



Consultation Paper | CP2/22

# Definition of capital: updates to PRA Rules and supervisory expectations

February 2022





BANK OF ENGLAND  
PRUDENTIAL REGULATION  
AUTHORITY

Consultation Paper | CP2/22

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Responses are requested by Monday, 2 May 2022.

**The PRA prefers all responses to be sent by email to: [CP2\\_22@bankofengland.co.uk](mailto:CP2_22@bankofengland.co.uk).**

Alternatively, please address any comments or enquiries to:

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## Contents

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<b>1</b>	<b>Overview</b>	<b>1</b>
<b>2</b>	<b>Proposals</b>	<b>4</b>
<b>3</b>	<b>The PRA's statutory obligations</b>	<b>8</b>
<b>Appendices</b>		<b>12</b>

## 1 Overview

1.1 This Consultation Paper (CP) sets out the Prudential Regulation Authority's (PRA) proposed approach to transferring the UK Technical Standards for own funds requirements for institutions<sup>1</sup> ('UKTS') into PRA rules, with amendments to reflect revisions to the Capital Requirements Regulation<sup>2</sup> ('CRR') which applied from 27 June 2019.<sup>3</sup> These changes to the CRR were not reflected in the relevant EU Regulatory Technical Standard (RTS) before the end of the EU withdrawal transition period and are therefore not currently included in the UKTS on own funds. It also proposes updates to PRA Supervisory Statement (SS) 7/13 'Definition of capital (CRR firms)'<sup>4</sup> to clarify the PRA's expectations of CRR firms regarding capital issuances and reductions.

1.2 The proposals in this CP would amend the Own Funds and Eligible Liabilities (CRR) Part of the PRA Rulebook (Appendix 1) and SS7/13 (Appendix 3).

1.3 This CP is relevant to banks, building societies, PRA-designated investment firms and PRA-approved, or PRA-designated, financial or mixed financial holding companies ('firms').

1.4 The purpose of the proposals in this CP is to revoke the UKTS and replicate it in the PRA Rulebook with proposed amendments to align with updates to the CRR, in particular the rules relating to the prior permission regime to reduce own funds instruments. The proposed updates to SS7/13 aim to enhance the quality of capital instruments issued by firms, simplify procedures where appropriate, and clarify PRA expectations in relation to permissions to reduce own funds instruments.

1.5 The PRA has taken into account the interaction between its primary and secondary objectives, and the 'have regards', including in relation to international standards, the relative standing of the UK, and finance for the real economy. Overall, the PRA considers that the proposals further the PRA's statutory objective of promoting the safety and soundness of firms through effective supervision. The PRA considers that the proposals also align with the 'have regards', in particular, the efficient and effective use of PRA resources without imposing unnecessary burdens on firms.

1.6 The PRA expects that firms would not incur significant additional costs as a result of the proposals in this CP. The proposals would transfer the UKTS to the PRA Rulebook with minimal amendments. The proposed updates to SS7/13 provide further transparency concerning the PRA's expectations on complex or new features in capital instruments issued by firms, and the permission requirements when reducing own funds instruments. Overall, this would allow firms to appropriately structure capital instruments and seek permission when reducing these instruments without incurring additional costs.

1.7 In this consultation paper and the annexed SS7/13 containing the PRA's proposed changes, the term 'own funds' is synonymous and used interchangeably with 'capital'. For example, 'own funds instruments' means the same as 'capital instruments'. The term 'own funds' is used in this consultation when referring to material in the draft rules instrument, as this term has been used in the instrument to ensure coherence with the CRR; while the term 'capital' is used when referring to material in SS7/13, as that is the term used by the PRA. The PRA will keep this approach under review and aim to ensure coherence in the language of its policies as part of the changes proposed in HM Treasury's Future Regulatory Framework.

<sup>1</sup> Regulation (EU) 241/2014, as amended by The EU Exit Instrument: The Technical Standards (Capital Requirements) (EU Exit) (no. 3) Instrument 2019.

<sup>2</sup> Regulation (EU) 575/2013, as amended by the Capital Requirements (Amendment) (EU Exit) Regulations 2018 and 2019, and the Capital Requirements Regulation (Amendment) Regulations 2021.

<sup>3</sup> In this consultation paper, unless otherwise stated, any references to EU or EU-derived legislation refer to the version of that legislation which forms part of retained EU law.

<sup>4</sup> March 2020: [SS7/13 'Definition of capital \(CRR firms\)'](#).

