considered that the substitution approach proposed required further specification, could potentially impact the

smooth functioning and liquidity of repo and securities markets, and could require significant operational changes to implement. The PRA considered the benefits for safety and soundness of implementing a substitution requirement and the concerns that respondents raised. The PRA has decided not to implement its proposed approach at this time, but to develop its proposed approach in more detail. The PRA will also undertake further analysis of the potential impact on the liquidity of repo and securities markets.

Implementation of international standards

2.11 The PRA received a number of general comments relating to the compliance of its proposed approach to implementation of international standards, focusing on those set by the BCBS.

2.12 One respondent requested further details on how the PRA will implement international standards in the future, including when the PRA might require firms to exceed international standards. Another respondent expressed concern that specific parts of the Basel III standards could undermine UK competitiveness, particularly in relation to global derivatives activity.

2.13 Two respondents encouraged the UK to continue to engage at an international level. One expressed a view that a lack of granularity is leading to market fragmentation, while the other respondent asked the PRA to raise industry concerns at Basel meetings to ensure consistency across jurisdictions.

2.14 The PRA considers the consistent and timely implementation of international standards to be crucial to ensure the safety and soundness of firms and a level playing field. The PRA engages actively in international fora and will take any new, or updated, international standards into account when making future policy.

Future Regulatory Framework

2.15 Three respondents commented on the future of the regulatory framework.

2.16 In October 2020, HM Treasury published a consultation paper on Phase II of the Future Regulatory Framework (FRF) Review.¹⁸ This consultation paper examined the overall regulatory framework for regulation of financial services in the UK.

2.17 One respondent welcomed the restatement of the CRR provisions to implement Basel III in the PRA Rulebook, and suggested that an FRF in which prudential regulations are fully contained in rules and supervisory statements will be more coherent and less complex. This respondent noted that some industry participants find the onshored legislative framework difficult to navigate. Another respondent asked how the PRA may approach onshored EU law in the future. They stated that the FRF should provide regulatory certainty for industry and an appropriate level of policymaking flexibility for the PRA. Another respondent requested guidance in the interim period before the completion of the FRF project.

2.18 Although not directly related to the proposals in CP5/21, the PRA has considered these comments. The PRA invites respondents to provide their views in future consultations. HM Treasury established the FRF Review to determine how the overall approach to the regulation of financial services needs to adapt to the UK's new position outside the EU. The FS Act represents a first step towards the FRF. Subject to the outcome of HM Treasury's review, the PRA is committed to the

¹⁸ October 2020, HM Treasury, 'Financial Services Future Regulatory Framework Review – Phase II Consultation': https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/927316/141020_Final_Phase_II_ondoc_For_Publication_for_print.pdf.

timely and effective implementation of the FRF. HM Treasury plans to publish a second consultation paper on Phase II of the FRF by the end of 2021.

2.19 One respondent asked the PRA to review the onshored acquis and delete, simplify, or modify those sections to ensure their appropriateness for the UK. This respondent also expressed a view that firms would find it beneficial to have clarity on how Basel standards will be implemented in future. They suggested that the PRA should clarify the tests for when higher standards should be applied or the approach that the PRA will take when the Basel standards should be supplemented by a technical standard.

2.20 Future changes to the onshored acquis and implementation of Basel standards are outside the scope of CP5/21. The PRA has noted these comments and may consider these points in future policy development.

Implementation in rules and technical standards

2.21 One respondent raised a question in respect of the PRA's ability to waive or modify the CRR rules, given that the use of waivers and modification of PRA rules was previously limited by EU law. When the CRR rules published as near-final in this PS come into effect, they will be subject to the PRA's usual waiver or modification powers.¹⁹

2.22 One respondent asked whether technical standards made under the CRR that relate to provisions that are moving into PRA rules would be repealed by HM Treasury. HM Treasury is using its powers under the FS Act to revoke technical standards that are made under mandates that are being deleted from the CRR.

Proportionality

2.23 The PRA proposed a number of measures in the CP intended to enhance proportionality for smaller firms. These included:

- revised counterparty credit risk requirements, including a simpler, more conservative SA-CCR approach (the simplified SA-CCR, or sSA-CCR) for certain smaller firms, and amendments to the original exposures method (OEM);
- a simpler, more conservative NSFR (the simplified NSFR, or sNSFR) that certain smaller firms could choose to use;
- increased the scope of more proportionate market risk capital requirements and exemptions from new market risk reporting requirements; and
- tailored disclosure requirements.

2.24 Three respondents welcomed the broad objective to simplify the prudential framework for smaller firms and the specific proportionality measures proposed in the CP.

2.25 Two respondents suggested that the prudential framework for smaller firms could be simplified further, identifying reporting and disclosure as areas that could be made more proportionate. The PRA is considering further simplifications to the prudential framework for smaller and non-systemic firms. As noted above, the PRA has published a DP on the topic: DP1/21 'A strong

¹⁹ Section 138A of FSMA. Further details can be found here: <https://www.bankofengland.co.uk/prudential-regulation/authorisations/waivers-and-modifications-of-rules>.

and simple prudential framework for non-systemic banks and building societies'. Two respondents noted that they look forward to engaging with the PRA on DP1/21.

2.26 One respondent suggested that the PRA could apply the sNSFR and proportionate disclosure requirements to a broader range of firms. Under the PRA's proposed rules, these treatments would be available to firms that qualify as 'small and non-complex' institutions under the definition set out in the CRR. The respondent also suggested that the €5 billion threshold for total assets in the definition of small and non-complex institutions in the CRR could be changed to £5 billion.

2.27 Having considered the responses, the PRA intends to continue to use the CRR definition of small and non-complex institutions in the related PRA rules at this time. The PRA will consider further the proportionality measures that should be available, and relevant thresholds for their use, as part of its strong and simple approach covered by DP1/21. The PRA will consider definitions that relate to proportionality further in light of responses to that work.

2.28 One respondent noted that implementing even simplified reporting and disclosure frameworks would generate some operational costs for smaller firms. As a result, some firms may choose not to apply more proportionate treatments, particularly where these required interaction with third-party software suppliers. The respondent also expressed concern that the PRA's strong and simple reforms to reporting and disclosure that may happen in the future could result in a subsequent set of resource intensive changes for smaller firms.

2.29 The PRA recognises that all changes to reporting and disclosure requirements generate costs for firms to implement. The measures in this PS are designed to enhance proportionality for smaller firms in the shorter-term, prior to the design and implementation of a simpler regime for smaller firms. The design and implementation of proposed prudential rules for defining whether a firm is in scope of a simpler regime is addressed by DP1/21. The proposed requirements under that regime are likely to take a number of years to complete. As a result, the PRA considers that the proportionality measures set out in this PS would offer significant potential benefits for firms in the interim period. In developing further measures to simplify regulation for smaller firms, the PRA will have regard to the proportionality measures already introduced and the period that firms would require to implement a simpler regime.

2.30 One respondent expressed disappointment that the PRA's cost benefit analysis suggested that the SA-CCR would lead to a small increase in risk-weighted assets for small firms. The PRA acknowledges that the SA-CCR may lead to a small increase in risk-weighted assets for small firms. The PRA notes that certain smaller firms will be able to calculate their counterparty credit risk exposure value using either the sSA-CCR or the OEM approaches. These methodologies have been designed to be more conservative and less complex, with a lower operational cost for firms to implement and maintain. The PRA considers that certain smaller firms will derive significant potential benefit in applying these simplified approaches.

2.31 One respondent noted that counterparty credit risk was an area where proportionality was of particular importance to smaller firms. The respondent welcomed the availability of both the sSA-CCR and the OEM approaches, and recognised that they had been designed to be more conservative.

Cost benefit analysis

2.32 One respondent commented on the impact of the overall package of measures in CP5/21. They stated that the true benefit of the proposals would be marginal given other prudential developments, while the true cost would be a reduction in lending to the UK real economy. They thought the PRA should therefore be prepared to implement measures that would support

innovative UK challenger banks. The PRA accepts that there is a cost in terms of reduced lending during non-crisis periods, which is implicitly captured within the PRA's estimates of the GDP cost impact.

2.33 However, the PRA notes that the proposals also contribute to preventing costly financial crises, and when both benefits and costs are considered, the proposals are still highly net beneficial. Moreover, the proposals help ensure that banks appropriately take into account risks relevant to their business, and that any capital they hold against these risks is genuinely capable of absorbing any losses when these risks are realised. Any increase in capital requirements reflects appropriate consideration of the risks (including any appropriate reduction in lending that may result) and the capacity to absorb any losses.

Out of scope comments

2.34 A number of respondents provided comments that were outside the scope of the proposals in the CP. In particular, three responses commented on policy areas that are not covered by the CP, relating to credit insurance, credit risk mitigation, synthetic risk transfer instruments, secured lending, finance to the economy, treatment of sovereigns, and minimum requirement for own funds and eligible liabilities (MREL). While not related to the proposals in the CP, the PRA notes these comments, and may take them into account when developing future policy.

3 Interpretative provisions

3.1 In the interpretative provisions chapter of the CP, the PRA proposed to amend the Interpretation Part of the PRA Rulebook in a number of areas. One respondent expressed support for the proposals (which include an interpretative provision that terms used in the new rules have the same meaning they have in the CRR). This respondent suggested it would be useful to identify more clearly the CRR-defined terms in the PRA Rulebook. The PRA has considered this suggestion and sees merit in showing (eg by linking to the definition) where a term is defined in the CRR. Due to the difficulty in completing this task in the time available, the PRA will consider whether more links to externally defined terms could be inserted into the PRA Rulebook.

4 Scope of application

4.1 The PRA proposed to replicate the scope of application of prudential requirements set out within the CRR for the measures proposed in the CP.

4.2 No responses were received in relation to this proposal. The PRA will therefore publish the policy as proposed.

Net stable funding ratio

4.3 The PRA proposed to apply the NSFR to credit institutions and PRA-designated investment firms (DIFs).

4.4 Seven respondents commented on the potential application of the NSFR to DIFs.

4.5 One respondent supported the application of the NSFR to DIFs, considering that this would ensure a level playing field between DIFs and banks that provide similar products. Three respondents broadly supported the goals of the NSFR, with one respondent noting that the PRA's proposed rules appear broadly prudentially appropriate and proportionate, and another recognising the appropriateness of reducing banks' reliance on short term funding. One respondent also recognised that the experience of the financial crisis required an increased focus on firms' funding profiles.

4.6 Six respondents considered the NSFR and its calibration not to be appropriate for the business activities of a DIF. Two respondents considered that the NSFR appears to have been designed for credit institutions rather than DIFs. One respondent considered that applying the requirements of the NSFR would be a particular challenge for market-making firms.

4.7 One respondent stated that the NSFR does not take into account the diversity of product types that are required to facilitate clients' requirements. Another respondent considered the NSFR not to reflect the true funding risk of certain investment firm activities. One respondent highlighted that investment firms specialise in activities that are short-term and funding neutral.

4.8 Five respondents considered that the NSFR could have a variety of adverse impacts on DIFs, citing lower profitability, higher funding costs, and a reduction in certain business lines. Two respondents considered the application of the NSFR could lead to imprudent asset and liability management, as it would require investment firms to raise long-term funding for activities that are short term in nature or do not require funding. Another respondent stated that DIFs might develop complex funding structures in order to meet the requirements of the NSFR. Two respondents considered that the application of the NSFR to investment firms could affect the relative standing of the UK. They further suggested that investment firms might move business to jurisdictions that do not apply the NSFR to investment firms. One firm stated that it had already moved some business to a different jurisdiction in which the NSFR does not apply to investment firms.

4.9 The PRA has considered the responses and decided to maintain its approach. The PRA considers the application of the NSFR to DIFs to enhance their safety and soundness and to facilitate effective competition. However, the PRA considers it to be prudent and proportionate to make a number of changes to the NSFR stable funding treatment of certain activities common to DIFs and certain banks, which will ensure the NSFR is more aligned to the risks of those activities. These are set out in Chapter 13.

5 Levels of application

5.1 The PRA proposed to make rules specifying the levels of application for the new Large Exposures (CRR), Liquidity (CRR), Liquidity Coverage Ratio (CRR), Reporting (CRR), and Disclosure (CRR) Parts of the PRA Rulebook, where the PRA is making rules to replace parts of the CRR that HM Treasury is proposing to revoke in their entirety, relating to large exposures, liquidity, reporting, and disclosure.²⁰ The proposed rules sought to ensure that the requirements in those parts of the PRA Rulebook would continue to be applied at an individual, consolidated, and sub-consolidated level by replicating the levels of application provisions within the CRR.

5.2 Two respondents raised concerns about the level of application of the proposed NSFR rules. One respondent suggested that application of the standard to firms on a solo (ie individual) basis is not consistent with the Basel standard. Another highlighted that a potential unintended consequence arising from the application of the rules to solo institutions is the increasing complexity of consolidated groups' balance sheets due to intergroup funding arrangements.

5.3 The PRA has considered the responses and has decided not to change its approach. The PRA notes its proposed approach is consistent with the level of application of Basel standards.²¹ The PRA considers that additional complexity resulting from the solo application of the NSFR requirements is proportionate to the benefits to firms' safety and soundness from the application of the NSFR.

5.4 The PRA also proposed to make rules for the Own Funds and Eligible Liabilities (CRR), Trading Book (CRR), Standardised Approach and Internal Ratings Based Approach to Credit Risk (CRR), Counterparty Credit Risk (CRR), Operational Risk (CRR), and Credit Valuation Adjustment Risk (CRR) Parts of the PRA Rulebook to clarify that the level of application provisions for those rules will remain within the CRR.

5.5 The PRA received no responses to the other proposals listed above in paragraphs 5.1 and 5.4. The PRA will therefore publish the policy as proposed.

Individual consolidation

5.6 The PRA proposed to automatically extend existing permissions granted to firms that apply individual consolidation for the purposes of requirements set out in the CRR relating to the proposed Large Exposures (CRR) and Reporting (CRR) Parts.

5.7 One respondent supported the proposed approach to individual consolidation and to maintaining current permissions. The PRA will therefore publish the policy as proposed.

Liquidity: Domestic liquidity sub-groups

5.8 The PRA proposed to replicate in PRA rules the requirements of the CRR in relation to Domestic Liquidity Sub-Groups (DoLSubs), and to introduce requirements specific to the NSFR in order for the scope of a DoLSub permission to include the NSFR.

5.9 Two respondents noted that firms would be unable to apply for a DoLSub waiver if the entities in the proposed DoLSub have an intermediate holding company parent. One respondent considered that the proposed approach to DoLSubs gave insufficient regard to the cost of implementation compared to the prudential benefit. Another respondent considered the PRA's proposed approach

²⁰ Parts 4, 6, 7A, and 8 of the CRR.

²¹ SCO10.3 and footnote 2 of the Basel III standards.

not to give sufficient regard to the variety of business models and group structures that firms may have.

5.10 In light of these responses, the PRA has decided to further consider the conditions under which a DoLSub may be granted. The PRA will clarify its intended approach to DoLSubs at the earliest opportunity.

Required Stable Funding (RSF) factor

5.11 The PRA proposed to require that firms apply, upon consolidation, locally applicable ASF and RSF factors. Locally applicable ASF factors are applied where they are lower than the PRA ASF factor. Locally applicable RSF factors are applied where they are higher than the PRA RSF factor.

5.12 Three respondents considered this to be overly prudent because it removes a number of beneficial treatments available in other jurisdictions, and is not required by – and is potentially super-equivalent to – the Basel III standards. The respondents commented that this provision should be deleted or that less conservative factors should be allowed to offset more conservative factors at the level of a subsidiary.

5.13 The PRA also proposed to require firms to apply the highest RSF factor where more than one RSF factor could apply. Two respondents considered that proposal overly conservative and not consistent with the rest of the liquidity framework.

5.14 The PRA has considered the responses received and has decided to maintain its proposed approach. The PRA considers that the application of more conservative ASF and RSF factors upon consolidation is appropriately prudent and proportionate, because recognition of more conservative values upon consolidation ensures that additional risks perceived by local regulators in third countries are recognised in firms' consolidated NSFRs. The PRA considers that application of the highest RSF factor where more than one could apply is appropriately prudent, considering the uncertainty that could exist as to the true risk posed by assets that can be allocated more than one RSF factor.

Consolidated application

5.15 The PRA proposed to introduce new rules in each of the new Large Exposures (CRR), Liquidity (CRR), Liquidity Coverage Ratio (CRR), Reporting (CRR), and Disclosure (CRR) Parts of the PRA Rulebook, requiring parent firms and approved holding companies to meet those requirements on a consolidated basis.

5.16 The PRA proposed to apply the requirements on a consolidated basis by referring to 'CRR consolidation entities', thereby introducing a new definition of this into the PRA Glossary. The PRA also proposed to continue to determine the methods of prudential consolidation and make a number of minor changes in the Groups Part to reflect the revised approach, as set out in the levels of application chapter of the CP.

5.17 Furthermore, the PRA proposed to introduce new rules in each of the new Large Exposures (CRR), Liquidity (CRR), Liquidity Coverage Ratio (CRR), Reporting (CRR), and Disclosure (CRR) Parts of the PRA Rulebook to require firms and CRR consolidation entities to meet appropriate organisational structure and control mechanism requirements on a consolidated basis.

5.18 The PRA received no responses to these proposals. The PRA will therefore publish the policy as proposed.

Sub-consolidated application

5.19 The PRA proposed to require an institution to comply with the requirements in the Large Exposures (CRR), Liquidity (CRR), Liquidity Coverage Ratio (CRR), Reporting (CRR), and Disclosure (CRR) Parts of the PRA Rulebook, on a sub-consolidated basis, where that institution is required to comply with Parts Two and Three of the CRR on that basis.

5.20 One respondent supported the PRA's proposed approach, commenting that this would ensure the integrity of ring-fencing. No other responses were received in relation to these proposals. The PRA will therefore publish the policy as proposed.

Third country sub-consolidation

5.21 The PRA did not propose to implement a general rule on third country sub-consolidation to replace the CRR requirement that HM Treasury proposed to revoke, and instead proposed to use its requirement power in individual cases. The PRA also proposed to amend SS15/13 'Groups' to clarify that one instance in which it may use its powers to require sub-consolidation is where the risks posed to a firm by its third country subsidiary or subsidiaries warrant it on a case-by-case basis.

5.22 The PRA received no responses to these proposals. The PRA will therefore publish the policy as proposed. Furthermore, the PRA had proposed to make some consequential changes to the Capital Buffers and ICAA Parts of the PRA Rulebook, to amend rules relating to specific third country sub-consolidation requirements. The PRA now considers it more appropriate to delete those requirements in their entirety.

Other issues

5.23 The PRA proposed to introduce a requirement in the Groups Part of the PRA Rulebook for firms to notify the PRA before using an exemption allowing firms to exclude a small subsidiary or subsidiaries from consolidation.

5.24 The PRA received no responses to this proposal. However, in CP12/21 'Financial holding companies: Further implementation', the PRA has proposed to amend the notification requirement so that it also applies to approved or designated holding companies.²² The consultation period for CP12/21 closes on Thursday 22 July 2021.

5.25 The PRA will therefore await the responses to CP12/21. If the notification requirement rule is made, it will also apply to approved or designated holding companies, and take effect on Saturday 1 January 2022.

²² June 2021: <https://www.bankofengland.co.uk/prudential-regulation/publication/2021/june/financial-holding-companies-further-implementation>.

6 Definition of capital

Deduction of software assets from CET1

6.1 The PRA proposed to require full deduction from CET1 capital of all intangible assets, with no exception for software assets. This would enhance firms' safety and soundness and enable the PRA to supervise the quality of firms' CET1 capital effectively.

6.2 The PRA received eight responses to this proposal. One respondent was supportive of the proposal. Two other respondents agreed that there is currently a lack of evidence for the realisable value of software, stating that software is usually bespoke to an individual firm and therefore would have minimum realisable value on its own. Seven respondents commented on the implications of the PRA's policy on its secondary competition objective and the have regards relating to international level playing field, competitiveness and UK standing, technology innovation, and finance to real economy.

6.3 One respondent stated that the PRA's proposal would not significantly enhance firms' safety and soundness. The respondent did not explain their reasons for that view. Another respondent recognised the importance of the PRA's proposal in meeting the PRA's safety and soundness objective, but raised concerns that it could disadvantage banks and their customers, in particular small and medium-sized enterprises (SMEs). One respondent stated that software assets are important for firms' operational resilience.

6.4 The PRA considers the proposed approach is necessary and effective in enhancing their safety and soundness, as it ensures that items that are not sufficiently reliable in absorbing losses on a going concern basis are not included in CET1 capital. The PRA's approach is also consistent with the Basel standards to which it must have regard. The PRA recognises the importance of software for operational resilience, but considers high quality CET1 capital to be essential to enhance firms' resilience to financial shocks, including in periods of stress.

6.5 Two respondents considered that the PRA's proposal could have a disproportionately negative impact on smaller banks, and discourage technological innovation in smaller banks. Three respondents commented that the proposal would reduce the incentive for firms to invest in software. One of these respondents added that it might create a barrier to new challenger banks' entry into the UK market, thereby undermining the PRA's secondary competition objective.

6.6 The PRA considers that its proposal would facilitate effective competition. The proposed treatment of software assets applies equally to all PRA-regulated CRR firms, irrespective of their size. The amount required to be deducted is proportionate to the amount of intangible software assets of the firm. A relatively higher amount of software assets in a particular firm would not reduce the need for that firm to support its activities with high quality CET1 capital. The PRA has authorised 26 banks since 2014, when a full deduction requirement was applied to intangible software assets under the CRR. The PRA considers that this provides evidence of new firms' willingness and ability to enter the market notwithstanding the full deduction requirement.

6.7 Two respondents considered that the proposal would afford a competitive advantage in the development and use of software by non-regulated companies, as they are not subject to the PRA's rules. The PRA has considered this comment, but maintains that its proposed approach is necessary to enhance firms' safety and soundness, by ensuring that PRA-regulated firms remain sufficiently resilient to financial shocks. Unregulated entities may not pose the same risks to the PRA's objectives as regulated firms.

6.8 Five respondents commented that the proposed approach would adversely impact UK firms' international competitiveness. They considered that it could put UK firms at a competitive disadvantage when compared with some other jurisdictions (such as the US and EU). One respondent stated that the treatment of intangible assets under the Basel III standards is not harmonised internationally because of the differences in definitions of intangible assets under the applicable accounting frameworks. Three respondents suggested the PRA should seek that the BCBS conduct a further review of the treatment of software assets. Two respondents considered that the proposed approach conflicted with UK government policy, including in relation to international competitiveness. Another respondent suggested that the proposed approach would diminish UK firms' ability to compete in the acquisition of financial technology companies.

