FINANCIAL CONDUCT AUTHORITY

Consultation Paper

CP25/15***

A prudential regime for cryptoasset firms

May 2025

How to respond

We are asking for comments on this Consultation Paper (CP) by **31 July 2025**.

You can send them to us using the form on our website.

Or in writing to:

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Contents

Chapter 1

Summary

Why we are consulting

1.1 In 2023, HM Treasury (the Treasury) announced plans to legislate for a financial regulatory regime for cryptoassets. Currently our regulatory remit for cryptoassets is limited to the Money Laundering, Terrorist Financing, and Transfer of Funds (Information on the Payer) Regulations 2017 (MLRs), the financial promotions regime, and consumer protection legislation (including, the Consumer Rights Act 2015 and Consumer Protection from Unfair Trading Regulations 2008).

1.2 This Consultation Paper (CP) follows Discussion Paper (DP23/4) on our proposed approach to regulating stablecoins. We are consulting on proposed prudential rules and guidance for the activities of issuing a qualifying stablecoin and safeguarding qualifying cryptoassets, including qualifying stablecoins. Following this CP, we will also consult on applying prudential rules to firms safeguarding qualifying cryptoassets while also offering additional services, such as operating a trading venue or staking, as well as prudential rules for other cryptoasset activities. See Table 2 in Chapter 2 for timings.

1.3 Clear prudential rules and expectations will reduce regulatory uncertainty, encouraging firms to set up in the UK to offer cryptoasset services. And prudential stability will give both firms and consumers greater confidence to do business.

1.4 Qualifying stablecoins are defined in the Treasury's draft legislation. They are cryptoassets which seek to maintain their value against a fiat currency (a government-issued currency, such as pound sterling or US dollar) by the issuer holding, or arranging for the holding, of fiat currency or fiat currency and other assets. Stablecoins are designed to be stable, money-like instruments and qualifying stablecoins have certain features and use cases that require protections for stability.

1.5 This CP sets out the risks we want to prevent, the outcomes we want for consumers and markets and the proposals we seek to implement. Our proposals set appropriate standards that are proportionate, and which we will expect firms to meet. Our regime will bring certainty, and firms and consumers will be able to place trust in qualifying stablecoins. However, most cryptoassets remain high risk, speculative investments and consumers should be prepared to lose all their money if they buy them.

1.6 This CP does not include proposed requirements for firms carrying out payments using qualifying stablecoins. As use cases are developed, we anticipate the Treasury will bring retail payments made with qualifying stablecoins within our perimeter.

1.7 We are publishing this CP alongside our Stablecoins and Custody CP (CP25/14). These CPs should be read together, and will be followed by further consultation papers as part of our cryptoasset roadmap. We will consider responses to these consultations and set out our final rules and guidance in Policy Statement(s) ahead of implementation.

FCA Crypto Roadmap

This outlines planned FCA policy publications for cryptoassets where we are seeking feedback and the content they are expected to cover.

Not exhaustive; all timelines are subject to change according to parliamentary time and/or further steers from government

Financial Promotions rules go live

Stablecoins issuance and custody

DP

Trading platform rules including location, access, matching and transparency requirements

Intermediation rules including order handling and execution requirements

Lending rules including ownership, access and disclosures

Staking rules including ownership and disclosures

Prudential considerations for cryptoasset exposures

DP

Conduct and firm standards for all Regulated Activities Order (RAO) activities
Systems and controls including Operational Resilience and Financial Crime

Consumer Duty

Complaints

Conduct (COBS)

Governance including Senior Managers and Certification Regime (SMCR)

CP

Final rules
All Policy Statements published

PS

Regime go-live

Gateway opens

Q1 2020 | Q4 2023 | Q4 2024 | Q1/Q2 2025 | Q3 2025 | Q4 2025/ Q1 2026 | 2026

Gateway readiness

Money Laundering Regulations
legislation applies

DP

Admission and disclosures
Admission/rejection processes

Disclosures

Liability

Due diligence

National Storage Mechanism (NSM)

Market abuse
Systems and controls

Information sharing

Inside information disclosure

CP

Stablecoins
Backing assets

Redemption

Custody
Recordkeeping

Reconciliations

Segregation of assets

Use of 3rd parties

Prudential
Introduction of a new prudential sourcebook, including capital, liquidity and risk management

CP

Admissions and Disclosures
As per DP

Market Abuse
As per DP

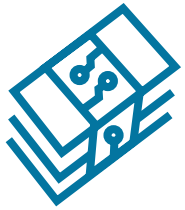
CP

Trading platforms, intermediation, lending and staking
As per DP +

Resolution

Remaining material for prudential sourcebook
Groups

Reporting



Key

DP Discussion Paper/s

CP Consultation Paper/s

PS Policy statement

1.8 We want detailed feedback on this CP's proposals. These proposals include draft rules and Handbook guidance, as well as an assessment of the potential costs and benefits for firms, consumers wider industry, markets and the FCA.

FCA strategy and objectives for cryptoasset regulation

1.9 Our proposals have been guided by our statutory objectives and 2025-30 Strategy. In particular we aim to:

- **Support growth:** Aligning with relevant international standards, and building predictable, proportionate regulation for cryptoassets, we are designing a regime which supports innovation and investment in the UK. This regime will allow firms that set up in the UK to compete internationally and supports UK growth in the medium to long term.
- **Help consumers:** We want consumers to be informed, have appropriate levels of protection, and access to products that meet their needs and offer fair value.

1.10 We have also considered our secondary international competitiveness and growth objective. We have considered a sample of international regimes' requirements (the EU's MiCA, the Monetary Authority of Singapore's and Hong Kong Monetary Authority's stablecoin issuance regimes) alongside existing FCA regulatory regimes (such as electronic money issuers, and for investment firms which safeguard and administer assets). Our proposed regime cannot be compared like for like to the standards devised by other jurisdictions. However, when considering the practical impact of the levels of capital and liquidity required for firms, we believe we are either broadly aligned or more competitive than international counterparts.

Consultation with the CBA Panel and other statutory panels

1.11 We have consulted the Cost Benefit Analysis (CBA) Panel in preparing the CBA (see link in Annex 2), in line with the requirements of s138IA(2)(a) of the Financial Services and Market Act (FSMA). The CBA is the same as that for CP25/14. A summary of their main recommendations and our subsequent changes are in the 'Consultation with the FCA Cost Benefit Analysis Panel' section of the CBA, which is published alongside CP25/14.

1.12 We have also engaged with the Financial Services Consumer Panel, Practitioner Panel, and Smaller Business Practitioner Panel, and considered their input and views.

Who this applies to

1.13 The draft rules in this CP cover firms seeking authorisation and regulation for the Regulated Activities of issuing qualifying stablecoins and safeguarding qualifying cryptoassets. However, some of the topics may also be relevant to firms seeking authorisation and regulation for other regulated cryptoasset activities. This is because

these topics apply common standards across firms and sectors. We explain this in Chapter 2 under the new, integrated prudential approach heading and in Table 1.

1.14 Who else needs to read this document:

- firms that wish to use qualifying stablecoins within wider activities (eg on-and off-ramping)
- industry groups, law firms and trade bodies representing firms in the cryptoasset sector
- auditors providing services to cryptoasset firms
- professional advisors in the cryptoasset sector
- groups representing consumer interest

1.15 Who may be affected by the proposed rules and guidance:

- consumers and firms who do or propose to use, or interact with, qualifying stablecoins, qualifying cryptoassets or other cryptoassets

1.16 It may also interest:

- policymakers and other regulatory bodies
- academics and think tanks
- industry experts and commentators
- issuers of electronic money and payment service providers

Measuring success

1.17 We will apply proportionate prudential standards that support the development of cryptoasset markets in the UK while maintaining their integrity and reducing the potential harms that firms in these markets can cause. We would expect to see benefits such as:

- Reduced firm failure, measured by comparing rates of firm failure before and after regulation.
- Reduced harm from disorderly firm failure (reduced market disruption and impact on consumers), measured by comparing rates of disorderly firm failure before and after regulation.
- Improved market confidence and resilience, measured by market research.
- Effective and proportionate prudential risk management, measured through firm assessment.
- Effective competition, measured by firm participation in the UK market.
- Increased likelihood that firms can use own funds to restore consumer positions where it is liable for consumer harm
- Prudently managed firms with adequate financial resources are more likely to deliver better conduct outcomes for consumers

1.18 We will use data from issuers of qualifying stablecoins and firms safeguarding qualifying cryptoassets, to assess changes in firms and the market over time, identify firms that fail to meet our prudential standards and take action as appropriate.

1.19 We will evaluate the wider prudential regime for cryptoassets when the industry has had time to adapt to the new requirements. We will examine evidence on firms' adaptation to the new regime, their adherence to our rules and other relevant factors to determine whether the regime is delivering good outcomes.

