Bank of England

Financial Stability in Focus: The bank capital framework

Financial Policy Committee
July 2026

Financial Stability in Focus

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The primary responsibility of the Financial Policy Committee (FPC), a committee of the Bank of England, is to contribute to the Bank of England's financial stability objective. It does this primarily by identifying, monitoring and taking action to remove or reduce systemic risks, with a view to protecting and enhancing the resilience of the UK financial system. Subject to that, it supports the economic policy of His Majesty's Government, including its objectives for growth and employment.

The Financial Stability in Focus (FSiF) sets out the FPC's view on specific topics related to financial stability. It complements the Financial Stability Report, which is published twice a year, and sets out the FPC's overall view of the outlook for UK financial stability, including its assessment of the resilience of the UK financial system and the main risks to UK financial stability, and the action it is taking to remove or reduce those risks.

The Financial Policy Committee:

Andrew Bailey, Governor
Sarah Breeden, Deputy Governor responsible for financial stability
Clare Lombardelli, Deputy Governor responsible for monetary policy
Dave Ramsden, Deputy Governor responsible for markets and banking
Sam Woods, Deputy Governor responsible for prudential regulation (until 30 June)*
Nathanaël Benjamin, Executive Director of financial stability strategy and risk
Nikhil Rathi, Chief Executive of the Financial Conduct Authority
Stephen Blyth
Jon Hall
Randall Kroszner
Liz Oakes
Carolyn Wilkins
Gwyneth Nurse attends as the Treasury member in a non-voting capacity.

This document, unless otherwise stated, uses data available as at 25 June 2026.

For the avoidance of doubt, the Financial Stability in Focus is not intended to satisfy the requirements of Section 9W of the Bank of England Act 1998.

* Katharine Braddick assumed the role of Deputy Governor for prudential regulation on 1 July.

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Executive summary

The FPC, working with the PRA, is modernising the bank capital framework. The Committee is announcing a package of proposed changes that will help ensure the framework is simpler, more effective, more proportionate and better calibrated to the risks in today's financial system, while also ensuring that the UK banking system remains resilient and able to support the economy when it needs it most. This package will address unintended consequences in the leverage framework and strengthen the releasability and usability of buffers. The measures will make it easier for banks to use capital to support lending and the functioning of core markets in stress, while maintaining overall consistency with international standards.

In December 2025, the FPC revisited its assessment of appropriate capital requirements for the UK banking system. The Committee judged that the appropriate benchmark for system-wide Tier 1 capital requirements was around 13% of risk-weighted assets – equivalent to a Common Equity Tier 1 (CET1) ratio of around 11%.[1] That assessment was made with a view to maximising long-run growth in the UK economy by weighing the macroeconomic costs of capital, which stem from the impact of higher capital on borrowing costs, against the macroeconomic benefits of capital, which arise because higher bank capital reduces the likelihood and costs of future financial crises.

The FPC also identified areas where the capital framework might warrant adjustment to make it more effective, efficient and proportionate in future, and to address any unintended consequences within the existing regime. In particular, the FPC said it would work to enhance further the usability of regulatory capital buffers, review the implementation of the leverage ratio in the UK to ensure it functions as intended, and support further work to consider proportionality and complexity in the framework, including the way that capital requirements related to domestic exposures interact.

The FPC welcomed feedback received from a broad group of stakeholders on the issues covered in its **December 2025 Financial Stability in Focus** (FSiF) (summarised in Box A). This included feedback on the overall level of capital requirements, international comparisons, the functioning of the capital buffer framework and the leverage ratio, and capital requirements related to domestic exposures.

The FPC considers the range of views received on the overall level of bank capital requirements to be broadly reflective of the issues the Committee had weighed in its December assessment. The Committee therefore reaffirms its judgement that the appropriate benchmark for system-wide Tier 1 capital requirements is around 13% of risk-weighted assets – equivalent to a CET1 ratio of around 11%.

Since December, the FPC, working with the PRA, has progressed its analysis of buffer usability and the leverage ratio, and is announcing a package of reforms informed by the feedback it has received.

Further enhancing the usability and releasability of regulatory capital buffers

Capital buffers are intended to be used to absorb losses and to help maintain the provision of financial services to the real economy in a downturn by reducing the need for banks to deleverage to preserve capital. But a range of interrelated factors can impede the usability of regulatory capital buffers in practice. These factors can also contribute to banks maintaining capital substantially above regulatory requirements and so reducing their capacity to lend.

The FPC sees a clear macroprudential case for a simpler and more effective capital buffer framework that reduces impediments to buffer usability. Other regulators internationally have also set out thinking and are engaging in discussions within their jurisdictions on different ways that their banking capital frameworks could be simplified domestically with a view to making them more effective and efficient. The Committee will work with the PRA and international authorities to pursue broad reform of the capital buffer framework and move towards a goal of a single buffer that is releasable in stress, and that can be used without automatic distribution restrictions.

In the near term, the FPC and PRA are taking steps domestically to support buffer usability by making clear that systemic buffers for domestic systemically important banks will be releasable in a stress. The FPC welcomes the **PRA's intention** to use its existing discretionary powers to release the other systemically important institution (O-SII) buffer that applies to certain domestic systemically important firms[2] in the event of systemic stress, engaging with the FPC when doing so.

The impact of releasing the O-SII buffer would be similar in many ways to releasing the countercyclical capital buffer (CCyB). It would lower the level of capital at which distribution restrictions automatically apply, which would reduce banks' incentives to take defensive actions such as counterproductive deleveraging. The pace of return to normal-times O-SII buffer rates would depend on banks' ability to rebuild capital while continuing to lend to creditworthy UK households and businesses. The FPC and PRA recognise that when banks' capital ratios decline in a stress, their combined regulatory buffers may then need to be rebuilt over multiple years, as has been the case with previous releases of the CCyB. Otherwise, the prospect of a rapid rebuild could undermine banks' incentives to use the released capital. The PRA will consult on its approach to setting O-SII buffers in 2026 H2 (**PRA statement**).

In addition to the steps being taken to enhance releasability and lower the level of capital at which automatic distribution restrictions apply in stress, the PRA will consider firms' feedback that greater clarity on the use of the PRA buffer in circumstances outside periods of systemic stress could help buffer usability. The PRA will also consider whether further engagement with relevant stakeholders, including investors and rating agencies, could support understanding of the role of regulatory capital buffers and how the framework is intended to operate.

The implementation of the leverage ratio in the UK

The leverage ratio – the ratio of a bank's capital to a gross measure of its exposures – is an important part of the capital framework. Complementing the risk-weighted requirement with a leverage ratio requirement makes the capital framework more robust against the inherent errors and uncertainties in measuring risk when assigning risk weights. More generally, leverage ratio capital requirements can help to curtail balance sheet growth that is unsustainable from a systemic perspective.

In the UK, leverage ratio requirements comprise a minimum of 3.25% of the UK leverage exposure measure (excluding central bank reserves), a systemic buffer (known as the additional leverage ratio buffer or ALRB[3]) for global systemically important banks (G-SIBs) and certain other systemically important institutions (O-SIIs), and the countercyclical leverage buffer (CCLB). At present, the ALRB and the CCLB are applied at 35% of the equivalent risk-based buffers.

In its December FSiF, the FPC committed to review the implementation of the leverage ratio in the UK to ensure that it functions as intended, prioritising reviewing the UK's approach to regulatory buffers in leverage requirements. This work has highlighted a number of features of the UK's leverage ratio framework:

- The decline in average risk weights in the UK has contributed to leverage ratio requirements becoming more binding. This is to be expected to some extent in a framework with both leverage and risk-based capital requirements, as banks structure their balance sheets in a way that most efficiently meets both. While there is some evidence that the decline in average risk weights has been driven by a reduction in the riskiness of banks' exposures over the past decade, there has also been growth in more complex and opaque forms of lending where the leverage ratio may be particularly effective in guarding against errors in risk measurement. Taken together, these trends highlight the continued importance of the leverage ratio framework.
- Although the calibration of UK leverage ratio requirements is consistent overall with international standards, the UK's implementation of some elements of the leverage ratio framework differs from those standards, including its approach to setting leverage ratio buffers. When the FPC designed its leverage ratio framework, it included both a systemic component and countercyclical component to maintain the relative bindingness of the

leverage regime for systemically important firms and during times of high system-wide risk, setting the level of those buffers at 35% of their risk-weighted counterparts. This preceded the finalisation of the Basel standards, which included a single leverage ratio buffer set at 50% of systemic risk-weighted buffers for G-SIBs.

- The presence of usable capital buffers is a desirable feature of the leverage ratio regime. Such leverage buffers help ensure that banks whose activity is relatively concentrated in lower-risk weighted lending to the real economy, such as mortgage lending, can absorb losses and continue to support the economy in an economic stress. They also help ensure that banks whose activity is relatively concentrated in lower risk weighted financial market activity, including in core sterling markets, can absorb shocks and continue to support market functioning in a financial market stress.
- Nevertheless, the UK's current approach to leverage ratio buffers has a number of features that could be made more proportionate and more effective by being better targeted to achieve financial stability goals. In particular:
  - Following the FPC's decision in 2019 to increase the neutral rate for the UK CCyB from 1% to 2%, risk-weighted minimum capital requirements were adjusted so that overall regulatory loss-absorbing capacity was kept broadly unchanged. An equivalent offsetting adjustment was not made in the leverage framework. As a result, leverage ratio requirements increased when the UK CCyB rate increased to 2%, making the leverage ratio more likely to bind for a given risk profile. This unintended consequence affected all banks subject to leverage requirements. The most notable impact, however, was on banks with greater relative exposure to UK domestic lending, especially those with lower average risk weights.
  - Although leverage buffers help to ensure resilience in the provision of services to financial markets as well as lending to the real economy, the CCLB is not well targeted to serve both of these purposes. The CCLB that applies to each individual bank is determined by the share of their relevant credit exposures (largely real economy exposures) in each jurisdiction, and varies in line with each jurisdiction's CCyB rate. But many banks to which the CCLB applies have business models that are focused on the provision of services to financial markets, including core sterling markets, rather than the real economy. The fact that the CCLB's calibration is driven by the mix of banks' real economy exposures means that the FPC's current countercyclical policy framework is not well designed to support market functioning.

To address these issues, the FPC and PRA intend to consult on a package of measures to make the leverage ratio framework more proportionate and more effective by being better targeted. This package would:

- Remove the CCLB from banks' leverage requirements to address the unintended consequence of how it has been implemented and reflecting the fact that its calibration is

not closely linked to the systemically important financial market activity for which the leverage ratio is a key prudential constraint.

- Move the calibration of the ALRB for firms with systemic buffers into line with international standards – to 50% of risk-weighted systemic buffers. Like its risk-weighted counterpart, the ALRB for domestically systemic firms would be releasable in a stress.
- Make a greater share of leverage requirements and buffers releasable: the leverage ratio Tier 1 minimum requirements would be reduced from 3.25% to 3% and a simple general leverage ratio buffer would be applied to firms subject to leverage requirements, set at 25 basis points of the leverage exposure measure (which currently excludes central bank reserves).

The general leverage ratio buffer would be releasable, if necessary to zero, to help ensure that banks can absorb losses in an economic or financial market stress while continuing to support the real economy and the functioning of financial markets. If, on the other hand, the FPC were to in future judge that risks were heightened and that additional resilience was warranted, it could consider increasing the general leverage ratio buffer above 25 basis points. Like all buffer requirements in the UK capital framework, the general leverage ratio buffer would be met with CET1 capital.

In its Bank Capital Stress Test, the Bank typically assesses the capital resilience of individual banks against a leverage ratio hurdle rate that includes minimum leverage ratio requirements and the ALRB. To ensure that the capital banks need to remain above the hurdle rate in the Bank Capital Stress Test did not increase as a result of this package, the Bank would expect to adjust the leverage ratio hurdle rate. Specifically, alongside these proposals, the Bank would expect to set leverage hurdle rates for the test as minimum requirements plus 40% of banks' risk-weighted systemic buffers (lower than the 50% ALRB of risk-weighted systemic buffers that would apply to banks' regulatory requirements).

When taking into account both regulatory requirements and the capital needed to remain above the leverage ratio hurdle rate in the Bank Capital Stress Test, the changes would reduce the leverage ratio that large UK banks subject to the leverage requirement need to maintain by around 20 basis points in aggregate, with the impact varying by bank. This would leave leverage ratio requirements for UK large domestically focused banks and G-SIBs within the range of other jurisdictions globally.

