BANK OF ENGLAND
PRUDENTIAL REGULATION AUTHORITY

Publication

Supervisory Statement | SS15/13

Groups

December 2020

(Updating July 2016)

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Prudential Regulation Authority | 20 Moorgate | London EC2R 6DA

Contents

1 Introduction

1.1 This supervisory statement is relevant to all banks, building societies, and designated investment firms and all PRA-approved or PRA-designated holding companies.

1.2 This statement sets out the Prudential Regulation Authority's (PRA's) expectations about applications relating to:

(a) its approach to consolidation, in particular individual consolidation (CRR Article 9) and the method of consolidation for entities falling within CRR Article 18(5); and

(b) excluding certain entities from consolidation (CRR Article 19(2)).

1.3 This statement should be read in conjunction with the CRR articles listed, the requirements in the Groups Part of the PRA Rulebook and the high-level expectations outlined in The PRA's approach to banking supervision.[1] For RFBs, as defined in the Financial Services and Markets Act (FSMA), section 142A, or any other PRA-authorised person that is a member of a group containing an RFB, this statement should be read alongside the PRA's Supervisory Statement 8/16 'Ring-fenced bodies (RFBs)'.[2]

2 Approach to consolidation

2.1 Where a parent institution wishes to apply for individual consolidation, it will be expected to make a formal application to the PRA. The PRA expects the application to demonstrate how the conditions set out in CRR Article 9 and 396(2) are met.

2.2 The PRA will assess individual consolidation applications against CRR Article 9 and 396(2) on a case by case basis. Where the conditions in CRR Article 9 and 396(2) are met, the PRA will assess whether it is still appropriate to permit the treatment, if doing so risks conflict with its statutory objectives. The PRA will apply a high level of scrutiny to applications under CRR Article 9 as per the PRA's previous solo consolidation regime.

2.2A An RFB, or any other PRA-authorised person that is a member of a group containing an RFB, should note that the PRA will assess whether it remains appropriate to permit the treatment where the conditions set out in CRR Article 9 and 396(2) are met, including an assessment of the impact of the proposed treatment on the ability of the RFB and any other members of its group to fulfil their ring-fencing obligations, and on the PRA's general safety and soundness objective in relation to ring-fencing.[3]

2.3 Where a parent institution does not wish to proportionately consolidate its undertakings subject to CRR Article 18(5), it will be expected to make a formal application to the PRA. The application should seek to demonstrate how proportionately consolidating those undertakings is disproportionate to the risk carried by the firm.

2.3A CRR Article 18(7) permits the PRA to allow or require a firm to use a method other than the equity method for valuing certain holdings where specific criteria are met. Where a parent

1 www.bankofengland.co.uk/publications/Pages/other/pra/supervisoryapproach.aspx.
2 PRA Supervisory Statement 8/16 'Ring-fenced bodies', July 2016, available at: www.bankofengland.co.uk/pra/Pages/publications/ss/2016/ss816.aspx.
3 See section 2B of FSMA.

institution does not wish to apply the equity method, but instead wishes to use another valuation method, it will be expected to make a formal application. The application should seek to demonstrate how the criteria set out in Article 18(7) are met. The PRA may then be able to permit the use of a different method, such as the one used by the firm under its applicable accounting framework, where the relevant criteria are met. The PRA may also require a firm to use a different valuation method if it determines that the equity method is unduly burdensome or does not adequately reflect the risks of a holding.

2.3B CRR Article 18(8) permits the PRA to require the full or proportional consolidation of certain undertakings where an institution has a subsidiary or participation relationship with them and where there is 'substantial step-in risk'.[4] This is consistent with the Basel Committee's guidelines on the 'Identification and management of step-in risk'.[5] The PRA intends to exercise this power on a case-by-case basis where it assesses that there is evidence that such substantial step-in risk exists.

Application of criteria

2.4 CRR Article 9(2) requires parent institutions to demonstrate fully to the PRA, as competent authority, that there are no material practical or legal impediments to the prompt transfer of own funds or repayment of liabilities when due by the subsidiary to its parent undertaking.

2.5 When making this assessment, the PRA will consider whether any minority interest may represent an impediment of any kind to the prompt transfer of own funds or repayment of liabilities from subsidiary undertaking to parent. The PRA expects that the parent institution should demonstrate that any minority interest in a subsidiary institution will not result in the potential blocking or delay of prompt transfer of own funds or repayment of liabilities.

2.6 It is possible for a firm to meet the condition in CRR Article 7(1)(d) but not meet the condition in CRR Article 9(2).

2.7 The PRA will consider the non-exhaustive list below when determining whether the conditions in CRR Article 9(2) are met:

(a) the speed with which funds can be transferred or liabilities repaid to the firm and the simplicity of the method for the transfer or repayment;

(b) whether there are any interests other than those of the firm in the subsidiary undertaking and what impact those other interests may have on the firm's control over the subsidiary undertaking and on the ability of the firm to require a transfer of funds or repayment of liabilities. As part of the PRA's overall assessment, it would consider one of the indicators to achieving prompt transfer as being ownership of 75% or more of the subsidiary undertaking;[6]

(c) whether the prompt transfer of funds or repayment of liabilities to the firm might harm the reputation of the firm or its subsidiary undertakings;

(d) whether there are any tax disadvantages for the firm or the subsidiary undertaking as a result of the transfer of funds or repayment of liabilities;

4 Defined in CRR Article 18(8)(b) as, 'a substantial risk that the institution decides to provide financial support to that undertaking in stressed conditions, in the absence of, or in excess of any contractual obligations to provide such support'.