1.20 These success measures should be considered alongside those in CP25/14. We discuss our intended improvements to consumer and market outcomes in more detail in the Cost Benefit Analysis (CBA) (see link in Annex 2).

Summary of feedback to DP23/4 and our response

1.21 We received 28 responses on prudential questions in DP23/4, with responses from industry, trade bodies, individuals, and civil society stakeholders. Throughout this CP, we address prevalent themes in the responses to DP23/4. This includes how we have considered them in our proposed rules and made refinements based on feedback. We also set out where we have considered feedback but have not made changes to our approach and provided our rationale. Where we asked questions in DP23/4 that are beyond the scope of this CP, we have signposted where these responses will be considered as part of the wider roadmap.

Chapter 2

Scope of this consultation

A new, integrated prudential approach

2.1 We are the largest prudential regulator by number of firms in Europe. We prudentially supervise around 40,000 firms across various sectors. Our rules for these firms span across multiple sourcebooks that cover similar objectives.

2.2 While developing new prudential rules for regulated cryptoasset activities we have also been working on our broader strategy to be a smarter regulator and make the FCA prudential framework more accessible and consistent for solo regulated FCA firms. As part of this, our long-term vision is to establish an integrated prudential sourcebook that brings together core prudential requirements common across the different types of firms we prudentially regulate. This will then be supplemented by sector specific sourcebooks that will build on the common requirements. This approach offers several benefits:

1. A shorter Handbook with reduced duplication.
2. Clear structure – requirements organised logically by theme.
3. Consistent approach – common definitions, principles and reporting where appropriate, including where a single firm is authorised to conduct multiple regulated activities across different sectors.
4. Easy navigation – firms can quickly find relevant requirements.
5. Flexibility – modular design allows for sector-specific needs.

2.3 We intend to develop and apply this new sourcebook only to firms carrying on regulated cryptoasset activities initially. So, elements of the proposed prudential regime we are consulting on in this CP will be placed in the integrated prudential sourcebook, known as COREPRU. We intend, in the future, to consult on moving other types of regulated firms into COREPRU.

Sectoral specific requirements

2.4 The sector specific requirements will build on the core requirements, calibrating them to the specific activity in question. In this CP, we propose that the sector specific requirements for firms doing regulated cryptoasset activities will be in a sourcebook known as CRYPTOPRU. We refer to firms that will be subject to our proposed prudential rules as CRYPTOPRU firms. COREPRU and CRYPTOPRU will apply to CRYPTOPRU firms.

2.5 In the subsequent chapters of this CP we will indicate where a requirement will be placed in COREPRU and where a requirement will be placed in CRYPTOPRU. Table 1 gives a summary of where requirements in this CP will be placed. We will include an updated version of this table when we consult on the remaining requirements for the prudential sourcebooks (CP2) in accordance with the FCA Crypto Roadmap.

Table 1

COREPRU	CRYPTOPRU
Overall Financial Adequacy	Permanent minimum requirement
Definition of own funds	K-factor requirement
Own funds requirement (overall calculation)	Issuer liquid asset requirement
Fixed overhead requirement	
Concentration risk monitoring	
Basic liquid asset requirement	

2.6 This CP is focused only on some aspects of the prudential regime for CRYPTOPRU firms. For firms to understand how we plan to consult on the additional aspects of the regime not covered in this CP, we have set out in Table 2 below the planned consultations and what they cover.

Table 2

Area	CP25/15	CP 2
Overall Financial Adequacy	X	
Requirements for cryptoasset firm groups		X
Definition of Own Funds	X	
Own funds requirement (overall calculation)	X	
Permanent minimum requirement – Stablecoin and Custody	X	
Permanent minimum requirement – other activities not covered in this CP		X
Fixed overhead requirement	X	
K-factor requirements – Stablecoin and Custody	X	
K-factor requirements – other activities not covered in this CP		X
Concentration risk requirements	X	X
Basic liquid asset requirement	X	
Issuer liquid asset requirement	X	
Internal Capital Adequacy and Risk Assessment		X
Public disclosure of prudential information		X

Interaction with existing sourcebooks

2.7 There may be instances where a CRYPTOPRU firm is subject to other prudential requirements in our handbook, when they are conducting other relevant activities that bring them into scope of those rules. For example, a qualifying cryptoasset custodian

may also be conducting investment business in the traditional finance space as a MIFIDPRU investment firm. This would bring them into scope of both MIFIDPRU and CRYPTOPRU/COREPRU.

2.8 The impact of each interaction will vary depending on which sourcebooks and/or requirements apply. In Chapter 4 (paragraph 4.53) of this CP we set out our proposals for how the relevant own funds requirements for a CRYPTOPRU firm interact with the own funds requirements where it is also a MIFIDPRU investment firm. This reflects the similar design principles for CRYPTOPRU/COREPRU and MIFIDPRU.

2.9 We intend to consult on how our different prudential sourcebooks (as well as other aspects of MIFIDPRU beyond own funds requirements) will interact with requirements for cryptoasset firms in CP2.

Overall Financial Adequacy

2.10 The overall financial adequacy rule (OFAR) requires that a firm, at all times, maintains financial resources that are adequate in both amount and quality for the business it undertakes. The OFAR supplements our overarching requirements on threshold conditions and principles of business, under which firms must have appropriate resources in relation to the regulated activities carried out. The OFAR covers all activity undertaken by a firm and forms the basis for which a firm conducts its internal capital adequacy and risk assessment process (ICARA), which we intend to consult on in CP2.

Chapter 3

Own funds – definition and composition of capital

3.1 This chapter, for CRYPTOPRU firms, outlines our proposals on:

- The definition and types or 'tiers' of capital that are eligible as regulatory capital, known as 'own funds', including specific deductions that need to be made from own funds.
- Prior permissions that are required from the FCA to count certain items as regulatory capital.
- Prior permissions that are required from the FCA to reduce regulatory capital.
- The minimum proportions in which own funds must be held to meet the own funds requirements at individual firm level.

For firms that are part of a group, we expect to make further proposals applicable at group level in CP2.

3.2 Our proposed rules for own funds are in COREPRU 3. We intend our approach to the calculation of own funds to be consistent across sectors in the future. So we consider COREPRU to be the appropriate sourcebook.

Definition of own funds

3.3 As explained in DP23/4, the quality of what is allowed to count as capital to meet any regulatory capital requirements will help to determine firms' financial resilience in the event of unexpected losses. We propose that the types and treatment of own funds will be the same as those for MIFIDPRU firms. We recently consulted on steps to simplify and clarify rules on own funds for MIFIDPRU firms in CP25/10. We recommend anyone interested in this section to also read CP25/10. Own funds will comprise the following 3 classes of capital:

- Common Equity Tier 1 (or CET1) capital
- Additional Tier 1 (or AT1) capital
- Tier 2 (or T2) capital

3.4 The definition of own funds we propose to apply prescribes certain deductions and filters for the different tiers of capital (see 3.9 below). These help to make sure that a firm measures its own funds in a way that reflects its ability to absorb losses in a variety of stress events, by adjusting accounting values that:

- are subject to significant valuation uncertainty
- may not reflect realisable values in stress
- include gains or losses that may be temporary or reversible
- or are only realisable if the firm continues to operate as a going concern

3.5 The items that need to be deducted from the different tiers of own funds are set out in COREPRU 3. These are also based on the deductions for MIFIDPRU firms, and include:

- intangible assets
- deferred tax assets that rely on future profitability
- investments in the capital instruments of financial sector entities
- direct holdings of a firm's own capital instruments
- cryptoassets held by the firm that it has issued itself or are issued by a connected party, or where they are in control of the supply

3.6 We propose requiring a CRYPTOPRU firm to deduct cryptoassets it holds that it has issued itself, or cryptoassets issued by a connected party (for example, a group entity or an employee). We also propose to apply the deduction to any holding of a cryptoasset if the firm or a connected party controls the supply of the cryptoasset. For example, this might be because the firm holds a position in the market that allows it to behave independently of other market participants to control supply. This deduction is to prevent the artificial inflation of a firm's balance sheet (and therefore its capital position).

3.7 However, regulated stablecoin which are backed in line with our regulatory requirements would not be required to be deducted, as we would expect the value of such assets to be stable.

3.8 We believe these proposals ensure a quality of regulatory capital that will result in resilient CRYPTOPRU firms, with increased capacity to absorb losses.

Requirements for the different tiers of capital

3.9 The tables below summarises the essential requirements applying to different components of CET1, AT1 and T2 capital. They follow the tables in CP25/10.