## Background

1.8 UK own funds regulation currently includes the CRR and the UKTS on own funds. These instruments were incorporated into UK law by the EU (Withdrawal) Act 2018 and amended by HMT<sup>5</sup> and PRA EU Exit Instruments<sup>6</sup> respectively. The legislation is complemented by SS7/13, which sets out the PRA's expectations of CRR firms in relation to the quality of their capital resources.

1.9 The CRR includes various amendments to the own funds provisions made under the revised Capital Requirements Regulation ('CRR II').<sup>7</sup> These amendments applied from 27 June 2019, and include:

- revisions to the application requirements for firms when reducing own funds and eligible liabilities, and the corresponding PRA approval process;
- a general prior permission granted by the PRA to firms when reducing a predetermined amount of own funds instruments over a specific period (CRR Article 78(1));
- a new supervisory permission requirement when reducing share premiums (CRR Article 77(1)(b)); and
- new eligibility requirements for eligible liabilities and supervisory permission requirements when reducing eligible liabilities instruments (CRR Article 72a – 72l; CRR Article 78a).

1.10 The UKTS sets out specific requirements when applying the CRR requirements. Following its withdrawal from the EU, the UK is now responsible for making all revisions to the UKTS in light of the CRR II amendments.

## Approach to making rules

1.11 Under PRA Policy Statement (PS) 22/21 'Implementation of Basel Standards: Final rules', Articles 13 to 19 of the UKTS which relate to deductions from Common Equity Tier 1 (CET 1) were moved to the Own Funds and Eligible Liabilities (CRR) Part of the PRA Rulebook from 1 January 2022. The PRA will replicate the remaining provisions of the UKTS in the same Part of the PRA Rulebook, in order to ensure that the entire UKTS is located in one place. This will make it easier for firms to access and comply with these provisions. In order to achieve this outcome, the PRA will exercise its power under section 138P of the Financial Services and Markets Act 2000 (FSMA) to revoke the UKTS, and the PRA general rulemaking power under section 137G of FSMA to replicate the remaining provisions of the UKTS, including the proposed updates and amendments, in the PRA Rulebook through a new PRA CRR rule instrument. This CP sets out the proposed new PRA CRR rules in full, including parts of the CRR that are not changing but are being transferred into PRA rules – although where these do not change, they do not form part of this consultation.

## Summary of proposals

1.12 The policy proposals included in this CP are as follows:

- (a) Alongside replicating the UKTS requirements in the PRA Rulebook, the PRA proposes to update the relevant provisions in the Own Funds and Eligible Liabilities (CRR) Part to align with the changes introduced to the CRR in 2019. This includes updates to the requirements on firms regarding: information which must be provided when seeking PRA permission to reduce capital instruments; the new general prior permission process; and the process for reductions in share premium accounts.

<sup>5</sup> The Capital Requirements (Amendment) (EU Exit) Regulations 2018 and 2019, and the Capital Requirements Regulation (Amendment) Regulations 2021.

<sup>6</sup> EU Exit Instrument: The Technical Standards (Capital Requirements) (EU Exit) (no. 3) Instrument 2019.

<sup>7</sup> Regulation (EU) 2019/876.

- (b) The PRA also proposes to update SS7/13 to clarify its expectations of CRR firms regarding the quality of capital instruments, in light of recent supervisory experience. The proposals also set out PRA expectations on liability-accounted Additional Tier 1 (AT1) instruments, update existing references on subordinated swaps, and introduce an expectation for firms to seek PRA views prior to issuing any new Tier 2 instruments which include new or complex features. The PRA also clarifies its expectation that firms seek PRA permission for any forms of reduction of own funds instruments, and that firms should inform supervisory contacts when there is sufficient certainty regarding capital reduction transactions in order to facilitate publication of the related PRA permission.

1.13 The Bank of England ('The Bank'), in its capacity as UK resolution authority, is responsible for making UKTS relating to eligible liabilities, and has indicated it does not intend to make Technical Standards on eligible liabilities at this stage. As such, the PRA proposes to only consult on updates to the own funds-related provisions for PRA-regulated CRR firms.

### **Implementation**

1.14 The PRA proposes that the implementation date for the changes resulting from this CP would be September 2022.

### **Responses and next steps**

1.15 This consultation closes on Monday 2 May 2022. The PRA invites feedback on the proposals set out in this consultation. Please indicate in your response if you believe any of the proposals in this consultation paper are likely to impact persons who share protected characteristics under the Equality Act 2010, and if so, please explain which groups and what the impact on such groups might be. Please address any comments or enquiries to [CP2\\_22@bankofengland.co.uk](mailto:CP2_22@bankofengland.co.uk).