6.9 The PRA recognises that there are differences in the implementation of this particular aspect of the Basel III standards in some jurisdictions. In some cases, they result from local accounting standards; in others, they reflect a policy choice. The PRA considered the potential impact of full deduction on firms' CET1 levels and international competitiveness in developing its proposal. While full deduction may have some adverse effect on UK firms' relative standing, the magnitude of any such effect is not clear. Some market participants have already indicated that, in assessing banks' resilience levels, they may discount software assets that are treated as part of CET1 capital, thereby removing any apparent advantage to some firms. Furthermore, the full deduction of UK firms' intangible software assets could also have beneficial effects for competitiveness, by enhancing confidence in the quality of UK firms' capitalisation and their ability to withstand financial shocks and maintain lending to the real economy.

6.10 Four respondents considered that the proposed approach would disincentivise future investments in software and associated innovation, and one respondent considered that this could pose systemic risk to the industry. One respondent suggested that the proposed approach would inappropriately conflict with UK fiscal measures designed to encourage software investment.

6.11 The PRA considers that firms' decisions to invest in technologies are driven by a range of other factors. These could include a desire or need to differentiate business from other firms, to understand and serve customers better, to improve their ability to cross sell, or to measure or manage risk more effectively. Notwithstanding the requirement to deduct software assets fully under the original CRR, UK firms' investment in software assets has increased substantially during recent years, and is expected to continue to rise in the coming years. The previous and continuing investment in software is supportive of there being significant other drivers of investment in software. This is consistent with regulatory capital treatment not being a determining factor in the decision to invest in software.

6.12 Two respondents stated that the proposed CET1 deduction would adversely impact their ability to lend to the real economy. One of those respondents stated that the cost benefit analysis in the CP did not include analysis of the potential adverse impact of the proposed approach on lending to the real economy. They suggested it was plausible that the proposed approach would result in £3 billion additional capital being required by the largest five UK firms, resulting in £15–£25 billion in lending restrictions to borrowers such as SMEs. They believed that the potential adverse impact on lending had not been a key consideration in the PRA's approach.

6.13 The PRA considers that firms must be resilient to financial shocks in order to be able to lend to the UK real economy on a strong and sustainable basis. By ensuring that capital is supported by assets with proven realisable values, the proposed approach would ensure that firms' CET1 capital can absorb losses in times of stress, helping firms to remain a going concern and sustain lending to the real economy. In the statement published on Wednesday 30 December 2020, the PRA

recommended that firms should not base their lending and distribution decisions on any capital increase from software assets included in their regulatory capital. Consistent with that, the PRA considers that its approach would not have a significant adverse impact on lending, as such decisions are likely to have been made with knowledge of the PRA's recommendation and its intention to consult on proposals that exclude intangible software assets from firms' CET1 capital in future.

6.14 One respondent considered that the PRA's statement that there is an absence of evidence that software assets have value in stress was not correct. While they recognised the PRA's concern that software assets may not meet all the requirements of CET1 capital, and could not absorb losses in a stress while a firm remains a going concern, they considered that software assets could be sold to generate income to absorb losses in a winding up of the firm. The respondent did not provide evidence to support their view.

6.15 This respondent, and three other respondents, commented that software assets have some intrinsic value in certain resolution strategies. For example, they might have value in a bail-in or in a business sale, as software assets are essential to enable the firm to continue to function. One respondent suggested that the PRA's approach should not focus narrowly on value in liquidation or stress, and that greater recognition of software assets in CET1 was warranted. They suggested that the PRA should consider value and useful life of assets over time rather than the amount of loss they would absorb. They noted that the accounting value of software assets is subject to external audit. One respondent considered the PRA's concerns about the quality of software assets to be at least partly mitigated by the UK resolution regime, stating that software in many firms is essential to support their continued operations in a bail-in or sale, and so can be considered to have value. They thought that the value of software assets should be recognised in the PRA's approach where they are integral to a firm's business proposition, or they support resolution, citing such recognition in the accounting framework.

6.16 One respondent expected the software assets of some firms with business models dependent on technology platforms to have value in the event of liquidation or stress, but they acknowledged that this has not yet been tested in practice. Another respondent considered proprietary software to be an important part of the value of their business. A separate respondent commented that the accounting value of software assets already reflects its benefit over its useful life, and that it takes into account any potential impairment from obsolescence or following an acquisition. This respondent also considered that aligning the accounting and capital value of software assets would be sensible, prudent, and pragmatic.

6.17 The PRA considers that ensuring safety and soundness requires a focus on the reliable realisable value of software assets to absorb losses in a going concern, especially in a stress. The potential for software assets to have value in gone concern is not relevant to their recognition as a form of going concern capital. The consultation responses did not provide evidence of the realisable value of software assets in a going concern, including in a stress.

6.18 The PRA considers that the accounting value of a non-trading asset is largely based on its value-in-use. For prudential regulation purposes, a firm's capital base must be supported by asset items that have reliable realisable value. The PRA does not consider the accounting value is designed to represent the realisable value of a software asset available to absorb losses on a going concern basis, including in a stress.

6.19 One respondent agreed that there is a lack of evidence to support the value of software at the point of non-viability, but they considered that lack of evidence to have resulted from the significant

enhancements that have been made to the prudential and accounting frameworks in the recent years, which improve the soundness of the financial system.

6.20 One aim of the Basel III standards was to enhance the quality of capital to bolster firms' resilience to future financial shocks. The PRA considers quality of capital to be the foundation of the prudential safety and soundness of firms. Other enhancements to the prudential framework are not an effective substitute for high quality capital.

6.21 Three respondents proposed alternative approaches to the full CET1 deduction that the PRA proposed. One respondent stated that the PRA should maintain the approach currently applied in the CRR until the BCBS has reviewed the treatment of software assets.

6.22 The PRA considers that the current CRR approach can result in an overstatement of a firm's CET1 available to absorb losses in a going concern. The PRA approach implements the current Basel III standards.

6.23 One respondent considered that the PRA buffer requirement, based on stress testing and/or a bank's estimate of wind down cost (which considers the value of all assets to be liquidated, including software assets) would already limit the benefits of their inclusion in CET1. The respondent suggested that the PRA should implement the EU approach, ie partial deduction of software assets, but impose a higher Pillar 2 capital requirement on those firms that could not satisfy the PRA that their software assets had value in resolution.

6.24 The PRA considers that it is important to ensure that the CET1 capital of a firm represents the true loss absorbing capacity of the firm. The PRA considers that the Pillar 1 requirement for full deduction from CET1 capital is the most appropriate approach to intangible software assets given the lack of evidence of their realisable values. It is also a simpler, more effective and transparent approach for all firms.

6.25 The respondent also suggested that software assets could be exempted from the CET1 deduction, but the PRA could impose a higher risk weight on software assets (eg 100%, or more) to mitigate any undercapitalisation risk from their non-deduction. Under this alternative, the maximum amount of software assets not deducted could be capped at 10% CET1, for consistency with the approach to other items not deducted from CET1. Given the lack of evidence on the realisable value of software assets, the PRA considers that full deduction from CET1 capital is appropriately prudent. In addition, imposing a limit on the software assets not deducted would limit but not sufficiently address the PRA's concern that CET1 capital could otherwise be potentially overstated.

6.26 Another respondent suggested the PRA could apply a full deduction, but consider adding the amount of software assets deducted back to the capital used to meet Pillar 2 requirements where a firm was able to demonstrate the value of its software. The respondent did not provide any evidence of the realisable value of software assets. In the absence of any credible evidence on realisable values of software assets, the PRA does not consider such a change to be appropriate.

6.27 After considering the responses received, the PRA has decided not to change the proposed policy. The PRA considers the full deduction of intangible software assets from CET1 to be necessary to ensure that UK firms' CET1 capital – the highest quality form of capital – is able to absorb losses on a going concern basis, including in a stress.

6.28 In the CP, the PRA proposed to make an instrument under section 138P (Technical Standards) of FSMA to remove Article 13a of the Commission Delegated Regulation (EU) 241/2014 (RTS) in respect of software assets before Saturday 1 January 2022. No respondents commented on this

proposal. The PRA now considers that implementation before Saturday 1 January 2022 may not provide sufficient time for some firms to implement the revised requirement. Therefore the PRA has decided not to make this instrument as proposed. Article 13a of the RTS will in any event be deleted by HM Treasury, along with the CRR Article 36, on Saturday 1 January 2022 under the FS Act. This, along with the new rule noted in paragraph 6.27 above, means that the requirement for CET1 deduction of intangible software assets will be fully implemented on Saturday 1 January 2022.

7 Market risk

7.1 The PRA proposed to make a number of changes to the market risk framework that would:

- make explicit that prudent valuation requirements apply to trading and non-trading book positions measured at fair value;
- replicate in the Trading Book (CRR) Part of the PRA Rulebook the UK Technical Standards Instrument due to be repealed that prescribes additional prudent valuation requirements;
- require that, in order to be included in the trading book, a position must be revalued at fair value on at least a daily basis, and the changes in the value of those positions must be reported in the profit and loss account of the firm;
- incorporate requirements on management of the trading book and internal hedges between the trading book and non-trading book into the Trading Book (CRR) Part of the PRA Rulebook; and
- amend the eligibility requirements for use of the derogation for small trading book business.

7.2 One respondent requested clarification on the status of CRR Level 2 Regulations for which the mandate falls under the CRR Level 1 Articles that have been deleted by the FS Act, in particular regarding Commission Delegated Regulation (EU) 2016/101 relating to the proposals on prudent valuation. One respondent supported the proposals to require daily revaluation at fair value of trading book positions. Two respondents supported the proposals relating to the derogation for small trading book business on the basis of proportionality.

7.3 Beyond the specific proposals in the CP, one respondent suggested that the PRA should remove deviations from the Basel III standards from the CRR to support global consistency, citing in particular differences in the list of foreign exchange rates that firms need to consider when calculating capital requirements for options.²³ Two respondents suggested that the PRA should align the capital treatment of banking book CIUs with that of trading book CIUs.

7.4 Having considered the responses, the PRA has decided to publish the policy as proposed. Paragraph 6.8 of CP5/21 clarifies that the provisions of Commission Delegated Regulation (EU) 2016/101 are being replicated in the Trading Book (CRR) Part of the PRA Rulebook. The PRA notes that the issues related to deviations from the Basel III standards and market risk capital requirements for CIUs exposures in the trading book are outside the scope of this consultation. The substance of the requirements within the Pillar 1 market risk framework will be considered as part of future consultation on Basel 3.1 implementation.

²³ For options, the market risk framework requires firms to estimate the losses that they could suffer if the implied volatility of a range of foreign exchange rates were to change. The CRR definition of the foreign exchange rates to be included in the calculation differs from the definition in the Basel III standards.

8 Collective investment undertakings

8.1 The PRA proposed to implement in PRA rules the Basel III capital requirements for firms' equity exposures to collective investment undertakings (CIUs) in the non-trading book.

Hierarchy of approaches

8.2 The proposed rules set out a revised hierarchy of approaches to determine capital requirements for CIUs exposures under the standardised approach (SA) and the internal ratings based (IRB) approaches to credit risk: a revised look-through approach (LTA), a mandate based approach (MBA), and a fall-back approach (FBA). The PRA proposed to permit firms to apply a combination of the LTA, MBA, and FBA to its CIUs exposures, provided the relevant conditions for their use are met.

8.3 No responses were received in relation to this proposal. The PRA will therefore publish the policy as proposed.

Additional criteria for using the LTA and the MBA: Criteria relating to supervisory oversight of CIUs

8.4 In implementing into PRA rules the revised Basel III standard²⁴ for firms' equity exposures to CIUs in the non-trading book, the PRA proposed to permit firms to use the LTA and the MBA subject to certain conditions. One of these conditions would require the company managing the CIUs to be subject to FCA supervision, or equivalent supervision for companies supervised in a third country.²⁵

8.5 Four respondents considered that the proposed jurisdictional equivalence condition should be removed to support the competitiveness of UK firms and to ensure consistency with Basel standards. Three respondents suggested that an alternative to applying the equivalence condition would be for firms to commission an independent third party assessment of the regulatory and supervisory approaches of other jurisdictions.

8.6 HM Treasury consulted on the UK's intended approach to the implementation of some areas of the Basel III standards.²⁶ Following the responses to its consultation and having reviewed the costs and prudential benefits of the approach to Article 132 of the CRR, and having consulted the FCA and the PRA, HM Treasury decided that applying the equivalence provision would be disproportionate. HM Treasury decided, on proportionality grounds, to remove the relevant equivalence provision from the CRR. In its consultation response, HM Treasury stated that the PRA could address any risks that arise as a result of a firm's exposure to funds located and managed in overseas jurisdictions.

8.7 The PRA has amended its rules relating to the use of the equivalence condition accordingly, such that the use of the LTA or MBA no longer depends on conditions relating to supervisory oversight of third country fund managers.

8.8 To enable the PRA to monitor the risks of exposures to CIUs managed by third country fund managers, the PRA has decided to introduce a requirement for firms to notify it when they apply the LTA or MBA to a material amount of exposures to CIUs that are managed outside the UK.²⁷

²⁴ Basel standards CRE60.1 – 60.20.

²⁵ This approach was consistent with the proposals made by HM Treasury to retain the jurisdictional equivalence provision set out in Article 132(3)(a) of the CRR.

²⁶ <https://www.gov.uk/government/consultations/implementation-of-the-investment-firms-prudential-regime-and-basel-3-standards-consultation>.

²⁷ New Article 132(8).

8.9 Any firm must notify the PRA if either:

- the total risk-weighted exposure amounts for all of its exposures in the form of units or shares in relevant CIUs²⁸ exceed 0.5% of the firm's total risk-weighted exposures for credit risk or dilution risk, or
- if the total exposure values for all of its exposures in the form of units or shares in relevant CIUs exceed £500 million.

8.10 Exposures must be calculated on an individual and a consolidated basis. Firms must notify the PRA whenever either of the thresholds is reached, and on an annual basis thereafter, until both the total risk-weighted exposure amounts and total exposure values are below the relevant thresholds. The notification should list all the countries in which fund managers of all relevant CIUs to which it is exposed are located, and the total exposure values and total risk-weighted exposure amounts in relevant CIUs for each of those countries.

8.11 The PRA considers that this notification would enhance the safety and soundness of firms, as it would inform the PRA about possible risks from a firm's exposure to funds located and managed in overseas jurisdictions. The PRA expects the cost to firms of reporting this information to the PRA would not be material.

8.12 The PRA notes that, as part of firms' Internal Capital Adequacy Assessment Process (ICAAP) assessments (detailed in SS31/15 'The Internal Capital Adequacy Assessment Process (ICAAP) and the Supervisory Review and Evaluation Process (SREP)'), the PRA expects firms to reflect the risks not captured or not adequately captured in Pillar 1 in their application of the existing Pillar 2 framework.²⁹ This includes material risks not addressed or adequately addressed in Pillar 1 that result from exposures to third country CIUs that are subject to supervision and regulation that differs from that applied in the UK.

Additional criteria for using the LTA and the MBA

8.13 The PRA's proposed additional criteria for using the LTA and the MBA includes a requirement for a CIU or its management company to report exposures at least as frequently as the PRA regulatory reporting requirement of the firm holding the CIU exposures.

8.14 Three respondents asked for clarification on how frequently information must be disclosed by a CIU or its management company in order for a firm to apply the LTA or MBA. Two respondents considered it should not be more frequent than quarterly.

8.15 After considering the responses, the PRA has amended its approach to clarify that reporting by a CIU or its management company on at least a quarterly basis is sufficient. Some elements of PRA regulatory reporting requirements apply on a monthly basis to certain firms. However, the PRA does not consider that it would be proportionate to require reporting from a CIU or its management company on a monthly basis in order to meet the relevant condition.

²⁸ A 'relevant CIU' is CIU to which a firm applies the LTA or MBA and is managed by a company which is registered in a third country.

²⁹ April 2021: <https://www.bankofengland.co.uk/prudential-regulation/publication/2013/the-internal-capital-adequacy-assessment-process-and-supervisory-review-ss>.

Application of LTA by firms applying IRB for credit risk

8.16 The PRA proposed to specify the approach to be used for equity exposures, securitisations positions, and all other exposures where a firm has permission to use the IRB for credit risk, but the conditions for using an IRB are not met for all or part of the underlying exposures of a CIU.

8.17 No responses were received in relation to these proposals. The PRA will therefore publish the policy as proposed.

Leverage adjustment

8.18 The PRA proposed an approach for firms to use in order to take leverage into account when calculating capital requirements for CIUs exposures. The PRA also proposed an alternative calculation for off-balance sheet exposures, and in cases where the accounting treatment specified in Article 132(7) of the Standardised Approach and Internal Ratings Based Approach to Credit Risk (CRR) Part of the PRA Rulebook applies.

8.19 No responses were received in relation to these proposals. The PRA will therefore publish the policy as proposed.

Reliance on third party calculations

8.20 The PRA proposed to allow firms to rely on the calculations of certain third parties where they do not have access to sufficient data to apply the LTA or the MBA.

8.21 One respondent requested clarification on the requirement for information in such cases to be verified by an independent third party, and confirmation of how this requirement would be applied.

8.22 After considering this response, the PRA has decided to maintain the requirement for verification of the information on the underlying exposures by an independent third party. The PRA considers this requirement generally appropriate to ensure the accuracy of data used for calculating capital requirements. The PRA considers that the PRA's waiver/modification power is available, and can be exercised, in individual cases, where the PRA considers that the application of the unmodified rule would impose an undue burden on a firm or would not achieve the purpose for which the rule was intended.

CIUs that invest in other CIUs

8.23 When an exposure of a CIU is an exposure to another CIU, the PRA proposed to permit the LTA to be applied to the underlying assets provided the relevant eligibility criteria are met. The PRA also proposed to implement restrictions on the approaches that can be applied to subsequent layers of investment in other CIUs.

8.24 No responses were received in relation to this proposal. The PRA will therefore publish the policy as proposed.

Exclusions

8.25 In line with the Basel III standard, the PRA proposed to exclude exposures to CIUs made under 'legislated programmes' to promote specified sectors of the economy. This exemption applies to legislated programmes that provide the institution with significant subsidies for the investment, and which involve some form of government oversight and restrictions on the equity investments.

8.26 Three respondents suggested a specific treatment for investments that are made to satisfy government requirements or to support government-endorsed investment programmes. This would

include cases where such investments may not qualify as legislative programmes under the Basel III standards.

8.27 After considering these responses, the PRA has decided to publish the policy as proposed. However, the PRA notes that exposures to these funds may benefit from HM Treasury's removal of the equivalence condition, as set out above.

Derivative exposures

8.28 The PRA proposed a simplified calculation in the MBA to calculate the requirements for counterparty credit risk (CCR). This approach is available where all the necessary information is not provided by the CIU. For both the LTA and MBA approach, the PRA also proposed a simplified calculation for the credit valuation adjustment (CVA) risk to a CIU's derivative exposures. The PRA also proposed to permit firms to exclude from a CVA capital requirement exposures to a CIU that would be excluded from the CVA requirement if the firm had a direct exposure to the relevant underlying assets.

8.29 Two respondents noted that fund mandates may not provide sufficient information on derivatives for exposures to those CIUs to meet the conditions to apply the MBA. As a result, the PRA's proposed approach may require the firm to apply the FBA for exposures to such funds.

8.30 The PRA has considered the responses and decided to maintain the policy as proposed. The PRA considers that for derivatives there is a simplified calculation that firms can use when all the required inputs are not available, and further considers that its proposed approach represents an appropriate balance between transparency, accuracy, and simplicity.

Definitions

8.31 The PRA proposed to define within PRA rules several terms set out in the Alternative Investment Fund Managers Regulations 2013, and to introduce a definition of the term UK UCITS (cross-referring to the definition in FSMA).

8.32 No responses were received in relation to these proposals. However, following HM Treasury's removal of the relevant CRR equivalence provision, the PRA will not introduce a definition of the term UK UCITS in its rules. The PRA will define the term 'relevant CIU' in PRA rules in order to specify the exposures in respect of which notification is required.

Other consequential changes

8.33 The PRA proposed that exposures to CIUs would not qualify as items associated with particular high risk.

8.34 No responses were received in relation to this proposal. The PRA will therefore publish the policy as proposed.

Other responses

8.35 Two respondents requested clarity on whether the approach is intended to apply to CIU exposures used as collateral, as well as to direct exposures. The PRA confirms that where Articles in the credit risk mitigation (CRM) section of the CRR refer to Article 132, they will remain unchanged, but will now relate to the updated version of Article 132.

8.36 One respondent pointed out a rule drafting error in relation to references to remaining CRR Articles. The PRA has considered the response and updated its approach to correct the error.

8.37 One respondent emphasised the importance of consistency across banking book and trading book treatments of CIUs. This is out of scope of the CP proposals and therefore has not been addressed in the PS, but may be considered further as part of future policy development.

8.38 Three respondents requested that the PRA clarify whether CIUs should be considered financial institutions, and therefore subject to prudential consolidation requirements. The CRR definition of financial institutions is out of scope of the CP proposals, and has therefore not been addressed in this PS.

9 Counterparty credit risk

9.1 The PRA proposed to implement new and updated methodologies for counterparty credit risk. These included the new Basel standardised approach for measuring counterparty credit risk exposures (SA-CCR), and a revised framework for capital requirements for firms' exposures to central counterparties (CCPs). They also included two simplified approaches (the simplified SA-CCR (sSA-CCR) and the original exposures method (OEM)) for smaller firms with limited derivatives exposures, to enhance the proportionality of the proposed framework.

SA-CCR

9.2 The CP proposed to replace the current Counterparty Credit Risk Part of the PRA Rulebook with the PRA's implementation of SA-CCR for firms that do not have permission to use the internal models method (IMM). SA-CCR improves upon the risk sensitivity of the existing non-modelled approaches by differentiating between margined and unmargined trades, as well as bilateral and cleared trades. It addresses known deficiencies³⁰ of the existing non-modelled approaches, and minimises discretion used by national authorities and firms. The PRA's main proposals on the technical aspects of the SA-CCR framework were as follows:

- On mapping transactions to risk categories and asset classes, the PRA proposed not to prescribe a specific methodology at this stage. The PRA proposed to consider whether further prescription may be necessary and appropriate in light of the experience of firms' implementation of the SA-CCR framework.
- The PRA proposed to add an additional 'other risks' category to provide flexibility for the future, in the event that asset classes are developed that cannot be readily mapped to one of the five categories.
- The PRA proposed to introduce a new 'climatic conditions' hedging set under the commodity risk category to ensure that transactions aimed at addressing climate risks are specifically identified and addressed.
- The PRA proposed to implement a λ adjustment to the supervisory delta equation for the interest rate risk category, to ensure the supervisory delta can be calculated in low interest rate environments.
- The PRA proposed not to refine further the Basel III standards' definitions of commodities at this stage. The PRA proposed to address such definitional risks on a case-by-case basis, and to consider whether further prescription in PRA rules is warranted in light of the experience of implementation of the framework.