Next steps

The FPC considers that the package of proposed leverage ratio reforms will make the UK leverage ratio framework more proportionate and more effective by being better targeted. The Committee also agrees that the implications of the proposals for the resilience of UK markets merit further consideration. The FPC will therefore work, alongside the PRA, to identify

whether the proposed package of changes to the leverage framework would leave any financial stability gaps that would need to be managed and whether that might justify further adjustments to the policy package. This analysis, which will take into account the FPC's work on gilt repo market resilience and impacts of the proposal on market functioning, will be completed by, and considered at, the Q3 FPC meeting to allow any potential consultation on this element alongside the rest of the proposal.

Separately, the FPC expects to update on its assessment of the interaction of capital requirements that are related to domestic exposures in the Q4 2026 FSR. Capital requirements related to domestic exposures include the UK CCyB, O-SII buffers, and Pillar 2A requirements for geographic credit concentration risk, which each serve different purposes in the capital framework but are all calibrated based on measures of domestic lending. The FPC and the PRA intend to draw on several sources of information when conducting this work, including on the impact of systemic failures and credit concentration, and banks' stress-test results.

The FPC also supports other initiatives by the Bank to respond to feedback on interactions, proportionality and complexity in the capital framework. This includes the PRA's work to develop a systematic approach to updating the regulatory thresholds, the PRA's contribution to the Government's review of the ring-fencing regime, and the PRA's work to assess firms' feedback and supporting evidence on a range of possible changes to internal ratings based (IRB) models for mortgage lending.

1: Background – the FPC's assessment of bank capital requirements and priority areas for review

In December 2025, the FPC revisited its assessment of appropriate capital requirements for the UK banking system. The Committee judged that the appropriate benchmark for system-wide Tier 1 capital requirements was around 13% of risk-weighted assets – equivalent to a CET1 ratio of around 11%.

Ensuring a resilient financial system – one which can absorb rather than amplify shocks – is the most important contribution the FPC can make, not only to promote financial stability, but also to support economic growth. The banking system is a critical part of the financial system and it plays a vital role in the economy by providing financial services, including lending, to households and businesses right across the country. It is crucial that the banking system is resilient enough to support UK growth, in both good and bad times.

As set out in the **December 2025 Financial Stability in Focus (FSiF) publication**, the FPC's assessment of appropriate system-wide capital requirements is based on analysis of the level of capital that is most likely to maximise long-term growth in the UK economy.

In revising its assessment of the appropriate benchmark for the level of system-wide Tier 1 capital requirements to around 13% of risk-weighted assets (RWAs) – lower than the previous level of around 14% – the Committee took account of the experience of the 10 years since it first assessed the appropriate overall level of capital requirements, including a reduction in the systemic importance of some banks and improvements in risk measurement. The FPC considered that the inbuilt responsiveness of nominal capital requirements in the banking system – to falls in average risk weights, decreases in UK banks' systemic importance, and improvements in the measurement of risk weights – reflected desirable flexibility in the capital framework.

The FPC also judged that post-crisis reforms – including a credible and effective resolution regime, effective supervision, and the Committee's active use of the UK CCyB[4] – would continue to reduce the cost and probability of future crises, supporting previous judgements taken by the Committee which reduced the benchmark for system-wide capital requirements.

Having considered feedback received since December, the FPC reaffirms its judgement that the appropriate benchmark for system-wide Tier 1 capital requirements is around 13% of RWAs. As set out later in this FSiF, the FPC and PRA are continuing to work to make the capital framework more effective and efficient.

Following the FPC and PRA's request for feedback, the Bank has received views from a broad range of stakeholders, including on the overall calibration of bank capital requirements (summarised in Box A).

Some respondents noted that, as set out in the December FSiF, the FPC's benchmark lies towards the lower end of estimates of the optimal level of capital across several academic studies, and argued that heightened macroeconomic risks pointed towards maintaining or increasing the FPC's benchmark rather than reducing it. Others argued that the banking system's performance through recent shocks, as well as Bank of England stress test results, demonstrated that capital requirements could be reduced without undermining resilience, reflecting the effectiveness of post-crisis reforms.

There were differing views on the role of resolution frameworks in the assessment of appropriate capital requirements. Some cautioned against relying heavily on resolution to justify lower capital, citing recent international episodes of banking stress in which they observed that some authorities intervened extensively outside of formal resolution regimes. Others emphasised that resolution arrangements, which were now fully operational, were materially more credible than in the past. This made the system more resilient to stress, so it was appropriate to continue to reflect this fact in assessments of capital needs.

Banks and industry groups saw the FPC's decision to revise its Tier 1 benchmark as a welcome signal of confidence in the UK banking system. But because the reduction in the FPC's benchmark largely mirrored expected changes in actual capital requirements as a proportion of risk-weighted assets, several respondents noted that the reduction in the benchmark was expected to have limited impact on banks' desired capital positions in and of itself. They also noted that requirements for individual banks could be higher than the systemwide benchmark, reflecting: the relative weight of CCyB rates applied in different jurisdictions that banks were active in; the application of firm-specific PRA buffers; and the bindingness of leverage requirements for some banks.

> **There were a range of perspectives on what the macroeconomic impact of a reduction in bank capital requirements might be.**

Some stakeholders noted that indicators of UK credit conditions suggested capital was not currently a constraint on the supply of credit for most sectors, and it was more likely that lower capital requirements would result in greater distributions of profits, rather than directly increasing the supply of bank lending. Others noted that lower capital requirements would provide greater capacity for re-investment by banks of profits into business growth, and that increased distributions to shareholders would support economic activity and increase the attractiveness of the UK to investors. Some argued that with lower capital requirements, the cost of borrowing for households and businesses would be reduced as banks' funding costs would be lower with less relatively costly equity funding. In turn, this could boost demand for

borrowing and economic activity. Others countered that the directional relationship between cost of capital and bank capitalisation levels was not clear cut, citing academic studies that had shown that higher levels of capital were associated with higher lending, as higher levels of solvency reduced overall funding costs.

Overall credit conditions have tended to evolve in line with the macroeconomic outlook in recent years, with no evidence that banks have been restricting lending to defend their capital positions (refer to Section 6 in the July FSR). Major UK banks have also continued to report robust earnings, with price to tangible book ratios near post-global financial crisis (GFC) highs, and continued distributions to shareholders through buybacks and dividends. This suggests that bank capital has not been a material constraint on the overall provision of sustainable lending to the economy. The primary macroeconomic impacts of any changes in bank capital requirements would therefore probably come via their impact on borrowing costs to the real economy, as captured in the FPC's cost-benefit assessment.

> **Some respondents argued that the level of bank capital requirements had displaced the provision of lending from banks, moving it towards non-bank finance, where transparency and prudential oversight are weaker.**

The supply of credit to UK corporates has diversified since the GFC, with a shift towards greater market-based provision of corporate finance. Non-bank financial institutions (NBFIs) can be better placed than banks to provide certain forms of riskier lending because of fundamental differences in their liability structures. Banks create money in the form of deposit liabilities, the fixed nominal value of which is key to maintaining financial stability, including because of the role that deposits play as a means of payment. In contrast, non-banks do not create money, and their liabilities may fluctuate in value. This means that some riskier lending may appropriately be undertaken by NBFIs whose funding is longer-term or whose investors are better placed to absorb losses.

Although bank capital has increased considerably since the GFC, equity remains a relatively small component of banks' overall cost of funding. Banks typically have a higher share of debt funding – predominantly in the form of deposits – compared to private credit funds, despite being subject to capital requirements. Because deposits are typically a relatively inexpensive way to fund lending, the resulting overall funding costs for banks are likely lower than for those funds.

That said, this difference appears to have narrowed in recent years: higher risk-free rates have pushed up financing costs for both types of lender, but for private credit funds this has been offset as liquidity premia and other spreads demanded by their funding providers have declined, and as some funds have increased their leverage. The Committee is taking a

number of steps to address financial stability risks from market-based finance. Initiatives include running the private markets System-Wide Exploratory Scenario and taking forward reforms to enhance gilt repo market resilience.

The UK banking system increasingly supports market-based finance through the provision of lending and other services to NBFIs. These interlinkages can support credit provision to the real economy, while also helping banks manage their credit risk and capital positions. As set out in Section 6 of the July 2026 FSR, they can also create channels through which risks can be transmitted back to banks, meaning effective monitoring and risk management of these interconnections is important.

> **Overall, the FPC considered the range of views and richness of feedback received to be broadly reflective of the issues the Committee had weighed in its December assessment of the appropriate benchmark for system-wide capital requirements.**

That assessment was made with a view to maximising long-run growth in the UK economy by weighing the macroeconomic costs of capital, which stem from the impact of higher capital on borrowing costs, against the macroeconomic benefits of capital, which arise because higher bank capital reduces the likelihood and costs of future financial crises.

> **The FPC takes account of international standards and comparisons in assessing the UK bank capital framework.**

Robust regulatory standards and international co-operation are important to maintain the resilience of the global financial system, limit regulatory arbitrage, and to prevent and respond to shocks in order to support sustainable economic growth over the long term. As an open economy with a large international financial centre, this is of particular importance to the UK.

The December FSiF included analysis that compared capital requirements across jurisdictions. It concluded that the level of risk-based capital requirements for large banks in the UK is broadly similar to that in the euro area, and that after adjusting for key differences in the way that risks are captured, risk-based requirements appeared to be lower in the UK than in the US. It noted that requirements appeared to be higher than other jurisdictions in some specific aspects and cohorts, particularly leverage ratio requirements for large domestically focused banks.

The December FSiF also noted the challenges in comparing capital requirements across jurisdictions given differences in how risks are captured in different regulatory frameworks, and the FPC welcomed feedback on the approach taken. Most of the feedback focused on the comparison between the US and UK risk-based capital requirements.

Respondents acknowledged the inherent complexity of international comparisons but argued that alternative approaches and structural differences could affect the conclusions. In particular, some challenged the magnitude of the adjustment made in the comparison to

account for differences in how risks are captured in Pillar 2A requirements in the UK relative to the way they are captured in the US framework. While it is the case that there are many ways to compare regulatory frameworks, which could indeed lead to different conclusions, further consideration of how these risks are captured in the US framework continues to suggest a sizeable adjustment for differences in approach to capturing these risks in capital requirements is appropriate when making comparisons between the two jurisdictions.

As set out in Box B, capital frameworks are changing across jurisdictions, as Basel 3.1 and other rules are being finalised and implemented. That means comparing requirements across jurisdictions is likely to remain complex and subject to change. The FPC and the PRA will, in line with their respective secondary objectives and have regards, continue to take account of international standards, and their implementation in other jurisdictions, in assessing the UK bank capital framework.

> **In December, the FPC identified areas where the capital framework might warrant adjustment to make it more effective, efficient and proportionate in future, and to address any unintended consequences within the existing regime.**

Developments over the past decade, lessons on how the capital framework operates in stress, and information provided by the banking industry and other stakeholders suggested there are ways in which some parts of the capital framework could be adjusted to support growth while maintaining appropriate resilience.

> **The FPC and the PRA are taking steps to improve the functioning of the capital framework in the areas identified as priorities.**

The FPC has prioritised two broad areas since December:

- Working with the PRA and international authorities to enhance further the usability of regulatory capital buffers and so reduce banks' incentives to have capital in excess of regulatory requirements and buffers;
- Reviewing the implementation of the leverage ratio framework in the UK to ensure that it functions as intended, prioritising the UK's approach to regulatory buffers in leverage ratio requirements.

The FPC also supported initiatives by the Bank and PRA to respond to feedback on interactions, proportionality and complexity in the capital framework. Within this, the FPC supported further work to consider how the capital requirements that are related to domestic exposures – including the UK CCyB, O-SII buffer, and Pillar 2A requirements for geographic credit concentration risk – interact. This work is underway and the Committee will provide an update in the Q4 2026 FSR.

The remainder of this FSiF provides an update on the FPC's work to date – focusing on enhancing the usability and releasability of capital buffers and reviewing the functioning of the leverage ratio framework – and next steps for the remainder of its assessment of the capital framework.

2: Enhancing the usability and releasability of capital buffers

Capital buffers are intended to be used to absorb losses and to help maintain the provision of financial services to the real economy in a downturn by preventing the need for banks to protect their own capital positions through harmful and counterproductive deleveraging.

All regulatory buffers – including the PRA buffer, the CCyB, systemic buffers, and the capital conservation buffer – exist to be used as necessary in a stress to absorb losses so that banks can continue to support the real economy and market functioning. Impediments to regulatory capital buffer usability can have material negative consequences for the real economy if banks prioritise maintaining capital ratios by reducing the supply of lending to creditworthy households and businesses in a stress, thereby amplifying shocks.