1.16 References related to the UK's membership of the EU in SS7/13 have been updated as part of these proposals to reflect the UK's withdrawal from the EU. Unless otherwise stated, any remaining references to EU or EU-derived legislation refer to the version of that legislation which forms part of retained EU law.<sup>8</sup>

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<sup>8</sup> For further information please see <https://www.bankofengland.co.uk/eu-withdrawal/transitioning-to-post-exit-rules-and-standards>.

## 2 Proposals

2.1 This chapter sets out the PRA's proposals in relation to capital instruments upon transferring the UKTS to the PRA Rulebook, and its proposed updates to SS7/13.

### Updates to the Own Funds and Eligible Liabilities (CRR) Part of the PRA Rulebook

#### Information requirements

2.2 CRR II amended CRR Article 78(1)(b) to permit a reduction of own funds instruments by firms only where they demonstrate that following the transaction they would continue to exceed relevant regulatory requirements. CRR II also amended the conditions in CRR Article 78(4)(d) when reducing certain own funds instruments within five years of issuance.

2.3 As a result of these amendments, the PRA proposes to require additional information from firms to enable it to assess applications for permission to reduce own funds instruments against the relevant requirements. This would include information on, among other things, the current and forward-looking position on the leverage ratio, eligible liabilities requirements, and how the conditions under CRR Article 78(4)(d) are met. These proposals would ensure the consistency and comparability of information provided by firms to the PRA when applying for permission to reduce own funds.

#### General prior permission

2.4 CRR II also amended CRR Article 78(1) to allow competent authorities to grant firms a general prior permission (GPP) to reduce own funds instruments up to a predetermined amount within a specified period. GPP enables firms to undertake multiple transactions to reduce own funds instruments up to the predetermined amount over a specific period not exceeding 12 months from the permission date, instead of applying for separate permission for each reduction transaction. This GPP can be renewed before the permission expires. Accordingly, the provisions in Article 29 of the UKTS that specify the purposes and the predetermined amounts of GPP are not replicated in the Own Funds and Eligible Liabilities (CRR) Part.

2.5 The PRA proposes that, when a firm applies for GPP, the firm should provide the following information in order to enable the PRA to assess the GPP application against the requirements set out in the second subparagraph of CRR Article 78(1):

- the impact of the proposed permission on Common Equity Tier 1 resources;
- the amount of the relevant outstanding issue; and
- the total carrying amount of the outstanding instruments.

2.6 In addition, the PRA proposes that the GPP amount, once approved, should be deducted immediately from own funds. This would be prudent given that the permitted amount may be reduced from own funds at any time within the specified period and would no longer be available to absorb losses.

2.7 The PRA may renew a GPP provided that the firm does not request an increase in the predetermined amount, or change the rationale under the original request. In the case of such GPP renewals, the PRA proposes to exempt firms from providing certain information, including the rationale for permission, the present and forward-looking capital position, and any planned capital action for the next three years. The PRA considers that this proposal would reduce the operational burden on firms for renewals, and is proportionate to the prudential risk given the relatively small limit on the amounts permitted for GPP, and that the permitted amount would already be deducted from the firm's capital resources as proposed under paragraph 2.6.

## Supervisory permission to reduce share premiums

2.8 Following CRR II amendments to Article 77, firms are required to seek prior supervisory permission to reduce, distribute, or reclassify share premium accounts related to own funds instruments. The PRA therefore proposes to reflect this in the PRA rules implementing the CRR requirements on reduction of own funds instruments.

## Technical amendments

2.9 The PRA also proposes to make a number of minor technical amendments to ensure consistency between the PRA Rulebook and other aspects of the CRR. This includes:

- the redenomination of references to Euros (EUR) into Pounds Sterling (GBP) with the same average daily GBP/EUR spot exchange rate as that used under PRA rules implementing Basel Standards;<sup>9</sup>
- further drafting amendments to specific terminology within the CRR, for example, replacing the term ‘purchase’ by ‘acquisition of ownership’ under the requirements on eligibility criteria of own funds instruments; and
- adapting the draft rules or making changes where required, for example, not replicating chapter VA in the UKTS following the deletion of CRR Article 97 under the Investment Firms Prudential Regime rules.<sup>10</sup>

## Updates to SS7/13

2.10 As stated in SS7/13, the PRA expects firms to comply with internationally-agreed criteria concerning the definition of capital, both in spirit and letter. The PRA previously updated SS7/13 in March 2020 to clarify its expectations on complex capital features and structures. In addition, the PRA’s proposed amendments to the SS in this CP further clarify these expectations based on supervisory experience, including updates on:

- the implications of non-CET1 shares on the eligibility of CET1 shares;
- the use of side-agreements;<sup>11</sup> and
- the risks of barriers to recapitalisation from preferential distribution of share sales proceeds amongst shareholders or anti-dilution clauses.