9.3 Seven respondents commented on the SA-CCR proposals. Two responses were supportive of the implementation of a more risk-based standardised approach to measuring CCR exposures. One respondent supported the PRA's approach of not prescribing a specific methodology to mapping transactions to risk categories and asset classes at this stage. The section below outlines the PRA's feedback to the SA-CCR-related responses based on the comments received from the respondents. The responses focused in particular on:

³⁰ Deficiencies identified in the current approaches include that it did not sufficiently capture stress periods, and the recognition of netting benefits was too simplistic and not reflective of economically meaningful relationships.

- the aggregate impact of SA-CCR in the CCR framework;
- the impact of SA-CCR in other frameworks;
- potential impacts on derivative trades with commercial end-users (CEUs); and
- technical comments on the SA-CCR framework;

Aggregate impact of SA-CCR in the CCR framework

9.4 Three respondents highlighted potential increases in capital requirements resulting from the introduction of SA-CCR in the CCR framework. One respondent suggested that the introduction of SA-CCR could lead to a 50% increase in CCR risk-weighted assets (RWA) (based on 2017 data).

9.5 Linked to the potential capital impacts, respondents asserted that SA-CCR could:

- adversely affect the competitiveness of the UK (two responses);
- cause distortions in capital requirements when compared to those calculated under previous methods (one response); and
- impact market liquidity and hinder capital market development (one response).

9.6 The PRA undertook a quantitative impact study (QIS), and the results were presented in CP5/21. The PRA acknowledged in CP5/21 that the size and direction of the impact will depend on the characteristics of firms' portfolios (such as asset class, proportion margined and unmargined, direction, and netting arrangements), the proportion of those portfolios subject to the standardised approach rather than the IMM, and the proportion of trades subject to central clearing via qualifying CCPs (QCCPs). The CP identified that some large firms with significant trading activity are expected to experience reductions, and others increases, in RWA. This feature was a deliberate design choice in the Basel III standards to, among other things, incentivise central clearing. The analysis suggested that large and small firms predominantly undertaking lending are expected to see an increase in RWA of around £12.3 billion and £0.9 billion, respectively. In response, the analysis estimated that firms would be expected to raise CET1 capital resources by £1.6 billion.

9.7 Subsequent to the publication of the CP, the PRA updated the QIS and incorporated more recent estimates from firms of the SA-CCR impact. Consistent with the analysis in the CP, the PRA found that the SA-CCR impact varies considerably across firms. The new data that firms provided to the PRA showed a decreasing trend in the impact on some firms compared to the PRA's previous analysis. As a result, the PRA calculates that the total RWAs and CET1 capital resources impact on large and small firms predominantly undertaking lending is somewhat lower than that presented in the CP, and below the 50% presented by one respondent. In light of the above findings, the PRA considers that the assessment presented in the CP was a reasonable and conservative estimate of the impact.

9.8 Regarding the effect on the competitiveness of the UK, in July 2020, BCBS identified that 11 jurisdictions had a final SA-CCR rule in force and implemented by banks.³¹ In addition, at the time of publication of this PS, SA-CCR has come into force in the European Union. Mandatory adoption in the US for advanced approaches banking organisations is scheduled for 1 January 2022, having been optional in the US since April 2020. Given the number of jurisdictions that have already implemented

³¹ <https://www.bis.org/bcbs/publ/d506.pdf>.

SA-CCR, the PRA considers that implementing SA-CCR is unlikely to significantly affect UK competitiveness. The PRA further considers that delaying or reversing the proposal to implement SA-CCR would undermine the UK's commitment to implementing international standards to provide a global level playing field.

9.9 Regarding changes in capital requirements for derivatives when compared to current methodologies, the PRA considers that SA-CCR represents a necessary step forward to enhance the measurement of counterparty default risk. The current standardised methodologies (which SA-CCR replaces) were first introduced in the Basel I Accord. The existing methodologies have a number of limitations, and the PRA considers that these limitations themselves cause distortions, which SA-CCR is designed to address. As noted above, this includes a failure to capture stressed periods, and a failure to accurately reflect netting benefits or economic relationships. Furthermore, margined and unmargined transactions could not be appropriately differentiated. Given the development of central clearing for over-the-counter derivatives and introduction of mandatory margining rules after the 2008 financial crisis, the existing methodologies are no longer suitable for derivatives markets that have evolved and increased in size, scope, and complexity. Respondents did not provide analysis or evidence supporting the assertions of the adverse effect on the impact on market liquidity or capital market development. As discussed above, SA-CCR distinguishes between collateralised, uncollateralised, and over-collateralised trades on a relative basis as intended. The PRA considers that it is a more appropriate framework to estimate risks in capital markets.

9.10 Given the shortcomings in the existing standardised methodologies, the recent data showing a decreasing impact, the technical changes adopted below which will further reduce impact and align with Basel, and the progress in international implementation balanced against the concerns raised, the PRA considers that it is appropriate to proceed with the implementation of SA-CCR in the counterparty credit risk framework.

SA-CCR impact in other frameworks

9.11 Respondents raised concerns regarding the application of SA-CCR in other parts of the regulatory framework. This included requesting the PRA to conduct a further review before it is incorporated into: the large exposures and leverage ratio frameworks (four respondents), the output floor (two respondents), and the forthcoming CVA framework (two respondents).

9.12 The impact on the large exposure framework is considered in Chapter 11. The PRA notes that the responses related to the use of SA-CCR in other frameworks are outside the scope of the CP. The leverage ratio is subject to a separate consultation.³² The CVA framework and output floor will be considered as part of a future consultation on the implementation of Basel 3.1.

Potential impacts on derivative trades with CEUs

9.13 Respondents raised concerns that trades with CEUs could receive disproportionate capital requirements under SA-CCR. A number of reasons were identified:

- One respondent noted that SA-CCR does not recognise CEUs' investment grade status;
- One respondent noted that CEU trades are often unmargined, and CEUs often lodge collateral that would not qualify for credit risk mitigation (eg letters of credit, some types of security interests such as liens, and similar pledges).

³² CP14/21 'Consultations by the FPC and PRA on changes to the UK leverage ratio framework FPC Consultation Paper': <https://www.bankofengland.co.uk/prudential-regulation/publication/2021/june/changes-to-the-uk-leverage-ratio-framework>.

- One respondent noted that SA-CCR does not recognise the portfolio credit risk diversification benefits with exposures to CEUs, or the improved counterparty credit worthiness as CEUs hedge commercial risk through entering into derivatives contracts.
- Four respondents noted the international variations in implementation. In particular, three respondents commented that US prudential regulators had lowered the calibration of SA-CCR for derivative trades with CEUs by not applying the 'alpha' multiplier.³³ One respondent also noted that the EU did not have a CVA charge for CEUs.
- Two respondents noted concerns over the potential increased exposure from SA-CCR, including the calibration of 'alpha'.
- One respondent asserted that the risks that alpha is designed to capture in IMM (concentration risk, systematic market risk, and wrong-way risk) are not relevant for CEUs.
- One respondent noted that derivatives markets had undergone reform – through greater clearing and margining – since the calibration of alpha. The respondent asserted that it would not be consistent to apply a model uncertainty factor in IMM to the standardised approach, and that this would adversely impact counterparties where netting enforceability is not ensured.

9.14 Respondents suggested that the effects of the above would be:

- a potential increase in the costs of derivatives for CEUs (four respondents). This could in turn affect CEUs financial strength, competitiveness, and attractiveness to investors (one respondent); and
- a constraint on UK firms' capacity to support demand for derivative products at an acceptable cost (two respondents).

9.15 In the context of recovery from the Covid-19 pandemic, one respondent asserted that it is critical that CEUs can continue to hedge normal business risks, secure financing at reasonable rates, and continue to act to support economic growth.

9.16 Four respondents proposed a reduction or removal of the SA-CCR alpha multiplier for trades with CEUs to address the above concerns. This would reduce capital requirements for trades with these counterparties by approximately 30%. They suggested that changes to alpha should also apply to sSA-CCR and OEM. For these purposes, respondents proposed CEUs be variously defined as: those corporate counterparties out of scope of the mandatory margin requirements (two respondents); counterparties that are exempted from firms' CVA capital charge (one respondent); or any market participant other than a bank, an investment firm, or a hedge fund, including corporates and pension funds (one respondent).

9.17 Regarding the concerns raised over the recognition of various CEU characteristics in SA-CCR, the PRA notes that by design, the CCR framework does not incorporate investment grade status, nor does it set the collateral eligibility requirements for any counterparty; these are addressed in the credit risk and credit risk mitigation frameworks respectively. The CCR framework also does not adjust exposures by counterparties, such as CEUs. Instead, exposures are calculated based on the risks underlying instruments or portfolios, reflecting the legal framework. Characteristics of

³³ In SA-CCR (and IMM, the sSA-CCR, and OEM), the exposure calculation is multiplied, in a final step, by 1.4 ('alpha'). In IMM, 'alpha' is intended to increase capital requirements to address concentration risk, systematic market risk, and wrong-way risk.

individual counterparties, such as wider commercial risk, are assessed and incorporated into capital requirements in the next step in the capital calculation, that is, the credit risk framework.

9.18 Regarding the technical concerns about the need for the alpha multiplier, given the reforms in clearing and margining since SA-CCR was calibrated, the PRA considers that the SA-CCR framework has already incorporated changes in market practices. For example, it does so by providing greater recognition of margining in the calculation of exposures.

9.19 Regarding the overall impact on capital requirements on derivative trades with CEUs, the PRA notes that respondents generally highlighted the potential effects of SA-CCR in isolation when considering the impact on end-users, UK competitiveness concerns, and impacts on markets. The PRA considers that a holistic view of the capital requirements for derivative trades with CEUs is more appropriate, including the two frameworks that determine those capital requirements: the CCR framework and the CVA risk framework.

9.20 The CCR and CVA frameworks both contribute to the same objective: setting adequate capital requirements for derivatives exposures to counterparties. Therefore, looking at each component of the capital charge in isolation may not give the full picture with respect to prudential risks or competitive dynamics.

9.21 In that context, the impact of capital requirements for trades with CEUs should also acknowledge the current favourable capital treatment due to the various exemptions included in the CVA framework. At the point of implementation, capital requirements for derivative trades with CEUs that are below clearing and margining thresholds in the UK will consist of:

- a counterparty credit risk capital requirement (consistent with the international standard); and
- a 100% reduction in capital requirements for CVA (when compared to international standards). The UK is one of only two major jurisdictions globally to have exempted such trades from the CVA framework.

9.22 Given the current favourable treatment of derivative trades with CEUs under the CVA framework, the PRA considers that reducing the 'alpha' multiplier at this stage would in aggregate lead to material undercapitalisation of risks, and this would not be consistent with ensuring the safety and soundness of firms.

9.23 The FS Act grants HM Treasury the power to revoke aspects of the CRR to enable the implementation of the Basel 3.1 standards through rules made by the PRA, including own funds requirements for CVA risk. This will provide an opportunity to review capital requirements for derivatives exposures to CEUs holistically, including:

- the appropriate balance between CVA and SA-CCR capital requirements;
- the need for CVA exemptions and/or adjustments to the calibration of alpha; and
- ensuring that counterparty credit risks are captured appropriately, but not excessively, within the capital framework.

9.24 Ahead of this, the PRA has commenced a data collection from firms with derivatives activities to assess the impact of capital requirements (including CCR and CVA capital requirements) on different firms and counterparties.

Technical comments on the SA-CCR framework

9.25 Respondents commented on a number of technical aspects of the SA-CCR framework. These comments are detailed below alongside the PRA's feedback.

λ adjustment to the supervisory delta

9.26 In the CP, the PRA proposed to introduce a λ adjustment to the supervisory delta equation, consistent with the Basel III standards. This was to ensure the supervisory delta could be calculated in low interest rate environments, where interest rates could become negative. The adjustment would be applied at a currency level (ie all trades in the same currency would have the same adjustment, regardless of maturity or other characteristics).

9.27 One respondent welcomed this proposal, and two respondents suggested two changes. One change was to make it more risk-sensitive by applying it at a trade level, which would permit different adjustments depending on maturity/volatility of each derivative. The second proposal related to application of the adjustment to interest rates only. The respondents asserted that other asset classes could also have negative prices (eg commodities), so the approach should not be limited to one asset class.

9.28 The PRA considers that while applying the λ adjustment at trade level could improve accuracy, it would introduce significant complexity and reduce comparability across firms. Therefore, it is appropriate at this stage to remain aligned with the treatment in the Basel III standards and not make changes to the rules to apply the adjustment at trade level. On the second suggestion, the PRA agrees that other asset classes could also have negative prices. It would therefore be appropriate to allow the same approach to be applied so that it remains possible for the supervisory delta to be calculated in those circumstances. The PRA has amended the definition of λ in the rules to make it asset-class agnostic.

Basel FAQs on applying multiple margin agreements to a single netting set, and the liquidation period for collateral haircuts

9.29 The proposed rules did not provide for recognition of netting benefits for trades that are in the same netting set but subject to different margin agreements. Three respondents asked for the treatment to be aligned with a Basel FAQ that clarifies that some netting benefits can be recognised in this scenario.³⁴

9.30 The proposed rules also required firms to apply a one-year liquidation period to calculate haircuts on collateral received or posted for the replacement cost of unmarginated netting sets. Three respondents suggested the text be adjusted to align with a Basel FAQ, which would permit shorter liquidation periods where trades in the netting set have a maximum maturity of less than one year.³⁵

9.31 The PRA considers that implementing these changes would provide a closer alignment between capital requirements and risk without undermining the safety and soundness of firms, and would improve alignment with the Basel III standards. Consequently, the PRA has aligned the rules with the BCBS clarifications.

Basel clarification on the treatment of one-way margin agreements

9.32 The proposed rules were not explicit on the treatment of variation margin posted in one-way margin agreements. The Basel III standards specify that netting sets that include margin agreements

³⁴ FAQ 1 for CRE 52.74.

³⁵ FAQ 1 for CRE 52.10.

that require the firm to post variation margin to a counterparty, without the entitlement to receive variation margin from the same counterparty, should be treated as unmargined. The variation margin posted should be recognised as an exposure to the counterparty for the purpose of calculating the replacement cost. One respondent suggested this treatment be clarified in PRA rules. This clarification would provide a prudent clarification of the rules and closer alignment with Basel III standards. The PRA has therefore clarified the treatment in the rules, and extended this treatment to sSA-CCR to ensure consistency.

Flexibility in using firms' own definitions and methodologies

9.33 SA-CCR is designed as a standardised measurement of counterparty credit risk exposure. In several areas, it provides fixed definitions and calculation methodologies. One respondent suggested that firms should be allowed to use internal definitions to calculate the adjusted notional of derivatives where the definitions may be difficult to apply to certain contracts. This would align with firms' estimates of risk. The respondent suggested firms should also be allowed to use their internal methodologies to determine another input to the SA-CCR calculation – the supervisory delta – non-linear derivatives transactions.

9.34 The PRA considers that, as a standardised approach, SA-CCR must balance risk sensitivity with the need for it to be a simple and prudent methodology that produces consistent outcomes across a wide range of firms. The suggestions that the respondent made would introduce additional complexity, and reduce comparability across firms. The PRA considers that adding additional flexibility or complexity in these areas is not consistent with the aims of a standardised methodology, and has not adjusted the rules to introduce this flexibility.

The treatment of settled-to-market (STM) derivatives

9.35 The proposed rules distinguished between the treatment of margined and unmargined netting sets. Under the proposals, where payment of variation margin legally settles the contract, the contract is treated as unmargined. Where payment of variation margin is legally treated as collateralisation of the contract, the contract is treated as margined. Under the first approach, known as 'settled-to-market' (STM), the maturity of the contract is typically shorter (until the next settlement date), and the party posting variation margin has no right to receive any settled amount. In the second case, known as collateralised-to-market (CTM), trades do not settle, so maturity is typically longer, and variation margin is simply topped-up/repaid over the life of the contract, and set-off against any losses in default events. Under the proposed rules, CTM and STM trades would have to be split into two sub-netting sets, one margined and one unmargined, reflecting their different legal status.

9.36 One respondent proposed that banks should be able to elect to treat cleared STM derivative contracts as if they were cleared CTM derivative contracts. The respondent commented that the proposed treatment does not reflect the economic reality of these transactions where economically equivalent transactions should be subject to the same treatment. The respondent also suggested that, given the approach in another major clearing jurisdiction, the PRA should adopt a similar approach in the interest of a level playing field. The respondent asserted that allowing firms the option to treat cleared STM derivatives contracts as CTM contracts in the same netting set would allow a greater degree of netting to be applied, offsetting a higher maturity factor for CTM trades.

9.37 The PRA notes the different treatments between economically similar, but legally different, transactions. The different treatments between STM and CTM trades are, however, justified as reflecting their legal differences (for example, the fact that under STM the party posting collateral has no right to have it returned). Trades that settle when margin is exchanged have less legal risk, and benefit from a lower maturity factor. The PRA considers that the respondent's suggestion to

allow firms to choose, among other things, the most favourable treatment under different scenarios, would undermine safety and soundness. Allowing netting across trades with different legal status could underestimate risk. It would also reduce comparability and introduce more variability into the standardised framework. Therefore, the PRA has decided not to make any changes to this aspect of the rules.

Index decomposition

9.38 The proposed rules treat index positions differently from single-name equity and credit derivatives that reference specific entities or issuers directly. Two respondents suggested that the rules should permit firms to decompose equity, credit, and commodities indices into their underlying constituents. This would enable these underlying positions to be combined with any direct exposures to the same entities to increase hedging benefits.

9.39 The PRA notes that equity and credit index exposures already have a specific, generally favourable, treatment relative to exposure to single-name equity and credit derivatives. Permitting firms to decompose index positions into equivalent positions in the underlying constituents could underestimate risk in some areas, for example the risk that indices do not perfectly track the performance of the underlying constituents. On balance, the PRA considers that permitting index decomposition will introduce complexity, reduce comparability, and potentially lead to risks not being adequately capitalised. Therefore, the PRA has decided not to make any changes in this regard.

Treatment of unsettled margin

9.40 Consistent with the Basel III standards, the proposed rules allowed margins received to reduce exposures, but did not explicitly specify whether the unsettled variation margin could be included in this calculation. Normally, there is a delay between collateral being called and received. As part of the Covid-19 response during 2020, the PRA clarified in SS12/13 that firms may recognise unsettled collateral in their internal models for counterparty credit risk, where the collateral remained unsettled due to the ordinary collateral call and normal settlement cycles. This clarification was introduced to minimise the procyclicality of CCR RWAs during the crisis.

9.41 One respondent proposed the above treatment be extended to SA-CCR to ensure consistency across approaches going forward. The PRA has considered the response and recognises the benefits of an alignment between IMM and SA-CCR, and continues to support the efforts to reduce procyclicality. However, there is a risk with unsettled margin. SS12/13 expects IMM firms to monitor and hold capital against this risk. The PRA considers, given the range of sophistication of firms that may use the SA-CCR, that it may be challenging for all to meet these requirements. Given these risks, the PRA has decided not to make any changes to the policy as proposed, but may consider this issue further in the future.

Non-nettable trades

9.42 One respondent requested clarification of how to treat trades that are combined under a single master agreement, but where a portion of, or the entire trade population, under the agreement is non-nettable. The respondent suggested a number of alternative treatments under different scenarios. The PRA considers that this is a specific technical issue with limited scope and impact and would benefit from further analysis in the absence of a clear technical solution in the Basel standards. As a result, the PRA has decided not to make any changes at this stage.

Other responses

9.43 One respondent pointed out an omission in the proposed Article 279c of Section 3 of Chapter 3 of the Counterparty Credit Risk (CCR) Part of the PRA Rulebook, where some of the variables for the calculation of the maturity factors were not clearly defined. This error has been corrected.

9.44 Two respondents raised a number of design and calibration issues on the SA-CCR framework, which they suggested could be included in any future review by the BCBS. The PRA has not provided feedback to these responses, as they were outside the scope of the consultation.

Proportionality

9.45 The PRA proposed that smaller firms meeting specific thresholds would have the option to consider using simplified methodologies to calculate counterparty credit risk exposures: the simplified SA-CCR (sSA-CCR) and the OEM. This was designed to ensure that the counterparty credit risk framework would remain proportionate for firms with limited derivatives exposures. The proposed approaches would be simpler than, but at least as conservative as, SA-CCR. As a result, they would offer a robust but proportionate alternative to implementing SA-CCR.

9.46 Two respondents welcomed the proposals and supported the PRA's efforts to enhance proportionality for smaller firms. Other respondents suggested a number of amendments, which are detailed below.

Thresholds calculation

9.47 The CP proposed a specific set of thresholds under which smaller firms would qualify to use simplified methodologies for calculating CCR exposures. The thresholds were calibrated based on the size of firms' on- and off-balance-sheet derivatives business.

9.48 One respondent asked for further clarification on how the 'size' should be defined. The PRA notes that the relevant details are in Article 273a(3).

Transitional period between methods

9.49 The proposed rules would require firms to implement the more complex methodology within three months if they cease to be eligible for either of the simplified methodologies (ie by breaching the relevant threshold).

9.50 One respondent raised the concern that three months to implement new methodologies could be operationally challenging for some small firms, and a longer transitional period of at least six months should be permitted. The respondent asserted that this would support more effective proportionality in practice.

9.51 The PRA has considered the response and, given that the simplified methodologies are generally more conservative, it does not expect any material prudential risk to arise from allowing a longer transitional period for moving to more complex methodologies. The PRA considers that allowing sufficient time for firms to switch to more advanced methodologies could help to improve the accuracy of risk measurement and result in more robust regulatory compliance, without imposing a disproportionate operational burden on small firms. The PRA has therefore amended the rules to allow a six-month transitional period.

9.52 The PRA did not receive any other comments on its proposals in relation to the sSA-CCR and the OEM. The PRA will therefore publish the policy as proposed.

Capital requirements for exposures to central counterparties

9.53 In the counterparty credit risk framework, firms transacting with QCCPs benefit from a significantly lower capital requirement. The Basel III standards revised the methodology for calculating capital requirements on firms' exposures to QCCPs, and the proposed rules implemented this Basel revision. The CP also proposed some consequential amendments to SS12/13 to update the list of CCPs that could be treated as QCCPs.