A range of interrelated factors can impede the usability of regulatory capital buffers in practice. These factors can also contribute to banks maintaining substantially more capital above regulatory requirements in normal times than they otherwise would.

Impediments to buffer usability reflect both regulatory and non-regulatory drivers. On the regulatory side, banks and other external stakeholders have highlighted the role of automatic maximum distributable amount (MDA) restrictions and uncertainty around the extent of the supervisory response when buffers are used. Uncertainty over regulatory expectations for the pace of rebuilding buffers once drawn down can also deter banks from using them. Important non-regulatory factors include concerns about signalling weakness to investors and ratings agencies, adverse peer comparisons, and the risk appetite of banks' boards (refer to Box A for further detail).

Insights from external stakeholder engagement and academic literature[5] point to a range of potential ways to reduce these impediments and support buffer usability. Individually, these would be unlikely to be definitive in eliminating impediments to buffer usability, meaning they should be used in combination. They include: explicit buffer releasability; clear and credible communication to increase the predictability of buffer release and rebuild; a simpler overall buffer structure; and smoother, more transparent MDA constraints to reduce perceived cliff-edge effects and stigma.

The FPC sees a clear macroprudential case for a simpler and more effective capital buffer framework that reduces impediments to buffer usability. This is likely to be best achieved through a package of measures built over time with international support.

The FPC's vision centres on a single buffer that is releasable in stress, and that can be used without automatic distribution restrictions. Buffers that are 'releasable' can be reduced – including to zero – in turn reducing banks' total regulatory capital requirements for the period of the stress and during the subsequent rebuild, as illustrated in Figure 1.

Evidence from the Covid period suggests that explicitly releasing capital buffers can support the real economy by reducing incentives for banks to take defensive actions, such as deleveraging, that weaken the macroeconomy during stress. For example, during Covid, banks whose requirements were reduced by most as a result of the release of the UK CCyB tightened lending conditions by less and were less likely to take defensive balance sheet actions (**Mathur et al (2023)**).

Because of their importance to the UK real economy, reducing incentives to take defensive actions is particularly important for large banks. That is why in the Bank Capital Stress Test the resilience of the largest and most systemic UK banks is assessed on the basis of their ability to withstand a severe but plausible stress while continuing to lend to creditworthy households and businesses.

The FPC's vision, as illustrated in Figure 2, would help reduce complexity in the framework and improve understanding and confidence in the usability of capital buffers. It would apply across systemic and non-systemic firms – including G-SIBs, O-SIIs, mid-tier banks, building societies, and UK subsidiaries of overseas banking groups – ensuring a more consistent and coherent approach to buffer design across the UK banking system.[6]

The FPC will work with the PRA and international authorities to pursue broad reform of the capital buffer framework and move towards this vision.

Figure 1: Stylised illustration of how releasing regulatory buffers in stress can help banks to absorb losses and continue supporting the economy without deleveraging

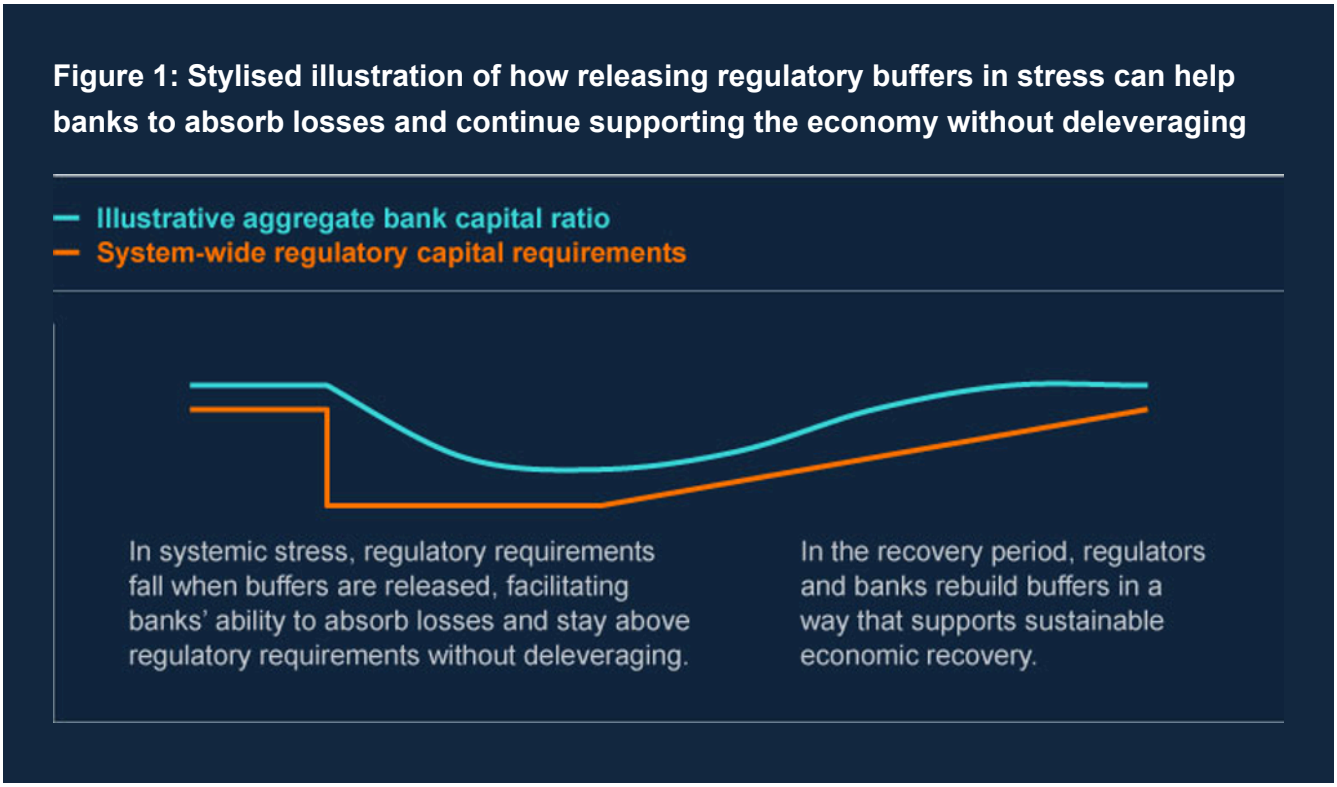
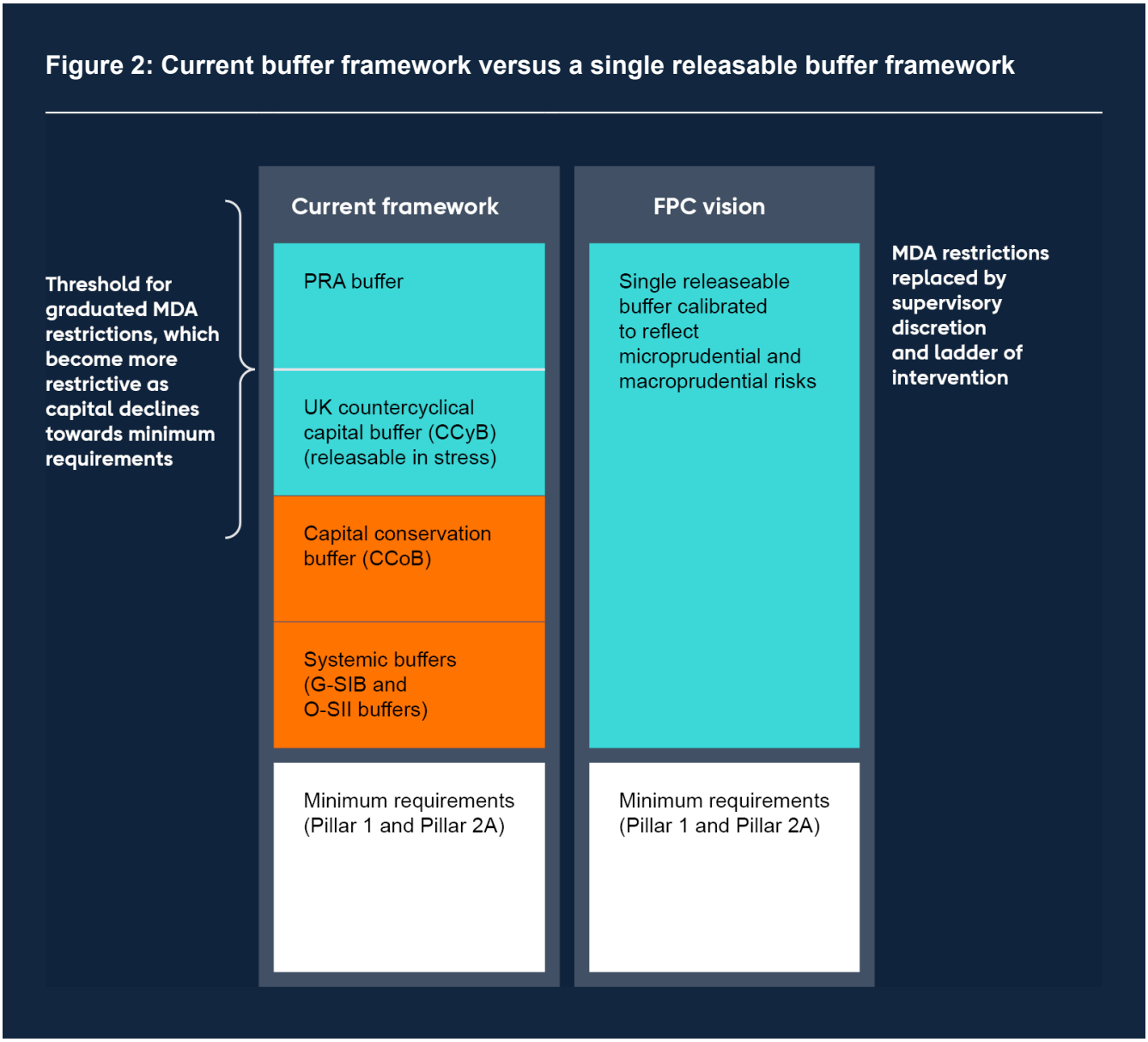


Figure 2: Current buffer framework versus a single releasable buffer framework



> **In the near term, the FPC and PRA are taking steps domestically to support buffer usability by making it clear that systemic buffers for domestic systemically important banks will be releasable in a stress.**

The FPC welcomes the **PRA's intention** to use its existing discretionary powers to release the O-SII buffer in the event of systemic stress and to engage with the FPC when doing so.

Releasing the O-SII buffer in a systemic stress would improve buffer usability, based on the evidence on the impact of releasing the UK CCyB. Releasing the O-SII buffer would lower the level of capital at which MDA restrictions automatically apply. In turn, this would reduce banks' incentives to take defensive actions that could amplify shocks, such as restricting the supply of lending to creditworthy households and businesses.

As is the case with the CCyB, upon releasing the O-SII buffer, an indicative period would be provided over which no increase would be expected. This would be to better allow the capital that has been released to be used.

Consistent with current UK CCyB policy strategy, the pace of return to normal-times O-SII buffer rates would depend on banks' ability to rebuild capital while continuing to lend to creditworthy UK households and businesses. The FPC and PRA would expect to consider a number of factors in making that assessment, including the expected evolution of the economic recovery, prevailing financial conditions and the outlook for banks' capital. The FPC and PRA recognise that if banks' capital ratios decline in a stress, their combined regulatory buffers may then need to be rebuilt over multiple years, as otherwise the prospect of a rapid rebuild could undermine banks' incentives to use the released capital.

An alternative approach that sought to set a rebuild pace for the combined buffer that would apply for all stresses would be unlikely to endure over time, as it would not always be appropriate from the perspective of promoting financial stability. That is illustrated by the variety of stresses experienced over recent decades that needed different policy responses – the GFC, aftermath of the Brexit referendum, Covid-19. Those stresses delivered different outcomes with respect to: magnitudes of losses (or profits) across individual banks, banks' profitability outlooks, and the lengths of macroeconomic downturns and subsequent recoveries.

When increasing the UK CCyB rate in the past, the FPC has considered banks' ability to meet the higher rate and the potential economic costs of doing so, including based on the factors above. For example, when the FPC agreed to increase the UK CCyB rate by 50 basis points in June 2017, it noted the benefits of a gradual increase, in part reflecting the weak outlook for bank profitability at the time. And when the FPC agreed to increase the UK CCyB rate to 2% in July 2022, it noted that major UK banks were expected to maintain sufficient capital headroom to accommodate the higher rate, and that the Committee would be prepared to cut the UK CCyB rate if economic conditions deteriorated in a manner that might otherwise lead banks to restrict lending.