## Liability-accounted AT1 instruments

2.11 While most AT1 instruments issued by PRA-authorized firms are accounted for as equity, firms may prefer to issue liability-accounted AT1 instruments with features or arrangements to manage certain market risks, such as currency exchange risk when issuing in currencies other than their reporting currency. The PRA considers that some of these features or arrangements could undermine the subordination of payments (for example, by hedging the cash flow from the AT1 instrument) or affect the ability of the instrument to effectively absorb losses, and as such give rise to wider prudential concerns. The PRA therefore proposes to reiterate its expectation that firms refrain from including features in capital instruments or related arrangements which may reduce its effectiveness in absorbing losses.

<sup>9</sup> July 2021: [PS17/21 'Implementation of Basel standards'](#), Chapter 16.

<sup>10</sup> [Financial Services Act 2021](#): Schedule 1, paragraph 19.

<sup>11</sup> The [Glossary Part of the PRA Rulebook](#) states that a side agreement ‘means any document containing an agreement or other arrangement, including a proposed agreement or other arrangement, related to the capital instrument (whether or not explicitly referred to in the instrument) which could affect the assessment of compliance of the instrument with Part Two of CRR.’

### Holders of subordinated instruments

2.12 As stated in Chapter 5 of SS7/13, all capital instruments must be subordinated to all senior creditors. It is important that subordinated creditors cannot force early repayment on a subordinated capital instrument while the issuer may still be technically solvent. Chapter 5 of SS7/13 noted that this is important so as not to hinder the efforts of the authorities in the context of recovery or resolution actions in relation to the issuer.

2.13 The PRA proposes to clarify that the Bank's resolution actions as UK resolution authority are not affected by or limited as a result of the actions of subordinated creditors. The PRA considers the reference to resolution actions in Chapter 5 of SS7/13 is not appropriate and should be removed.

### Subordinated swaps

2.14 Chapter 6 of SS7/13 sets an expectation that the value of a hedging instrument in a fair value hedge relationship could be included in the value of the hedged capital instrument only if it was also subordinated. However, the CRR does not permit hedging instruments to be included in hedged capital instrument where a fair value hedge is used. The PRA considers that this expectation is not relevant under the CRR and therefore proposes deleting Chapter 6 of SS7/13.

### Tier 2 instrument notification

2.15 The PRA requires firms to notify the PRA on, or immediately after the date of issuance or amendments to Tier 2 instruments.<sup>12</sup> This reflects the PRA's observation that most Tier 2 instruments issued by PRA-authorized firms have been simple in structure, and have not raised material prudential concerns. However, the PRA has noted potential new features in Tier 2 instruments including for example instruments marketed as 'Green', 'Social', or 'Environmental, Social, Governance (ESG)'. Firms should consider where these instruments include any features that may affect the ability of these instruments to absorb losses, or their eligibility as Tier 2 instruments under the CRR. The PRA therefore proposes to introduce an expectation that, notwithstanding the post-issuance notification requirement for Tier 2 instruments, firms should discuss such instruments with the PRA prior to issuing Tier 2 instruments with such new or complex features as set out in paragraph 2.3 to 2.5 of SS7/13.

### Permission for all forms of reductions in own funds instruments and share premiums

2.16 CRR Article 77(1)(c) requires firms to seek permission to 'effect the call, redemption, repayment or repurchase of Additional Tier 1 or Tier 2 instruments as applicable, prior to the date of their contractual maturity'.<sup>13</sup> The PRA proposes to clarify that it expects firms to seek prior PRA permission for any forms of reduction to own funds instruments, including:

- cancellation or conversion of own funds instruments;<sup>14</sup>
- de-recognising an instrument as own funds; or
- any transactions that would have the effect of reducing a firm's own funds instruments and related share premiums.

### Notifications to the PRA

2.17 The PRA has a statutory duty to publish all permissions, including permissions granted to firms to reduce capital instruments, unless the PRA considers such publication unnecessary or inappropriate. The PRA generally accepts firms' requests to co-ordinate this publication with their announcements to the market. The PRA proposes that firms should inform their usual supervisory

<sup>12</sup> PRA Rulebook, Definition of Capital Part, Rule 7C

<sup>13</sup> CRR Article 77(1)(c).