CET1 requirements:

Component	Essential requirements	How presented in COREPRU 3
Eligible items	• Fully paid-up capital instruments • Share premium accounts • Retained earnings • Other reserves	Clear criteria for each item type, with emphasis on immediate availability for loss absorption
Required deductions	• Intangible assets • Certain holdings • Items not providing genuine loss absorption	Simple calculation approach with clear rationale for each deduction
Prudential filters	• Valuation adjustments for the trading book • Hedging effects • Changes in own credit standing	Focused upon achieving prudent valuations without unnecessary complexity

AT1 requirements:

Component	Essential requirements	How presented in COREPRU 3
Eligible items	• Additional tier 1 instruments • Share premium accounts related to AT1 instruments	Clear eligibility criteria organised by core characteristics (perpetuity, loss absorption, distribution flexibility)
Required deductions	• Holdings of own AT1 instruments • Reciprocal cross holdings with financial sector entities • Holdings of AT1 instruments of financial sector entities • Excess of tier 2 deductions • Foreseeable tax charges	Clear deduction framework with consistent approach across all tiers of capital
Loss absorption mechanism	• Conversion to CET1 or write-down when triggered • Trigger when CET1 falls below 64% of the firm's own funds requirement • Full conversion/write-down upon trigger	Requirements focusing upon key outcomes rather than prescriptive procedures

T2 requirements:

Component	Essential requirements	How presented in COREPRU 3
Eligible items	• Tier 2 instruments • Share premium accounts related to T2 instruments	Clear eligibility criteria focusing on subordination, minimum maturity, and loss absorption in liquidation
Required deductions	• Holdings of own T2 instruments • Reciprocal cross holdings with financial sector entities • Holdings of T2 instruments of financial sector entities not held in the trading book	Consistent approach to deductions aligned with CET1 and AT1 frameworks
Maturity and amortisation	• Minimum 5-year original maturity • Progressive amortisation over final 5 years • No incentives for early redemption	Straightforward rules for amortisation that reflect diminishing loss absorption capacity as instruments approach maturity

3.10 In each case, the table is an overview of the most relevant proposals that may apply, rather than an exhaustive statement of all potentially applicable requirements and conditions. The tables are not a substitute for detailed reading of the proposed rules.

Prior permissions required from the FCA for CET1 capital

3.11 Under our proposed rules, CRYPTOPRU firms will need prior permission from us to issue capital instruments as CET1 capital. This is to make sure that if a firm is relying on a capital instrument to count as CET1 for regulatory purposes, it meets the conditions outlined in our rules.

3.12 If a CRYPTOPRU firm already has permission to issue instruments as CET1 capital, we do not propose requiring it to get permission to subsequently issue the same form of instruments. This is provided that the provisions of the new instruments are substantially the same. But we must be given sufficient notice of the subsequent issuance.

3.13 Firms may include interim profits in CET1 capital before formal year-end decisions by notification to the FCA provided they meet the applicable requirements, such as verification by persons independent of the firm who are responsible for auditing the accounts. The verification must confirm that profits have been evaluated in line with applicable accounting standards.

Calculating the type of own funds held to meet own funds requirements

3.14 Under our proposals, a CRYPTOPRU firm must hold own funds to meet its own funds requirement (see Chapter 3) in the following proportions:

- CET1 ≥ 56% of total own funds requirement.
- CET1 + AT1 ≥ 75% of total own funds requirement.
- CET1 + AT1 + T2 ≥ 100% of total own funds requirement.

3.15 These are minimum levels and it is entirely possible and normal that a firm may choose to rely entirely on ordinary shares and retained earnings (which is CET1 capital) to meet their own funds requirement.

Question 1: **Do you have any comments on our proposals for the definitions and types of, and deductions from, regulatory capital that CRYPTOPRU firms should use to calculate their own funds?**

Question 2: **Do you have any views on our proposed requirements for deductions from CET1 capital, in particular cryptoassets held by firms which they have issued or are in control of the supply of?**

Chapter 4

Own funds requirements:

4.1 This chapter explains that:

- We propose to add to COREPRU the calculation of a fixed overheads requirement (FOR) that will apply cross-sector.
- We propose to add to CRYPTOPRU
  - A permanent minimum capital requirement (PMR) for issuers of qualifying stablecoin and for qualifying cryptoasset custodians.
  - How to calculate each of the specific K-Factors that will apply to issuers of qualifying stablecoin and qualifying cryptoasset custodians.

Response to DP23/4

4.2 In DP23/4, we discussed the suitability of an approach to own funds requirements that uses 3 components: a permanent minimum requirement (PMR); a fixed overhead requirement (FOR); and an activity-based 'K-factor' requirement (KFR), with the highest to apply. Some respondents argued that the business model for issuing qualifying stablecoin was comparable to that for issuing e-money and questioned the use of an approach more akin to that for FCA investment firms. Our proposed framework is structured in a similar way to the requirements for FCA investment firms, and will be prescribed in FCA rules, whereas requirements for e-money issuers are prescribed in a Regulation. However, an element of this (the KFR for stablecoin issuers) is comparable to capital requirements for e-money issuers. We further address this feedback through the detailed explanation of own funds requirements in this chapter.

Own funds requirement (OFR)

4.3 We propose a minimum own funds requirement (OFR) that will be the higher of the following components:

- permanent minimum requirement
- fixed overhead requirement
- K-factor requirement

4.4 Each of the above components aim to address a specific purpose, which we describe below.

4.5 In DP23/4 para 4.2, we discussed introducing an internal capital adequacy and risk assessment process (ICARA) for CRYPTOPRU firms, similar to what currently applies to MIFIDPRU firms. This would require firms to consider the potential for harm from both ongoing activities and in a wind-down scenario. Based on this, a firm may find the

amount of own funds it requires to be greater than the OFR. While we will consult on this process in CP 2, we refer to an ICARA process in this CP to show how it may interact with the requirements in this consultation.

Ongoing permanent minimum requirement (PMR)

4.6 In DP23/4, we proposed that cryptoasset firms should be required to meet a permanent minimum requirement (PMR) on an ongoing basis. There were no specific concerns raised with the concept of a PMR and we still consider it a suitable approach. A CRYPTOPRU firm should, at all times, operate with a minimum level of own funds based on the cryptoasset services and activities it has permission to undertake. This is its PMR. Table 3 sets out the PMR that we propose will apply to a CRYPTOPRU firm for the activities of issuing a qualifying stablecoin and custody of qualifying crypto assets. In setting these figures, we have considered the need for confidence in market integrity and resilience with the importance of UK market development. And had regard to other prudential regimes for similar activities in both the UK and internationally. We have avoided creating an uneven playing field between traditional finance and crypto where the risk of harm from activities is similar. For example, we view the activity of a stablecoin issuer to be similar to an e-money issuer and their equivalent capital requirement broadly aligns with our proposed PMR.

Table 3

PMR (£)	Regulated Crypto Activity
350,000	Issuing qualifying stablecoin
150,000	Safeguarding of qualifying cryptoassets

4.7 Where a firm undertakes a combination of regulated crypto activities the higher PMR would apply. So, if an authorised firm added a new activity with a higher PMR its PMR would increase.

4.8 We plan to consult on the PMR for other regulated cryptoasset activities in CP 2 along with the remaining prudential framework (see Table 2 in Chapter 2).

Fixed overheads requirement (FOR)

4.9 In DP23/4, we proposed that cryptoasset firms should be required to meet a fixed overheads requirement (FOR) on an ongoing basis. There were no specific concerns raised with the concept of a FOR and we still consider it a suitable approach. We propose that the fixed overheads requirement (FOR) will apply to all CRYPTOPRU firms. The proposed rules for the FOR are in COREPRU 4.3.

4.10 The FOR calculation represents a minimum amount of capital that a CRYPTOPRU firm would need to absorb losses if it winds-down or exits the market. It is used in other prudential regimes.

4.11 We propose that a CRYPTOPRU firm's FOR will be equal to one quarter of its relevant expenditure in the previous year, calculated from figures in its most recent audited annual financial statements. Where these are not available, a CRYPTOPRU firm may use unaudited financial statements until audited annual financial statements are available.

Calculating the FOR

4.12 To calculate relevant expenditure for the FOR, we propose that a CRYPTOPRU firm will first determine its total expenditure before it has distributed any profits. It may then deduct certain other expenses (to the extent that those items have been included in expenditure) if they are fully discretionary and have not already been treated as a distribution of profits. Examples include staff bonuses and other variable remuneration; employees', directors', and partners' shares in profits; other appropriations of profits. Additional examples of expenses that can be deducted are in the draft Handbook text in Appendix 1.

- A respondent to DP23/4 noted the need to consider a suitable definition for variable costs in the context of the FOR. They gave an example considering rent and salaries. On balance we have concluded that there is considerable benefit in keeping definitions straightforward and note that the FOR is designed to only approximate wind-down costs.

4.13 A simple example of the FOR is:

1. A firm determines that its total expenditure in the preceding financial year is £2m.
2. Of this total expenditure, £400k was fully discretionary staff bonuses and £100k was attributed to expenditure that is non-reoccurring from non-ordinary activities.
3. This gives a total relevant expenditure of £1.5m.
4. The total relevant expenditure is divided by 4 to give the FOR of £375k.