The PRA will consult on its approach to setting O-SII buffers in 2026 H2 (**see PRA statement**). This will include some further qualitative guidance (e.g. example scenarios based on different types of stress and recovery) on rebuild expectations.

> **In future Bank Capital Stress Tests the FPC and PRC intend the hurdle rate for O-SIIs to reflect the prevailing O-SII buffer rates. This will ensure that once the O-SII buffer has been released following a real stress, banks will only need to rebuild their buffers at the pace set by the FPC and PRC.**

In its Bank Capital Stress Test exercise, the Bank typically assesses the capital resilience of individual banks against a hurdle rate that includes minimum capital requirements and systemic risk buffers. This is consistent with international standards that imply systemic banks should be expected to withstand a stress that is more severe than non-systemic banks, given the additional costs their distress would impose on the wider economy.

To enhance the usability of O-SII buffers upon their release, the FPC and PRC intend the O-SII buffer rates included in the hurdle rates for future stress tests to reflect the prevailing settings at the time of each test. For example, when stress tests are carried out in normal times the hurdle rate will reflect banks' standard individual O-SII buffer rates, whereas if the O-SII buffer had been fully released, the stress test hurdle rate would reflect the prevailing O-SII buffer rate of 0%. This will ensure that, in a real stress where O-SII buffers had been released, stress testing would not require firms to restore capital ratios more quickly than intended by the path set by the FPC and PRC. And in normal times, systemic banks will continue to be held to a higher standard; that is, they will continue to be expected to be able to withstand a more severe stress, reflecting their relative importance for the economy.

> **Alongside taking steps towards the FPC's vision for buffer releasability, the PRA will consider other steps that could enhance buffer usability.**

As set out above and in Box A, some feedback regarding impediments to buffer usability related to understanding of regulatory expectations when buffers are used.

In addition to the steps being taken to enhance releasability and lower the level of capital at which automatic distribution restrictions apply in stress, the PRA will consider firms' feedback that greater clarity on the use of the PRA buffer in circumstances outside periods of systemic stress could help buffer usability. It will also consider whether further engagement with relevant stakeholders, including investors and rating agencies, could support understanding of the role of regulatory capital buffers and how the framework is intended to operate.

The FPC's proposed changes to leverage buffers (set out below) also support the Committee's objective to move towards a more effective overall buffer framework.

3: The functioning of the leverage ratio requirement and the role of leverage buffers

Leverage ratio capital requirements are an important part of the capital framework and an effective complement to risk-weighted capital requirements.

The leverage ratio is a ratio that relates a bank's capital resources to a gross measure of its exposures, treating all exposures equally regardless of their estimated risk. As described in **the Financial Policy Committee's powers over leverage ratio tools**, the leverage ratio requirement can guard against the danger that models or standardised regulatory requirements fail to assign risk weights that reflect the true underlying risk of assets. This is a particular concern in environments that are characterised by complexity, small samples and uncertainties. The leverage ratio can also protect banks against scenarios which are thought to be 'low risk' or are unforeseen altogether until they occur. When financial leverage is high, the risk that shocks are amplified by the financial system increases.

Leverage ratio capital requirements can also help to curtail balance sheet growth that is unsustainable from a systemic perspective. The leverage ratio framework, which applies to banks whose failure could pose material threats to financial stability, provides an important prudential constraint on unsustainable leverage in the economy and in core markets. Increasing the resilience of the supply of liquidity in stress in core financial markets remains one of the FPC's priorities.

In December 2025, the FPC committed to review the implementation of the leverage ratio in the UK to ensure that it functions as intended. It noted that the leverage ratio had become more binding over time, and that the Committee would explore the extent to which this had happened as a result of underlying reductions in the riskiness of banks' exposures. It also noted that it would prioritise reviewing the UK's approach to regulatory buffers in the leverage ratio framework. While there are reasons for the way the leverage ratio framework is applied in the UK, including previous macroprudential decisions by the FPC to apply buffers alongside Basel minimum standards, international comparisons pointed to some potentially important areas to consider for reform.

Work since December has highlighted a number of features of the UK's leverage ratio framework, which have, along with feedback from external stakeholders, informed proposed changes to the framework.

The increased bindingness of the leverage ratio in the UK reflects both declining average risk weights and the evolution of leverage requirements relative to risk-weighted requirements.

Over recent years, banks' average risk weights have fallen in aggregate. And while leverage requirements have risen only slightly overall, domestically focused lenders have experienced larger increases in these requirements.

The phenomenon of declining average risk weights is to some extent to beexpected in a framework with both leverage and risk-based capital requirements. Banks facing these dual requirements are incentivised to allocate capital and structure exposures to minimise the binding constraint. If risk-based requirements bind, banks could be expected to shift toward assets with lower risk weights to use their balance sheets more efficiently, moving towards the point where leverage ratio and risk-based requirements bind equally. Therefore, an increase in leverage ratio bindingness due to a decline in average risk weights does not, in itself, suggest that a broad reduction in leverage ratio requirements and buffers is warranted. Nevertheless, it is important to understand what has driven this decline as this can provide important context for evaluating whether the leverage ratio framework is operating as intended.

While there is some evidence that the decline in average risk weights has been driven by a reduction in the underlying riskiness of banks' exposures over the past decade, there has also been growth in more complex and opaque forms of lending.

As set out in Box C, there is evidence of a reduction in the underlying riskiness of banks' exposures as a driver of the decline in banks' average risk weights since the start of 2016. This includes banks shifting their portfolios towards lower risk-weighted lending as well as derisking within asset classes. But over the same period there has also been growth in more complex and opaque forms of lending where the leverage ratio may be particularly effective in guarding against errors in risk measurement. This includes lending that has supported the growth of NBFI activities. Limited transparency and reliance on non-standard or less verifiable data may make risks harder to assess for some of these exposures. Banks have also increased their securities financing transactions activity, which has low risk weights. This has implications for the level of leverage in the financial system, and for gilt and gilt repo market resilience. Taken together, these trends highlight the continued importance of the leverage ratio framework and its relevance for the resilience of core markets.

Although the calibration of UK leverage ratio requirements is consistent overall with international standards, the UK's implementation for some elements of the leverage ratio framework differs from those standards.

The UK implemented a leverage ratio framework in advance of the Basel Committee's finalisation of its leverage ratio minimum standards. In designing this framework, the FPC included an additional leverage ratio buffer (the ALRB), for firms with systemic buffers to reflect the higher risk the distress of these firms would pose to the economy, and a countercyclical leverage ratio buffer (the CCLB), so that leverage requirements would vary in line with cyclical risks to financial stability. The ALRB and CCLB are set equal to 35% of the

firm-specific risk-based systemic buffer rate (G-SIB or O-SII) and CCyB rate, respectively.[7] UK firms subject to the leverage ratio requirement must also meet a minimum requirement of 3.25% of their leverage exposure measure. The minimum requirement increased from 3% to 3.25% following a recalibration to account for the FPC's exclusion of central bank reserves from the UK leverage exposure measure in 2016, having regard to the interaction between monetary and macroprudential policy. Maintaining a proportionate relationship between leverage ratio and risk-based requirements was intended to ensure that the leverage ratio retained its relative bindingness for systemically important firms, and during periods of elevated risks when the FPC decides to set the UK CCyB rate above its neutral rate.

When the Basel Committee subsequently finalised its leverage ratio minimum standards, these included a single leverage ratio buffer for G-SIBs equivalent to 50% of their risk-based systemic buffers. While implementation of the leverage ratio framework varies across jurisdictions, a number of other jurisdictions have also set higher leverage ratio requirements for domestic systemically important institutions, even though these are not required to meet Basel minimum standards. No other jurisdiction has chosen to implement a CCLB.

> **The presence of usable capital buffers is a desirable feature of the leverage ratio framework. These buffers help to ensure that banks can absorb losses and maintain the provision of services in an economic stress, as well as helping to ensure resilience in core sterling markets.**

Leverage buffers help to ensure that banks whose activity is relatively concentrated in lower-risk weighted lending to the real economy, such as mortgage lending, can absorb losses and continue to support the economy in an economic stress. They also help ensure that banks whose activity is relatively concentrated in lower-risk-weighted financial market activity, including in core sterling markets, can absorb shocks and continue to support market functioning in a financial market stress. Finally, they help ensure that risk-weighted buffers are not rendered unusable in practice because of a binding leverage ratio requirement.

> **Based on its analysis of how the UK leverage ratio is functioning, the FPC has identified a number of features of the current approach to leverage ratio buffers that could be made more proportionate and more effective by being better targeted to achieve financial stability goals.**

Following the FPC's decision to increase the neutral rate for the UK CCyB from 1% to 2% in 2019, the PRA reduced Pillar 2A minimum capital requirements in the risk-based framework in a way that kept overall regulatory loss-absorbing capacity broadly unchanged.[8] The CCLB increased with the CCyB, in line with the 35% conversion factor, but there was no corresponding reduction in the leverage ratio minimum requirement. As the leverage ratio was less binding in 2019, this had less impact on overall capital requirements than it does now. But as a result, leverage ratio requirements increased when the UK CCyB rate increased to 2% making the leverage ratio more likely to bind for a given risk profile. This unintended

consequence affected all banks subject to leverage requirements. The most notable impact, however, was on banks with greater relative exposure to UK domestic lending, especially those with lower average risk weights.

Although leverage buffers help to ensure resilience in the provision of services to financial markets as well as lending to the real economy, the CCLB is not well targeted to serve both of these purposes. The CCLB that applies to each individual bank is determined by the share of their relevant credit exposures (largely real economy exposures) in each jurisdiction, rather than by their financial market exposures. It also varies in line with each jurisdiction's CCyB rate. But many banks to which the CCLB applies have business models that are focused on the provision of services to financial markets, including core sterling markets, rather than the real economy. The fact that the CCLB's calibration is driven by the mix of banks' real economy exposures means that the FPC's current countercyclical policy framework is not well designed to support market functioning.

> **The FPC and PRA intend to consult on a package of measures to make the leverage ratio framework more proportionate and more effective by being better targeted.**

This package of measures would include three key elements.

First, it would remove the CCLB to address the unintended consequences associated with its implementation, and reflecting the fact that its calibration is not closely linked to the systemically important financial market activity for which the leverage ratio is a key prudential constraint.

Second, it would move the calibration of the ALRB for firms subject to systemic buffers in line with international standards – to 50% of risk-weighted systemic buffers. Like its risk-weighted counterpart, the ALRB for domestic systemically important firms would be releasable in a stress.

Third, it would make a greater share of leverage requirements and buffers releasable: leverage ratio Tier 1 minimum requirements would be reduced from 3.25% to 3% and a simple general leverage ratio buffer would be established, set at 25 basis points of the leverage exposure measure (which currently excludes central bank reserves). The general leverage ratio buffer would apply to the same set of firms currently subject to leverage requirements. As with other leverage buffers, it would need to be met with CET1 and would not be subject to MDA restrictions.

The general leverage ratio buffer would be releasable, if necessary to zero, to help ensure that banks can absorb losses in an economic or financial market stress while continuing to support the real economy and the functioning of financial markets. The releasability provided

by the general leverage ratio buffer when combined with O-SII buffer release would increase the total amount of releasable capital in a standard risk environment relative to the current framework.

If the FPC were to in future judge that risks were heightened and that additional resilience was warranted, it could consider increasing the general leverage ratio buffer above 25 basis points.

> **Alongside this package to reform leverage ratio buffers, the Bank would expect to adjust the leverage ratio hurdle rate in the Bank Capital Stress Test to ensure that the capital banks need to meet hurdle rates in the stress test does not increase as a result of the proposed changes.**

In their feedback on the December FSiF, some banks noted that their overall capital targets reflect both capital requirements and the capital needed to remain above their hurdle rates in the stress test.

The Bank typically assesses the capital resilience of individual banks against a hurdle rate that includes minimum capital requirements and systemic risk buffers.[9] This is consistent with international standards that imply that systemic banks should be held to a higher standard and so should be expected to withstand a stress that is more severe than non-systemic banks, given the additional costs their distress would impose on the wider economy. To date, the leverage ratio hurdle rate for each bank has generally been set to include the ALRB for that bank, which is currently 35% of their risk-weighted systemic buffer. The CCLB is not part of the hurdle rate for bank capital stress tests.

The changes included in the above package would have implications for the amount of capital banks need to remain above the leverage ratio hurdle rate in the stress test. Lowering Tier 1 leverage ratio minimum requirements to 3% would reduce the capital needed to remain above the leverage hurdle rate. The general leverage ratio buffer would be excluded from the hurdle rate. Increasing the ALRB to 50% of risk-weighted systemic buffers would act to increase the amount of capital some banks need to remain above the hurdle rate.