<sup>14</sup> Except for conversions of AT1 instruments at a predetermined automatic trigger, or conversion of capital instruments at the point of non-viability.

contact as soon as there is sufficient certainty regarding the capital reduction transaction, in order for the PRA to publish the related permissions accordingly.

## Questions

Q1: Do you agree with the proposals set out in this chapter regarding updates to PRA CRR rules and PRA expectations on own funds?

Q2: Do you agree with the proposal for the PRA to expect firms to discuss with the PRA prior to issuance of new Tier 2 instruments with new or complex features?

## Objective and justification of proposals

2.18 The proposals set out in this chapter would enable the PRA to fully align with the CRR as amended by CRR II, and ensure that capital instruments are structured appropriately. The proposals would advance the PRA's statutory objective to promote the safety and soundness of firms by requiring that permissions are appropriately sought, granted based on suitable and consistent information, and published in a timely manner. The proposals also seek to ensure that capital instruments are appropriately structured to absorb losses, and that issuances are clear and transparent.

2.19 The PRA has considered the 'have regards' in relation to the proposals in this chapter, including the efficient and effective use of PRA resources, ensuring the burden of the proposals are proportionate to the benefits, and relevant international standards. The PRA considers that these proposals would not result in any significant cost implications for firms. Most of the proposed rules replicate the UKTS requirements in the PRA Rulebook without changes. Where these requirements are modified, the amendments are necessary to implement CRR requirements. With respect to the proposed additional information required for permissions to reduce own funds instruments, firms are already expected to have this information readily available in order to comply with other regulatory requirements (eg leverage ratio disclosure), or for general capital management purposes. Many firms have already been providing similar information to the PRA as part of their applications for permissions to reduce own funds instruments. The proposals to strengthen supervisory expectations under the SS would similarly add clarity without imposing an additional burden on firms.

### 3 The PRA's statutory obligations

3.1 In carrying out its policy making functions, the PRA is required to comply with several legal obligations. The PRA has a statutory duty to consult when introducing new rules (FSMA s138J). When not making rules, the PRA has a public law duty to consult widely where it would be fair to do so.

3.2 The PRA fulfils its statutory obligations and public law duties by providing the following in relation to the proposed policy:

- (i) **a cost benefit analysis;**
- (ii) **compatibility with the PRA's objectives:** an explanation of the PRA's reasons for considering that making the proposed rules is compatible with the PRA's duty to act in a way that advances its general objective and secondary competition objective;<sup>15</sup>
- (iii) **FSMA regulatory principles:** an explanation of the ways in which having regard to the regulatory principles has affected the proposed rules;<sup>16</sup>
- (iv) **CRR rules:** in addition to the above, FSMA requires the PRA to 'have regard' to several further matters when making CRR rules.<sup>17</sup> It also requires the PRA to explain how the new 'have regards' have affected its proposed rules.<sup>18</sup> Furthermore, when making CRR rules, the PRA is required to 'consider, and consult HM Treasury about, the likely effect of the rules on relevant equivalence decisions';<sup>19</sup>
- (v) **impact on mutuals:** a statement as to whether the impact of the proposed rules will be significantly different to mutuals than to other persons;<sup>20</sup>
- (vi) **HM Treasury recommendation letter:** the Prudential Regulation Committee (PRC) should have regard to aspects of the Government's economic policy as recommended by HM Treasury;<sup>21</sup> and
- (vii) **equality and diversity:** the PRA is also required by the Equality Act 2010<sup>22</sup> to have due regard to the need to eliminate discrimination and to promote equality of opportunity in carrying out its policies, services, and functions.

3.3 Appendix 4 lists the statutory obligations applicable to the PRA's policy development process. The analysis in this chapter explains how the proposals have had regard to the most relevant matters listed in paragraph 3.2, including an explanation of the ways in which having regard to these matters has affected the proposals.

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<sup>15</sup> Section 2H(1) of FSMA.

<sup>16</sup> Sections 2H(2) and 3B of FSMA.

<sup>17</sup> Section 144C(1) of FSMA. Part 9D FSMA (s144) defines CRR rules as PRA general rules related to either (i) provisions of the UK CRR revoked by HMT or (ii) 'CRR Basel standards' (as defined under s4 of the FS Act 2021). CRR rules also include rules made under section 192XA, which gives powers to the PRA to make rules in relation to specific matters and applying to financial holding companies and mixed financial holding companies that are approved or designated by the PRA ('Holdco rules').