Expenses incurred on behalf of the firm by third parties

4.14 An arrangement may exist between a firm and a third party that causes the third party to incur expenses on behalf of the firm. Such arrangements will have an impact on costs expected by the firm if it has to wind-down. A CRYPTOPRU firm must add to its total expenses any relevant expenditure (as defined in paragraph 4.12 above) incurred on its behalf by third parties.

Material change in relevant expenditure during the year

4.15 A significant event, such as changes to business lines, buying or selling a business or investing in a major upgrade or restructuring programme, may cause material change to a CRYPTOPRU firm's relevant expenditure. Where these events are planned, we propose to expect the CRYPTOPRU firm to calculate the expected impact on both its FOR and basic

liquid assets requirement before making the relevant change. We describe the basic liquid asset requirement in Chapter 5. Where the change leads to an increase in its FOR, the CRYPTOPRU firm must make sure that it has sufficient own funds to cover this increase.

4.16 We propose that where a material increase in relevant expenditure has occurred during a financial year, the CRYPTOPRU firm must immediately recalculate its FOR based on the revised relevant expenditure. We also propose that the CRYPTOPRU firm immediately recalculates its basic liquid assets requirement, which is calculated by reference to the FOR.

4.17 In defining a material increase we do not see any reason for a CRYPTOPRU firm's requirements to differ from an FCA investment firm (and where in practice we have not seen any difficulties). So it is defined in our proposals as either:

- A projected increase in relevant expenditure for the current year of 30% or more, or
- An increase in the FOR of £2m or more based on projected relevant expenditure for the current year.

4.18 Where there is a material decrease in a CRYPTOPRU firm's relevant expenditure during a financial year, we propose that the firm can recalculate its FOR based on the revised relevant expenditure. It may then substitute the revised FOR in place of its existing FOR as long as it gets our prior permission.

4.19 Using the same rationale applied to a material increase above, a material decrease is defined in our proposals as either:

- A projected decrease in relevant expenditure for the current year of 30% or more, or
- A decrease in the FOR of £2m or more based on projected relevant expenditure for the current year.

CRYPTOPRU firms that have been operating for less than a year

4.20 If a CRYPTOPRU firm has been in business for less than a year, it should use the relevant expenditure in its projections. These will have been included in its application for authorisation.

K-factor requirement (KFR)

4.21 In DP23/4, we proposed that the third component of a cryptoasset firm's own funds requirements would be a variable activity based requirement. This 'K-factor' requirement (KFR) helps address the potential for harm arising from a firm's ongoing operations. This approach was broadly accepted.

4.22 The K-factor capital requirements are either activity or exposure based. Which K-factors will apply to an individual CRYPTOPRU firm will depend on the activities it undertakes, with the amount of each requirement growing with the scale of business undertaken. Where a firm conducts multiple regulated cryptoasset activities, the overall K-factor would be the sum total of the K-factors for each relevant cryptoasset activity

undertaken by the firm. Some feedback to DP23/4 asserted that there should not be capital charges for custodians where a capital charge had already been applied to a qualifying stablecoin issuer. However, the purpose of each K-Factor is to reflect the risk of a particular activity and that the risks from issuing a qualifying stablecoin differ from those for custody of qualifying cryptoassets.

4.23 In this section, we only cover the K-factors for issuers of qualifying stablecoins and qualifying cryptoasset custodians. The K-factors for the remaining cryptoasset activities will be covered in CP 2 as in Table 2.

4.24 Even if an activity does not contribute towards the K-factor requirement, we are likely to propose in CP2 that a CRYPTOPRU firm should still consider the potential for harm arising from that activity under the ICARA process. This is because an ICARA process should reflect all the material risks a firm faces, including from its unregulated business.

The K-Factor for qualifying stablecoin in issuance (K-SII)

4.25 K-SII is the K-factor requirement for the amount of capital qualifying stablecoin issuers must hold against the risks from issuing a qualifying stablecoin. As discussed in DP23/4, there are several operational risks when issuing qualifying stablecoin that may lead to losses.

4.26 As a qualifying stablecoin issuer scales its business operations, the increased volume of qualifying stablecoins in issuance inherently increases the amount of potential harm to markets and consumers if a risk materialises.

4.27 K-SII would be measured and calculated as follows:

- 2% of the average qualifying stablecoin in issuance (SII)

4.28 To calculate the average SII a firm must:

- Take the total amount of SII at the end of each business day for the previous 9 months.
- Exclude the values for the most recent 3 months, and
- Calculate the arithmetic mean of daily values for the remaining 6 months.
- K-SII is then calculated on the first business day of each calendar month

4.29 Qualifying stablecoin in issuance (SII) equals the qualifying stablecoins that the qualifying stablecoin issuer is liable to redeem. The attached draft instrument provides guidance on what should be included as SII in CRYPTOPRU 4.5.6G. This definition ensures that the capital requirement covers the operational risk of holding the qualifying stablecoin.

4.30 We believe this averaging approach is appropriate as it captures the frequent variation of SII and reduces volatility when calculating K-SII. The data used will also be readily available to a qualifying stablecoin issuer. By excluding the values for the most recent 3 months there is a lagging effect on K-SII. This will allow firms to plan for changes in their capital requirement and manage capital more effectively. One respondent to DP23/4 said this approach may delay necessary capital changes. However, we believe that for the minimum rules the lagging effect is appropriate as, without it, capital may also decrease suddenly.

4.31 Responses to DP23/4 included a proposal that a lower percentage would be sufficient for a qualifying stablecoin issuer. On balance, our view is that K-SII should provide a reasonable buffer against losses and 2% was appropriate for the operational risks from issuance. There would be an anomaly if issuers of qualifying stablecoins were subject to lower requirements than those applied to business models with similar risks, such as e-money.

Issuers that have been operating for less than 9 months

4.32 We propose using a modified calculation for determining average SII where a CRYPTOPRU firm has been acting as an issuer for less than 9 months. We set this out in CRYPTOPRU 4.5.7R in Appendix 1. The aim of this modification is to ensure firms can still calculate a k-factor requirement for activities where they have not built up sufficient data to run the base calculation.

The K-Factor for qualifying cryptoassets safeguarded - K-QCS

Measuring QCS

4.33 The definition of qualifying cryptoassets safeguarded (QCS) includes all qualifying cryptoassets a firm is safeguarding. (DP23/4 suggested that initially QCS would capture only qualifying stablecoins and security tokens). The definition QCS does not include qualifying cryptoassets held by firms for reasons other than safeguarding.

4.34 Where a qualifying cryptoasset custodian is unsure if relevant cryptoassets are held for safeguarding purposes, it should include them as QCS until satisfied otherwise.

4.35 A CRYPTOPRU firm should use the market value of assets when measuring QCS or an alternative measure of fair value, including an estimated value calculated on a best-efforts basis, if a market value is not available.

K-QCS

4.36 K-QCS is the proposed K-factor requirement to capture the risks from safeguarding qualifying cryptoassets for clients (ie when acting as custodians). A respondent to DP23/4 made a comparison with MICA which has the equivalent of a PMR and FOR for custodians but no K-Factor. However, our proposed K-factor provides equivalence to the similar traditional finance activity of administering and safeguarding assets. The K-QCS only applies when it exceeds the PMR and FOR and has been set at a level where we expect it would only be binding for the largest firms. We therefore consider it a proportionate requirement.

4.37 Undertaking custodian activity has operational risks that can potentially cause harm. Failing to properly safeguard qualifying cryptoassets may delay their return, increase costs for both custodians and clients or cause loss of qualifying cryptoassets entirely. Qualifying cryptoassets may also be stolen if a custodian's client accounts are hacked. As a firm grows and takes on the responsibility of safeguarding larger amounts of qualifying cryptoasset, the impact of potential harm increases.

4.38 We are proposing that K-QCS be calculated as follows:

- 0.04% of a cryptoasset custodian's average QCS (0.04% aligns with equivalent traditional finance activity)

4.39 To arrive at average QCS, a firm would:

- Take the total amount of QCS, measured at the end of each calendar day, for the previous 9 months.
- Exclude the values for the most recent 3 months, and
- Calculate the arithmetic mean of daily values for the remaining 6 months.

4.40 K-QCS is then calculated on the first calendar day of each calendar month.

4.41 As with K-SII, we believe that this averaging approach is appropriate, as it captures frequent variations of QCS and should reduce volatility when calculating K-QCS. It also uses data that should be readily available to firms. See also 4.30 above on the lagging effect of this calculation method.

4.42 As with K-SII, we propose using a modified calculation for determining average QCS where a CRYPTOPRU firm has been acting as an issuer for less than 9 months.