The FPC and PRA have therefore considered the appropriate amount of the ALRB to be included in each bank's stress test hurdle rate. In future, the Bank would expect to include 40% of each bank's risk-weighted systemic buffers in their leverage ratio hurdle rate (lower than the ALRB of 50% of risk-weighted systemic buffers that would apply to banks' regulatory requirements). This would ensure that the capital banks need to meet hurdle rates in the stress test does not increase as a result of the proposed changes.

> **These changes would make the leverage ratio more proportionate and more effective by being better targeted while continuing to support financial stability.**

The FPC considers that the package of proposed leverage ratio reforms would make the UK leverage ratio framework more proportionate and more effective by being better targeted. The FPC also judges that it is appropriate for the package of changes to unwind the unintended consequences of raising the neutral rate of the CCyB, and that this would result in some reduction in the aggregate leverage ratio that the banking system needed to maintain, whilst maintaining the overall resilience of the banking system.

When taking into account both regulatory requirements and the capital needed to remain above the leverage ratio hurdle rate in the Bank Capital Stress Test, the proposed changes would reduce the leverage ratio that large UK banks subject to the leverage requirement need to maintain by around 20 basis points in aggregate, with the impact varying by bank. This would leave leverage ratio requirements for UK large domestically focused banks and G-SIBs within the range of other jurisdictions globally.

Notwithstanding the benefits of the proposed changes, the FPC agreed that the implications of the proposals for the resilience of core UK markets merited further consideration, given the importance of the leverage ratio in determining capital requirements associated with activity in core sterling markets (see Section 4).

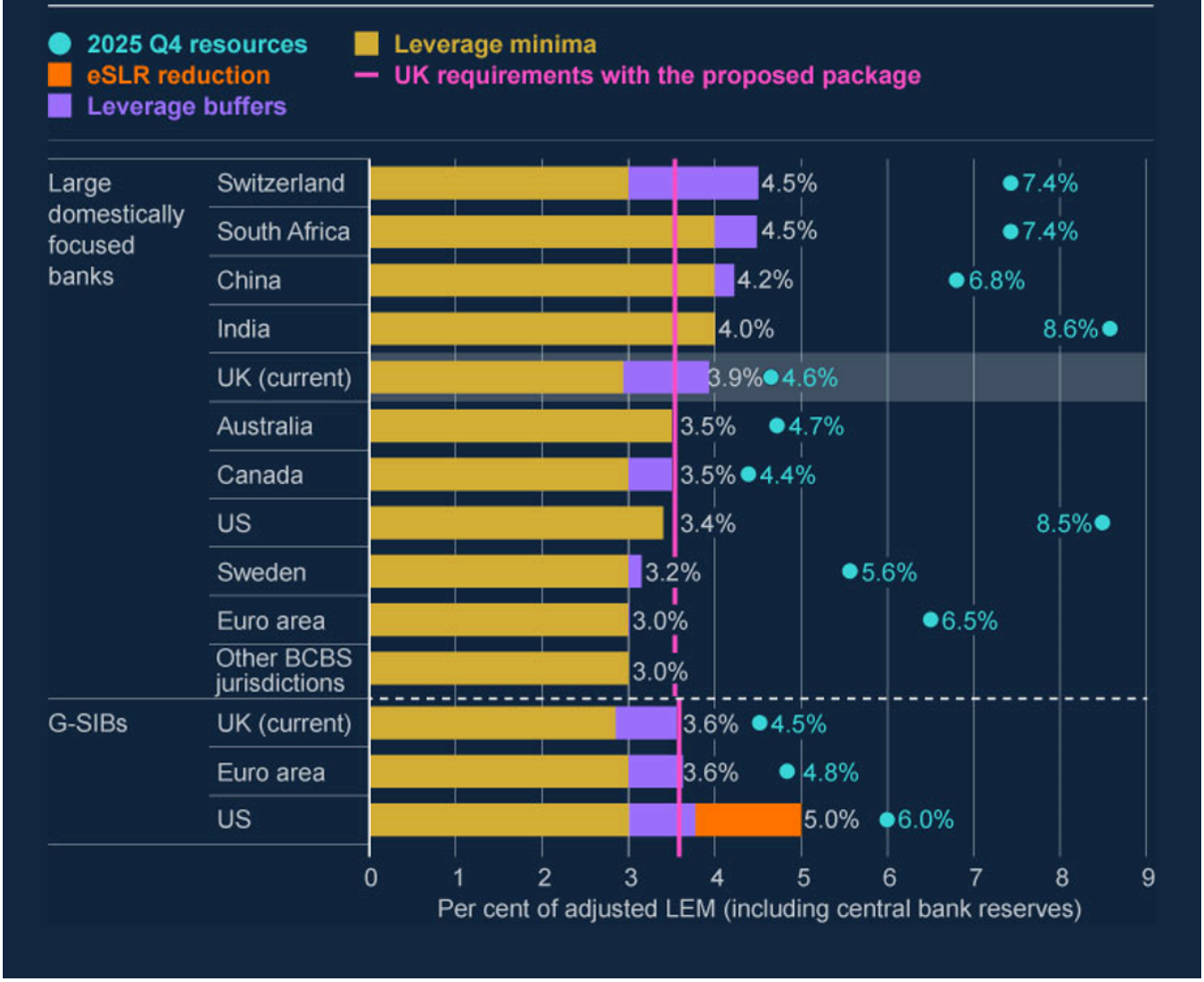
This proposed reform of leverage buffers supports the FPC's vision to move towards a more effective overall buffer framework, which the FPC will continue to pursue with international authorities (as noted in Section 2).

> **The package would leave leverage ratio requirements for UK large domestically focused banks and UK G-SIBs within the range of other jurisdictions globally.**

The proposed package would align leverage ratio requirements for large domestically focused UK banks[10] more closely with international peers and with UK G-SIBs (Chart 1). Leverage ratio requirements for UK G-SIBs would also remain in line with international peers, reflecting an overall level of resilience that is at least consistent with a robust implementation of international standards. As noted in the December FSiF, large UK banks have a smaller gap between their leverage ratios and leverage requirements, relative to US and euro-area peers. These relatively low leverage ratios – including when compared with other firms in other jurisdictions globally – may be driven by a range of business factors (for example, higher asset risk for some banks may help explain why they maintain higher leverage ratios).

Chart 1: Under the proposed package, UK leverage ratio requirements would remain within the range of international peers for both large domestically focused banks and G-SIBs

Comparison of Tier 1 leverage ratio requirements and resources(a) for large domestically focused banks(b) across BCBS jurisdictions and UK, euro-area and US G-SIBs(c)



Sources: Published banks' results, domestic and international supervisory authorities' publications, PRA regulatory returns, and Bank calculations.

(a) The chart shows leverage ratio requirements and Tier 1 capital resources as a percentage of the leverage exposure measure (LEM), including central bank reserves, on a weighted average basis, as of December 2025.
(b) The comparison for large domestically focused banks covers leverage ratio requirements across BCBS member jurisdictions, based on firms identified as domestically systemic under local supervisory definitions. To aid comparability, the euro-area and US samples focus on deposit-taking, retail-oriented banking groups, excluding broker dealers, securities-focused institutions and other specialised banking models. Residual differences in business models may still affect cross-jurisdictional comparability. 'Other BCBS jurisdictions' are Argentina, Brazil, Hong Kong, Indonesia, Saudi Arabia, Singapore, South Korea, Russia, and Turkey, which apply a 3% minimum leverage ratio with no additional leverage buffer specific to large domestically focused institutions. In Australia, a leverage ratio of 3.25% of CET1 is due to take effect from 1 January 2027, replacing the current 3.5% Tier 1 requirement following the phase-out of AT1 capital instruments. For the US sample, the binding constraint is generally the US leverage ratio rather than the Supplementary Leverage Ratio (SLR). This is set at 4% of total assets, and requirements have been converted to a Basel-comparable leverage exposure measure (LEM). For

the euro area, the leverage buffer reflects the weighted-average Pillar 2 leverage requirement (P2R-LR); Pillar 2 leverage guidance (P2G-LR) is not included as it is not publicly available. For Sweden, the leverage buffer reflects the weighted-average P2G-LR, as the P2R-LR is set at zero.
(c) Requirements are shown as at end-2025. The chart, refers to a reduction in the US enhanced supplementary leverage ratio (eSLR), reflecting its amendment which was implemented on 1 April 2026, although banks subject to it could adopt it from 1 January 2026.

4: Next steps to making the bank capital framework more effective

The FPC considered that the package of proposed leverage ratio reforms would make the UK leverage framework more proportionate and more effective by being better targeted. The Committee also agreed that the implications of the proposals for the resilience of UK markets merited further consideration.

The FPC will work, alongside the PRA, to identify whether the proposed package of changes to the leverage framework would leave any financial stability gaps that would need to be managed and whether this would justify further adjustments to the policy package. This analysis, which will take into account the FPC's work on gilt repo market resilience and impacts of the proposal on market functioning, will be completed by, and considered at, the Q3 FPC meeting to allow any potential consultation on this element alongside the rest of the proposal.

As well as working to enhance buffer usability and reviewing the implementation of the leverage ratio in the UK, the FPC also supports other initiatives by the Bank to ensure the capital framework is effective, efficient and proportionate. An update on this work is provided below.

Reviewing how capital requirements that apply to domestic exposures interact

The Bank is reviewing how capital requirements that are related to domestic exposures interact. These include the UK CCyB, O-SII buffer and Pillar 2A requirements for geographic credit concentration risk, which each serve different purposes in the capital framework.

The Bank and PRA are reviewing the extent to which these individual elements address risks appropriately, and as part of that, assessing how they interact. In making this assessment, the size of UK banks' domestic losses in stress test scenarios can be used as complementary evidence, alongside evidence on the impact of systemic failures on the broader financial system, and the impact of credit concentration on the likelihood of orderly resolution.

The FPC expects to provide an update on its assessment of the interactions of capital requirements that are related to domestic exposures in the Q4 2026 FSR.

Automatic regulatory threshold indexation

The FPC has welcomed the continuing work by the Bank and PRA to develop a systematic approach to updating the regulatory thresholds that define which parts of the regulatory framework apply to firms, to ensure they reflect economic growth – such as through automatic indexation.

Although some policy thresholds have been updated to account for nominal GDP growth since they were implemented, others have not. This can lead to 'prudential drag' as the economy grows, with more firms being subject to policies than may be consistent with Committees' original risk appetite. The Bank is developing an approach for automatic indexation of regulatory thresholds, which would provide greater transparency and predictability to industry. The PRA intends to consult on a proposed approach later in the year.

Supporting the PRA's contribution to the Government's review of the ring-fencing regime

The Bank continues to support the Government's review of the ring-fencing regime. In May, the PRA announced plans to consult on reforming rules around shared operational services for ring-fenced banks.

The PRA will publish a consultation shortly that will propose allowing firms more flexibility as to how they share operational resources across the ring fence. Reform in this area will seek to streamline requirements and unlock new flexibilities and cost savings for firms, for example in how groups with ring-fenced entities utilise operational services, such as data-processing services, information technology and back-office functions, across the group.

Supporting the PRA's work on risk weight modelling for mortgage lending

The FPC supports the PRA's work to assess firms' feedback and supporting evidence on a range of possible changes to internal ratings based (IRB) models for mortgage lending outlined in DP1/25.

This work was prompted by the PRA's observation that medium-sized firms encounter challenges in developing IRB models for loss given default and probability of default estimation. The PRA has been progressing this work and intends to publish a consultation paper in Q4 2026 or Q1 2027.

Box A: Feedback on the December 2025 Financial Stability in Focus

The FPC welcomes the feedback it has received on the Committee's assessment of bank capital requirements.

This box covers feedback on the FPC's assessment of bank capital requirements, as published in the **December 2025 FSiF**. A wide variety of stakeholders including academics, banks, industry bodies, investors and ratings agencies contributed perspectives and evidence, both in writing and via **a stakeholder evidence gathering event** hosted by the Bank in March 2026.

The feedback covered the overall calibration of bank capital requirements in the UK and the areas the FPC had identified for further work, which were: the usability of buffers; the functioning of the leverage ratio framework; and the interactions between different elements of the capital stack, particularly in relation to domestic exposures.

The overall calibration of UK bank capital requirements

There were a range of views on the FPC's decision to lower its benchmark for system-wide capital.