<sup>18</sup> Section 144D of FSMA.

<sup>19</sup> Section 144C(3) of FSMA.

<sup>20</sup> Section 138K of FSMA.

<sup>21</sup> Section 30B of the Bank of England Act 1998.

<sup>22</sup> Section 149.

## Updates to the Own Funds and Eligible Liabilities (CRR) Part of the PRA Rulebook, and updates to SS7/13

3.4 The PRA proposes to delete the UKTS and replicate it in the PRA Rulebook, with proposed amendments to account for changes introduced to the CRR in June 2019. It also proposes to set out its expectations in relation to the quality of capital instruments issued by firms and permissions when reducing own funds instruments. The proposed changes would ensure the operability of the CRR and provide consistent and comparable information to assist with supervisory decision-making.

3.5 The PRA considers that its proposed approach would advance its primary objective, ensuring any burden to firms is proportionate to benefits, and improve transparency.

### PRA objectives

3.6 The PRA's proposals will enable it to implement the CRR rules as amended by CRR II and ensure that capital instruments are structured appropriately. These proposals advance the PRA's statutory objective to promote the safety and soundness of firms by requiring that permissions are appropriately sought, granted based on suitable and consistent information, and published in a timely manner. This would facilitate more effective supervisory decision-making, and therefore contribute to the PRA's objective of promoting the safety and soundness of firms.

3.7 The proposals would also enhance and maintain the quality of firms' capital resources with a focus on CET1, which is the highest quality of capital. The proposals will contribute to the PRA's objectives of promoting the safety and soundness of firms by improving the transparency of capital instruments and the efficiency of supervisory decision-making.

3.8 The PRA has assessed whether the proposals in this CP facilitate effective competition. The proposals may reduce the ability for the smaller firms to attract capital investments from certain investors that may prefer alternative arrangements for preferential capital returns. However, the PRA considers that these proposals are important to promote the safety and soundness of firms, and would also advance the PRA's secondary objective by improving transparency on how the PRA exercises its functions.

### 'Have regards'

#### *FSMA regulatory principles*

3.9 In developing these proposals, the PRA has had regard to the FSMA regulatory principles (the 'have regards'). The following five principles are of particular relevance:

- (i) **The principle that a burden or restriction which is imposed on a person should be proportionate to the benefits which are expected to result from the imposition of that burden:** The PRA considers that the proposals do not materially increase the burden on firms relative to current requirements. The PRA has proposed a proportionate approach to certain requirements such as renewal of GPP applications. The PRA considers the proposals would improve the ease with which firms can understand and access the full set of requirements by locating them all in a single place, rather than leaving them dispersed across different locations.
- (ii) **Efficient and effective use of PRA resources:** The PRA's proposals seek to achieve the most prudential benefit from the use of PRA resources. The proposals ensure that all relevant information is made available to the PRA when assessing an application, thereby promoting the efficient and effective use of PRA resources. The proposed expectation that firms inform the PRA when there is sufficient certainty regarding a transaction would further ensure efficient use of PRA resources by avoiding detailed supervisory dialogue with firms concerning updates prior to publishing a permission.

- (iii) **The desirability of sustainable growth in the economy of the UK in the medium or long term:** The proposals help to ensure that banks maintain sufficient loss absorbing capital, which is a necessary condition to ensuring they are able to continue to lend and support productive investment throughout the economic cycle.
- (iv) **The principle that the PRA should exercise its functions transparently:** The PRA considers that the proposals would ensure that PRA rules reflect the changes introduced by CRR II and clarify the PRA's expectations on permissions to reduce own funds instruments, thereby improving transparency on how the PRA exercises its functions.
- (v) **Recognition of differences in, and nature of, businesses:** The proposals would apply to all banks, building societies, PRA-designated investment firms and PRA-approved, or PRA-designated, financial or mixed financial holding companies. Although the nature of these types of entities differs, they are all subject to the directly applicable CRR requirements. The PRA's proposals on co-ordinating publication of permissions would facilitate orderly compliance with firms' market disclosure obligations, and as such demonstrate sensitivity to firms' other regulatory obligations.

3.10 The PRA has considered the remaining FSMA regulatory principles (see references in Appendix 4), and considers that they are not relevant to these proposals.

#### *CRR rules*

3.11 The proposed rules in this CP are 'CRR rules' (as defined in section 144A of FSMA). As a result, in developing the proposals in this CP, the PRA considered the additional 'have regards' applicable to CRR rules.