9.54 The proposed amendments to SS12/13 specified that QCCPs are identified as: (i) authorised CCPs; (ii) recognised third-country CCPs, including third-country CCPs that enter the Temporary Recognition Regime (TRR) in accordance with the Central Counterparties (Amendments, etc., and Transitional Provision) (EU Exit) Regulations 2018; and (iii) any other third country CCPs benefiting from the transitional provisions under Article 497 of the CRR.

9.55 One respondent commented that linking the prudential QCCPs status with the UK QCCP recognition and authorisation regime in SS12/13 is unnecessary and could create a cliff-edge in UK firms' capital requirements if they are members of third country CCPs that lose UK QCCP recognition. A CCP may be authorised in other jurisdictions and follow the relevant standards to be a QCCP. Without UK recognition, any UK clearing members (or branches in third countries) would not benefit from lower capital requirements. The respondent commented that third country QCCPs supervised in home jurisdictions with established domestic rules and regulations consistent with relevant international standards should automatically be recognised as QCCPs for prudential purposes in the UK.

9.56 The PRA has considered this response but notes that the consequential amendments made in SS12/13 do not represent a policy change from the current approach. Due to the wide coverage of the existing transitional arrangements, the PRA expects no immediate impact on UK firms. Given the preferential treatment on firms' exposures to QCCPs, the PRA considers that there are prudential benefits in linking QCCP status to the UK recognition and authorisation regime, including the associated strengthened supervisory oversight. The PRA therefore has decided to maintain its approach. However, the PRA may review this link in the future.

Consequential amendments to SS12/13 'Counterparty credit risk' and SoP 'The PRA's methodologies for setting Pillar 2 capital'

9.57 As a result of the proposed changes to implement the relevant Basel III standards, the PRA proposed consequential amendments to SS12/13 'Counterparty credit risk', including updating the list of CCPs that could be treated as QCCPs for calculating firms' exposures to CCPs. The PRA also proposed changes to Chapter 5 of the SoP 'The PRA's methodologies for setting Pillar 2 capital', to remove references to existing standardised approaches to measuring counterparty credit risk exposures. The PRA received one comment on the consequential amendments to SS12/13, in relation to the identification of QCCPs. This is discussed above in paragraph 9.55. No responses were received in relation to the proposed changes to the Pillar 2 SoP. The PRA will therefore publish the policy as proposed.

Implementation date and transitional arrangements

9.58 The PRA proposed to implement the final rules in this Chapter with an effective date of Saturday 1 January 2022. The PRA did not receive any responses to this proposal and has therefore finalised the implementation date as proposed. The PRA considers the temporary transitional power not to be applicable, as these rules are introduced to implement new Basel III standards in the UK, rather than restating existing CRR provisions (for further details on the temporary transitional power, see Chapter 17).

10 Operational risk

10.1 The PRA proposed to restate provisions in relation to the Business Indicator Approach (BIA) in PRA rules.³⁶ It proposed to modify requirements for the calculation of the Relevant Indicator (RI) to permit firms to include interest income and expenses from financial and operating leases in the calculation of the RI.

10.2 The PRA received two responses to this proposal. One respondent agreed that it is desirable to restate the BIA provisions as proposed. The second respondent did not consider it necessary to revoke this aspect from the CRR, and suggested that the same effect could be achieved by the PRA providing guidance on the application of the RI instead. The respondent also asked for clarification regarding the scope of the proposed change, considering it to be appropriate not only to the BIA but also to the Standardised Approach (SA) to Operational Risk.

10.3 Having considered the responses, the PRA has decided to maintain its proposal and transfer Article 316 of the CRR to PRA rules. This approach is consistent with the PRA's overall approach to the implementation of Basel III standards.

10.4 The PRA also clarifies that the modifications to the calculation of the RI are applicable under the SA. Article 317(2) of the CRR references use of the RI in the SA calculation; the SA will consequentially reference the amended RI, and no changes are required under the SA framework.

³⁶ Article 316 of the CRR.

11 Large exposures

Incorporation of large exposures requirements from the CRR

11.1 The PRA proposed to transfer the following items into the PRA Rulebook:

- (a) the large exposure requirements as set out in Part Four of the CRR; and
- (b) Regulation No. 1187/2014 for determining the overall exposures to a client or a group of connected clients in respect of transactions with underlying assets.

11.2 The PRA proposed to restate in the PRA Rulebook most of the requirements in the Large Exposures Part of the CRR, but also proposed not to replicate certain discretionary requirements that the PRA has not exercised³⁷ and provisions that place requirements on the PRA rather than on firms. The PRA also proposed to implement new Basel III standards on large exposures through amendments to:

- the definition of capital;
- the calculation of exposure values;
- the definition of an institution;
- reporting requirements;
- exposures to globally systemically important institutions (G-SIIs);
- credit risk mitigation (CRM); and
- exemptions from large exposures limits.

11.3 The PRA received seven responses in total relating to its large exposures proposals. One respondent commented in support of the restatement of the CRR Large Exposure provisions in the PRA Rulebook.

11.4 Four respondents commented on discretions available under the CRR covering:

- (a) the potential application of Credit Conversion Factors (CCFs) to off-balance sheet items when calculating the exposure amount for large exposure purposes; and
- (b) the potential full or partial exemption of certain covered bond exposures from large exposures limits.

11.5 The PRA did not exercise these discretions under CRR, EU Regulations, or Directives. These discretions were out of scope of CP5/21. Therefore, the PRA is not providing feedback to these responses, but may consider the points raised in future policy development.

11.6 Two respondents referred to the CRR provision that allows the large exposure limit to be exceeded for items in the trading book.³⁸ They stated that it is clear that the trading book exposures

³⁷ Articles 388, 390(8), 390(9), 394(4), 395(1A), 395(6), 400(2) (a)–(b), (d)–(f), and (i)–(k) of the CRR.

³⁸ Article 395(5) of the CRR.

include counterparty credit risk, but asked that this could be made explicit in the rules.³⁹ The respondents also suggested some amendments. Having considered the responses and suggested amendments, the PRA considers that the existing provision is sufficiently clear and therefore has decided not to change the policy as proposed.

11.7 Two respondents referred to the exemption for exposures to sovereigns that receive a 0% risk weight under the SA-CCR. Exposures to certain sovereigns are assigned a 0% risk-weight where the exposures are ‘denominated and funded in the domestic currency’.⁴⁰ The respondents considered that the term ‘denominated and funded in the domestic currency’ is ambiguous. These provisions are within the CRR and were outside the scope of the CP. The PRA may consider the points raised in future policy development.

11.8 The rules on determining the overall exposure of transactions with underlying assets specify the methodologies for determining a firm’s exposure to the underlying assets, and whether the firm has an additional exposure to the transaction itself. If a transaction has legal and operational structures in place to prevent the redirection of cash in the transaction to persons who are not entitled to receive them, the firm is not considered to have an additional exposure to the transaction. Under Regulation 1187/2014 and the PRA’s proposed approach, UK UCITs and similar structures in an equivalent third country are automatically assumed to meet this condition. Two respondents asked which list of equivalence determinations should be used for this purpose, and considered that the equivalence provision for CIUs in the credit risk framework could be used.⁴¹

11.9 As set out in Chapter 8 of this PS, HM Treasury has decided to remove the equivalence provision for CIUs in the credit risk framework.⁴² The PRA will review this provision in light of this amendment and will consider it as part of future policy development. Until the PRA has conducted this review, firms can continue to treat similar structures in third countries, which would have been considered equivalent under the current provision, as meeting the conditions set out above.

Definition of capital

11.10 The PRA proposed to amend a Tier 1 definition of capital that will cover the definition of a large exposure and the limits applied. One respondent stated that they are content with the change from eligible capital to Tier 1 capital. Three respondents highlighted that the proposed rules on determining the overall exposure of transactions with underlying assets refers to eligible capital rather than Tier 1 capital.⁴³ The PRA considers that for all aspects of large exposures, one definition of capital should apply, and will amend these references to Tier 1 capital.

Calculation of the exposure value

Retained provision

11.11 The PRA proposed to retain the substance of CRR requirements that are not being amended for covering the calculation of the exposure value, but to amend the paragraph order of some of these provisions.⁴⁴ The PRA received no responses to this proposal and will therefore publish the policy as proposed.

³⁹ Article 397 of the CRR.

⁴⁰ Article 114(4) and (7) of the CRR.

⁴¹ Article 132 of the CRR.

⁴² HM Treasury ‘Implementation of the Investment Firms Prudential Regime and Basel 3 standards: Consultation Response’, June 2021: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/995628/OFFICIAL_-_MARKET_SENSITIVE_Prudential_Consultation_Updated_220621.pdf.

⁴³ Large Exposures (CRR) – Chapter 5 Article 6.

⁴⁴ Article 390 of the CRR.

Exposures deducted from capital

11.12 The PRA proposed that amounts deducted from Tier 2 capital would be included in the definition of exposures for large exposure purposes. The PRA received no responses to this proposal and will therefore publish the policy as proposed.

Calculation of exposure value for derivatives

11.13 The PRA proposed that total exposures to a client must include the exposures arising from derivative contracts and credit derivative contracts, where the contract was not directly entered into with that client, but the underlying debt or equity instrument was issued by that client.⁴⁵

11.14 The CRR contains a provision for the PRA to make draft regulatory technical standards on how to determine the indirect exposures arising from derivative contracts and credit derivative contracts.⁴⁶ The PRA did not propose to transpose these provisions into the PRA Rulebook given that it is not a requirement on firms. One respondent asked for clarity and for the PRA to provide guidance and technical standards on these aspects. The PRA will consider clarifying these aspects as part of future policy development.

11.15 The PRA proposed that firms could continue to use the method for determining the exposure value for derivatives that they are using for risk-based capital requirements, but not be permitted to use the internal model method (IMM) for large exposure methods.

11.16 One respondent stated that they consider the use of SA-CCR in its current form to be inappropriate for large exposure purposes, and recommended continuing to permit the use of IMM for large exposures purposes. They suggested that for intragroup exposures, both SA-CCR and the simultaneous reduction in eligible capital could make the existing limits much more restrictive, even though the real risk is unchanged. They requested that the PRA consider recalibrating the limits applied to intragroup large exposures. Two respondents also suggested that applying the full large exposures exemption that is allowable under the CRR to intragroup exposures would provide additional flexibility. One respondent also suggested that SA-CCR should be used on a standalone basis before using it in other areas of the prudential framework. Another respondent urged the PRA to consider a review of the impact and the appropriateness of SA-CCR before it is implemented in other parts of the capital framework. The respondent suggested that this review should consider adjustments and design improvements to SA-CCR that take account of its impact beyond capital requirements for counterparty credit risk.

11.17 The PRA considers that the use of SA-CCR is appropriate for large exposure purposes and aligns with the objective of the large exposure framework, which is to capture the peak loss that a firm could potentially suffer if a client or a group of connected clients were to default. The PRA has assessed the impact of SA-CCR on firms' large exposures to third parties and found it generally not to be material. However, the PRA identified that the impact of moving from IMM to SA-CCR could have a material impact on a number of firms' intragroup exposures and subsequent additional own fund requirements for large exposures in the trading book. After considering the responses, the PRA will publish the policy as proposed. However, in cases in which the impact of applying SA-CCR for large exposures purposes has a significant impact on a firm's large exposures to its non-core large exposures group (NCLEG), the PRA would consider applications to modify the relevant NCLEG limits to offset the impact of applying SA-CCR rather than IMM.

⁴⁵ Article 390(5) of the CRR.

⁴⁶ Article 390(9) of the CRR.

Calculation of exposure value for securities financing transactions (SFTs)

11.18 The PRA proposed that firms that have permission to use the IMM could continue to use it for calculating the exposure value for SFTs.

11.19 Three respondents stated that the references to SFTs in the CRR provision are unclear.⁴⁷ The PRA agrees that clarification is needed and therefore has amended the provision to specify the calculation methods that can be used for SFTs.

Netting long and short positions

11.20 The PRA proposed that firms would still be permitted to offset long and short positions in the same financial instrument, as well as for different instruments issued by a given client. This is provided that the short position was junior or equal in seniority to the long position.

11.21 Two respondents stated that it is not clear whether indirect exposures would be subjected to the netting provisions as set out in PRA rules.⁴⁸ The PRA considers that the CRR provision distinguishes between direct and indirect exposures where a distinction is needed. Where the provision refers to 'exposures', the PRA considers it clear that both direct and indirect exposures are relevant. The PRA has therefore decided not to change the policy as proposed, but can confirm that indirect exposures are subject to the netting provisions.

Definition of an institution

11.22 For large exposures purposes, the CRR includes in the definition of an 'institution' non-UK investment firms which: (i) would qualify as an 'institution' if they were established in the UK; and (ii) are subject to prudential supervisory and regulatory requirements at least equivalent to those applied in the UK.⁴⁹ The PRA proposed to restate the institution definition in the PRA Rulebook, but to amend it to reflect the CRR requirement that equivalence decisions are made by HM Treasury.

11.23 One respondent stated that the instructions for reporting on large exposures and concentration risk⁵⁰ refers to the definition of 'institution' as set out in the definitions for CRR,⁵¹ but that a separate definition of an institution is included in the Large Exposures Part of the CRR.⁵² They asked for clarification of the purpose of each definition that would be used in the large exposures framework and reporting.

11.24 Three respondents raised concerns that non-EEA firms would not qualify as institutions for large exposure purposes. As a result, under the proposed approach, they could be required to report exposures to those entities as exposures to shadow banks.

11.25 Having considered the responses, the PRA has decided to publish the policy as proposed. The CRR definition of an institution includes credit institutions and investment firms where those investment firms are subject to UK requirements.⁵³ The purpose of the provision in the Large Exposure Part is to widen the scope of the term 'institution' to include entities that are not subject to requirements imposed by the UK, but would fulfil the definition of the term 'institution' were it established in the UK and authorised in an overseas jurisdiction that has been determined to be equivalent. For the purposes of large exposures, the large exposure limit that applies to 'institutions' would also apply to these overseas entities that meet the condition.

⁴⁷ Article 390(4) of the CRR.

⁴⁸ Article 390(3) of the CRR

⁴⁹ Article 391 of the CRR.

⁵⁰ Paragraph 12 of Annex IX – Instructions for reporting on large exposures and concentration risk.

⁵¹ Article 4(1)(3) of the CRR.

⁵² Article 391 of the CRR.

⁵³ UK legislation that implemented [Directive 2014/65/EU](#).

11.26 HM Treasury has confirmed its intention to put in place a transitional measure whereby firms can continue to use the equivalence determinations under other articles in the CRR for large exposure purposes.⁵⁴

Reporting requirements

11.27 The PRA proposed to introduce a requirement for firms to report on their ten largest exposures, on a consolidated basis, to shadow banking entities that carry out banking activities outside the regulated framework. One respondent noted that the PRA did not include the current CRR requirement to report the ten largest exposures on a consolidated basis to institutions and asked whether this was intentional. The PRA confirms that it omitted in error the current CRR requirement for reporting on exposures to institutions. The PRA will amend the rules to maintain the current reporting requirement of a firm's ten largest exposures to institutions on a consolidated basis, as well as to include the new requirement to report its ten largest exposures to shadow banking on a consolidated basis.

11.28 The CRR contains a provision for the PRA to make technical standards on the criteria for the identification of shadow banking entities.⁵⁵ The PRA did not propose to include these provisions in the PRA Rulebook, given that it is not a requirement for firms. One respondent asked for clarity on whether the PRA proposed to provide guidance and technical standards on these criteria. The PRA has considered this response and has decided not to change its approach. The Bank of England and the PRA have set out their approach to EU guidelines and recommendations after the UK's withdrawal from the EU.⁵⁶ Firms can continue to apply the definition of shadow banking entities as set out in the EBA's guidelines on limits on exposures to shadow banking entities.⁵⁷ However, the PRA will consider providing guidance on the criteria for identifying shadow banking entities as part of future policy development.

Exposures to G-SIIs

11.29 The PRA proposed to limit to 15% of Tier 1 capital any exposure of a G-SII for which the PRA is the lead supervisory authority to another G-SII.

11.30 The PRA received no responses to this proposal and will therefore publish the policy as proposed.

Credit Risk Mitigation

Eligible credit mitigation techniques

11.31 The PRA proposed that credit risk mitigation techniques that are available only to firms using one of the IRB approaches should not be used to reduce exposure values for large exposure purposes, except for certain exposures secured by immovable property.

11.32 The PRA received no responses to this proposal and will therefore publish the policy as proposed.

⁵⁴ HM Treasury 'Implementation of the Investment Firms Prudential Regime and Basel 3 standards: Consultation response', June 2021: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/995628/OFFICIAL_-_MARKET_SENSITIVE_Prudential_Consultation_Updated_220621.pdf.

⁵⁵ Article 394(4) of the CRR.

⁵⁶ 'Interpretation of EU guidelines and recommendations: The Bank of England and the PRA approach after the UK's withdrawal from the EU', December 2020: <https://www.bankofengland.co.uk/-/media/boe/files/paper/2019/interpretation-of-eu-guidelines-and-recommendations-boe-and-pra-approach-sop-december-2020.pdf>.

⁵⁷ 'Guidelines on limits on exposures to shadow banking entities': <https://www.bankofengland.co.uk/-/media/boe/files/paper/2020/december/Guidelines%20on%20limits%20on%20exposures%20to%20shadow%20banking.pdf>.

Calculating the effect of the use of credit risk mitigation techniques

11.33 The PRA proposed that for calculating the effect of using credit risk mitigation, firms use the Financial Collateral Comprehensive Method (FCCM), regardless of the method used for calculating the own funds requirement for credit risk, with the exception of firms using the Financial Collateral Simple Method.

11.34 The PRA received no responses to this proposal and will therefore publish the policy as proposed.

Substitution approach

11.35 The PRA proposed to apply a mandatory substitution approach and to allow firms to choose to either report the exposure to a collateral issuer or the full amount of the limit that the firm has instructed its tri-party agent to apply to securities issued by the collateral issuer. Five respondents commented on the mandatory substitution approach.

11.36 Three respondents questioned the economic rationale for the substitution approach and one respondent was concerned that this could lead to reduction in liquidity in the repo market. Two respondents stated that the risk-weight requirement could give rise to a perverse incentive to source lower quality collateral or to undertake unsecured lending to avoid large exposure breaches. Four respondents considered that sovereign exposures should not fall within the scope of mandatory substitution requirements, and that the framework should not constrain the use of government bond collateral.

11.37 Four respondents stated that the rules contained significant ambiguities, which would likely lead to inconsistent implementation. Specifically, they thought it was unclear whether the substitution approach should be applied in cases where the FCCM or master netting agreements (MNA) are used, or how it should apply for different transaction types such as securities financing transactions and collateralised derivatives. One respondent requested additional clarification on how to calculate additional own funds requirements for large exposures in the trading book for an exposure that is assigned to a collateral provider or guarantor.

11.38 One respondent suggested that additional time beyond January 2022 is required to build reporting capabilities and to allow banks time to reposition their portfolios in order to comply with the new large exposures framework.

11.39 One respondent recognised the need for banks to be able to aggregate exposures across direct exposures and exposures through collateral and guarantees. This respondent proposed that the rules be clarified, followed by a period of reporting and time for calibration/adaptation of business models, before subjecting collateral and received guarantees to the large exposure limit.

11.40 Having considered these responses, the PRA has decided not to implement the proposed substitution approach at this time. Although the PRA considers that the mandatory substitution approach is an important change to the large exposures framework in order to limit large concentrations to collateral issuers, the PRA agrees that further policy development is needed to specify its application in more detail. This will also allow more time in order for the PRA to conduct further assessment of its potential impact. The PRA has amended its approach to maintain the current optional substitution approach.

11.41 The PRA did not receive any comments on the proposal to allow firms to choose either to report the exposure to a collateral issuer or the full amount of the limit that the firm has instructed

its tri-party agent to apply to securities issued by the collateral issuer. The PRA will therefore publish the policy as proposed.

Consequential amendments

11.42 In order to implement the relevant Basel III standards, the PRA proposed consequential amendments to SS16/13 'Large Exposures'.

11.43 The PRA received no comments on the proposed changes to SS16/13 and will therefore publish the SS as proposed.

Other amendments

11.44 During the consultation period, the PRA identified an error in the draft Large Exposures (CRR) Part of the PRA Rulebook. In the list of exposures that are exempt from the application of large exposure limits, the draft rule incorrectly included an exemption for minimum value commitments that meet conditions set out in the CRR.⁵⁸ Given that there are no provisions for minimum value commitments in the CRR, this exemption will be deleted. The PRA has not proposed a specific treatment for minimum value commitments and they are not otherwise addressed in the CRR.

Other responses

11.45 In 2019, the PRA introduced a reciprocal measure to place stricter limits on exposures from UK G-SIIs and other systemically important institutions (O-SIIs) to certain 'highly-indebted' French non-financial corporations, similar to the measure imposed by the Haut Conseil de stabilité financière (HCSF) in France in 2018. This was done on macroprudential grounds. Two respondents questioned whether this measure is still required, given the UK's departure from the EU, and asked that it be discontinued. The PRA considers that this measure is in line with the Financial Policy Committee's previously stated intention of reciprocating foreign non-countercyclical capital buffer (CCyB) macroprudential capital actions where appropriate. It recognises both the likely benefits to UK financial stability and maintains consistency with its approach to reciprocating other jurisdictions' CCyB rates. The PRA considers that the measure is not affected by the UK's departure from the EU.

11.46 The PRA received a number of responses on provisions that are currently in the CRR or in the reporting instructions that are being restated in PRA rules without amendments. One respondent asked for the PRA to review its discretion on exemption of intragroup exposures from large exposures limits. Three respondents commented on the potential exemption of exposures to sovereign entities that are not assigned a 0% risk-weight under the SA-CCR. One respondent asked to remove the existing reporting requirement for exposures that are greater than €300 million in order to reduce the reporting burden on firms. The PRA considers its current approach to be prudent and appropriate and will publish the policy as proposed.

11.47 One respondent considered that the provisions on the netting of collateral within the Basel rules lack clarity. The PRA has not provided feedback to this response as it was outside the scope of the CP.

⁵⁸ Article 400(1)(n) of the CRR.

12 Liquidity coverage ratio

12.1 The PRA proposed to:

- replicate in PRA rules the LCR requirements of the CRR and Delegated Acts by introducing a new Liquidity Coverage Ratio (LCR) Part of the PRA Rulebook and Liquidity (LCR) Part of the PRA Rulebook;
- restate the definitions from the CRR in the Liquidity (LCR) Part, and introduce and clarify a number of definitions that apply to the LCR requirements;
- amend the notification and reporting requirements in the event a firm's LCR or NSFR falls below 100%; and
- replicate LCR permissions from the CRR in PRA rules, and set out the factors that the PRA proposes to consider when assessing permission applications, in a new Statement of Policy (SoP) 'Liquidity and funding permissions'.