There was a range of feedback on the overall calibration of UK bank capital requirements following the publication of the FPC's assessment of the appropriate benchmark for system-wide Tier 1 capital. That assessment was made with a view to maximising long-run growth in the UK economy by weighing the macroeconomic costs of capital, which stem from the impact of higher capital pushing up on borrowing costs, against the benefits of capital, which come about because higher bank capital reduces the likelihood and costs of financial crises.

Some respondents argued that heightened macroeconomic and geopolitical uncertainty, alongside reduced fiscal headroom globally, pointed towards maintaining or increasing the FPC's bank capital benchmark rather than reducing it. It was also noted, as set out in the FPC's December assessment, that the FPC's benchmark lies towards the lower end of estimates of the optimal level of capital in several academic studies. Others argued that the banking system's performance through recent shocks, as well as Bank of England stress test results, demonstrated that capital requirements could be reduced without undermining resilience, reflecting the effectiveness of post financial crisis reforms.

Banks and industry groups saw the FPC's decision to revise its Tier 1 benchmark as a welcome signal of confidence in the UK banking system. But because the reduction in the FPC's benchmark largely mirrored expected changes in actual capital requirements as a proportion of risk weighted assets, several participants noted that the reduction in the FPC's benchmark was expected to have limited impact on banks' desired capital positions in and of itself. They also noted that requirements for individual banks could be higher than the system-wide benchmark, reflecting: the relative weight of CCyB rates applied in different jurisdictions that banks were active in; the application of firm-specific PRA buffers; and the bindingness of leverage requirements for some banks.

There were differing views on the role of resolution frameworks in the assessment of appropriate capital requirements. Some cautioned against relying heavily on resolution to justify lower capital, citing recent international episodes of banking stress in which they observed that some authorities intervened extensively outside of formal resolution regimes. Others emphasised that resolution arrangements, which were now fully operational, were materially more credible than in the past. This made the system more resilient to stress, so it was appropriate to continue to reflect this fact in assessments of capital needs.

One respondent, emphasising banks' role as creators of credit, argued that macroprudential policy should be reformed significantly: the FPC should adjust capital requirements to target system-wide leverage, analogous to the way the MPC targets inflation.

> **There was also a range of perspectives on what the macroeconomic impact of a reduction in bank capital might be.**

Some stakeholders noted that indicators of UK credit conditions suggested capital was not currently a constraint on the supply of credit for most sectors, and that it was more likely lower capital requirements would result in greater distributions of profits rather than directly increasing supply of bank lending. Others noted that lower capital requirements would provide greater capacity for re-investment by banks of profits into business growth, and that increased distributions to shareholders would support economic activity and increase the attractiveness of the UK to investors.

Some argued that with lower capital requirements, the ongoing cost of borrowing for households and businesses would be reduced as banks' funding costs would be lower with less relatively costly equity funding. In turn, this could boost demand for borrowing and economic activity. Others countered that the directional relationship between cost

of capital and bank capitalisation levels was not clear cut, citing academic studies that had shown that higher levels of capital were associated with higher lending, as higher levels of solvency reduced overall funding costs.

The effect of capital on small and medium enterprise (SME) lending was discussed, with some arguing that lower capital requirements would allow for faster growth by banks active in this sector. Others noted different factors that were weighing on the volume of SME lending, including the greater profitability of other types of lending from the perspective of banks,[11] a perceived lack of opportunity on the part of some small businesses to engage with lenders, and evidence of wariness from SMEs about borrowing from banks. Lower bank capital requirements would not have a significant impact on many of these factors.

Some respondents argued that the level of bank capital requirements had displaced the provision of lending from banks, moving it towards non-bank finance, where transparency and prudential oversight are weaker. Respondents cautioned that such displacement could have financial stability implications.

Feedback highlighted that regulatory requirements do not determine banks' capital positions in isolation. Investors and other participants indicated that market discipline, including expectations from investors, creditors and rating agencies, played a significant role in shaping banks' target capital levels, with more highly capitalised banks (relative to peers) often having higher equity prices.

Overall, the FPC judges that the range of views received is reflective of the issues it considered in December when making its assessment on the appropriate benchmark for system-wide Tier 1 capital, and the Committee reaffirms its assessment that the appropriate benchmark is around 13%. In recent years overall credit conditions have tended to evolve in line with the macroeconomic outlook, suggesting that banks have not been restricting lending to defend their capital positions. The Committee remains committed to using the UK CCyB actively to help ensure capital levels respond to the risk environment. The Committee also notes steps it is taking to address financial stability risks from market-based finance, including through its system wide exploratory exercises, and work on gilt repo market resilience.

International comparisons

> **Feedback on analysis comparing capital requirements across jurisdictions focused on comparisons of risk-weighted requirements in the UK and the US.**

The December FSiF included analysis that compared capital requirements across jurisdictions. It concluded that the level of risk-based capital requirements for large banks in the UK is broadly similar to that in the euro area, and that after adjusting for

key differences in the way that risks are captured, risk-weighted requirements appeared to be lower in the UK than in the US. It noted that requirements appeared to be higher than other jurisdictions in some specific aspects and cohorts, particularly leverage ratio requirements for large domestically focused banks.

The December FSiF noted the challenges in comparing capital requirements across jurisdictions given differences in how risks are captured in different regulatory frameworks and the FPC welcomed feedback on the approach taken. Most of the responses focused on the comparison between the US and UK risk-based capital requirements. Respondents acknowledged the inherent complexity of international comparisons but noted that alternative approaches and structural differences could affect the conclusions. They noted that differences in capital requirements across jurisdictions could affect the relative incentives to lend in the UK over other jurisdictions and could lead to capital requirements being lower for international banks operating in the UK than for domestic banks.[12]

Adjustment for Pillar 2A and operational risk

As set out in the December FSiF, to aid comparability with capital requirements in the US – where risk weights are higher but there are no capital add-ons equivalent to UK Pillar 2A/ EU Pillar 2R – Bank staff made an adjustment to UK and EU RWAs. Respondents challenged that adjustment applied to UK and EU RWAs. Several banks and other industry representatives argued that the magnitude of the adjustment (around 30%) overstated differences. Some respondents argued that risks captured in UK Pillar 2A, notably operational risk, were not directly comparable to US Pillar 1 treatment and that the adjustment therefore distorted conclusions.

Respondents proposed alternative approaches, including comparisons based on an assumption that US advanced-model RWAs capture the same risks as UK RWAs, and suggested a materially smaller uplift in the range of 4–6%. Under those approaches, respondents argued that UK requirements appeared higher than those of US peers across several firm cohorts.

While it is the case that there are many ways to compare regulatory frameworks, which could indeed lead to different conclusions, further consideration of how these risks are captured in the US framework continues to suggest a sizeable adjustment for differences in approach to capturing these risks in capital requirements is appropriate when making comparisons between the two jurisdictions.

Choice of peer cohorts

The comparison presented in the December FSiF compared UK G-SIBs and O-SIIs at the highest level of consolidation with the closest peer groups in EU and US. It was acknowledged that there was some heterogeneity in firms across the sample.

Respondents tended to focus on UK – US comparisons and argued that some of the analysis in the FSiF used cohorts of firms that were not suitable for comparison because they were too heterogenous in terms of size, complexity and business model. Respondents also argued that use of a smaller subset of peer groups would conclude that UK requirements appear higher than US requirements.

Comparing firms from different jurisdictions is complex, in part because firms with similar size balance sheets can be considered systemic in a smaller jurisdiction but non-systemic in a larger jurisdiction. For example, a UK domestically focused O-SII might be the same size as a US category 3 bank but the latter is not treated as being systemically important to the US economy, while the former is systemically important in the UK economy. Finding suitable peer groups for comparison is also complex because business models are in part driven by local regulatory frameworks, and structural differences across financial markets. A larger sample size of firms in the analysis may be a better representation of firms across jurisdictions, and aid comparability between inherently heterogenous groups of firms.

Other differences

Finally, respondents emphasised structural differences across jurisdictions that complicate comparison, as acknowledged in the December FSiF. For example, a key driver of RWA differences between the UK and US was the extent to which banks tended to keep low risk mortgages on their balance sheets. In the US, these tend to be securitised to a greater degree.

The different treatment of software assets in the US compared to the UK was noted and respondents argued that this discrepancy should be factored into the international comparison[13]. As set out in the December FSiF, however, it is difficult to make a quantitative adjustment for the full range of differences in the measurement of regulatory capital across jurisdictions, including where they arise from differences in accounting treatment.

As set out in Box B, capital frameworks are changing across jurisdictions, as Basel 3.1 and other rules are being finalised and implemented. That means comparing requirements across jurisdictions is likely to remain complex and subject to change.

The FPC and the PRA will, in line with their respective secondary objectives and have regards, continue to take account of international standards, and their implementation in other jurisdictions, in assessing the UK bank capital framework.

The usability of bank capital buffers

> **Feedback cited a range of non-regulatory and regulatory drivers of banks' reluctance to use regulatory buffers and their desire to maintain capital in excess of them.**

Factors cited included:

- Investor and analyst expectations that banks operate with sufficient headroom above regulatory requirements, particularly given the consequences of breaching Maximum Distributable Amount (MDA) thresholds (see below);
- Rating-agency methodologies that penalise proximity to regulatory minima and compare banks with peers;
- Earnings and RWA volatility, including from model changes and in stress tests;
- Internal board risk appetite and governance thresholds;
- Uncertainty about supervisory reactions to buffer use and about the pace, cost and conditions of post-stress capital rebuild;
- A perceived lack of predictability in the setting of Pillar 2A and in stress test results;
- Several respondents also argued that inclusion of systemic buffers in stress-test hurdle rates undermines claims that those buffers are usable in a real world stress.

The MDA framework was widely cited as a key deterrent to buffer use. Respondents described the automatic and binary nature of MDA restrictions as creating "cliff-edge" effects, particularly given the interaction with AT1 coupon payments, which are restricted if MDA thresholds are breached and cannot be received by investors at a later date if missed (in contrast to equity distributions). While the release of system-wide buffers would reduce MDA, such buffers would not be expected to be released for idiosyncratic stress.

A range of proposals were put forward, such as:

- lowering the MDA trigger or excluding usable buffers from the MDA calculation
- excluding Pillar 2A when determining the region of the capital stack within which MDAs apply or rebalancing buffer composition so that more capital sat outside buffers subject to MDAs if breached
- applying MDA restrictions to CET1 distributions – such as dividends on common equity – but allowing other distributions (such as bonus and AT1 payments) to

continue
- replacing automatic MDA restrictions with greater supervisory discretion

> **Several respondents argued that usability could be improved by increasing the share of the capital stack that is clearly releasable in stress.**

Proposals included:

- Rebalancing the capital stack away from fixed buffers and towards buffers that the FPC can credibly release;
- Introducing a single, integrated domestic buffer, similar to the Canadian Domestic Stability Buffer, encompassing structural and cyclical risks, and not subject to MDAs;
- Improving consistency across CET1, AT1/T2, MREL and stress-test requirements to avoid buffer use in one part of the stack triggering pressure elsewhere

As set out in Section 2, the FPC sees a clear macroprudential case for a simpler and more effective capital buffer framework that reduces impediments to buffer usability. The Committee will work with the PRA and international authorities to pursue broad reform of the capital buffer framework and move towards a goal of a single buffer that is releasable in stress, and that can be used without automatic distribution restrictions. In the near term, the FPC and PRA are taking steps domestically to support buffer usability by making clear that systemic buffers for domestic systemically important banks will be releasable in a stress. In addition, the PRA will consider firms' feedback that greater clarity on the use of the PRA buffer in circumstances outside periods of systemic stress could help buffer usability, and also whether further engagement with relevant stakeholders could support understanding of the role of regulatory capital buffers and how the framework is intended to operate.

The operation of the leverage ratio

> **Several stakeholders noted that the leverage ratio had become more binding. But there was some difference in views amongst stakeholders over the extent to which this was expected and appropriate.**

Some argued that strengthened supervision, improved risk management and resolution reduced the usefulness of the leverage ratio, while others emphasised that risk measurement remained imperfect, meaning that the leverage ratio continued to play an important role. While some noted that the Basel 3.1 output floor on modelled risk weights meant that the leverage ratio would be less important as a guard rail

against risk weight mismeasurement in future, others countered that standardised risk weights could also be under-calibrated, including in asset classes where there was less historical data on which to base risk weights.

Some stakeholders argued that the leverage ratio becoming more binding was influencing capital allocation in an unhelpful way, reducing banks' sensitivity to risk. But others noted that if the FPC were to reduce the leverage ratio requirement further, this would incentivise more low risk-weighted business, such as repo lending to non-bank financials, rather than encourage riskier but growth-supporting bank lending to the parts of the real economy that drive improvements in productivity.