3.12 **Finance for the real economy, growth, and sustainable growth:** The proposed rules clarify supervisory processes, and are unlikely to have a significant impact on capital requirements, balance sheet structure or business activities. The proposed rules are unlikely to have any material impact on finance for the real economy, therefore the PRA does not expect the impact on growth and sustainable growth to be significant.

3.13 **Relative standing of the UK and competitiveness:** The PRA considers the proposed changes in relation to own funds reductions are in line with those proposed by the European Banking Authority<sup>23</sup> and therefore should not affect the relative standing of the UK and its competitiveness.

3.14 **International standards:** The Basel Standards do not specify supervisory processes in relation to reduction of own funds. The PRA's proposals are broadly consistent with the EU approach to own funds, while allowing for some proportionality where the PRA considers this to be appropriate.

3.15 **Climate change Act 2008 (Carbon target for 2050):** The PRA does not consider that the proposals will have any adverse impact on the carbon target for 2050 as set out in section 1 of the Climate Change Act 2008. The PRA's proposals seek to ensure that all instruments, including those issued with environmental, social and governance features that are classified as regulatory capital can absorb losses effectively.

3.16 The PRA has considered the remaining matters to which it should have regard when making CRR rules (see references in Appendix 4), and considers that they are not relevant to this proposal.

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<sup>23</sup> Available at: [https://www.eba.europa.eu/sites/default/documents/files/document\\_library/Publications/Draft%20Technical%20Standards/2021/1012878/Final%20Report%20on%20draft%20RTS%20on%20Ofs%20and%20ELs.pdf](https://www.eba.europa.eu/sites/default/documents/files/document_library/Publications/Draft%20Technical%20Standards/2021/1012878/Final%20Report%20on%20draft%20RTS%20on%20Ofs%20and%20ELs.pdf).

*Impact on mutuals*

3.17 FSMA requires that the PRA assesses whether, in its opinion, the impact of the proposed rules on mutuals will be significantly different from the impact on other firms, and if so, provide details of the difference. The proposed rules would apply equally to all PRA-authorized firms including mutuals. The PRA therefore considers that the impact of the proposed rule changes on mutuals would be no different from the impact on other firms.

*HM Treasury recommendation letter*

3.18 HM Treasury has made recommendations to the Prudential Regulation Committee (PRC) about aspects of the Government's economic policy to which the PRC should have regard when considering how to advance the PRA's objectives and apply the regulatory principles.

3.19 **Competitiveness:** The PRA considers the proposed changes to move the UKTS to the PRA Rulebook should not affect the relative standing of the UK and its competitiveness. As noted above, the PRA proposals in relation to own funds reductions are in line with those proposed by the European Banking Authority.

3.20 **Competition:** The PRA has assessed whether the proposals in this CP facilitate effective competition. The proposals in relation to simple capital structure may reduce the ability for the smaller firms to attract capital investments from certain investors that may prefer alternative arrangements for preferential capital returns. However, the PRA considers that its proposals are important to promote the safety and soundness of firms, and would also advance the PRA's secondary objective by improving transparency on how the PRA exercises its functions.

3.21 **Innovation:** The proposals are aimed at improving the PRA's supervisory approach to capital reduction and issuances by firms, and would not affect innovation by firms.

3.22 **Growth, trade and better outcomes for consumers:** The PRA considers that the proposals do not give rise to implications related to this 'have regard'.

3.23 **Climate change:** The PRA considers that the proposals do not give rise to implications related to this 'have regard'.

3.24 The PRA has considered the remaining aspects of government economic policy as laid out in the HM Treasury recommendation letter (see references in Appendix 4), and considers that they are not relevant to this proposal.

*Equality and diversity*

3.25 The PRA considers that the proposals do not give rise to equality and diversity implications.

*Cost benefit analysis*

3.26 The PRA considers that these proposals would not result in any significant cost implications for firms. Most of the proposed rules replicate the UKTS requirements without changes. Where they are modified, the amendments are necessary to implement CRR requirements. With respect to the proposed additional information required for permissions to reduce own funds instruments, firms are expected to have this information readily available in order to comply with other regulatory requirements (eg leverage ratio disclosure) or for general capital management purposes. Many firms have already been providing similar information to the PRA as part of their applications for permissions to reduce own funds instruments. The PRA considers the proposals strengthen supervisory expectations and add clarity, without imposing additional burden on firms.