Implementation of the LCR in PRA Rules

12.2 The PRA proposed to replicate in PRA rules the LCR requirements of the CRR and Delegated Acts. In doing so, the PRA proposed to make a variety of amendments to ensure the requirements work effectively within PRA rules.

12.3 One respondent supported the transposing of the LCR into the PRA Rulebook. Another respondent generally supported the introduction (restatement) of the LCR in PRA rules, but – citing the Historical Look-Back Approach (HLBA) and the treatment of gold – stated that some elements of the LCR require a reconsideration or recalibration of their methodology (see section on 'Other comments' below).

Permissions

12.4 The PRA proposed to replicate LCR permissions in PRA rules. The PRA set out the factors to which the PRA proposes to have regard when considering relevant applications for permission, in a new proposed SoP on liquidity and funding permissions.

12.5 One respondent commented on the LCR permission⁵⁹ that allows firms to calculate a liquidity outflow net of an interdependent inflow, subject to certain conditions being met. The respondent stated that the LCR is not clear on how conditional cash flows could be treated where there are contractual pass-throughs. They considered a case-by-case permission to net interdependent flows to be highly onerous, and would prefer requirements that provide for the automatic netting of pass-through cash-flows where certain conditions are met.

12.6 The PRA has considered the response and has decided not to change its approach. Given the significant reduction in liquidity requirements that are afforded by the IA&L permission, the PRA considers a permissions process to be prudent and proportionate.

Other outflow rates

12.7 In CP5/21, the PRA proposed not to prescribe the outflow rates for certain products and services,⁶⁰ including credit cards, overdrafts, stable retail deposits, and other retail deposits. As a

⁵⁹ Article 26 of the CRR.

⁶⁰ As set out in Liquidity Coverage Ratio (LCR) Articles 23–25.

result, the PRA removed certain provisions that relate to outflow rates from these Articles when restating them in PRA rules.

12.8 Three respondents requested clarity as to the PRA's policy on reducing the outflow rate applicable to stable retail deposits from 5% to 3%. Two respondents noted that the PRA's proposed rules did not restate an authorisation that allowed competent authorities to permit the use of the 3% outflow rate. The respondents stated that the PRA had not published any analysis to support deleting this provision and stated that the EU, the BCBS, and a number of other jurisdictions support the existence of a 3% outflow rate. One respondent considered the PRA's proposed approach alongside a proposed rule⁶¹ that required firms to apply the higher of any third country or PRA outflow rate when consolidating a subsidiary in a third country. The respondent suggested that not including an authorisation specifying a 3% outflow rate, and requiring the application of higher third country outflow rates, could result in the unfair treatment of stable retail deposits.

12.9 The PRA has considered the responses received and decided not to change its approach. The PRA has never granted an authorisation that allows firms to apply a 3% outflow rate to stable retail deposits, and considers that a 5% outflow rate is appropriate at this time. The PRA expects to keep the liquidity framework under review and will consider this as part of future policy development.

12.10 The PRA's proposed rules included amendments to specify when a higher outflow rate would apply to retail deposits.⁶² These amendments stated that credit institutions shall apply a higher outflow rate to such deposits, where required to by the PRA. The PRA's restated Article also did not include a provision from the Delegated Act stating that a competent authority may apply a higher outflow rate to retail deposits where it is justified by the specific circumstances of the credit institution.

12.11 One respondent welcomed the proposed amendments. The respondent considered higher-risk retail deposits to be better addressed under the Pillar 2 process than through Pillar 1 requirements. The PRA will publish the policy as proposed.

CRR Part Six

12.12 The PRA proposed to incorporate Part Six of the CRR in the Liquidity (CRR) Part of the PRA Rulebook, making a number of minor amendments to ensure consistency between PRA rules and other aspects of the CRR.

12.13 One respondent noted that CRR Articles put in place to specify LCR reporting requirements before the implementation of the LCR Delegated Act have been superseded by the Liquidity Coverage Ratio (CRR) Part of the PRA Rulebook. This respondent suggested that removing these redundant Articles could help to simplify the PRA Rulebook. Having considered the respondent's concerns, the PRA has decided to maintain its proposed approach. However, the PRA intends to consider in future whether there are rules that can be rationalised further.

Reporting currency

12.14 The PRA proposed to introduce a definition of the term 'reporting currency' in the Liquidity (CRR) Part of the PRA Rulebook, that defined 'reporting currency' as pounds sterling (GBP), unless a firm's annual accounts are prepared in a different currency, in which case a firm may use that currency as its reporting currency.

⁶¹ Liquidity Coverage Ratio (CRR) Articles 2(3)(b) – 2(3)(c).

⁶² Liquidity Coverage Ratio (CRR) Article 25(3).

12.15 The PRA received no comments on this provision and will therefore publish the policy as proposed.

Compliance with the LCR and NSFR

12.16 The PRA proposed to restate in PRA rules CRR requirements on firms' compliance with liquidity requirements,⁶³ with an amendment to state that firms must provide a notification of any LCR or NSFR shortfall (or expected shortfall) 'without delay' rather than 'immediately'.

12.17 One respondent requested clarity as to the PRA's expectations of the frequency of monitoring and production of the NSFR in light of this proposal, and the PRA's statement that it would not be proportionate to require firms to provide or be capable of providing daily NSFR reporting to the PRA.

12.18 The PRA considers that the amendments that have been made to the restated CRR should not affect the frequency with which firms monitor their NSFR or LCR positions. Rather, the PRA's proposed amendments aim to specify a more proportionate notification requirement for firms during a stress. The PRA reiterates that it does not expect firms to provide daily NSFR reporting during a stress.

Other Comments

LCR treatment of derivative client clearing activities

12.19 The PRA proposed to restate in PRA rules LCR provisions that specify outflow rates and inflow rates for various categories of item. This includes an 'inflow cap' that limits a firms' LCR eligible inflows to a proportion of its outflows.

12.20 One respondent considered this to result in an overall treatment in the LCR of derivative client clearing that is punitive, and that this activity should be excluded from LCR requirements. The respondent highlighted a number of ways in which they consider the LCR treatment of derivative client clearing to be inappropriate given the nature and extent of the risks associated with this activity.

12.21 The respondent suggested that the impact of the LCR treatment of derivatives client clearing is most acutely felt by entities that are bound by the inflow cap, which are often subsidiaries of large banking groups, and entities with large portfolios of secured financing transactions. For such entities, the respondent stated that derivative client clearing can be a large driver of liquidity requirements even though it does not represent a source of liquidity risk.

12.22 The PRA recognises the contribution of central clearing to broader financial stability, however, the PRA has decided not to change the policy as proposed. The PRA considers that the LCR treatment of this activity enhances the safety and soundness of firms, in particular given the short-term nature of the LCR. The PRA considers the aggregate cap on total inflows to be necessary and proportionate to ensure that firms do not rely solely on anticipated inflows to meet their LCR and to ensure a minimum level of high-quality liquid asset (HQLA) holdings. The PRA also notes that the Basel III standard does not provide for an exemption from the inflow cap for derivative client clearing. Finally, there is little evidence that the policy has been an impediment to clearing activity, but the PRA will continue to monitor developments.

LCR treatment of sovereign debt externally rated below credit quality step 1

12.23 The PRA proposed to restate a provision of the LCR Delegated Act specifying that sovereign debt rated at credit quality step 1 may be categorised as a Level 1 HQLA. The PRA did not restate a

⁶³ Liquidity (CRR) Article 414.

provision of the Delegated Act specifying that all EU member state sovereign debt, regardless of credit quality, may be categorised as Level 1 HQLA.

12.24 Two respondents requested clarity as to the PRA's proposed treatment of EU government securities that are rated below credit quality step 1.

12.25 The PRA has considered the responses received and notes that such securities should be treated in the same way as any other third country sovereign debt.

LCR treatment of gold

12.26 The PRA proposed to restate in PRA rules LCR provisions that specify eligibility criteria for HQLA. These criteria do not provide for the classification of gold as HQLA.

12.27 Two respondents considered that gold should be treated as some level of HQLA. Respondents cited aggregated historical trade data and stated that this data confirms that gold retains consistent liquidity characteristics and has proved highly resilient to global liquidity shocks, including those that occurred in early 2020. The respondents considered that not treating gold as HQLA is contrary to the practice of central banks, which hold gold assets as a reserve for their own purposes. The respondents asserted that in this context, gold assets are not significantly different in substance from holdings of foreign currency deposits, which are treated as cash in the liquid asset buffer.

12.28 The PRA has considered these respondents' comments and will publish the policy as proposed. The PRA considers that while gold is a commonly traded and held asset, including as a reserve asset by central banks, the PRA has not found sufficient evidence of its liquidity, risk characteristics, and price stability to warrant treatment as HQLA. The PRA also notes that the Basel III LCR standard does not include gold within HQLA.

Consolidation of liquidity requirements

12.29 The PRA proposed to restate in PRA rules an LCR provision that requires firms to apply, upon consolidation, locally applicable outflow rates and inflow rates. Locally applicable outflow rates are applied where they are higher than the PRA outflow rate. Locally applicable inflow rates are applied when they are lower than the PRA inflow rate.

12.30 One respondent considered this approach to be overly prudent, as it precludes firms from applying, upon consolidation, more lenient outflow or inflow rates that may be specified in third countries. The respondent also stated that this provision is not included in the Basel standard. The respondent made several suggestions as to how the PRA should change this provision, including: that this provision be deleted, that upon consolidation more lenient outflow rates should be applied, or that more lenient outflow or inflow rates should be permitted to offset less lenient outflow or inflow rates.

12.31 The PRA has considered this response and will publish the policy as proposed. The PRA considers that specifying the use upon consolidation of higher locally applicable outflow rates, or lower locally applicable inflow rates, is appropriately prudent and proportionate. The PRA considers that recognition of more conservative values upon consolidation ensures that higher risks perceived by local regulators in third countries are adequately addressed in firms' consolidated LCRs. The PRA notes that this approach could lead to higher consolidated requirements where third country jurisdictions apply higher outflow rates or lower inflow rates than those specified in the Basel standard. The PRA has not yet identified material areas of international super-equivalence that could result in this outcome.

Procyclicality

12.32 The PRA proposed to restate in PRA rules an LCR provision that specifies a HLBA methodology.⁶⁴ This methodology uses a historical 24-month look-back period to determine the HQLA that firms must hold against the risk that they experience large derivative collateral needs resulting from an adverse market scenario.

12.33 Seven respondents stated that the HLBA methodology is procyclical, as the liquidity requirement that the HLBA generates is likely to increase during a period of market stress. One respondent stated that the methodology assumes that past events are representative of future events, which may not be the case. Two respondents considered the look-back period not to be sensitive to changes in the composition or characteristics of firms' derivatives portfolios or business model changes. Three respondents suggested ways in which the requirement could be changed, including that the PRA reconsider the methodology as a whole and that the PRA delay increases in the HLBA requirement for a period of up to 30 days. One respondent stated that the HLBA does not provide guidance for events that are not related to an adverse market scenario.

12.34 The PRA has considered the responses and decided to publish the policy as proposed. Given that market practice requires full collateralisation of mark to market exposures on derivative transactions, the PRA considers that the HLBA reflects a significant risk to which firms with derivatives portfolios are exposed.

12.35 One respondent requested additional communication from the PRA regarding the use of liquid asset buffers during a stress, and suggested that the PRA's rules include an option to 'flex down' liquidity requirements during a stress.

12.36 The PRA has considered the response and decided to publish the policy as proposed. The PRA will consider further how best to ensure that prudential buffers are usable during a stress, and notes that, as stated in SS24/15 'The PRA's approach to liquidity and funding risk', firms may draw down their liquid asset buffers as required in times of stress.⁶⁵

Additional comments

12.37 The PRA did not make specific proposals in relation to the treatment of synthetic securitisations. One respondent expressed concern that as a result the PRA's proposed rules could not facilitate the expected growth in synthetic on-balance sheet securitisations, because the eligibility in the LCR of transactions that qualify under the 'Significant Risk Transfer' process is unclear.

12.38 The PRA has considered this response and decided not to change its approach. The PRA intends to keep the LCR standard under review, including in the context of new products that arise from time to time.

Definitions

12.39 The PRA proposed to incorporate in the proposed Liquidity (CRR) Part of the PRA Rulebook the liquidity definitions that are set out in the CRR and applicable to the LCR and NSFR. The PRA also proposed to introduce a definition of the term 'reporting currency' applicable to NSFR reporting as well as the LCR, and to amend the definition of 'financial customer'.

⁶⁴ As specified in Article 1 of Chapter 4 of the LCR (CRR) Part.

⁶⁵ On 20 April 2020, the PRA also published a set of Q&As on the usability of liquidity and capital buffers and their operation as set out in the PRA rules and guidelines and in response to the Covid-19 outbreak: <https://www.bankofengland.co.uk/prudential-regulation/publication/2020/buffer-usability-qanda>.

The PRA has considered the responses received and outlines its final policy in the NSFR chapter.

13 Net stable funding ratio

13.1 In CP5/21, the PRA consulted on proposals to implement the net stable funding ratio (NSFR).

13.2 The NSFR is intended to help ensure that firms maintain a stable funding profile in relation to the composition of their assets and off-balance sheet activities. The NSFR focuses on protecting against liquidity risks over a longer horizon than the LCR metric.

13.3 The PRA proposed to:

- introduce an NSFR framework that implements the Basel III standard, including new definitions applicable to the NSFR and specifying available stable funding (ASF) and required stable funding (RSF) factors;
- introduce a simplified NSFR (sNSFR) framework for small and non-complex firms; and
- introduce new regulatory permissions applicable to the NSFR, alongside a new 'Liquidity and funding permissions' SoP.

13.4 The PRA also proposed to make consequential changes to SS24/15 'The PRA's approach to supervising liquidity and funding risks' to reflect the introduction of the NSFR.

General comments

13.5 Five respondents generally supported the PRA's proposed rules and their intended outcome: to ensure that firms have sufficient diverse and stable funding under normal and stressed conditions.

13.6 One respondent considered that the PRA's proposals lean towards the more conservative approach among CRR II and Basel III standards, citing the proposed treatment of derivative client clearing activities as an example.

13.7 Two respondents considered it important to ensure a level playing field by minimising material deviations from the Basel III standard. One respondent commented that the PRA's implementation should be aligned with the EU's. In two cases – on-balance sheet trade finance and derivative client clearing – respondents highlighted areas in which they would prefer greater alignment with the rules set out in the EU. In most cases, respondents suggested revisions that would result in different rules than those set out in the EU.

NSFR definition and requirement

13.8 The PRA proposed to define the NSFR as the ratio of a firm's amount of ASF to the amount of its RSF over a 1-year horizon, and to require that level to be at least 100% on an ongoing basis. The PRA also set out its proposed approach if a firm's NSFR fell below 100%.

13.9 No responses were received on these aspects of the PRA's proposals, and the PRA will therefore publish the policy as proposed.

Regulatory permissions

13.10 The PRA proposed to codify the conditions for regulatory permissions relating to the NSFR in the SoP 'Liquidity funding and permissions'.

13.11 No responses were received on these aspects of the PRA's proposals, and the PRA will therefore publish the policy as proposed.

Categories of ASF and RSF factor

Secured Financing Transactions (SFTs)

13.12 In CP5/21, the PRA proposed to apply asymmetric ASF and RSF factors to different legs of short-term SFTs secured by Level 1 Assets. The PRA proposed to set:

- the RSF and ASF at 0% for SFTs with <6 months' residual maturity that are collateralised by Level 1 HQLA with re-hypothecation rights; and
- the RSF at 5% and the ASF at 0% for SFTs with <6 months' residual maturity that are not collateralised by Level 1 HQLA with re-hypothecation rights.

13.13 Two respondents welcomed the treatment proposed for transactions collateralised by Level 1 HQLA collateral. One respondent asked if the PRA will reconsider the RSF and ASF applied to SFTs. Three respondents noted the remaining asymmetries in the ASF and RSF applied to SFTs, with one stating that even a small asymmetry could have a material impact on firms' stable funding requirements.

13.14 Having considered the responses received, the PRA considers it appropriate to maintain the asymmetrical treatment of certain SFTs. This asymmetry is intended to reflect the fact that such transactions may unwind asymmetrically, with transactions that generate funding rolling off before or in greater proportion than transactions that require funding. Moreover, the remaining asymmetries are intended to address short-term funding links between firms and financial customers that could pose risks to firms' safety and soundness.

13.15 In line with the Basel III standard, the PRA's proposed rules treated SFTs in a manner that is consistent with their balance sheet treatment. Three respondents considered this would result in a treatment of collateral swaps that is overly conservative and inconsistent with the LCR treatment of collateral swaps, and/or the NSFR treatment of repos, even though collateral swaps and repos often have similar characteristics. One respondent stated that the counterparties to such transactions are usually entities to which a favourable ASF factor would be applied if the transactions were repos rather than collateral swaps. Two respondents were concerned that the proposed approach would be inconsistent with the LCR, which does not distinguish materially in its treatment of collateral swaps and repos. In particular, they considered that collateral swaps in which a firm receives Level 1 HQLA securities should be recognised as a potential source of stable funding and assigned an ASF factor, consistent with the proposed treatment of repos.

13.16 Having considered the responses received, the PRA has decided to maintain its proposed approach. The NSFR is a balance-sheet based metric that generally does not treat off-balance sheet assets or liabilities as providing or requiring stable funding, focusing primarily on assets and liabilities on a firm's balance sheet. This is a basic principle of the NSFR and the approach applies also to collateral swaps. By contrast, the LCR is not a balance-sheet based metric, and considers inflows, outflows, and assets, irrespective of whether they arise from on- or off-balance sheet items. The PRA considers that a change to the rules would be at odds with the design principles of the standard under Basel III, and make the standard significantly more complex and costly to implement for firms. Moreover, the PRA notes that the off-balance sheet treatment of collateral swaps also precludes the application of an RSF factor to securities that could otherwise require stable funding. This limits the overall impact that treating collateral swaps in this way could have on firms' RSF requirements.

13.17 Consistent with Basel III standards, the PRA proposed that firms should not generally apply an RSF factor to assets borrowed in SFTs, and only do so if they are on the firm's balance sheet or where a firm has 'beneficial ownership' of that asset. Four respondents requested greater clarity on

the meaning of the term 'beneficial ownership'. They considered it to be capable of being interpreted as requiring firms to hold stable funding against any securities that have been borrowed or otherwise acquired in SFTs, which they considered not to have been the intent of the standard.

13.18 The PRA has considered the responses and recognises the potential lack of clarity. The PRA intended to apply an RSF factor to only one leg⁶⁶ of an SFT transaction, in a manner that is consistent with the balance sheet treatment of such transactions. In order to make this clearer, the PRA has decided to remove the concept of beneficial ownership from the rules on SFTs. Instead, the PRA has clarified that firms should apply an RSF factor to assets they have borrowed or otherwise acquired in SFTs only if they are on balance sheet, or exposed to all or substantially all of the economic risk and reward of those assets. The PRA considers this approach would link the NSFR treatment of assets received in an SFT to the economic substance of a transaction, rather than its legal form.

Holdings of Level 1 Assets

13.19 The PRA proposed to apply a 0% RSF factor to certain unencumbered Level 1 assets, including marketable securities representing claims on, or guaranteed by, central governments and certain other public authorities that are assigned a 0% risk weight under the Basel III standard's approach to credit risk.

13.20 No responses were received on this aspect of the PRA's proposals, and the PRA will therefore publish the policy as proposed.

Holdings of high-quality covered bonds

13.21 The PRA proposed to apply a 7% RSF factor to holdings of covered bonds that qualify as Level 1 HQLA.

13.22 One respondent welcomed the application of a 7% RSF factor to such bonds. The PRA will publish the policy as proposed.

Variation margin

13.23 The PRA proposed that a firm may use both cash and other Level 1 HQLA received as variation margin, excluding extremely high-quality covered bonds, to calculate its net derivatives position.

13.24 Two respondents supported the PRA's inclusion of other Level 1 HQLA as eligible variation margin. Three respondents proposed that non-Level 1 HQLA also be eligible for deduction against derivative positions. One respondent suggested that the proposed rule could have a particular impact on corporate clients with more limited access to Level 1 assets. That respondent stated that the credit support annexes used for derivative contracts already reflect the risks arising from taking non-Level 1 assets as collateral, including through the use of haircuts. The respondent stated that the NSFR would have no impact on the extent to which they provide derivatives products to corporate clients. Two respondents considered the proposed approach not to reflect the funding value of non-Level 1 collateral, which they considered to be recognised in other aspects of the NSFR, and that the PRA had not sufficiently justified its proposed approach.

13.25 The PRA has considered the responses and decided to maintain its proposed approach. The PRA's proposed approach recognised Level 1 HQLA excluding covered bonds as variation margin. The

⁶⁶ The PRA notes that the NSFR's treatment of encumbered assets can mean that the RSF factor applied to the collateral posted under an SFT also increases, which can result in changes to the funding factors applied to both 'legs' of an SFT (despite the statement in paragraph 1.15). However, firms should note that the RSF factor applied to collateral posted in the context of a repo is a consequence of the NSFR's treatment of encumbered assets rather than the standard's treatment of SFTs as such.

PRA considers that approach to be prudent and proportionate given their risk characteristics, but that recognition of a broader range of assets would not be consistent with firms' safety and soundness.

13.26 The PRA proposed that variation margin posted (received) against derivatives netting sets would be required to be deducted from the fair value of a netting set with negative (positive) fair value, and that to avoid double counting, collateral assets recognised as variation margin posted shall otherwise be excluded from the calculation of required stable funding. Two respondents commented that the proposed treatment of excess variation margin was unclear. They considered it unclear whether excess variation margin posted should receive an RSF factor, and if so what RSF factor should be applied.

13.27 The PRA has considered these responses and decided to clarify the treatment of variation margin to specify that variation margin posted or received shall be deducted from the fair value of a netting set only up to the extent that it results in the netting set having zero fair value. Any assets posted as excess variation margin should be included in the calculation of required stable funding, and receive the appropriate RSF factor for the asset type. This reflects the need for stable funding that such assets generate.

13.28 The PRA also proposed that firms should determine the fair value of derivative contracts gross of any collateral posted, or settlement payments and receipts related to market valuation changes.

13.29 Two respondents suggested it could be challenging to obtain the data necessary to determine the fair value of STM derivative transactions on this basis, with one stating that it is difficult to reconcile the relevant data with an independent source of information. Such reconciliations are used as a check of data quality.