Using third parties for safeguarding

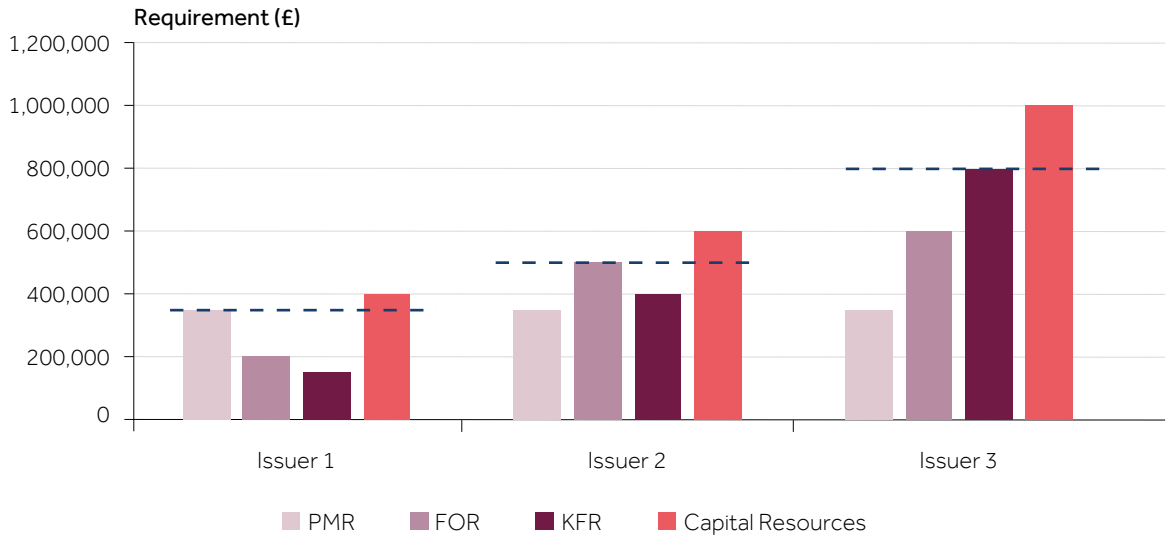
4.43 Where a firm has appointed a third party to safeguard qualifying cryptoassets, or has itself been appointed by a third party to safeguard qualifying cryptoassets, the firm must include the value of those qualifying cryptoassets in the measurement of its QCS. We do not consider this to be a 'double counting' of the assets. There is a potential risk of harm from a qualifying cryptoasset custodian's direct safeguarding responsibilities. This includes where it has been appointed a third party for the purposes of safeguarding by another entity. It also has responsibilities in its arrangements for appointing a third party for safeguarding. The selection, appointment and periodic review of any third party which the firm has appointed for safeguarding is a separate potential source of harm, caused by the increased operational complexity and the additional controls and oversight required. It means that a qualifying cryptoasset custodian cannot reduce its level of QCS by appointing a third party for the purposes of safeguarding.

Illustrated examples of minimum requirements

4.44 To help illustrate how the PMR, FOR and KFR interact for individual firms, we have given hypothetical examples using 3 different sized firms for both issuers of qualifying stablecoins and custodians of qualifying cryptoassets. The blue bars in the figures below represent a firm's capital requirements. The green bar represents a firm's potential capital resources. The red dotted line represents the binding minimum capital resources requirement. The overall capital resources requirement will be the highest of the 3 components (ie PMR, FOR or KFR).

4.45 Figure 1 below demonstrates how the basic capital requirements will apply to 3 qualifying stablecoin issuers, Issuer 1, Issuer 2 and Issuer 3, that are at different stages of maturity and size.

Figure 1: Regulated stablecoin issuer examples



4.46 **Issuer 1 (a new firm – PMR is the applicable requirement):**

- PMR = £350,000.
- Annual relevant expenditure is £800k. FOR =3/12 x 800,000 = £200,000.
- Average SII of £7.5m. KFR = 0.02 x £7,500,000 = £150,000.

PMR determines the own funds requirement as it is the highest of the 3 components.

4.47 **Issuer 2 (a growing firm with expanding cost base – FOR is the applicable requirement):**

- PMR = £350,000.
- Annual relevant expenditure is £2m. FOR =3/12 X £2,000,000 = £500,000.
- Average SII of 20m. KFR = 0.02 x £20,000,000 = £400,000.

FOR determines the own funds requirement as it is the highest of the 3 components.

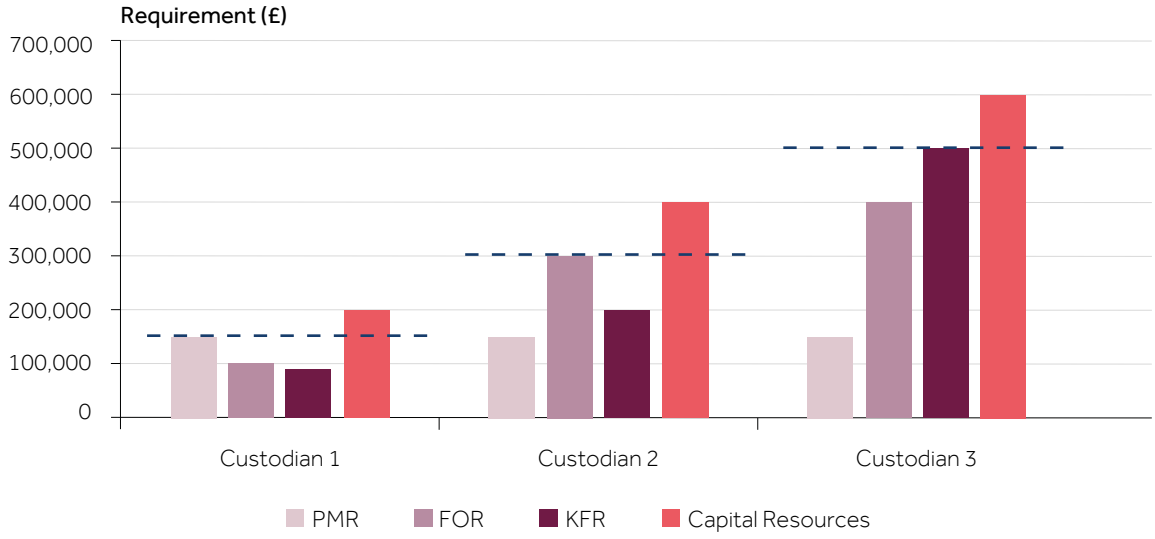
4.48 **Issuer 3 (a mature firm with increased presence – KFR is applicable requirement):**

- PMR = £350,000.
- Annual relevant expenditure is £2.4m. FOR = 3/12 x £2,400,000 = £600,000.
- Average SII of £40m. KFR = 0.02 x £40,000,000 = £800,000.

KFR determines the own funds requirement as it is the highest of the 3 components.

4.49 Figure 2 below demonstrates how the basic capital requirements will apply to 3 cryptoasset custodians, Custodians 1, 2 and 3, that are at different stages of maturity and size.

Figure 2: Cryptoasset custodian examples



4.50 **Custodian 1: (a new firm – PMR is the applicable requirement)**

- PMR = £150,000.
- Firm's annual relevant expenditure is £400k. FOR = 3/12 x £400,000 = £100,000.
- Firm's Average QCS is £225m. KFR = 0.0004 x £225,000,000 = £90,000

PMR determines the own funds requirement as it is the highest of the 3 components.

4.51 **Custodian 2: (a growing firm with expanding cost base – FOR is the applicable requirement)**

- PMR = £150,000.
- Firm's annual relevant expenditure is £1.2m. FOR = 3/12 x £1,200,000 = £300,000.
- Firm's Average QCS is £500m. KFR = 0.0004 x £500,000,000 = £200,000.

FOR determines the own funds requirement as it is the highest of the 3 components.

4.52 **Custodian 3: (a mature firm with increased presence – KFR is the applicable requirement)**

- PMR = £150,000.
- Firm's annual relevant expenditure is £1.6m. FOR = 3/12 x £1,600,000 = £400,000.
- Firm's Average QCS is £1.25bn. KFR = 0.0004 x £1,250,000,000 = £500,000.

KFR determines the own funds requirement as it is the highest of the 3 components.

CRYPTOPRU firms who are also MIFIDPRU firms

4.53 An advantage of our proposed integrated approach to prudential requirements, and the similar requirements for MIFIDPRU firms, is that we can be clear about how the relevant own funds requirements interact with the requirements in MIFIDPRU (where a firm is subject to both CRYPTOPRU and MIFIDPRU). We propose that:

- The PMR will be the highest applicable PMR across the 2 sourcebooks.
- The FOR will be consistent across the different sourcebooks, and
- The KFR will be the sum total of all K-factor requirements applicable across the different sourcebooks.