In a mechanical sense, lower average risk weights have been a key factor making the leverage ratio more binding. Feedback from the banking industry argued that declining average risk weights reflected structural de-risking and business model shifts rather than risk-weight model weakness. Some banks provided firm-level analysis showing reductions in RWAs driven by exits from investment banking, growth in mortgages and sovereign exposures, and increased holdings of central bank reserves.

Respondents argued that greater leverage ratio bindingness was also driven by a number of other factors, including:

- The application of the ALRB to O-SIIs and, uniquely amongst international comparators, the CCLB;
- The interaction with ring-fencing, which separates balance sheets and reduces diversification;
- The interaction with stress testing, which in effect requires banks to hold sufficient capital in normal times to remain above the hurdle rate in the stress test;
- The higher capital quality requirement with CET1 in the minimum requirement and in leverage buffers;
- For firms with relatively low levels of reserves, the central bank reserves exclusion and corresponding move to a leverage ratio minimum of 3.25% had caused an effective increase in requirements;
- The inclusion of gilt holdings in leverage exposure measure.

Banks were critical of the CCLB, arguing that it was unique to the UK and unnecessary given the leverage exposure measure's limited procyclicality as reflected in stress tests. Several suggested either removal or, at a minimum, recalibration or offset mechanisms to compensate for the higher UK CCyB level.

Views on the application of the ALRB to non-GSIBs were similar. Many respondents argued it duplicated other UK-specific safeguards, including systemic buffers in the risk-weighted framework and ring-fencing. Others argued against its removal to avoid competitive distortions domestically, suggesting a rebasing of the ALRB scalar to 50% for all firms if the CCLB were to be removed.

Respondents argued that even if leverage buffers were removed, stress-test evidence indicated that leverage ratios would remain well above minimum levels in a severe stress. Some suggested that the leverage ratio's role in the Bank's capital stress test should be reconsidered alongside the review of leverage buffers.

The FPC and PRA intend to consult on a package of measures to make the leverage ratio framework more proportionate and more effective in the way that it supports the economy and the functioning of financial markets. This package would include three key elements. First, it would remove the CCLB. Second, it would move the calibration of the ALRB for firms subject to systemic buffers into line with international standards – to 50% of risk-weighted systemic buffers. Third, it would make a greater share of leverage requirements and buffers releasable: leverage ratio Tier 1 minimum requirements would be reduced from 3.25% to 3% and a simple general leverage ratio buffer would be established, set at 25 basis points of the leverage exposure measure. Refer to Section 3 for further detail.

Capital requirements related to domestic exposures

> **Stakeholders broadly agreed that strong overall bank capitalisation remains essential but differed on whether the cumulative calibration of requirements and buffers related to domestic exposures remained proportionate.**

Banking industry stakeholders argued that the calibration of multiple capital requirements that apply to UK exposures – including the geographic concentration component of Pillar 2A requirements, the O-SII buffer and the UK component of the CCyB – were highly correlated resulting in some overlap in risks that were being capitalised. They contended that alongside ring-fencing and the UK resolution regime, which were also important mitigants to macroeconomic risks, this led to banks having more capital against these risks than justified by historical losses. In turn, this affected the pricing of UK-focused lending. Although respondents acknowledged that these tools have different formal objectives, they argued that in practice they are calibrated against the same underlying exposure – UK domestic lending.

Other stakeholders noted that while arguments could be made about the calibration of individual elements of the capital stack, the FPC's overall benchmark – which balanced the costs and benefits to GDP growth based on losses in historical crises – still

provided an anchor for overall capital requirements that would need to be met across the system. They also emphasised that different elements of the capital stack related to domestic exposures target different risks – concentration risks, systemic risks, and those related to the financial cycle – even if they are correlated, as well as noting that the UK economy is particularly susceptible to the impact of macroeconomic shocks.

The evidence provided to support the arguments in favour of overlap focused on international comparisons and stress test results. For example, it was noted that there was a high correlation between CCyB and O-SII buffers for UK banks, whereas in comparable EU jurisdictions the correlation was low. This was due to the O-SII buffer being determined largely by balance sheet size in the UK; banks suggested that their buffers would be materially lower if calculated using EU methodology. Several respondents argued that domestically focused UK banks faced higher combined macroprudential buffers than European peers, and in some cases higher requirements than internationally active G-SIBs, and that combined buffers were larger than stress test capital drawdowns.

The FPC set out its approach to setting the UK CCyB rate in the December FSiF, including an explanation of the adjustment it had made to Pillar 2A requirements to keep overall regulatory loss-absorbing capacity, defined as minimum requirements for own funds and eligible liabilities (MREL) plus buffers, broadly unchanged. Nevertheless, various respondents proposed that the FPC should reduce the UK CCyB neutral rate, pointing to lower rates in other jurisdictions, with some proposing amendments to the calibration of Pillar 2A as an alternative way to reduce CET1 requirements.

Several banks and industry groups argued that risk weights were overly conservative, pointing to improved underwriting standards, lower LTVs, and historically low losses. They also criticised the requirement to model losses back to the early 1990s. Some respondents noted similar issues in social housing portfolios.

Views diverged on whether capital was a constraint on the provision of lending to the UK real economy. Some emphasised that mortgage markets were competitive and bank lending to corporates had been growing strongly. Others argued that the UK economy was under-leveraged, noting that the growth of credit had been weak relative to GDP since the financial crisis and this had contributed to weak productivity growth.

The Bank and PRA are reviewing the extent to which these individual elements address risks appropriately, and as part of that, will assess how they interact. The FPC will provide an update on its assessment of the interaction of capital requirements that are related to domestic exposures in the Q4 2026 FSR.

Other issues raised by stakeholders

Stakeholders raised a range of other issues, including around risk-weight modelling, regulatory thresholds.

Some respondents argued that rules regarding the measurement and modelling of RWAs needed updating. It was said that several of elements of IRB modelling are more conservative than US equivalents, and the level of IRB model coverage expected was in some cases disproportionate. According to some respondents, updates to mortgage IRB models had added significant amounts of capital, despite an improvement in the underlying quality of mortgage books. Some banks argued that the UK's approach was more judgement based, for example, in the way in which the UK Pillar 1 regime requires interpretation (compared to the EU and US), which created uncertainty and contributed to conservatism.

Respondents highlighted the number of regulatory thresholds and lack of indexation as creating prudential drag. Stakeholders were in favour of a more systematic approach to updating thresholds. As outlined in Section 4, the PRA is continuing work on the automatic updating of thresholds.

Some stakeholders argued that a capital framework designed primarily for large shareholder-owned banks is disproportionate when applied to mutuals and building societies. Applying the same capital stack to those firms as systemic banks was said to result in multiple layers of capital for the same low-risk exposures, materially in excess of historical losses and stress-test outcomes, crowding out lending to households and first-time buyers. They noted that although the Strong and Simple regime was welcome, the biggest mutual lenders sit outside its perimeter and therefore remain subject to the full capital framework.

These stakeholders also argued mutuals and building societies face greater difficulty rebuilding capital following stress or buffer drawdown than banks because they cannot issue external equity. This strengthened the case for buffer calibration, usability and rebuild expectations to reflect mutuals’ structural capital constraints.

Box B: International capital framework developments

The December 2025 FSiF included a comparison of international capital requirements based on existing requirements across UK, US and EU. The comparison did not consider future changes to the frameworks.[14] This box includes an overview of progress with respect to Basel implementation across these three jurisdictions, efforts to simplify requirements, and other policy developments recently proposed or implemented.

> **The majority of BCBS member jurisdictions have published and implemented the final Basel III post-crisis reforms.**

Member jurisdictions of the Basel Committee for Banking Supervision (BCBS) are close to the finalisation of the Basel III post-crisis reforms (Basel III), also known as Basel 3.1 in the UK. The US, UK and EU are all implementing the reforms on different timelines.

> **In the UK, the new Basel 3.1 rules will be implemented on 1 January 2027. The EU has already implemented the majority of Basel III as of 2025, and in the US, federal banking regulators have recently consulted on Basel III implementation.**

On 1 January 2027, UK Basel 3.1 rules come into force, alongside the related restatement of the remainder of the Capital Requirements Regulation in the PRA Rulebook [15]. These rules will introduce material changes to the UK capital framework, such as improving the risk sensitivity of the framework and reducing excessive variability of modelled risk weights.

While the EU has already implemented the majority of Basel III, the jurisdiction is still working on developing final elements, such as technical standards. The European Banking Authority has published a **roadmap** for the delivery of these final elements. The roadmap consists of around 140 mandates for technical standards implementation, guidelines, reports, opinions and more, all accompanying the Basel III rules. The largest number of these changes will be to the credit risk framework, but the mandates will also impact market risk, operational risk, reporting and disclosure.

In March 2026, the US Federal Reserve, the Federal Deposit Insurance Corporation (FDIC) and the Office of the Comptroller of the Currency (OCC) published **three new joint proposals** aiming to modernise the regulatory capital framework, as part of their Basel III implementation.

The first proposal, which applies to large banks, would simplify the risk-based capital framework by subjecting these banks to a single set of risk-based capital ratios and remove the use of models for risks other than market risk, under a new "expanded risk-based approach". The second proposal, which applies to all other banking organisations, includes proposals to revise the risk-based capital treatment under the standardised approach by improving the calibration and risk sensitivity of risk weights. The third proposal relates to the GSIB surcharge, where regulators propose to modify one of the methods for calculating the surcharge. Together, these proposals alongside proposed changes to the US stress tests are projected to decrease CET1 capital requirements for the largest US banks by 4.8% of current nominal requirements.

The UK and EU are planning to make changes to their market risk frameworks.

While the UK and the EU have published final Basel III policies, both jurisdictions are making additional targeted changes to their market risk policy frameworks.

In the UK, the PRA published **CP9/26 – Basel 3.1: adjustments to the internal model approach (IMA) for market risk** on 19 June 2026. The consultation paper sets out proposed targeted refinements to the Basel 3.1 market risk internal model rules, aimed at improving risk sensitivity, proportionality and operational efficiency, while maintaining robust prudential standards. The PRA proposes to implement changes resulting from the consultation paper, alongside the planned implementation of the internal model approach framework, on 1 January 2028.

In the EU, the European Commission has recently adopted a delegated act, which, like the UK proposals, temporarily introduces targeted changes to the market risk framework (**Market risks – own funds requirements (delegated act)**). These changes will limit the anticipated increase in capital requirements from the final Basel III market risk framework. The policy is due to be implemented on 1 January 2027.

Taken together, the US Basel III proposals, the proposed changes to the UK market risk framework, and the delegated act adopted by the European commission would likely bring US requirements closer in line with those applied in the UK and EU.

Both the UK and EU are developing policies aimed at simplifying their regulatory frameworks.

In April 2021, the PRA published a Discussion Paper (DP) which set out ideas for developing a 'strong and simple' framework, which introduces simpler prudential framework for firms that are neither systemically important nor internationally active. On 1 January 2027, the second phase of the PRA's **Strong and Simple framework** will come into force. This phase introduces a new, simpler capital regime for Small

Domestic Deposit Takers (SDDTs) that includes the introduction of a single capital buffer instead of the current capital buffers and simplifications to Pillar 1 and 2A for SDDTs.

EU authorities are also working to simplify various aspects of the regulatory framework. The European Central Bank (ECB) created a **High-Level Task Force on Simplification**, to develop recommendations for simplifying the European prudential regulatory, supervisory and reporting framework for banks. The **recommendations** of the Task Force (which were endorsed by the ECB in December 2025) included:

- reducing the number of elements in the risk-weighted and leverage ratio frameworks (which could be achieved by combining some of the existing capital buffers);
- introducing a materially simpler prudential regime for smaller banks, which expands on the existing EU regime;
- introducing a European governance mechanism that takes a holistic view of the overall level of capital.

These points were cited in the Eurosystem's April 2026 **response** to the European Commission's targeted consultation on the competitiveness of the EU banking sector.

As part of the simplification agenda, on 1 October 2025, the EBA published **a report on the efficiency of the regulatory and supervisory framework.** In it, the EBA puts forward 21 recommendations to improve efficiency. One of these recommendations was to reflect on how to streamline requirements, and in June 2026 the EBA published a **report** on how this could be achieved.