5 Basel Committee on Banking Supervision, 'Guidelines: Identification and management of step-in risk', October 2017: https://www.bis.org/bcbs/publ/d423.htm.

6 75% or more shareholders can pass a special resolution.

(e) whether there are any exchange controls that may have an impact on the transfer of funds or repayment of liabilities;

(f) whether there are assets in the subsidiary undertaking available either to be transferred or liquidated for the purposes of the transfer of funds or repayment of liabilities;

(g) whether any regulatory requirements affect the ability of the subsidiary undertaking to transfer funds or repay liabilities promptly;

(h) whether the legal structure of the subsidiary undertaking prejudices the prompt transfer of funds or repayment of liabilities;

(i) whether the contractual relationships of the subsidiary undertaking with the firm and other third parties prejudices the prompt transfer of funds or repayment of liabilities;

(j) whether past and proposed flows of funds between the subsidiary undertaking and the firm demonstrate the ability to make prompt transfer of funds or repayment of liabilities; and

(k) whether past and proposed flows of funds between the subsidiary undertaking and the firm demonstrate the ability to make prompt transfer of funds or repayment of liabilities; and

(l) whether the degree of individual consolidation by the firm undermines the PRA's ability to assess the soundness of the firm as a legal entity.

3 CRR Article 19(2) — entities excluded from the scope of prudential consolidation

Application process

3.1 Where a firm wishes to exclude entities from the scope of prudential consolidation, it will be expected to make a formal application to the PRA. This application should seek to articulate how one of the conditions set out in CRR Article 19(2) (a), (b) or (c) is met.

3.2 The PRA will assess applications to exclude entities from the scope of prudential consolidation under CRR Article 19(2) on a case by case basis. The PRA will only grant this treatment with respect to undertakings where one of the conditions in CRR Article 19(2) is met. Even where a CRR Article 19(2) condition is met, the PRA will make its own judgment whether to permit this treatment.

Application of criteria

3.3 CRR Article 19(2) allows the consolidating supervisor to decide that an institution, financial institution or ancillary services undertaking, which is a subsidiary or in which a participation is held, need not be included in the consolidation in the following cases:

(a) where the undertaking concerned is situated in a third country where there are legal impediments to the transfer of necessary information; or

(b) where the undertaking concerned is of negligible interest only with respect to the objectives of monitoring credit institutions.

3.4 If several undertakings meet the criterion in (b) above, and are collectively of non-negligible interest with respect of the specified objectives, the PRA may not agree to exclude them all from the consolidation.

3.5 The PRA may ask a firm to provide information about the undertakings excluded from consolidation

4 Intermediate parent undertakings

4.1 Chapter 4 of the Groups Part of the PRA Rulebook, reflecting Article 21 (b) CRD, requires a significant third country group that has two or more bank or investment firm subsidiaries and EU assets of €40 billion or more, but which had EU assets of less than €40 billion on 27 June 2019 to structure itself under a single EU intermediate parent undertaking (IPU).

Use of two IPUs

4.2 Article 21(b) CRD permits groups to restructure under two IPUs in certain circumstances rather than only one. The PRA has given effect to this provision using its existing powers under Section 138A FSMA to waive or modify rules provided statutory tests are met.

Application process

4.3 A firm or parent institution wishing to restructure under two IPUs should make a formal application to the PRA demonstrating, as envisaged by Article 21(b)(2) CRD, that the establishment of a single IPU would either:

(i) be incompatible with a mandatory requirement for the separation of activities imposed by the rules or supervisory authorities of the third country where the ultimate parent undertaking of the third country group has its head office; or

(ii) render resolvability less efficient than would be the case with two IPUs according to an assessment carried out by the competent resolution authority of the proposed IPU.

4.4 The PRA will assess applications on a case by case basis and will permit two IPUs where it is satisfied that one of the above conditions is met. Even where it is so satisfied, the PRA will make its own judgment as to whether to grant the waiver or modification

Annex: Changes to SS15/13

This annex details changes made to SS15/13 following its initial publication in December 2013.

December 2020

This SS was updated following publication of Policy Statement (PS) 26/20 'Capital Requirements Directive V'.[7] The changes set out the application process for firms to apply to use two IPUs. The statement has also been updated to reflect:

- the change in the PRA's rules to require proportional consolidation where a firm has a relationship with an undertaking as set out in CRR Article 18(5);
- the PRA's approach to the discretion to require a valuation method other than the equity method for certain subsidiaries (CRR Article 18(7)): and
- the PRA's approach to the discretion to require full or proportional consolidation of certain undertakings where there is substantial step-in risk (CRR Article 18(8)).

These revisions are found in Chapter 2 and Chapter 4.

The PRA also made minor formatting changes throughout this SS to improve readability.

July 2016

On 7 July 2016, this supervisory statement (SS) was updated following publication of Policy Statement (PS) 20/16 'The implementation of ring-fencing: prudential requirements, intragroup arrangements and use of financial market infrastructures' which included final ring-fencing rules and Supervisory Statement 8/16 'Ring-fenced bodies (RFBs)'. Specifically, paragraph 1.3 has been updated to take into account SS8/16 and paragraph 2.2A has been added to set out expectations of the PRA's approach to applications by an RFB, or any other person that is a member of a group containing an RFB, for permission to use individual consolidation.

7 December 2020: https://www.bankofengland.co.uk/prudential-regulation/publication/2020/capital-requirements-directive-v.