Question 3: **Do you have any comments on our proposed overall approach on the Own Funds Requirement (OFR), and the detailed provisions of the specific components: (i) PMR, (ii) FOR, (iii) K-SII, and (iv) K-QCS?**

Question 4: **Do you have any views on the items to be deducted from total expenditure when calculating the FOR, are there any others that may be relevant for cryptoasset firms and if so, why?**

Question 5: **Do you agree with our proposal that the value of qualifying cryptoassets appointed by or to a third party custodian for the purposes of safeguarding must be included in the measurement of QCS? If not, how else would you suggest that the risk of potential harm from the use of third parties is mitigated?**

Chapter 5

Liquid assets requirement

5.1 This chapter sets out our proposals for the minimum liquidity requirements for CRYPTOPRU firms and the type of assets the firm can hold to meet them. We explain the following concepts:

- Basic liquid assets requirement (BLAR).
- Issuer liquid asset requirement (ILAR).

5.2 In DP23/4 we set out a proposal for a basic liquidity requirement for CRYPTOPRU firms. We also discussed liquidity needs specifically for stablecoin issuers. Responses included an approach using the ratio between balance sheet size and daily redemption to calculate the requirement. However, the basis used seems more suited to the liquidity requirements of a stablecoin backing asset pool than the issuer of a qualifying stablecoin. We set out our approach to the price risk element of stablecoin backing asset requirements in paragraphs 5.18 to 5.26 below. Another respondent questioned what appeared to be double counting for capital and liquidity due to both being based on the firm's overheads. While the basis used may be similar, the purpose is different – capital is for absorbing losses, while liquidity is for meeting liabilities as they fall due.

5.3 The BLAR is an amount equal to one third of a firm's fixed overheads requirement and applies to all CRYPTOPRU firms. The rules for the BLAR are in COREPRU 6. We explain our proposals on the fixed overheads requirement in Chapter 4 (Own Funds Requirements) of this CP and in COREPRU 4.3.

5.4 The ILAR only applies to CRYPTOPRU firms carrying out the regulated activity of issuing a qualifying stablecoin. It requires issuer firms to calculate what level of cash deposits they need to account for price volatility in the backing asset pool. Firms will then be able to promptly top up the backing pool if there is a shortfall. The ILAR applies in addition to a firm's BLAR.

5.5 The BLAR and ILAR (if applicable) are the minimum liquidity we would expect CRYPTOPRU firms to hold at all times. They form part of the overall framework that will apply to a CRYPTOPRU firm for assessing its individual liquidity needs. As stated earlier, we aim to consult on an ICARA type process for CRYPTOPRU firms in CP2. Through an ICARA process a CRYPTOPRU firm may determine it needs to hold additional liquid assets (above the minimum liquidity requirements) to ensure it can be wound down in an orderly way or address its funding for ongoing business needs.

Basic liquid assets requirement

5.6 We propose to require CRYPTOPRU firms to hold an amount of liquid assets that is at least equal to the sum of:

- One third of the amount of its fixed overheads requirement, and
- 1.6% of the total amount of any guarantees provided to clients.

5.7 This is to ensure that CRYPTOPRU firms always have a minimum stock of liquid assets to fund the initial stages of a wind-down process, if wind-down becomes necessary. This minimum stock of liquid assets will enable CRYPTOPRU firms to meet their relevant overheads for around 1 month if other sources of cash flow are unavailable. This will give them time to arrange cash flows to meet wind-down liabilities in the longer term. The basic liquid assets requirement builds upon the requirement that CRYPTOPRU firms have adequate financial resources to meet their liabilities as they fall due.

5.8 The BLAR includes a component for guarantees firms have given clients, to capture wider contractual obligations a firm may have entered into. This will be relevant to other crypto activities yet to be consulted on, as it currently does for existing investment firms. However, this component may still be relevant for issuers and custodians where they engage in providing guarantees outside of their main line of business.

5.9 Our view is that the basic liquid asset requirement is a proportionate minimum requirement that CRYPTOPRU firms should be able to meet as it only looks at liabilities due within the next month

Core liquid assets

5.10 We propose a list of core liquid assets that CRYPTOPRU firms can use to meet the BLAR. These are the straightforward liquid assets they are likely to hold and do not require any reduction (or 'haircut') given the timeframe over which they may need to be realised. Any amount of the following may be used:

- Coins and banknotes.
- Short-term deposits at a UK bank.
- Assets representing claims on or guaranteed by the UK government or the Bank of England (for example UK gilts and Treasury bonds).
- Units or shares in a short-term regulated money market fund, or in a comparable third country fund.

Sterling and non-sterling currencies

5.11 We are generally proposing that any core liquid assets used to meet the basic liquid assets requirement must be denominated in pound sterling. This is because we generally expect CRYPTOPRU firms to be UK incorporated firms, with a pound sterling denominated balance sheet, that have liquidity needs in pound sterling.

5.12 However, some CRYPTOPRU firms may incur relevant expenditure in other currencies. Where a different currency is involved, we propose to allow an CRYPTOPRU firm to use comparable core liquid assets denominated in a matching foreign currency. This includes deposits held at overseas banks and assets issued or guaranteed by overseas governments or central banks.

5.13 These assets can be included in the same proportion as the relevant expenditure that the CRYPTOPRU firm incurs in that currency. This is illustrated by the following example:

1. A firm has total fixed overheads with a value of £1,200,000, as follows:

    a. 20%, equivalent to £240,000, are incurred in U.S Dollars (USD); and
    b. 5%, equivalent to £60,000, are incurred in Swiss francs (CHF).

2. The firm's fixed overheads requirement (one quarter of its total fixed overheads calculated in accordance with COREPRU 4.3) is £300,000.
3. Under COREPRU 6.2.1R, the firm's basic liquid assets requirement is £100,000 (one third of the amount of its fixed overheads requirement).
4. To meet its requirement in COREPRU 6.2.1R, a firm may choose to use liquid assets listed in COREPRU 6.3.3R denominated in a currency other than pound sterling, up to a maximum equivalent to £25,000, as follows:

    a. Up to the equivalent of £20,000 may be held in USD denominated liquid assets (ie 20% of 100,000 = 20,000, to meet the requirement in COREPRU 6.2.1R; and
    b. Up to the equivalent of £5,000 may be held in CHF denominated liquid assets (ie 5% of 100,000 = 5,000, to meet the requirement in COREPRU 6.2.1R).

What does not count as a liquid asset

5.14 We are proposing to exclude from the definition of a core liquid asset any asset that:

- Belongs to a client (eg client money or client assets under our client assets sourcebook (CASS)), even if the asset is held in the firm's own name.
- Is encumbered or subject to some restriction that prevents it being realised. In these circumstances, the asset will not be available to meet a firm's short term funding requirements.

Price risk in stablecoin backing asset pools – stablecoin issuer liquid asset requirement (ILAR)

5.15 As discussed in DP 23/4, a qualifying stablecoin issuer may have additional need for liquidity due to the way in which their business model operates. Under our proposed rules in CP25/14 qualifying stablecoin issuers must maintain 1:1 backing of the qualifying stablecoin minted. They will also be subject to 'top up' requirements where there is a shortfall in the backing assets pool. Where a shortfall occurs, this may cause a strain on the liquidity of the qualifying stablecoin, and the qualifying stablecoin issuer may not be able to meet their safeguarding requirements. To minimise the risk of a firm being unable to top up, it should hold sufficient liquid assets to make up any shortfall by the end of the next business day.

5.16 While shortfalls may occur for several reasons, one of the main risks is price risk on any assets that have been invested in as part of the backing pool. CP25/14 provides that issuers can use either core backing assets or expanded backing assets as part of their backing pool. All non-cash assets carry an element of price risk, as their market value

may be subject to adverse movements. A firm conducting its reconciliations may find that the value of invested assets has decreased and no longer aligns with the 1:1 ratio required with the number of stablecoins in issuance.

5.17 The risk of a shortfall is increased where a firm is using expanded backing assets as outlined in CP25/14 (public debt with a longer residual maturity, repo, reverse repo and public debt constant net asset value money market funds (PDCNAV MMFs)).

5.18 We propose an issuer liquid asset requirement, or ILAR, which must be met with on demand deposits. The ILAR would be in addition to the BLAR. The aim of the ILAR is to ensure issuers can top up the backing pool using their own resources in the required timeframe of T+1 where they identify a shortfall. Accordingly, we consider that only deposits that are immediately available without restrictions would be appropriate to meet this requirement. Deposits with a break clause for early withdrawals will also meet this requirement, although firms will need to consider the impact of absorbing such penalties on their overall financial resources. The amount a firm will be required to hold to meet the ILAR will depend on the precise mix of non-cash assets held in the backing pool.