> **The UK and US are pursuing additional material changes to their regulatory frameworks.**

In July 2025, the PRA published **DP1/25 – Residential mortgages: Loss given default (LGD) and probability of default (PD) estimation**. This DP presented preliminary considerations and asked respondents to give their views on a range of possible policy changes to the treatment of residential mortgage exposures under the internal ratings based (IRB) approach to credit risk. The DP was motivated by the PRA's observation that medium-sized firms may face barriers in developing IRB models for LGD and PD estimation. The PRA is planning to publish a subsequent Consultation Paper on the topic in Q4 2026 – Q1 2027.[16]

In the US, the Fed, FDIC and OCC have introduced changes to the **enhanced supplementary leverage ratio (eSLR).** On 1 April 2026, the modification of eSLR standards applicable to US GSIBs were implemented, reducing the likelihood that

supplementary leverage ratio requirements would be a binding constraint. These changes made the US leverage framework consistent with Basel standards, bringing leverage requirements for US G-SIBs more into line with those for UK and EU G-SIBs (Chart 1, Section 3).

> **Given substantial changes to regulatory frameworks as Basel 3.1 and other rules are being finalised and implemented, comparisons of existing frameworks are likely to remain complex and subject to change.**

Assessing the overall impact of policy changes set out in this box is difficult given their varying stages of implementation – those that have not yet been finalised may differ from initial proposals. In addition, as ever, the eventual impact would also be affected by actions firms may take to adjust their portfolios or business models in response to regulatory change changes.

Box C: Trends in average risk weights

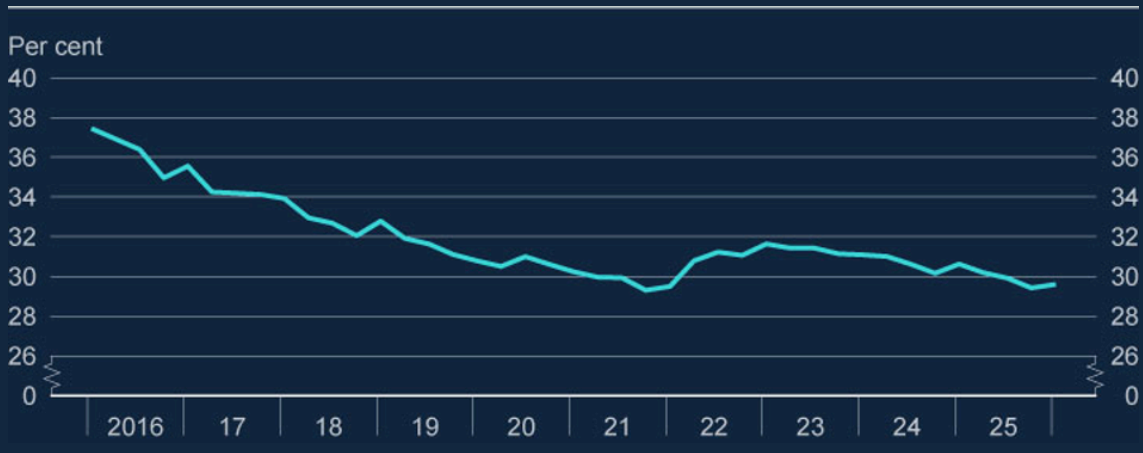
The average risk weight for major UK banks declined by around 8 percentage points from the start of 2016 to 2025 (Chart A).

The decline in average risk weights over the past decade is, to some extent, an expected consequence of a framework with both leverage and risk-based capital requirements, as banks structure their balance sheets in a way that most efficiently meets both. This is also part of a broader long-term trend, with average risk weights now significantly lower than they were prior to the GFC.

Understanding the extent to which this has been driven by underlying reductions in the riskiness of banks' exposures provides important context when considering whether the UK's leverage ratio framework is functioning as intended. Chart B summarises what has driven the decline in average risk weights. It focuses on the 5½ percentage point decline in average risk weights over the period from Q3 2016 to Q4 2025 as more reliable granular data is available after the UK leverage ratio reporting framework was fully implemented in Q3 2016.

Chart A: Major UK banks' average risk weights

Ratio of major UK banks' aggregate risk-weighted assets to UK leverage exposure measure (excluding central bank reserves) (a) (b)

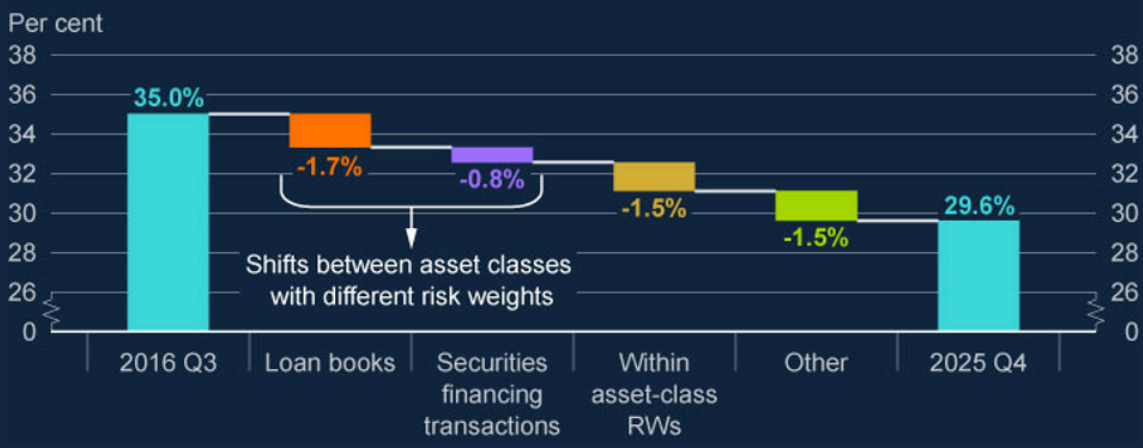


Sources: PRA regulatory returns and Bank calculations.

(a) Aggregate includes Barclays, HSBC, Lloyds Banking Group, Nationwide, NatWest Group, Santander UK, and Standard Chartered at the group consolidation level.
(b) For periods prior to Q3 2016, average risk weights excluding reserves have been calculated using a proxy for qualifying claims on central banks derived from regulatory data.

Chart B: Drivers of the decline in major UK banks' average risk weights

Decomposition of change in average risk weights from Q3 2016 to Q4 2025 (a) (b)



Sources: Regulatory reporting and Bank calculations.

(a) Analysis focusses on the period from Q3 2016 to Q4 2025 as more reliable granular data is available after the UK leverage ratio reporting framework was fully implemented in Q3 2016. Over this period, major UK banks' average risk weights declined by 5½ percentage points compared with around 8 percentage points over the full decade from the start of 2016 to 2025.
(b) Other includes RWAs for market risk, operational risk, derivatives (including credit valuation adjustment risk) plus a small interaction factor.

> **Almost half of the decline in average risk weights from Q3 2016 to 2025 can be accounted for by banks shifting their portfolios towards lower risk-weighted asset classes.**

Within their loan books, banks have increased their share of lower risk-weighted lending, such as residential mortgages, while reducing the share of higher risk-weighted corporate and unsecured retail lending. They have also increased their securities financing transactions (for example, repo agreements), which tend to have low risk weights as they are collateralised with lower-risk, predominantly government, securities.

There has also been growth in more complex and opaque forms of lending over the same period, which is mostly captured in the shift within banks' loan books. This includes lending that has supported the growth of NBFIs that provide an increasing share of lending to real economy borrowers. As set out in Section 6 of the July FSR, these exposures are often structured with features that can reduce expected losses to banks and therefore have lower risk weights compared with lending directly to

individual borrowers. While this can be an efficient way for banks to support the real economy indirectly while managing their own balance sheet risks, these features also increase complexity, making risks to banks harder to assess.

The Bank is strengthening its ability to identify and monitor risks in market-based finance, including through a second system-wide exploratory scenario (SWES) that will explore risks and dynamics associated with the private markets ecosystem.

> **There have also been declines in the average risk weight within different asset classes, accounting for around a third of the decline in average risk weights over the period.**

Such changes can arise for a number of reasons, including derisking, macroeconomic conditions, modelling approaches and movement towards lower risk-weighted assets within a given asset class.

Better asset quality in corporate lending has been a significant driver of lower average risk weights for some banks. Risk weight declines were also notable for NBFI exposures, equity and non-credit obligation assets and securitisations. While mortgage risk weights are low relative to some other types of lending, average mortgage risk weights have been little changed since Q3 2016 overall.

> **The remainder of the decline in average risk weights can be accounted for by other factors, including a decline in operational, market and credit valuation adjustment risk relative to the size of banks' balance sheets.**

Of those, the factor which has contributed the most to the decline in average risk weights is the reduction in credit valuation adjustment risk, as banks have moved more of their derivatives activities to central clearing. As a result, a larger proportion of banks' derivatives exposure is now to central counterparties that are closely supervised and risk-managed, and these exposures are often subject to daily margining. Operational and market risk have been relatively steady over the past decade, thus shrinking relative to banks' total Leverage Exposure Measure, which has increased over the period.

> **Overall, there is some evidence that the decline in average risk weights has been driven by a reduction in the underlying riskiness of banks' exposures over the past decade. But there has also been growth in more complex and opaque forms of lending where the leverage ratio may be particularly effective.**

One of the aims of the leverage ratio is to guard against the danger that models or standardised regulatory requirements fail to assign risk weights that reflect the true underlying risk of assets. This analysis of the decline in banks' average risk weights points to some factors that suggest a reduction in underlying risk, including the shift

towards lower risk-weighted lending types and highly collateralised exposures, de-risking of corporate exposures for some banks and the move to greater central clearing. However, there has also been growth in more complex and opaque forms of lending where the leverage ratio may be particularly effective in guarding against errors in risk measurement. Estimating risk weights is inherently uncertain and there are some risks that may be underestimated until they occur. These trends highlight the continued importance of the leverage ratio framework.

1. Throughout this document, references to ‘system-wide requirements’ refer to aggregate capital requirements and buffers for the major UK banks, excluding firm-specific PRA buffers and requirements set by overseas authorities such as the international component of the CCyB. Within the banking system, in practice, there will be a distribution of capital requirements reflecting individual banks’ business models, their level of systemic importance, the degree of gaps and mismeasurement in their RWAs, and the PRA’s view of firm-specific risks.
2. **O-SII buffer rates for ring fenced banks and large building societies**.
3. Throughout this document, 'ALRB' generally refers to both the ALRB and the 'Leverage Ratio Group Add-on' which may apply to a consolidated group where it includes a ring-fenced body sub-group which has an ALRB. For more information, see **Supervisory Statement (SS) 45/15**, section 2.3A.
4. Throughout this document, ‘UK CCyB’ refers to the UK component of the CCyB.
5. Including **Abad and Pascual (2022)**, **Abad et al (2025)**, **Andreeva et al (2020)**, **BCBS (2022)**, **Berrospide et al (2024)** and **Mathur et al (2023)**.
6. The PRA has already moved in the direction of a simpler capital buffer framework for small domestic deposit takers, which will be subject to the Single Capital Buffer (SCB) following the implementation of the Strong and Simple Framework. The SCB is not releasable, but its usability is supported by the absence of automatic MDA restrictions.
7. The 35% conversion factor was chosen when the leverage ratio framework was implemented to reflect the relative ratio of the original minimum leverage requirement (3%) and the sum of Tier 1 risk-weighted Pillar 1 minimum requirements (6%) and the Capital Conservation Buffer (2.5%) of 8.5%.
8. Overall regulatory loss absorbing capacity is defined as minimum requirements for own funds and eligible liabilities (MREL) plus buffers.
9. **Stress testing the UK banking system: key elements of the 2022/23 annual cyclical scenario**.
10. Lloyds Banking Group, Nationwide, NatWest Group, Santander UK.
11. See **What drives differences in commercial banks’ product level returns? | Bank of England**.
12. In practice, some foreign-owned banks may be subject to capital requirements that apply to UK ring-fenced entities. The PRA would expect foreign-owned banks operating in the UK to subsidiarise if they have a significant volume of retail or small and medium enterprise (SME) deposits, and as subsidiaries they may be captured by UK ring-fencing rules if they are large enough.
13. When the PRA made the decision to maintain the requirement for full capital deduction of software assets, it drew on evidence – including from firms – that the realisable or recoverable value of software assets could not absorb losses effectively in liquidation or in stress. It has not received evidence that leads it to change that assessment.

14. In the comparison of leverage frameworks, the US enhanced supplementary leverage ratio (eSLR) requirements were updated to reflect the approved framework following the conclusion of the US consultation. The revised eSLR was implemented on 1 April 2026, although banks subject to it could adopt it from 1 January 2026.

15. The Internal Model Approach for market risk is due to be implemented on 1 January 2028.

16. The PRA regularly publishes its planned and ongoing policy work in **The Regulatory Initiatives Forum Grid**, where additional upcoming changes are listed.