13.30 After considering the responses, the PRA has decided to publish the policy as proposed. The PRA notes the potential operational challenge of collecting this data. However, the PRA considers it appropriate to treat STM transactions in the same way as marked-to-market transactions, because such transactions in practice result in margin payments and receipts that are substantially the same as those generated by transactions that are collateralised to market. This helps to ensure the safety and soundness of firms which enter into STM transactions.

On-balance sheet trade finance

13.31 In line with the Basel standard, the PRA's proposed rules did not specify a distinct treatment of on-balance sheet trade finance. The PRA proposed that such assets attract the same RSF factors as loans, depending on the counterparty and collateralisation.

13.32 Four respondents considered this would require a 50% RSF factor to the majority of firms' on-balance sheet trade finance assets, as most of these assets are with non-financial counterparties and have a maturity of less than six months. They considered a 50% RSF factor to be punitive for typically short-term trade finance products that they considered to be low risk. They expressed concern about the impact of the proposed approach on the relative standing of the UK and the provision of finance to the real economy.

13.33 After considering the responses, and further data provided by firms, the PRA has decided to change the RSF factors applied to on-balance sheet trade finance products with non-financial customers, to 30% for transactions with a residual maturity of less than six months. The PRA considers this would better reflect the risks of such transactions, while also having regard to the

international standing of the UK as a place to do business, and the provision of finance to the UK real economy.

13.34 The PRA's proposed approach treated acceptances as an on-balance sheet product. One respondent commented that acceptances, while on-balance sheet for accounting purposes, are economically similar to off-balance sheet trade finance. They considered acceptances should be treated as off-balance sheet trade finance, and stated that the product could potentially benefit from the interdependent assets and liabilities (IA&L) permission.

13.35 The PRA has considered the response and decided to maintain its proposed approach to acceptances. The NSFR is a simple metric that generally uses the carrying values of assets and liabilities as stated on a firm's balance sheet. The PRA intends to consider applications for the IA&L permission in light of their compliance with the relevant criteria.

RSF factors

Gross derivatives liabilities

13.36 The PRA proposed to apply a 5% RSF factor to gross derivative liabilities.

13.37 One respondent welcomed the proposal. Another cited derivatives as the primary product for which the NSFR would require more stable funding than the underlying risk, and considered the 5% RSF factor not to be a perfect representation of the funding risk that derivatives pose.

13.38 The PRA has considered the responses and decided to maintain its proposed approach. The PRA considers the approach as proposed to be a simple but prudent way of addressing the funding needs generated by a firm's derivative activities. The PRA notes that this approach aligns with the discretion afforded by the Basel III standards.

Off-balance sheet exposures

13.39 For off-balance sheet assets other than off-balance sheet trade finance, the PRA proposed that firms regularly assess the amount of RSF they hold and determine the RSF factors to apply, in line with the high level principles set out in the standard for such assets. The PRA proposed to assess the appropriateness of the RSF factors that firms apply as part of its supervision of firms, including as part of the Liquidity-SREP process.

13.40 No responses were received on this aspect of the PRA's proposals, and the PRA will therefore publish the policy as proposed.

Off-balance sheet trade finance and factoring

13.41 The PRA proposed to apply RSF factors between 5% and 10% to off-balance sheet trade finance transactions, depending on their maturity.

13.42 Two respondents broadly supported having factors that vary based on the residual maturity of a transaction, but considered the proposed factors to be too high given the risks in this case. They cited industry data and research on the 'claims paid' rate for off-balance sheet trade finance products.

13.43 Having considered the responses and analysed additional data provided by firms during the consultation process, the PRA has decided to revise the RSF factors applied to off-balance sheet trade finance. The applicable RSF factors have been revised to 2.5% for transactions with a residual maturity of less than one year, and 5% for transactions with a residual maturity of one year or more. The PRA considers this to be prudent given its assessment of the tenor and risk of such transactions,

and having had regard to the international standing of the UK as a place to do business, and the provision of finance to the UK real economy.

13.44 Two respondents also commented on the RSF treatment of undrawn non-cash commitments, ie off-balance sheet commitments to issue guarantees or letters of credit. They considered the 5% RSF factor that would apply to this kind of undrawn facility to be overly conservative, as they considered non-cash commitments to generate a cash outflow only if a facility is drawn and if there is a contingent event due to which the commitment is called.

13.45 The PRA has considered respondents' comments and decided to maintain its proposed approach. The RSF factor applied to undrawn facilities uses the definition of credit and liquidity facilities in the proposed Liquidity Coverage Ratio (LCR) Part of the PRA Rulebook. To the extent that non-cash commitments result in outflows that are captured by the LCR, the PRA considers it to be prudent and appropriate also to reflect the funding risk generated by those facilities in the NSFR.

13.46 The PRA proposed to treat on-balance sheet factoring in the same way as a loan, consistent with the proposed treatment of on-balance sheet trade finance. One respondent considered on-balance sheet factoring to be economically similar to trade finance and so to warrant lower RSFs.

13.47 After considering the response, and in light of its revised approach to on-balance sheet trade finance, the PRA has decided to revise the treatment of factoring such that it may receive the same RSFs as trade finance, in accordance with the applicable accounting treatment and counterparty type. The PRA considers this to be prudent given the PRA's revised approach to trade finance and the similarities between the term, counterparty type, and purpose of factoring and trade finance.

Interdependent assets and liabilities (IA&L)

13.48 The PRA proposed to introduce a permission that would allow certain asset and liability items to be exempt from the NSFR where strict criteria were met that ensure that the liability could not fall due while the asset remains on the balance sheet.

13.49 Fourteen respondents noted that the PRA's proposed rules did not include a list of products that would automatically qualify for the IA&L permission. Seven respondents cited examples of products for which they considered the IA&L permission should always apply, including derivatives client clearing and total return swaps (TRSs).

13.50 Thirteen respondents considered derivatives client clearing to not create funding risks, without structural funding needs or any term funding risk or market risk. They considered the proposed approach not to be proportionate. The concerns that respondents raised included that clearing members generally do not derive a funding benefit from the initial margin they receive from clients, and that client clearing appears to be eligible for the IA&L permission in other jurisdictions. One respondent stated that any risk from such transactions is already captured by the LCR under the historical look-back approach. Respondents commented on the impact that the PRA's proposed approach could have. Respondents highlighted several effects, including that client clearing could be a significant driver of firms' RSF requirements overall; that the cost of raising long-term funding to support this business could increase costs for end users and/or make it unsustainable to conduct this activity in the UK; and that clients might relocate to other jurisdictions as a result. One respondent considered the proposed approach to be procyclical. Another considered it inconsistent with international initiatives to encourage central clearing of derivatives. One respondent requested a clarification of the treatment of excess client variation margin in the context of client clearing.

13.51 Two respondents noted that the PRA's proposed IA&L permission did not include a provision that allows for 'substantially matched' maturities between assets and liabilities. They considered it not to be necessary for IA&L to have identical maturities, because assets with 'substantially matched' maturities would still not generate a funding risk that the NSFR is designed to capture.

13.52 The PRA has considered the responses and decided to amend its approach to derivative client clearing. The PRA will exempt from the NSFR derivative client clearing activities with qualifying CCPs (QCCPs), provided that the institution does not provide to its clients guarantees of the performance of the QCCP and, as a result, does not incur any funding risk. Where derivative clearing clients post assets as excess initial margin, and those assets are on the balance sheet of the firm and provide a potential funding benefit for the firm (beyond being available to post to the QCCP), the relevant RSF factor will apply. The PRA has also amended its suggestions for the structure and content of firms' ILAAP documents, as set out in Appendix 1 of SS24/15, to state that firms should include in their assessment of ASF and RSF an overview of items that are excluded from the NSFR, including derivative client clearing items. The PRA considers this would be an appropriately prudent and proportionate treatment of centrally-cleared derivatives, and will help to maintain the international standing of the UK. After considering the response on the proposed treatment of excess client variation margin in the context of client clearing, the PRA has decided not to change its approach, as it considers it to be sufficiently clear in this context.

13.53 Three respondents considered that total return swaps should benefit from the IA&L permission. Five respondents cited examples of transactions they considered would be treated inappropriately conservatively by the NSFR given they consider them to be funding neutral, including sets of transactions that are facilitated by client short sales or short sales undertaken on a firm's own account.⁶⁷ They expressed concern that the NSFR does not generally recognise the off-balance sheet funding generated in the context of these transactions, but applies an RSF factor to the resulting on-balance sheet assets.

13.54 The PRA has considered the responses and decided not to change its approach. The PRA will consider applications for the IA&L permission based on their compliance with the relevant conditions.⁶⁸ The PRA considers that this promotes firms' safety and soundness by ensuring that the IA&L treatment is afforded only where the conditions for its use are met.

Required reserves

13.55 The PRA proposed to require firms to apply any locally applicable RSF factor to the reserves that a firm is required to place with a central bank.

13.56 No responses were received on this proposal, and therefore the PRA will publish the policy as proposed.

Temporary non-standard central bank operations and derivatives transactions with central banks

13.57 CP5/21 noted that Basel III standards include discretions for supervisors to discuss and agree with the relevant central bank concessionary RSF treatments of certain assets with central banks. The PRA indicated it would consider exercising these discretions and applying rule modifications should it be necessary.

⁶⁷ A funding neutral transaction is a transaction (or set of transactions) that require little to no external funding to maintain.

⁶⁸ See PRA Statement of Policy 'Liquidity and funding permissions': <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/statement-of-policy/2021/liquidity-and-funding-permissions-sop-jan-2022.pdf>.

13.58 Three respondents requested clarity as to why a specific permission had not been included in the PRA's proposed rules, and the PRA's overall policy in respect of such transactions.

13.59 The PRA has considered the responses and decided not to change its approach. The PRA does not consider it appropriate to include such a permission given the temporary, non-standard nature of such operations and the PRA's general ability to grant rule modifications.

Intragroup treatment

13.60 In CP5/21, the PRA proposed to introduce a permission that would allow firms to apply a lower RSF factor for intragroup assets, and/or a higher ASF factor for intragroup liabilities, where the firm and its group counterparty apply a reciprocal NSFR treatment. The PRA explained its preliminary view that this approach should not apply to intragroup assets and liabilities across a ring-fence or where the group counterparty is not supervised by the PRA.

13.61 No responses were received on these aspects of the PRA's proposals, and the PRA will therefore publish the policy as proposed.

RSF factor applied to exchange traded common equity shares

13.62 The PRA proposed to apply a 50% RSF to equities that qualify as Level 2B HQLA for the LCR, including exchange traded common equity shares. The test for determining whether equities were Level 2B was the same as in the LCR rules: that the value of the shares must not have fallen by more than 40% in any 30 day period. The PRA proposed to apply an 85% RSF factor to equities that did not qualify as Level 2B HQLA.

13.63 Two respondents considered the RSF factors proposed for equities generally to be too high. One respondent suggested that the proposed RSF factors were not consistent with assumptions made in the context of the PRA's Solvent Wind Down exercise. That respondent also considered that the proposed calibration could adversely affect some specific business lines, including equity underwriting; could reduce competition; and also could provide an advantage to firms with funding that attracts a high ASF factor, such as retail deposits.

13.64 Eleven respondents commented on the criteria proposed to determine whether an equity qualifies as Level 2B HQLA. Four respondents considered that applying the criteria for the LCR was not appropriate, as the NSFR is a longer-term measure of funding risk. Ten respondents considered the proposed price decline test to be procyclical and not sufficiently clearly specified.

13.65 The PRA has considered the treatment of equities under its proposed rules and decided to modify its approach to ensure the prudent and proportionate application of the NSFR. The PRA will adopt a definition of Level 2B equities for the purposes of the NSFR in the Liquidity (CRR) Part of the PRA Rulebook that is specific to the NSFR, and clarify the definition of a relevant period of significant liquidity stress for an equity, in the context of the NSFR.⁶⁹ The PRA considers it appropriate to define this period as one during which the major stock index on which the equity has traded has had a decline in value of 40% or more over a 30-day period or an increase in haircut over a 30-day period not exceeding 40 percentage points. The PRA has clarified this definition in SS24/15 'The PRA's approach to supervising liquidity and funding risks'.

13.66 Two respondents considered there to be an inconsistency between the single index defined as 'major' in the PRA's proposed rules (the FTSE 100) and lists of major indices that are maintained

⁶⁹ This applies the national supervisory discretion set out in Basel FAQ 7 LCR 30.45(3)(f).

by certain EU supervisory authorities, and suggested that the PRA should maintain a list of ‘major indices’.

13.67 The PRA has considered the definition of ‘major index’ under its proposed rules and has decided to maintain its proposed approach. However, the PRA has amended its suggestions for the structure and content of firms’ ILAAP documents, as set out in Appendix 1 of SS24/15, to state that firms should discuss in their ILAAP the approach they have taken to identifying major stock indices in third countries, and how the views of relevant public authorities have been taken into consideration.

13.68 Three respondents argued that precluding equities issued by financial institutions from qualifying as Level 2B equities does not reflect the funding risk of such equities.

13.69 The PRA has considered the responses and decided to maintain its proposed policy. The PRA considers that equities issued by financial institutions are more likely than equities issued by other types of entity to be illiquid during a time of market stress.

13.70 Two respondents asserted that it is not appropriate to specify a currency denomination requirement for equities in the context of a long-term funding metric such as the NSFR. One respondent stated that the PRA’s proposed requirement could lead to unintended consequences, such as variation in firms’ funding requirements, because of changes in outflows in a particular currency within 30 days.

13.71 The PRA has considered the equity currency denomination criterion under its proposed rules and has decided to modify its approach. The PRA will include a revised currency denomination criterion in the definition of level 2B equities for the NSFR in the Liquidity (CRR) Part of the PRA Rulebook, and states that Level 2B equities must be denominated in the domestic currency of a firm’s home jurisdiction or in the currency of the jurisdiction where a firm’s liquidity risk is taken. The PRA considers this would be prudent and proportionate.

RSF factor applied to unsecured loans to financial institutions with a residual maturity of less than six months

13.72 The PRA proposed to apply a 10% RSF factor to unsecured loans to financial institutions with a residual maturity of less than six months. The Basel standard applies a 15% RSF factor to such assets. The PRA’s proposed approach sought to align more closely the RSF factors applied to secured and unsecured transactions of this kind. The PRA considered this approach to be prudent and proportionate, given the nature of such assets.

13.73 The PRA received no responses on the proposed approach, and will therefore publish the policy as proposed.

Definitions

13.74 The PRA proposed to incorporate in the proposed Liquidity (CRR) Part of the PRA Rulebook the liquidity definitions that are set out in the CRR and applicable to the LCR and the NSFR. The PRA also proposed to introduce a definition of the term ‘reporting currency’ applicable to the NSFR reporting as well as the LCR, and to amend the definition of ‘financial customer’.

13.75 One respondent considered that the proposed definition of financial customer could result in arbitrage opportunities, but added that they did not believe firms pursue such opportunities in practice.

13.76 The PRA’s restated definition of deposit broker stated that entities may not be classified a deposit broker where they take deposits from financial institutions. Upon further consideration, the

PRA considers it appropriate to amend the definition of deposit broker to state that deposit brokers cannot include entities that take deposits from financial customers, rather than financial institutions. This amendment narrows the definition of deposit broker. The PRA considers this amendment to be appropriate as it enhances safety and soundness by ensuring that the preferential treatment afforded to deposit brokers encompasses only entities accepting deposits that would otherwise get preferential treatment in the LCR. This also results in greater consistency between the definitions in the PRA Rulebook.

13.77 The PRA has considered the responses received and decided not to change the proposed policy on definitions, other than in respect of the definition of deposit broker, and the other amendments set out elsewhere in this chapter.

Netting conditions for derivatives and SFTs

13.78 The PRA proposed to specify in the Liquidity (CRR) Part the conditions under which derivatives and SFTs may be netted for the purposes of determining the stable funding requirement. The PRA additionally proposed to prohibit the netting of transactions using Level 1 HQLA against transactions using non-Level 1 HQLA.

13.79 Seven respondents commented on the additional netting condition. Three respondents noted that it is inconsistent with the approach to netting applied for accounting purposes. As a result, it would require respondents to develop a specific netting approach for the NSFR, which could be costly. Respondents' concerns included that such costs would not be proportionate to the prudential benefits of this condition, because firms do not generally undertake transactions using different types of collateral with the same client. Four respondents noted the proposed condition is not applied in the Basel III NSFR standard.

13.80 The PRA has considered the responses received and has decided to remove the proposed additional condition. In view of the responses on the potential operational cost of implementing such a condition, although the PRA considers the approach to be prudent, it would be unlikely to be proportionate.

Proportionality: The simplified NSFR (sNSFR)

13.81 In order to enhance the proportionality of the NSFR framework, the PRA proposed to introduce a version of the NSFR that small and non-complex firms could choose to use that would be simpler than, and at least as conservative as, the full NSFR.

13.82 Two respondents supported the introduction of an sNSFR. However, one respondent considered the proposed basis for using it – the proposed definition of 'small and non-complex institution' – to be overly complex.⁷⁰ They suggested the PRA may wish to consider applying the sNSFR to a broader range of firms.

13.83 The same respondent also considered the 85% RSF factor proposed for residential mortgages to be an error, and unhelpful for firms that are primarily mortgage lenders. The respondent considered it would result in fewer firms choosing to adopt the sNSFR because the 85% factor is higher than available under the full NSFR. They suggested applying the 65% RSF factor available in the NSFR to residential mortgages under the sNSFR.⁷¹

⁷⁰ The criteria for designation as a small and non-complex institution are listed in UK CRR Article 4(1)(145).

⁷¹ Under the PRA's proposed approach in the full NSFR, unencumbered loans secured by mortgages on residential property with a residual maturity of one year or more -that qualify for a 35% risk weight or less receive an RSF factor of 65% (Article 428af).

13.84 Having considered the responses, the PRA intends to continue to use the CRR definition of small and non-complex institutions in the related PRA rules at this time. The PRA considers the proposed definition to provide an appropriate and proportionate basis on which to identify the firms eligible to use more proportionate approaches such as the sNSFR. The PRA will consider further the scope of application of more proportionate approaches in designing a strong and simple framework for non-systemic banks and building societies.⁷²

13.85 After considering the response on the RSF factor applied to residential mortgages under the sNSFR, the PRA has decided to change its approach. The PRA has decided to modify the sNSFR to apply the same RSF factors to unencumbered loans secured by mortgages on residential property that apply in the full NSFR. It would be consistent with the CRR's approach to determining the risk weights for such assets in the SA-CCR. It would also be prudent, applying the same RSF factors as those applicable under the full NSFR. The PRA has also amended the reporting instructions for the sNSFR to ensure the revised RSF factors can be reported appropriately in the sNSFR template using a weighted average approach.

Additional comments on RSF and ASF factors

RSF for total return swaps and prime brokerage related activities

13.86 Eleven respondents considered the PRA's proposed treatment of total return swaps to be overly conservative. They considered the RSF factor applied to securities held to hedge TRSs to be too high, as the securities are held only for the duration of the relatively short term of a TRS. They suggested that the PRA's approach should recognise the practice of using margin received to fund the purchase of the security used to hedge the TRS. Three respondents considered that the PRA's approach should recognise the relationship between the TRS and its hedge, as firms typically sell the security held as a hedge upon closing out a TRS. Two respondents considered the PRA's proposed rules could increase firms' costs, with one respondent citing costs for hedge funds and pension funds.

13.87 The PRA has considered the responses and decided to maintain its proposed approach. The NSFR does not generally differentiate between the purposes for which an individual asset or liability is held on a balance sheet. The PRA also considers it would not be consistent with firms' safety and soundness to apply an ASF factor to margin received; as such margin may become segregated in a way that that can limit, at short notice, the ability of a firm to use that margin as a funding source.

RSF for commodity-related activities

13.88 The PRA proposed to apply an 85% RSF factor to physically traded commodities, including gold but excluding commodity derivatives.

13.89 Three respondents considered the PRA's proposed rules not to be proportionate, and suggested that they could have a material impact on firms that specialise in precious metal-related products and activities, including precious metal deposit-taking and clearing activities, and precious metal lending activities. They considered the RSF factor proposed for precious metals to be too high and not to reflect the underlying risks. One respondent also cited the hedging of certain client-facing derivatives. Another respondent considered that the RSF factor that was proposed to apply to other commodities, such as oil, did not accurately reflect their liquidity during funding stresses.

13.90 Respondents thought that the PRA's proposed rules could have a material impact on both firms and the precious metals markets more generally. Three respondents considered the proposed

⁷² See DP1/21 'A strong and simple prudential framework for non-systemic banks and building societies' <https://www.bankofengland.co.uk/prudential-regulation/publication/2021/april/strong-and-simple-framework-banks>.

approach could result in increased costs for end users, and potentially result in firms exiting the market for these products. Three respondents suggested a number of alternative treatments of commodities-related transactions that they considered to be more appropriate. These included treating gold as a HQLA, treating gold as a currency, applying lower RSFs to precious metal assets associated with deposit-taking and clearing activities, applying the IA&L permission, and excluding physical unencumbered stock backing customer deposits from the NSFR.

13.91 The PRA has considered the responses and decided to amend its approach to precious metal holdings related to deposit-taking and clearing activities. The PRA has introduced an interdependent precious metals permission for which firms may apply in respect of their own unencumbered physical precious metal stock and customer precious metal deposit accounts.⁷³ When the permission is granted, firms would apply a 0% RSF factor to their unencumbered physical stock of precious metals, to the extent that it balances against customer deposits. The PRA has decided not to amend its approach for other aspects of the treatment of commodity-related activities. The PRA considers its overall approach to commodities in the NSFR to be generally appropriate. The PRA notes that it is able to waive or modify rules under section 138A of FSMA where a firm can demonstrate to the PRA's satisfaction that the application of the unmodified rule would impose an undue burden on a firm, or would fail to achieve its intended purpose, and where modifying it would not adversely affect the advancement of the PRA's objectives.

RSF factor for retained tranches of own issuance residential mortgage-backed securities

13.92 The PRA proposed to apply an 85% RSF factor to AAA-rated residential mortgage-backed securities (RMBS) that are not eligible as HQLA, consistent with the general treatment it proposed to apply to non-HQLA securities.

13.93 One respondent considered this approach to create a disincentive for firms wanting to convert mortgage loan assets into a more readily liquid and marketable format through own issuance of securitisations. The respondent considered it inconsistent with the 65% RSF factor applied to the underlying mortgage loans and the 25% RSF factor applied to otherwise identical senior AAA rated securitisations when they are not own issuance (ie for securitisations qualifying as Level 2B liquid assets under the LCR). They suggested that retained tranches of own issuance securitisations should attract an RSF factor that was closer to 25%.