## Appendices

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<b>1</b>	<b>Proposed rule instrument ‘PRA RULEBOOK: CRR FIRMS OWN FUNDS AND ELIGIBLE LIABILITIES INSTRUMENT 2022’</b>	<b>13</b>
<b>2</b>	<b>Proposed technical standards instrument ‘PRA STANDARDS INSTRUMENT: THE TECHNICAL STANDARDS (OWN FUNDS) INSTRUMENT 2022’</b>	<b>14</b>
<b>3</b>	<b>Proposed amendments to SS7/13, ‘Definition of capital (CRR firms)’</b>	<b>15</b>
<b>4</b>	<b>PRA statutory obligations</b>	<b>16</b>

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- 1 Proposed rule instrument 'PRA RULEBOOK: CRR FIRMS OWN FUNDS AND ELIGIBLE LIABILITIES INSTRUMENT 2022', available at:  
<https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/consultation-paper/2022/February/cp222app1.pdf>

- 2 Proposed technical standards instrument ‘PRA STANDARDS INSTRUMENT: THE TECHNICAL STANDARDS (OWN FUNDS) INSTRUMENT 2022’, available at:**  
<https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/consultation-paper/2022/February/cp222app2.pdf>

3 Proposed amendments to SS7/13, 'Definition of capital (CRR firms)', available at: <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/consultation-paper/2022/February/cp222app3.pdf>

## 4 PRA statutory obligations

**The statutory obligations applicable to the PRA's policy development process are set out below. This CP explains the policy assessment of relevant considerations.**

- Purpose of the policy proposals (FSMA s138J(2)(b)).
- Cost benefit analysis (FSMA s138J(2)(a) and (7)(a)); and an estimate of those costs and benefits (if reasonable) (FSMA s138J(8)).
- Analysis of whether the impact on mutuals is significantly different to the impact on other authorised firms (FSMA s138J(2)(c) and 138K).
- Compatibility with the PRA's primary objectives (FSMA s138J(2)(d)(i), 2B and 2C).
- Compatibility with the PRA's secondary competition objective (FSMA s138J(2)(d)(ii) and 2H(1)).
- Compatibility with the regulatory principles (FSMA s138J(2)(d)(ii), 2H(2) and 3B).
- Have regard to the HMT recommendation letter (BoE Act s30B).
- Have due regard to the public sector equality duty (Equality Act s149).
- Have regard, subject to any other requirement affecting the exercise of the regulatory function, to the principles of good regulation and when determining general policy or principles to the Regulators Code (Legislative and Regulatory Reform Act 2006 s21 & 22)
- Have regard, so far as consistent with the proper exercise of those functions, to the purpose of conserving biodiversity. Conserving biodiversity includes, in relation to a living organism or type of habitat, restoring or enhancing a population or habitat (Natural Environment and Rural Communities Act 2006, s40).
- Consultation of the FCA (FSMA s138J(1)(a)).
- *Where the consultation proposals a PRA rule change or amendment to onshored BTS that affects the processing of personal data - consultation with the Information Commissioner's Office (article 36(4) General Data Protection Regulation).*
- *For UK Technical Standards Instruments only:* FSMA s138J(1)(a) is replaced with: consultation of the FCA and/or Bank, where that Regulator has an interest in the technical standards (FSMA s138P(4) and (5)).
- *For UK Technical Standards Instruments only:* notice given to HMT of the consultation on the UKTS ('best efforts' basis).
- *For CRR rules only:* subject to certain exceptions, have regard to:
  - relevant standards recommended by the Basel Committee on Banking Supervision from time to time

- the likely effect of the rules on the relative standing of the United Kingdom as a place for internationally active credit institutions and investment firms to be based or to carry on activities. For these purposes, the PRA must consider the United Kingdom's standing in relation to the other countries and territories in which, in its opinion, internationally active credit institutions and investment firms are most likely to choose to be based or carry on activities
- the likely effect of the rules on the ability of CRR firms to continue to provide finance to businesses and consumers in the United Kingdom on a sustainable basis in the medium and long term
- the target in section 1 of the Climate Change Act 2008 (carbon target for 2050)

(s144C (1) & (2) FSMA – exceptions in s144E FSMA).

- *For CRR rules only* – explanation of the ways in which having regard to the matters specified above has affected the proposed rules (s144D FSMA).
- *For CRR rules only* – publication of a summary of the proposed CRR rules.
- *For CRR rules only* – consideration and consultation with the Treasury about the likely effect of the rules on relevant equivalence decisions (s144C (3) & (4) FSMA).