5.19 We propose that ILAR will be calculated by applying a specific charge for the value of each asset in the backing pool. When determining what an appropriate charge may be for qualifying stablecoin issuers, we have considered how existing regulatory approaches address price risk of government debt securities. These include the UK Capital Requirements Regulation (CRR) and collateral haircuts used by the Bank of England. We have also considered relevant available market data.

5.20 To calculate the ILAR, firms will need to establish the residual maturity, the state issuer and the coupon for each government debt security. Firms will then need to identify the relevant charge based on this information from the table in CRYPTOPRU 6 and apply this to the current total value of each position in the backing pool. The sum of these amounts will be a firm's total ILAR. In cases where a firm has multiple qualifying stablecoin issuances, the ILAR would need to be calculated for each individual issuance and held cumulatively.

5.21 Issuers may create qualifying stablecoin in a range of currencies. So we propose any on demand deposits used to contribute towards meeting the total ILAR must be denominated in the reference currency of the qualifying stablecoin(s). This may mean an issuer has a total ILAR that is met by on demand deposits of more than one currency, where it issues qualifying stablecoins in more than one reference currency.

5.22 Where a qualifying stablecoin is issued in a currency that is different to the issuer's functional currency, the firm would be exposed to foreign exchange risk from holding the relevant ILAR on its own balance sheet. Given the relative early stage of the market, we have not set out a proposal to address this.

5.23 As outlined in CP25/14, expanded backing assets include the use of repurchase transactions. For the purposes of the ILAR, we propose that an issuer would need to apply the relevant charge to government debt securities exchanged for the duration of a repurchase transaction. This would cover government debt securities either received or given out to be included in the ILAR calculation. We consider this to be a prudent

measure. This is because we assume firms will be exposed to the government debt instruments when they have been brought into the backing pool for the duration of the transaction or are due to return to the backing pool when the transaction is completed.

5.24 The following is an illustrative example of how a firm with an issuance of £1m with both core and expanded backing assets would arrive at the ILAR.

1. The firm has a backing asset composition as follows:
    a. £300,000 in on demand deposits.
    b. £500,000 in short-term government debt issued by the UK (a Level 1 asset) with a residual maturity of 3 months and a coupon of 5%.
    c. £200,000 in long-term government debt issued by the UK (a Level 1 asset) with a residual maturity of 5 years and a coupon of 4%.
2. The issuer liquid asset requirement should be calculated by multiplying the notional value of the short-term government debt and the long-term government debt by the charge found in the table in CRYPTOPRU 6.1.11R as follows:
    a. £500,000 x 0.2% = £1,000.
    b. £200,000 x 3.5% = £7,000.
3. The total ILAR is the sum of these amounts.
    a. £1,000 + £7,000 = £8,000.

5.25 Expanded backing assets also include PDCNAV MMFs. We propose firms look through to the underlying assets held by the fund, and apply the relevant price charges for government debt instruments to those underlying assets. This would effectively treat the holdings within the fund as direct positions held in the backing asset pool. Where firms are unable to look through, or choose not to do so, they would need to apply a 5% charge to the total of their fund position. This approach aligns with the treatment of collective investment undertaking positions under the Capital Requirements Regulation. We have simplified the approach by applying a 5% charge which would be the highest charge under the ILAR given the mandate of PDCNAV MMFs.

5.26 Our approach under the ILAR would not prescribe a specific capital charge for the risks from holding assets in the backing pool. While the value of underlying assets may move, this may be on a temporary basis. Issuers will not suffer a loss unless they receive significant redemptions that exhaust cash and core liquid assets. Given the idiosyncratic nature of losses from these business models, and uncertainty about the severity and scale, we do not consider it proportionate to apply a capital charge in addition to the ILAR. However, issuers may need to consider this as part of any subsequent ICARA process.

Question 6: **Do you agree with our proposals on the basic liquid asset requirement (BLAR)?**

Question 7: As part of the BLAR, can you identify any circumstances where the provision of guarantees provided to clients by firms might apply to cryptoasset custodians or qualifying stablecoin issuers?

Question 8: Do you agree with our proposals on the issuer liquid asset requirement (ILAR) to address price risk when government debt instruments are held in a backing pool (either directly, or indirectly in connection with certain funds and repo/reverse repo transactions)? If not, please explain why you do not agree with specific aspects and what alternative solutions would you suggest?

Question 9: Do respondents consider that the foreign exchange risk for qualifying stablecoin issuers described in paragraph 5.22 needs to be addressed through minimum requirements, for example would a specific capital charge be appropriate?

Chapter 6

Concentration risk

6.1 This chapter explains our proposals for monitoring requirements to address concentration risk. These will apply to all CRYPTOPRU firms.

6.2 Concentration risk is the potential for loss if a firm is overly exposed to one or more counterparties or type of asset. In DP23/4 we gave the example of Circle, and the impact on the secondary market price of its stablecoin (USDC) when Silicon Valley Bank collapsed.

6.3 Some respondents to DP23/4 offered suggestions to help mitigate concentration risk. These included using large exposure type limits, requirements for bankruptcy remoteness of deposits (from issuers) and using only banks that apply the Basel Framework. We have considered this and noted the potential difficulty qualifying stablecoin issuers may have in being able to diversify the location of backing pool assets. This has been a factor in deciding what types of asset are permitted for inclusion in the backing asset pool. In line with the proposed CASS rules, (see CP25/14) we would expect all assets held in the backing asset pool to be ring-fenced in trust.

General obligation to monitor concentration

6.4 To manage the potential for harm from different types of concentrated exposures or relationships, it is prudent that firms should monitor and control all their relevant sources of concentration risk, including:

- Assets (for example, trade debts).
- Off-balance sheet items.
- The location of client money and custody assets.
- The location of the firm's own cash deposits.
- The sources of earnings.
- When a CRYPTOPRU firm is issuing qualifying stablecoin, the backing assets held for the purpose of maintaining that coin's value.

6.5 To monitor and control concentration risk, firms should ensure they have sound administrative and accounting procedures supported by robust internal controls. For example, accounting procedures could identify and record counterparties and their associated level of earnings, measure them against internally agreed limits and report this information through governance arrangements. The firm can then decide whether to adjust its business accordingly.

6.6 When we refer to the location of custody assets or cash, including those used to back qualifying stablecoins, we envisage that firms should monitor and control how far these assets are concentrated at given banks, investment firms, CRYPTOPRU firms and other entities, including sub-custodians and funds (see Chapter 5 of COREPRU).

6.7 CRYPTOPRU firms should be able to identify not just individual clients but also groups of connected clients who may constitute a single risk because of their interconnectedness. Our proposed rules offer a detailed definition of what a group of connected clients means.

6.8 We would expect firms' considerations to include:

- A practical definition of what constitutes a material concentration in line with its risk tolerance.
- Adequate documentation and regular review of their concentration risk policy for ongoing appropriateness.
- Regular monitoring of the composition of backing assets against any potential concentration (where the firm is an issuer).
- Timely and accurate management information on concentration risk.

6.9 As reflected in the third bullet above, CRYPTOPRU firms that issue qualifying stablecoin should also carefully consider the concentration risk in the backing asset pool. If a qualifying stablecoin issuer finds its level of concentration risk is greater than its risk tolerance, it must take action to minimise this concentration within the backing asset pool. It may do this by diversifying its assets across multiple counterparties, unwinding concentrated positions and ensuring multiple banks are available for its cash deposits.

Question 10: **Do you have any comments on the proposal for monitoring and control of concentration risk? Please provide suggestions for any specific clarifications that you feel may be helpful.**

Annex 1

Questions in this paper

Question 1: Do you have any comments on our proposals for the definitions and types of, and deductions from, regulatory capital that CRYPTOPRU firms should use to calculate their own funds?

Question 2: Do you have any views on our proposed requirements for deductions from CET1 capital, in particular cryptoassets held by firms which they have issued or are in control of the supply of?

Question 3: Do you have any comments on our proposed overall approach on the Own Funds Requirement (OFR), and the detailed provisions of the specific components: (i) PMR, (ii) FOR, (iii) K-SII, and (iv) K-QCS?

Question 4: Do you have any views on the items to be deducted from total expenditure when calculating the FOR, are there any others that may be relevant for cryptoasset firms and if so, why?

Question 5: Do you agree with our proposal that the value of qualifying cryptoassets appointed by or to a third party custodian for the purposes of safeguarding must be included in the measurement of QCS? If not, how else would you suggest that the risk of potential harm from the use of third parties is mitigated?

Question 6: Do you agree with our proposals on the basic liquid asset requirement (BLAR)?

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Question 8: Do you agree with our proposals on the issuer liquid asset requirement (ILAR) to address price risk when government debt instruments are held in a backing pool (either directly, or indirectly in connection with certain funds and repo/reverse repo transactions)? If not, please explain why you do not agree with specific aspects and what alternative solutions would you suggest?