13.94 After considering the response, the PRA has decided to amend its approach to own issuance securitisation positions where the underlying assets would receive a 65% RSF factor, and subject to certain other conditions. In such cases, a 65% RSF factor would apply to:

- the senior tranche of retained own-issuance RMBS with a residual maturity of greater than or equal to one year; and
- all tranches of own issuance RMBS with a residual maturity of greater than or equal to one year, if the bank has retained all tranches.

13.95 The PRA considers that this approach would be prudent and proportionate, to align with the RSF factor applicable to underlying mortgages, and to address the potential disincentive to securitise mortgage assets that could otherwise apply.

⁷³ Liquidity (CRR) Article 428f(2)–(3).

ASF factor applied initial margin

13.96 The PRA proposed to specify several categories of liability to which ASF factors apply depending on their tenor, counterparty, and the type of funding. The proposed approach did not apply an ASF factor to initial margin (IM) received.

13.97 Three respondents suggested that the PRA should recognise re-hypothecatable IM received as a funding source, and asserted that the PRA's proposed rules did not treat IM and VM consistently, despite both being forms of margin that firms could use as a funding source.

13.98 The PRA has considered the responses and decided to maintain its proposed approach. The PRA considers that recognising IM as a funding source would not be consistent with firms' safety and soundness, as initial margin may become segregated in a way that that can limit, at short notice, the ability of a firm to use that margin as a funding source. The PRA also considers that the contribution of VM to a firm's overall stable funding requirements reflects the role that VM plays in reducing a firm's contingent funding risks, and does not reflect firms' use of VM as a source of funding.

Comments on other aspects of the PRA's proposed approach

Disclosures

13.99 The PRA proposed to require spot disclosures of firms' NSFR positions and component elements.

13.100 Nine respondents raised concerns about spot disclosures or stated that an average disclosure regime would be preferable. One respondent stated that an average disclosure regime would be particularly helpful for smaller firms. All respondents generally supported disclosure of a quarterly average.

13.101 Two respondents considered the PRA's proposed approach could result in procyclical market dynamics, because certain items that attract RSF factors, such as derivative assets, unfunded loans, and initial margin posted, may increase during a stress. One respondent suggested that the PRA introduce stress-specific liquidity requirements, and provide more clarity on the use of buffers. They suggested that the PRA should consider the potential impact on stressed markets to ensure that the NSFR as ultimately applied did not amplify market volatility.

13.102 The PRA has considered the responses and decided to require firms to disclose an NSFR that is calculated as an average of four quarter ends. This is intended to mitigate the risk of adverse signalling during a market stress, and will align the disclosure regime for the NSFR to that of other metrics, including the LCR.

13.103 In practice, this would result in the first disclosures being required after Sunday 1 January 2023, as determined by firms' accounting year-end and the applicable disclosure regime.

Reporting

13.104 One respondent requested clarity as to how firms should report the NSFR on a single-currency basis. The PRA recognises that additional clarity as to single currency reporting may be warranted, and will consider issuing a reporting Q&A on this topic in due course.

Currency mismatch requirements

13.105 The PRA proposed to require the distribution of a firms' funding by currency to be generally consistent with the distribution of its assets.

13.106 Three respondents considered this requirement not to be appropriate for NSFR because it is a balance sheet metric; the same requirement applies for LCR, but that is a cash-flow metric. Three respondents were concerned that firms typically manage structural funding mismatches through the use of off-balance sheet derivatives such as foreign exchange (FX) swaps, and that this practice could be considered inconsistent with the 'generally consistent' requirement.

13.107 The PRA has considered the responses and decided to modify its approach. The PRA expects the proposed requirement not to preclude the management of currency mismatches using off-balance sheet derivatives. The PRA has updated SS24/15 'The PRA's approach to supervising liquidity and funding risks' to make this expectation explicitly clear.

Requests for clarification

13.108 A number of respondents cited parts of the proposed rules that they believed require amendment or clarification:

13.109 One respondent commented on the treatment of interim (unaudited) retained earnings, which one respondent considered would not attract an RSF factor.

13.110 One respondent questioned whether a specific treatment of 'notional pools', a corporate banking service that is provided to corporate customers that enables cash to be managed across multiple legal entities, would apply also to the NSFR.

13.111 One respondent requested further detail on the encumbrance period to be used when an asset is encumbered for behavioural reasons.

13.112 One respondent suggested further clarification may be warranted on the use of internal models to determine the residual maturity of structured notes.

13.113 One respondent suggested central banks should be treated as corporate counterparties, rather than financial institutions, because deposits from central banks may behave similarly to those from corporate counterparties.

13.114 Three respondents suggested the list of multilateral development banks and international organisations that results in different LCR and NSFR treatments should be updated.⁷⁴

13.115 One respondent requested clarity as to the definition of small and medium-sized enterprises.

13.116 The PRA has considered the responses and decided not to change its approach. These points either do not require further prescription at this stage, are already sufficiently clear in the PRA approach, or are already defined in the CRR.

Unintended consequences, arbitrage, and incentives

13.117 One respondent stated that the standard could incentivise off-balance sheet activity, as well as the use of unsecured funding. Another respondent considered there would not be significant unintended consequences from introducing the NSFR.

13.118 The PRA has considered the responses and taken account of them in determining the aspects of the approach it has maintained or amended.

⁷⁴ Article 117 and 118 of the CRR.

14 Reporting

14.1 The PRA proposed to update the Regulatory Reporting Part of the PRA Rulebook and amend SS34/15. These proposals reflected changes to prudential risk methodologies proposed in CP5/21, and were aimed at increasing the alignment of data requirements and definitions between the reporting and disclosure requirements. Specifically, the PRA proposed to update core reporting (COREP) and financial reporting (FINREP), through a combination of new returns and amendments to existing reporting requirements. In doing so, the PRA proposed to align with the majority of the changes contained within EBA Taxonomy 3.0, to ensure that firms report to the PRA under a consistent taxonomy, in a proportionate manner.

14.2 The key proposals included:

- introducing new reporting templates and making minor changes to existing reporting templates on IRB credit risk;
- introducing new reporting templates, and making minor changes to existing reporting templates on counterparty credit risk;
- replacing existing stable funding reporting with new templates on the NSFR approach, including simplified reporting templates for certain firms;
- deletion of the C66 maturity ladder template;
- not introducing any additional reporting on total loss-absorbing capacity (TLAC), and instead using existing PRA reporting templates on TLAC to avoid any additional burden on firms;
- introducing new reporting templates on the FRTB alternative standardised approach for market risk;
- updating existing PRA reporting templates including Capital+, Financial Statements forecasts, and ring-fenced banks reporting to reflect consequential updates from changes to COREP and FINREP; and
- deletion of the FSA045 template to avoid potential new duplication arising from the proposed updates to IRB credit risk reporting in COREP.

14.3 The implementation date for all reporting changes was proposed as Saturday 1 January 2022.

14.4 The PRA received comments from seven respondents in relation to the reporting proposals in CP5/21, as well as regulatory reporting requirements and processes in general not directly in scope of CP5/21.

Implementation

14.5 One respondent welcomed the proposed alignment of reporting templates with those implemented in the EU, and the use of the EBA Taxonomy version 3.0. The same respondent also welcomed the proposed alignment of data requirements and definitions between reporting and disclosure.

14.6 One respondent called for explicit confirmation that the PRA is using the EBA Taxonomy version 3.0 to implement changes to UK COREP and UK FINREP, as well as an indication of when the

UK and EU reporting taxonomies are likely to diverge. Another respondent suggested that adopting version 3.0 of the taxonomy on Saturday 1 January 2022, after this has been implemented in the EU in 2021, is likely to be disruptive to implementation and firms' systems.

14.7 The PRA can confirm that it is using the EBA Taxonomy version 3.0 to implement changes to UK COREP and UK FINREP. While the PRA understands that the alignment of the implementation date proposed in CP5/21 with the EU's implementation of Taxonomy 3.0 may be convenient for some firms, the final implementation date has been set to provide all firms with adequate time to implement the changes. The necessary legislative amendments also need to be in place to give these reporting requirements legal force. Any future updates to the reporting taxonomy will follow any future changes to PRA reporting requirements, which are subject to the FSMA consultation process. The PRA cannot comment on the likely timing of future changes at this stage.

G-SII indicator reporting

14.8 Three respondents questioned the value of, and rationale for, introducing new quarterly reporting of G-SII indicator data via template G01.00. Two of these respondents asked the PRA to consider the costs and operational burden associated with reporting template G01.00 on a quarterly basis. The same respondents also questioned the necessity of fourth quarter submission of template G01.00 by 1 April, due to its proximity to the end-April Basel globally systemically important banks (G-SIB) assessment exercise. They requested that the PRA considers amending the remittance dates to be consistent with the timeline of the Basel G-SIB assessment exercise.

14.9 The PRA considers that reporting of G-SII indicator data on a quarterly basis is necessary to supervise the development of G-SII relevant activity through the year. The PRA expects that the incremental cost and operational burden associated with the quarterly reporting is likely to be lower once reporting processes are implemented.

14.10 The PRA does consider there to be some benefit in aligning the submission of the fourth quarter G01.00 template and the Basel G-SIB assessment exercise. Therefore, the PRA has amended the remittance dates for all four quarters of template G01.00 reporting to 30 April, 31 July, 31 October, and 31 January. This change ensures that firms can align their preparation processes for the fourth quarter template G01.00 with the Basel G-SIB assessment exercise, and results in a consistent remittance period across all four quarters of template G01.00 reporting.

Counterparty credit risk

14.11 One respondent acknowledged the need to introduce new reporting for the different CCR approaches, but called on the PRA to keep this reporting under review, and to consider removing templates that are of little benefit to regulators.

14.12 The PRA considers it important that reporting is aligned to the prudential methodologies in force, and when these change, it is necessary for the underlying reporting to change so that it remains relevant. The PRA also recognises that reporting requirements must remain appropriate and proportionate for ensuring firms' safety and soundness. The PRA will publish the policy as proposed, but intends to keep the overall reporting framework under review to ensure that reporting remains closely aligned with supervisory data needs.

IRB credit risk

14.13 Two respondents commented on the proposed changes to IRB credit risk reporting. One respondent sought clarity on how to report collateral in template C08.01, and questioned whether the value of reported collateral should be limited to the value of an individual exposure.

14.14 After reviewing both the instructions for the reporting template C08.01 and the disclosure template CR7-A, the PRA considers that both sets of instructions are clear on how collateral should be reported, which intentionally differs for reporting and disclosure purposes. The PRA does not consider that additional clarity in the instructions is necessary.

14.15 The same respondent also sought clarity on whether specific standardised (SA) exposures classes should be reported in template C08.07, for example, exposures in the form of units or shares in CIUs.

14.16 The PRA notes that the methodology to assign exposures is set out in Article 147 of the CRR, which defines the exposure classes relevant to the IRB approach. Although template C08.07 requires reporting of SA exposures, these need to be relevant to the IRB approach. Therefore, the PRA does not consider that additional changes are needed to the scope of exposure classes reported in template C08.07.

14.17 Another respondent commented that implementing the proposed changes to IRB credit risk reporting would have an impact on firms' resources. The PRA recognises that reporting changes do require additional implementation effort by firms. However, by aligning the content of reporting and disclosure of IRB credit risk requirements, the PRA has sought to make implementation more efficient, allowing firms to utilise the same data to meet both sets of requirements. Therefore, the PRA will publish the policy as proposed.

Liquidity

14.18 Two respondents supported the proposed deletion of the template C66 on the cash flow maturity ladder, and provided additional feedback on other liquidity reporting not directly in scope of the CP5/21 proposals. One respondent said that they have concerns on the granularity of template PRA110 (Cash Flow Mismatch). The other respondent requested that the PRA consider removing the Additional Liquidity Monitoring Metrics (ALMM) reporting requirements entirely. Both these requirements are essential to supervise liquidity. The PRA will publish the policy as proposed, but will keep these returns, as well as other reporting requirements not directly related to the proposals of CP5/21, under review.

14.19 One respondent requested clarity on the PRA's definition of 'a similar index' under the heading 'C69 Pricing for various lengths of funding' within the instructions for reporting on ALMM, that specified that firms should use 'three month EURIBOR for EUR or a similar index for other currencies' when reporting pricing for various lengths of funding. The respondent stated that the GBP risk free benchmark, SONIA, does not appear to constitute a similar benchmark to EURIBOR, as SONIA does not include any credit adjustment spreads. After reviewing these comments, the PRA considers that risk-free benchmarks, such as SONIA, may be regarded as similar indexes for the purpose of this return. The PRA has amended the Annex XIX of the Instructions for Reporting on ALMM to reflect this view.

NSFR

14.20 Two respondents commented on the reporting of the NSFR. One respondent supported the simplified version of the NSFR for smaller firms, but thought that firms would be able to retain the option for a limited period of time, should they prefer, of reporting the current templates on stable funding (C60 and C61), instead of the new NSFR returns. The other respondent queried the reporting date of the NSFR, any future changes to Taxonomy 3.0, and potential amendments to reporting and disclosure templates that the PRA may consider. The PRA clarifies that the NSFR templates have superseded templates C60 and C61. Firms will no longer be able to report templates C60 and C61 from Saturday 1 January 2022, and must comply with the NSFR reporting requirements set out in

Annexes XII and XVIII of the CRR Regulatory Reporting Part of the PRA Rulebook. The PRA cannot comment on any future changes at this stage. Any amendments to the reporting taxonomy or templates will follow future changes to PRA reporting and disclosure requirements, which are subject to the FSMA consultation process.

Market risk

14.21 Four respondents provided feedback on reporting requirements for the FRTB standardised approach (SA). One respondent welcomed the proposed alignment of the FRTB SA reporting templates with the corresponding EBA templates, and another respondent considered that implementation was feasible for Saturday 1 January 2022 on the basis that supporting technical instructions were finalised by the middle of 2021. Another two respondents encouraged the PRA to reconsider the proposed implementation timing, which would precede the implementation of the binding FRTB capital requirement.

14.22 The PRA set out in CP5/21 that it considered the early reporting of the FRTB SA templates to be beneficial to supervisors by providing access to data that quantifies market risk according to the new FRTB international standards. Following responses received to its consultation, HM Treasury has decided to implement the FRTB SA reporting requirements alongside any changes to FRTB revisions to Pillar 1 capital requirements (ie as part of Basel 3.1 and not from 1 January 2022).⁷⁵ To act consistently with this, the PRA has decided not to implement the proposed reporting requirement for the FRTB SA templates on Saturday 1 January 2022, and the proposed rules relating to FRTB SA reporting will not be published.

14.23 Although it was not consulted upon in CP5/21, two respondents sought clarity on the timeline of FRTB Internal Model Approach reporting (IMA), and supported a potential lag between FRTB IMA reporting and the associated capital requirement. One respondent also welcomed a roadmap for FRTB implementation. The PRA will consult on FRTB IMA reporting in due course as part of its implementation of future Basel 3.1 standards in the UK.

PRA Capital+ reporting

14.24 One respondent requested that the PRA does not change Capital+ returns for a period of time, noting that although the proposed changes to templates PRA101 and PRA102 were minor, these will require resources to implement. The PRA considers it important that this reporting is aligned to the prudential methodologies in use, and where these change, it is necessary for the underlying reporting to change. Notwithstanding, it is important that any changes are appropriately justified, and are proportionate to the supervisory benefits derived. The PRA will proceed with the changes to the reporting templates PRA101 and PRA102 within Capital+ as proposed, but will continue to consider proportionality and resource implications in all of its policymaking, including with regard to future changes to Capital+.

Reporting on internal ratings based (IRB) portfolio risk

14.25 One respondent queried whether template FSA045 would need to be reported in parallel with template C08.03 (IRB Approach to Capital Requirements: Breakdown by PD Ranges) before it is retired. The PRA proposed to remove template FSA045 on Saturday 1 January 2022. As the first reporting reference date for template C08.03 falls after this date, firms will not have to report templates FSA045 and C08.03 in parallel.

⁷⁵ 'Implementation of the Investment Firms Prudential Regime and Basel 3 standards Consultation response', see: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/995628/OFFICIAL_-_MARKET_SENSITIVE_Prudential_Consultation_Updated_220621.pdf.

Other responses

Losses stemming from lending collateralised by immovable property

14.26 One respondent highlighted continuing references to ‘the Union’ within the instructions for template C15.00 on losses stemming from lending collateralised by immovable property, and sought confirmation on the scope of immovable property markets captured by the template. Article 430a of the reporting rules in Annex J set out that separate reporting of immovable property exposures on a national basis is only required for the UK. The PRA has updated the reporting instructions to template C15.00 to reflect this Article, thereby clarifying the scope of information to be reported.

Remittance deadlines

14.27 One respondent called on the PRA to review year-end reporting deadlines to allow for greater alignment between disclosure and reporting. The general remittance dates were not in scope of CP5/21. The PRA considers the existing dates necessary to receive reporting data from all firms in a timely and consistent manner. Disclosure dates vary in accordance with the publication of firms’ annual reports, and the alignment of reporting to these dates may result in inconsistent reporting requirements across firms. Therefore, the PRA will not review year-end reporting deadlines at this time.

Additional guidance

14.28 One respondent highlighted that CP5/21 did not include a version of the EBA’s mapping tool, which sets out the link between disclosure data and reporting data. The respondent requested clarity on whether the PRA will publish its own mapping tool. The PRA considers that the reporting and disclosure instructions should be sufficiently clear to facilitate compliance by firms with both sets of requirements. CP5/21 proposed to align both reporting and disclosure requirements with those developed by the EBA for Taxonomy 3.0 and the Implementing Technical Standards (ITS) on disclosure. Firms may consider the appropriateness of using other guidance when implementing these requirements, and the PRA does not intend to publish additional compliance guidance.

14.29 One respondent provided comments on the EBA Q&A process, noting its importance under the EBA’s oversight over reporting requirements, and sought clarity on the PRA’s approach to answering reporting queries. While such a process is outside the scope of CP5/21, the PRA agrees that a mechanism to answer and make public queries on the application of reporting requirements is important to support consistent reporting by firms. The PRA will consider in due course how it may implement such a process, and provide guidance on the application of EBA Q&As published before the end of the transition period that are relevant to the reporting and disclosure requirements in the PRA Rulebook.⁷⁶

Other amendments

14.30 Through the course of the PRA’s own review, it has identified a small number of minor errors in the reporting templates consulted upon. This includes minor formatting and typographical errors in Capital+, PRA financial statements, and ring-fenced bank reporting. The PRA has also identified a deletion required to row 514 on the ‘Minimum value commitment shortfall’ in COREP template CA1 and Capital+, which the PRA is not implementing. The final reporting templates will be updated for these items.

⁷⁶ The EU (Withdrawal Agreement) Act 2020 defines transition period as 11pm on 31 December 2020.

15 Disclosure

15.1 The PRA proposed to introduce new rules via a new Disclosure Part of the PRA Rulebook, and supporting amendments to SS2/19⁷⁷ to align UK Pillar 3 disclosure requirements with phases 1 and 2 of the Basel III disclosure standards. The PRA also proposed to retire SS6/17⁷⁸ as part of the proposed introduction of new counterparty credit risk disclosures. The PRA proposed to implement these disclosure changes by aligning the format and content of the majority of disclosures with the EBA ITS on public disclosure.

15.2 The PRA proposed:

- introducing new disclosure templates for counterparty credit risk, and limiting the application of the disclosure template UK CCR5 on the composition of collateral to firms for which total collateral posted and total collateral received respectively both exceed £125 billion;
- introducing new disclosure templates for Interest Rate Risk in the Banking Book (IRRBB);
- introducing a new disclosure template for the NSFR for large and listed institutions, and revisions to the key metrics template to facilitate NSFR disclosure by small and non-complex institutions. The PRA asked firms whether the disclosure of the NSFR on a spot basis could lead to adverse signalling in times of stress;
- introducing new disclosure templates for securitisations;
- introducing a requirement for firms to make disclosures on TLAC, without setting the content and format of the disclosures; and
- updating SS2/19 on the interpretation of EU-based references in the new proposed remuneration disclosures.

15.3 The proposed implementation date for all disclosure changes was Saturday 1 January 2022.

15.4 The PRA received comments from six respondents on the disclosure chapter of CP5/21.

Proportionality

15.5 One respondent welcomed the PRA's proposals to vary the application and frequency of some disclosure templates for small and non-complex banks, but requested that the PRA provide a list of the disclosure requirements that only apply to such firms, to save time that may otherwise be spent assessing the application of the requirements. The PRA has set out, in Article 433b of the Disclosure (CRR) Part of the PRA Rulebook, a complete list of the disclosure articles applicable to small and non-complex banks. While the PRA has had regard to setting proportionate disclosure requirements, it is important for firms to evaluate for themselves which requirements may apply to them, and the PRA has not made any changes to the level of detail on the application of disclosure requirements.

15.6 One respondent proposed that the PRA revisit quarterly disclosure requirements, and consider limiting these to consolidated and ring-fenced entities only. In the CP, the PRA proposed to vary

⁷⁷ SS2/19 'PRA approach to interpreting reporting and disclosure requirements and regulatory transactions forms after the UK's withdrawal from the EU', April 2019: <https://www.bankofengland.co.uk/prudential-regulation/publication/2019/pr-a-approach-to-interpreting-reporting-and-disclosure-reqs-and-reg-trans-forms-ss>.

⁷⁸ SS6/17 'Compliance with the EBA's Guidelines on disclosure', September 2017: <https://www.bankofengland.co.uk/prudential-regulation/publication/2017/compliance-with-the-ebas-guidelines-on-disclosure>.

disclosure frequencies by firm size classification and listing status. For firm size classification, the PRA proposed to limit quarterly disclosure requirements to large firms. For the 'small and non-complex' and 'other firms' categories, the PRA proposed to focus key metrics. For listing status, the PRA proposed to require large listed firms to make detailed quarterly disclosures (ie by disclosing a greater number of granular templates. The PRA proposed to require non-listed large firms only to disclose on summary key metrics. Disclosure on a solo basis is limited to subsidiaries of third country firms, or where a firm is neither a parent nor subsidiary itself (ie a 'pure solo' firm).

15.7 Taken together, the PRA considers that these requirements are already proportionate, and has not changed the level of application of disclosure requirements.

Counterparty credit risk

15.8 One respondent agreed with the proposal to increase the application threshold limiting the disclosure of the UK CCR5 template on the composition of collateral in order to reduce the risk that emergency liquidity assistance (ELA) provided by the Bank of England may be detected in the disclosure of template UK CCR5. The respondent also supported the proposal to simplify the design of template UK CCR5 to further reduce the risk of ELA visibility.

Interest Rate Risk in the Banking Book (IRRBB)

15.9 One respondent raised a concern that the proposed IRRBB disclosure template contained information of a proprietary and commercially sensitive nature, particularly the quantitative disclosure of average repricing maturity assigned to non-maturity deposits (NMDs), and longest repricing maturity assigned to NMDs. After reviewing the contents of the disclosure templates in light of these comments, the PRA does not consider the required data to be sensitive in nature, and therefore has not made amendments to the disclosure requirements.

15.10 The same respondent welcomed further clarification on the first reporting dates and frequency of reporting expected for the quantitative and qualitative parts of IRRBB disclosure. Articles 433 to 433c of Annex K to the draft rule instrument set out the disclosure frequencies for all templates, including both templates UK IRRBBA and UK IRRBB1. Template UK IRRBBA is an annual disclosure. Template UK IRRBB1 is an annual disclosure for most firms, apart from large institutions, for which a semi-annual disclosure is required. The first disclosure reference date for all disclosure requirements is defined by the frequency set out in Articles 433 to 433c, following Saturday 1 January 2022. For example, many firms will disclose the annual UK IRRBBA template as at Saturday 31 December 2022.

15.11 The same respondent also commented that while template UK IRRBBA compares current versus prior periods, for the first disclosure made by firms, this would require disclosure for periods prior to the binding requirement. The PRA considers that the template must be disclosed using information following the date from which the revised IRRBB requirements apply in the UK. Therefore, for the first disclosure reference date, firms are not required to disclose comparative numbers (to prior periods) in template UK IRRBB1.

15.12 The PRA consulted on a proposed rule regarding disclosure of risks arising from potential changes in interest rates, including the assumptions used by firms for changes to the economic value of equity.⁷⁹ The PRA has updated this rule to refer to the PRA Rulebook and the disclosure instructions, instead of to SS31/15.

⁷⁹ Article 448(1)(e)(ii).

Disclosure of the NSFR on a spot basis

15.13 The PRA proposed to require spot disclosures of firms' NSFR positions and component elements.

15.14 Eight respondents supported the use of average disclosures of the NSFR, which is in line with the PRA's requirements for LCR disclosures. One respondent stated that average disclosures would make NSFR changes less visible to market participants. One respondent stated that disclosure on an average basis should provide a better view of a firm's position over a long-term horizon. One respondent stated that spot NSFR disclosures would lead to adverse signalling impacts that would be likely to affect disproportionately smaller and growing firms that may not have credit ratings for market participants to observe. The respondent commented that this would result in smaller firms needing to maintain a degree of conservatism in order to compete with bigger firms (who have other observable characteristics such as credit ratings). The respondent also stated that this could affect an orderly recovery or resolution.

15.15 The PRA has considered the responses received and decided to implement averaged disclosures of the NSFR based on the end of quarter NSFRs from the last four quarters. The PRA considers this approach prudent due to the possible unintended and adverse consequences that may follow a firm disclosing a potentially volatile spot number that is not indicative of the firm's funding risk.

G-SII indicator disclosure

15.16 Two respondents commented on the potential benefit of continuing to allow signposting to separate disclosures, citing remuneration and G-SII indicator disclosures as two potentially relevant examples. The PRA considers that it is important that all disclosures are made in a single location or medium for the benefit of users. Given the prescription and format of Pillar 3 disclosures, it is unlikely that disclosures made under other requirements are consistent with the detailed Pillar 3 requirements.

15.17 The PRA understands that G-SII disclosure is a unique case, as the data publicly disclosed in accordance with Pillar 3 requirements must be identical to that submitted by the end of April each year as part of the Basel G-SIB assessment exercise. Therefore, the PRA considers it reasonable to give firms the option to comply with Article 441 using the data submitted to the PRA for the purpose of the Basel G-SIB assessment exercise, and to publish this data separately to the Pillar 3 report to align with the timing of the Basel exercise. The PRA has added a new Article 434b on the timing and means of disclosures, to give firms the option to publish the information required under Article 441 within four months of their financial year-end, in which case these disclosures may be published through a separate medium or in a separate location to the Pillar 3 report. Firms that apply these derogations to the timing and means of disclosure requirements will be required to make a statement in their Pillar 3 report alerting users to the location and timing of the future Article 441 disclosure.

Other responses

IRB credit risk

15.18 One respondent commented on the instructions and the template on 'UK CR7-A IRB approach – Disclosure of the extent of the use of CRM techniques'. The respondent highlighted the potentially inconsistent approach to the presentation of risk-weighted exposure assets (RWEA) whereby the impact of the substitution effect should be excluded according to the template column title, but included according to the instructions. The PRA has considered how RWEA should be disclosed in template UK CR7-A, and concludes that the disclosure of RWEA in template UK CR7-A should reflect

the substitution effect. The PRA has amended the column titles in the template and instructions to reflect this approach.

15.19 The same respondent also requested that the instructions in relation to template 'CR6 IRB approach – Credit risk exposures by exposure class and PD range' be amended to explicitly exclude non-credit obligation assets for which it would be inappropriate to disclose by probability of default range. Although not specifically excluded within the instructions, the PRA agrees that these assets should not be disclosed in this template, and the instructions have been amended to reflect this.

Scope of consolidation

15.20 One respondent stated that the scope of template LI3, 'Outline of the differences in the scopes of consolidation (entity by entity)' 'reflects a degree of materiality'. However, the respondent did not provide an explanation of the nature of the potential materiality issues or suggest solutions. The template discloses the differences between the accounting and the regulatory scopes of consolidation on an entity-specific basis. As this report reconciles exceptions to consolidation scopes, the PRA considers that it is important for users to have a complete comparison, and has not made any changes to how template LI3 is disclosed.

Technical standards

15.21 One respondent raised a question in relation to whether the PRA will repeal disclosure technical standards in favour of adopting new technical standards. Chapter 2 of this PS explains the approach to be taken to the repealing of technical standards under the CRR where these are restated in PRA rules. There are, in addition, EBA Guidelines that provide presentational guidance on the disclosure requirements contained in Part Eight of the CRR, and on disclosure of the LCR. The disclosure templates and instructions that will be contained in the Disclosure Part of the PRA Rulebook establish the standardised formats and detailed specifications necessary for firms to comply with the PRA's disclosure rules. The PRA will update the SoP 'Interpretation of EU Guidelines and Recommendations: Bank of England and PRA approach after the UK's withdrawal from the EU'. This reflects the discontinued relevance of the EBA Guidelines on disclosure requirements under Part Eight of the CRR, and the EBA Guidelines on LCR disclosure, once the Disclosure Part of the PRA Rulebook comes into effect. This is a consequential change and it does not have any material effect on what firms need to do as compared to the draft policy.

16 Currency denomination of thresholds and monetary values

16.1 The PRA proposed generally to specify thresholds and monetary values in Pound Sterling (GBP) for the measures proposed in the CP. The only exception to this proposed approach was the threshold for disclosure of the number of individuals that receive remuneration of €1 million or more per financial year, due to interdependencies with the Remuneration Part of the PRA Rulebook.^{80 81}

16.2 For thresholds and monetary values in the CRR and Basel III standards set in Euros (EUR),⁸² the PRA proposed to use the same average daily GBP/EUR spot exchange rate as was used when transposing CRD V,⁸³ covering the 12-month period prior to Friday 10 July 2020, rounded to the nearest integer: £1 = €1.14. The PRA proposed also to round the redenominated EUR values to 2 significant figures.

16.3 One respondent agreed that thresholds and monetary values should be specified in GBP, but noted that the proposed methodology resulted in oddly-sized thresholds. The respondent suggested that the GBP thresholds and monetary values could be rounded up to 1 significant figure, but did not explain why this would result in more appropriately sized thresholds. One respondent noted that, while in the short-term no impact was expected from specifying thresholds and monetary values in GBP, in the long-term it would create inconsistencies for firms with entities in both the UK and EU, which could generate operational burden.

16.4 Having considered the responses, the PRA has decided to maintain the GBP thresholds and monetary values as proposed in the CP. The PRA considers that the specification of thresholds and monetary values in GBP would help to reduce the extent of change in the requirements applicable to firms that result from variations over time in the GBP/EUR exchange rate. The PRA has also applied a consistent methodology to the currency denomination of thresholds and monetary values, and considers that the resulting GBP thresholds and monetary values remain appropriate at this time. The appropriateness of thresholds determining whether firms qualify for more proportionate treatments may be considered further in light of the PRA's future work on a strong and simple regime for non-systemic banks and building societies.⁸⁴

16.5 The PRA recognises that there may be some small inconsistencies in the long term for firms with entities in both the UK and EU. However, the PRA expects these will be manageable for these firms and considers that, as the majority of PRA-regulated firms operate in GBP, there is still a net benefit to specifying the thresholds and monetary values in GBP.

16.6 One respondent highlighted an error in Paragraphs 8.19 and 8.23 of the CP, where the threshold for the size of derivative business below which firms can calculate their counterparty credit risk exposure value under the simplified SA-CCR was specified at £263 million. The PRA can clarify that £260 million is the correct value for this threshold, as reflected in Table 1 in Chapter 15 of

⁸⁰ CRR Article 450(1)(i) requires firms to disclose this information in payment bands of €500,000 for individuals earning between €1 million and €5 million, broken down into pay bands of €500,000, and broken down into pay bands of €1 million for remuneration of €5 million and above. The PRA's rules are in Article 450(1)(i) of the Disclosure (CRR) Part.

⁸¹ Chapter 18 of the Remuneration Part of the PRA Rulebook requires firms to report the same information to the PRA as this disclosure requirement. Both use the same template, which is denominated in EUR.

⁸² This is also the case for the EU CRR II requirements that the PRA used as a basis for developing its PRA rules.

⁸³ The PRA redenominated EUR thresholds in PRA rules relating to the identification of Material Risk Takers (MRTs) for remuneration purposes. December 2020: <https://www.bankofengland.co.uk/prudential-regulation/publication/2020/capital-requirements-directive-v-further-implementation>.

⁸⁴ April 2021: <https://www.bankofengland.co.uk/prudential-regulation/publication/2021/april/strong-and-simple-framework-banks>.

the CP, and in Article 273a (1)(b) of Chapter 3 of the Counterparty Credit Risk (CRR) Part of the draft PRA Rulebook (CRR) Instrument 2021.⁸⁵

⁸⁵ <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/consultation-paper/2021/february/cp521app9.pdf>.

17 The temporary transitional power (TTP)

17.1 The TTP enables the UK's financial services regulators to delay the application of firms' regulatory obligations where they have been subject to an onshoring change under the European Union (Withdrawal) Act 2018.⁸⁶ The PRA is using the TTP to provide broad transitional relief to firms until Thursday 31 March 2022, with key exceptions expressly provided for in the PRA's transitional direction.⁸⁷

17.2 In order to preserve the effect of the TTP for provisions in the CRR, and CRR Level 2 Regulations, that are to be transferred into PRA rules on Saturday 1 January 2022 ('CRR restatement provisions'), the PRA proposed to include a mirror provision in the Interpretation Part of the PRA Rulebook. This would replicate the effect of the PRA's transitional direction for CRR restatement provisions until Thursday 31 March 2022, when the direction is due to expire. The mirror provision would only apply to CRR restatement provisions. It could not apply to new PRA rules, or PRA rules which are materially changing, such as the NSFR.

17.3 The PRA also proposed to carve-out the Liquidity (CRR) Part of the PRA Rulebook, the Liquidity Coverage Ratio (CRR) Part of the PRA Rulebook, and the related liquidity reporting and disclosure rules in the Reporting and Disclosure Parts of the PRA Rulebook, from the application of the mirror provision. This was to ensure consistency across the LCR and the NSFR.

17.4 The PRA did not receive any responses to its proposals on the TTP mirror provision. The PRA will therefore publish the policy as proposed.

17.5 The PRA has updated its relevant TTP guidance documents to reflect these changes.⁸⁸

⁸⁶ The UK's withdrawal from the EU required changes to be made to UK legislation, including the body of EU law that was retained in the UK, to ensure that it remained functional after the end of the transition period. These changes are referred to as 'onshoring changes'.

⁸⁷ December 2020, Appendix 2: <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/policy-statement/2020/ps3020app2.pdf>.

⁸⁸ Available at: <https://www.bankofengland.co.uk/eu-withdrawal/temporary-transitional-power>.

Appendices

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- 1 Near-final CRR RULES INSTRUMENT 2021, available at:
<https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/policy-statement/2021/july/ps1721app1.pdf>

 - 2 Near-final PRA RULEBOOK: CRR FIRMS: (CRR 2 REVOCATIONS AND OTHER AMENDMENTS) INSTRUMENT 2021, available at: <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/policy-statement/2021/july/ps1721app2.pdf>

 - 3 SS15/13 'Groups', available at: <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/supervisory-statement/2021/ss1513-jan-2022.pdf>

 - 4 SS12/13 'Counterparty credit risk', available at: <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/supervisory-statement/2021/ss1213-jan-2022.pdf>

 - 5 Statement of Policy (SoP) 'The PRA's methodologies for setting Pillar 2 capital', available at: <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/statement-of-policy/2021/the-pras-methodologies-for-setting-pillar-2a-capital-jan-2022.pdf>

 - 6 SS16/13 'Large exposures', available at: <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/supervisory-statement/2021/ss1613-jan-2022.pdf>

 - 7 SoP 'Liquidity and funding permissions', available at: <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/statement-of-policy/2021/liquidity-and-funding-permissions-sop-jan-2022.pdf>

 - 8 SS24/15 'The PRA's approach to supervising liquidity and funding risks', available at: <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/supervisory-statement/2021/ss2415-jan-2022.pdf>

 - 9 SS34/15 'Guidelines for completing regulatory reports', available at: <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/supervisory-statement/2021/ss3415-jan-2022.pdf>

 - 10 SS2/19 'PRA approach to interpreting reporting and disclosure requirements and regulatory transaction forms after the UK's withdrawal from the EU', available at: <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/supervisory-statement/2021/ss219-jan-2022.pdf>

 - 11 SoP 'Interpretation of EU Guidelines and Recommendations: Bank of England and PRA approach after the UK's withdrawal from the EU', available at: <https://www.bankofengland.co.uk/-/media/boe/files/paper/2021/interpretation-of-eu-guidelines-and-recommendations-boe-and-pra-approach-sop-jan-2022.pdf>

 - 12 Detailed analysis of objectives and 'have regards', available at: <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/policy-statement/2021/july/ps1721app12.pdf>

 - 13 Summary of the purpose of the rules, available at: <https://www.bankofengland.co.uk/->

[/media/boe/files/prudential-regulation/policy-statement/2021/july/ps1721app13.pdf](https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/policy-statement/2021/july/ps1721app13.pdf)

- 14 Corresponding provisions, available at: <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/policy-statement/2021/july/ps1721app14.pdf>
- 15 Restatement provisions, available at: <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/policy-statement/2021/july/ps1721app15.pdf>
- 16 Reporting templates and instructions: see table below for links to each item.
- 17 Disclosure templates and instructions: see table below for links to each item.
- 18 SS16/17 'Compliance with the EBA's Guidelines on disclosure'. This SS would be repealed at the policy implementation date should policy become final. Current version is available at: <https://www.bankofengland.co.uk/prudential-regulation/publication/2017/compliance-with-the-ebas-guidelines-on-disclosure>

16 Reporting templates and instructions

PRA data items	Hyperlink
PRA101 Capital+ actuals and forecast	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pr101-template-jan-2022.xlsx
PRA102 Capital+ forecast semi-annual	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pr102-template-jan-2022.xlsx
PRA103 Capital+ forecast annual	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pr103-template-jan-2022.xlsx
PRA104 Balance sheet - forecast data (Assets)	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pr104-template-jan-2022.xlsx
PRA105 Balance sheet - forecast data (Liabilities)	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pr105-template-jan-2022.xlsx
PRA106 Balance sheet - forecast data (Equity)	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pr106-template-jan-2022.xlsx
PRA107 Statement of profit or loss - forecast data	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pr107-template-jan-2022.xlsx
PRA108 Memorandum items	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pr108-template-jan-2022.xlsx
RFB data items	
RFB001 Intragroup exposures	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/rfb001-template-jan-2022.xlsx
RFB003 Intragroup financial reporting (core)	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/rfb003-template-jan-2022.xlsx
RFB004 Intragroup financial reporting (detailed breakdown)	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/rfb004-template-jan-2022.xlsx
UK COREP and FINREP data items	

Annex I: Reporting on own funds and own funds requirements	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/corep-own-funds.xlsx
Annex III: Reporting financial information according to IFRS	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/finrep-ifs.xlsx
Annex IV: Reporting financial information according to national accounting frameworks	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/finrep-national-accounting-framework.xlsx
Annex VI: Reporting on losses stemming from lending collateralised by immovable property	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/corep-losses-immovable-property.xlsx
Annex VIII: Reporting on large exposures and concentration risk	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/corep-le-concentration-risk.xlsx
Annex XII: Reporting on net stable funding ratio	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/corep-nsfr.xlsx
Annex XVI: Reporting on asset encumbrance	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/finrep-asset-encumbrance.xlsx
Annex XVIII: Reporting on additional liquidity monitoring metrics	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/corep-additional-liquidity-metrics.xlsx
Annex XX: Reporting on counterbalancing capacity	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/corep-counterbalancing-capacity.xlsx
Annex XXIV: Reporting on liquidity	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/corep-liquidity.xlsx
Annex XXVI: Supplementary reporting for the purpose of identifying and assigning G-SII buffer rates	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/corep-g-sii-buffer-rates.xlsx
UK COREP and FINREP instructions	
Annex II: Instructions for reporting on own funds and own funds requirements	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/corep-own-funds-instructions.pdf
Annex V: Instructions for reporting financial information	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/finrep-instructions.pdf
Annex VII: Instructions for reporting on losses stemming from lending collateralised by immovable property	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/corep-losses-immovable-property-instructions.pdf
Annex IX: Instructions for reporting on large exposures and concentration risk	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/corep-le-concentration-risk-instructions.pdf
Annex XIII: Instructions for reporting on net stable funding ratio	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/corep-nsfr-instructions.pdf
Annex XIV: Single Data Point Model principles	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/single-data-point-model-principles.pdf
Annex XV: Validation rules	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/validation-rules.pdf
Annex XVII: Instructions for reporting on asset encumbrance	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/finrep-asset-encumbrance-instructions.pdf
Annex XIX: Instructions for reporting on additional liquidity monitoring metrics	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/corep-additional-liquidity-metrics-instructions.pdf
Annex XXI: Instructions for reporting on counterbalancing capacity	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/corep-counterbalancing-capacity-instructions.pdf
Annex XXV: Instructions for reporting on liquidity	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/corep-liquidity-instructions.pdf

Annex XXVII: Instructions for supplementary reporting for the purpose of identifying and assigning G-SII buffer rates	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/corep-g-sii-buffer-rates-instructions.pdf
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Disclosure templates and instructions

UK Pillar 3 disclosure data items	Hyperlink
Annex I: Disclosure of key metric and overview of risk weighted exposure amounts	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-risk-weighted-exposure.xlsx
Annex III: Disclosure of risk management objectives and policies	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-risk-management.xlsx
Annex V: Disclosure of the scope of application	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-scope-of-application.xlsx
Annex VII: Disclosure of own funds	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-own-funds.xlsx
Annex IX: Disclosure of countercyclical capital buffers	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-ccyb.xlsx
Annex XIII: Disclosure of liquidity requirements	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-liquidity.xlsx
Annex XV: Disclosure of credit risk quality	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-credit-risk-quality.xlsx
Annex XVII: Disclosure of the use of credit risk mitigation techniques	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-credit-risk-mitigation.xlsx
Annex XIX: Disclosure of the use of the standardised approach	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-standardised-approach.xlsx
Annex XXI: Disclosure of the use of the IRB approach to credit risk	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-irb-credit-risk.xlsx
Annex XXIII: Disclosure of specialised lending	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-specialised-lending.xlsx
Annex XXV: Disclosure of exposures to counterparty credit risk	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-counterparty-credit-risk.xlsx
Annex XXVII: Disclosure of exposures to securitisation positions	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-securitisation-positions.xlsx
Annex XXIX: Disclosure of use of standardised approach and internal model for market risk	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-sa-ima-market-risk.xlsx
Annex XXXI: Disclosure of operational risk	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-operational-risk.xlsx
Annex XXXIII: Disclosure of remuneration policy	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-remuneration.xlsx
Annex XXXV: Disclosure of encumbered and unencumbered assets	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-encumbered-unencumbered-assets.xlsx
Annex XXXVII: Disclosure of interest rate risk in the banking book (IRRBB)	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-irrbb.xlsx
UK Pillar 3 disclosure instructions	
Annex II: Instructions for disclosure of key metric and overview of risk weighted exposure amounts	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-risk-weighted-exposure-instructions.pdf
Annex IV: Instructions for disclosure of risk management objectives and policies	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-risk-management.pdf
Annex VI: Instructions for disclosure of	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-risk-weighted-exposure-instructions.pdf

the scope of application	regulation/regulatory-reporting/banking/pillar3-scope-of-application-instructions.pdf
Annex VIII: Instructions for disclosure of own funds	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-own-funds-instructions.pdf
Annex X: Instructions for disclosure of countercyclical capital buffers	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-ccb-instructions.pdf
Annex XIV: Instructions for disclosure of liquidity requirements	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-liquidity-instructions.pdf
Annex XVI: Instructions for disclosure of credit risk quality	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-credit-risk-quality-instructions.pdf
Annex XVIII: Instructions for disclosure of the use of credit risk mitigation techniques	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-credit-risk-mitigation-instructions.pdf
Annex XX: Instructions for disclosure of the use of the standardised approach	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-standardised-approach-instructions.pdf
Annex XXII: Instructions for disclosure of the use of the IRB approach to credit risk	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-irb-credit-risk-instructions.pdf
Annex XXIV: Instructions for disclosure of specialised lending	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-specialised-lending-instructions.pdf
Annex XXVI: Instructions for disclosure of exposures to counterparty credit risk	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-counterparty-credit-risk-instructions.pdf
Annex XXVIII: Instructions for disclosure of exposures to securitisation positions	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-securitisation-positions-instructions.pdf
Annex XXX: Instructions for disclosure of use of standardised approach and internal model for market risk	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-sa-ima-market-risk-instructions.pdf
Annex XXXII: Instructions for disclosure of operational risk	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-operational-risk-instructions.pdf
Annex XXXIV: Instructions for disclosure of remuneration policy	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-remuneration-instructions.pdf
Annex XXXVI: Instructions for disclosure of encumbered and unencumbered assets	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-encumbered-unencumbered-assets-instructions.pdf
Annex XXXVIII: Instructions for disclosure of interest rate risk in the banking book (IRRBB)	https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/regulatory-reporting/banking/pillar3-irrbb-instructions.pdf