Question 9: Do respondents consider that the foreign exchange risk for qualifying stablecoin issuers described in paragraph 5.22 needs to be addressed through minimum requirements, for example would a specific capital charge be appropriate?

Question 10: Do you have any comments on the proposal for monitoring and control of concentration risk? Please provide suggestions for any specific clarifications that you feel may be helpful.

Annex 2

Cost Benefit Analysis

Please see Cost Benefit Analysis (CBA), which is a joint CBA for CP25/15 and CP25/14 (Cryptoassets, Stablecoins, Custody and Prudential Requirements)

Annex 3

Compatibility statement

Compliance with legal requirements

1. This Annex records the FCA's compliance with a number of legal requirements applicable to the proposals in this consultation, including an explanation of the FCA's reasons for concluding that our proposals in this consultation are compatible with certain requirements under the Financial Services and Markets Act 2000 (FSMA).

2. When consulting on new rules, the FCA is required by section 138I(2)(d) FSMA to include an explanation of why it believes making the proposed rules:

a. is compatible with its general duty, under section 1B(1) FSMA, so far as reasonably possible, to act in a way which is compatible with its strategic objective and advances one or more of its operational objectives;
b. so far as reasonably possible, advances the secondary international competitiveness and growth objective, under section 1B(4A) FSMA; and
c. complies with its general duty under section 1B(5)(a) FSMA to have regard to the regulatory principles in section 3B FSMA.

3. The FCA is also required by s 138K(2) FSMA to state its opinion on whether the proposed rules will have a significantly different impact on mutual societies as opposed to other authorised persons.

4. This Annex also sets out the FCA's view of how the proposed rules are compatible with the duty on the FCA to discharge its general functions (which include rule-making) in a way which promotes effective competition in the interests of consumers (section 1B(4)). This duty applies in so far as promoting competition is compatible with advancing the FCA's consumer protection and/or integrity objectives.

5. In addition, this Annex explains how we have considered the recommendations made by the Treasury under s 1JA FSMA about aspects of the economic policy of His Majesty's Government to which we should have regard in connection with our general duties.

6. This Annex includes our assessment of the equality and diversity implications of these proposals.

7. Under the Legislative and Regulatory Reform Act 2006 (LRRA) the FCA is subject to requirements to have regard to a number of high-level 'Principles' in the exercise of some of our regulatory functions and to have regard to a 'Regulators' Code' when determining general policies and principles and giving general guidance (but not when exercising other legislative functions like making rules). This Annex sets out how we have complied with requirements under the LRRA.

The FCA's objectives and regulatory principles: Compatibility statement

8. The proposals set out in this consultation are primarily intended to advance the FCA's operational objective of protecting the integrity of the UK financial system. They are also relevant to the FCA's competition objective.

9. The proposals advance the integrity objective by setting minimum capital and liquidity requirements for crypto firms, and reducing concentration risk. Crypto firms will be more financially sound and if they need to wind-down will be able to do so in a more orderly manner. Crypto markets and any interconnected markets will benefit from increased stability and resilience. The relevant proposals are set out in Chapters 3, 4 and 5 of this CP. We therefore consider these proposals are compatible with the FCA's strategic objective of ensuring that the relevant markets function well. For the purposes of the FCA's strategic objective, "relevant markets" are defined by section 1F FSMA.

10. In drafting these proposals we have had regard for matters relating to the effectiveness of competition in the market, notably ease of new entry to the market and encouraging innovation.

11. We consider these proposals comply with the FCA's secondary objective in advancing competitiveness and growth because CRYPTOPRU will help to create a sound and resilient UK market for cryptoassets and these are attractive features for market participants. Our minimum requirements for own funds do not disadvantage the United Kingdom when compared to other jurisdictions that are also developing prudential regimes for firms undertaking cryptoasset activities.

In preparing the proposals set out in this consultation, the FCA has had regard to the regulatory principles set out in s 3B FSMA.

The need to use our resources in the most efficient and economic way

12. Our proposals are designed to be as proportionate as possible and ensure that our expectations are clear to firms. The information received from firms under the proposals will give us a better understanding of firms' capital and liquidity requirements. This will make our firm supervision more effective and help us better understand prudential risks.

The principle that a burden or restriction should be proportionate to the benefits

13. Please refer to the link for the Cost Benefit Analysis in Annex 2.

The need to contribute towards achieving compliance by the Secretary of State with section 1 of the Climate Change Act 2008 (UK net zero emissions target) [and section 5 of the Environment Act 2021 (environmental targets)]]

14. On balance, we do not think there is any contribution the proposals outlined in this consultation can make to these targets. However, we will be considering the ESG implications of our broader proposals in more detail in CP2 later this year, at which point we will welcome your feedback on this. We will continue to keep this under review when considering any final rules.

The general principle that consumers should take responsibility for their decisions

15. The proposals in this Consultation Paper are primarily concerned with reducing the harms that firms performing regulated activities for cryptoassets could cause on an ongoing basis and in wind-down. They focus on the actions of the firms themselves rather than decisions made by consumers. We will be consulting on public disclosures in our Admissions and Disclosures Consultation Paper.

The responsibilities of senior management

16. Senior management responsibilities with regard to regulated cryptoasset activities will be covered in our RAO Consultation Paper.

The desirability of recognising differences in the nature of, and objectives of, businesses carried on by different persons including mutual societies and other kinds of business organisation

17. We believe our proposals do not undermine this principle, and that we have appropriately had regard to the variety of firms affected by tailoring them to different firm types.

The desirability of publishing information relating to persons subject to requirements imposed under FSMA, or requiring them to publish information

18. This principle is not relevant to the matters covered in this Consultation Paper.

The principle that we should exercise of our functions as transparently as possible

19. We continue to engage with industry and other stakeholders to obtain feedback during the consultation process.

In formulating these proposals, the FCA has had regard to the importance of taking action intended to minimise the extent to which it is possible for a business carried on (i) by an authorised person or a recognised investment exchange; or (ii) in contravention

of the general prohibition, to be used for a purpose connected with financial crime (as required by s 1B(5)(b) FSMA). These proposals concern prudential requirements and do not relate to financial crime per se. However, a regime that requires sound financial management of firms is likely to disincentivise their use for financial crime.

Expected effect on mutual societies

20. The FCA does not expect the proposals in this paper to have a significantly different impact on mutual societies.

Compatibility with the duty to promote effective competition in the interests of consumers

21. In preparing the proposals as set out in this consultation, we have had regard to the FCA's duty to promote effective competition in the interests of consumers.

22. We consider that consumers will benefit from the existence of regulated prudential requirements and that cryptoasset markets and participants will gain closer prudential parity with their traditional financial counterparts as a result of these proposals.

23. We have also kept the competition objective in mind when framing how these proposals should be implemented, with a particular focus on whether there is a risk of weakening competitive pressure, disadvantaging smaller firms and potential new entrants.

Equality and diversity

24. We are required under the Equality Act 2010 in exercising our functions to 'have due regard' to the need to eliminate discrimination, harassment, victimisation and any other conduct prohibited by or under the Act, advance equality of opportunity between persons who share a relevant protected characteristic and those who do not, to and foster good relations between people who share a protected characteristic and those who do not.

25. As part of this, we have considered the equality and diversity issues that may arise from the proposals in this CP.

26. Overall, we do not consider that the proposals have a differential impact on any group sharing one of the characteristics protected under the Equality Act 2010. But we will continue to consider the equality and diversity implications of the proposals during the consultation period, and will revisit them when making the final rules.

Environmental, social & governance considerations

27. We have considered the environmental, social and governance (ESG) implications of our proposals, including our duty under ss. 1B(5) and 3B(c) of FSMA to have regard to contributing towards the Secretary of State achieving compliance with the net-zero emissions target under section 1 of the Climate Change Act 2008 [and environmental targets under s. 5 of the Environment Act 2021]. While we do not consider these proposals to be relevant to those targets, we welcome consultation feedback on any ESG implications.

Legislative and Regulatory Reform Act 2006 (LRRA)

28. We have had regard to the principles in the LRRA for the parts of the proposals that consist of general policies, principles or guidance and consider that the proposals will help firms understand and meet prudential requirements, leading to better outcomes for consumers and market integrity. We also believe the proposals are proportionate and take account of the variety of firms in scope.

We have had regard to the Regulators' Code for the parts of the proposals that consist of general policies, principles or guidance and consider that the proposals are proportionate and do not create an unnecessary burden on firms, or adversely affect competition.

HM Treasury recommendations about economic policy

29. The HM Treasury recommendations most relevant to our proposals, specifically on the government's economic policy, are:

- growing the financial services sector and increasing its international competitiveness, while enhancing its role in financing growth, safeguarding financial stability and consumer protection, and supporting the transition to a net zero economy
- aspects of the government's economic policy on maintaining and enhancing the UK's position as a world-leading global finance hub and a destination of choice for international financial services business

30. We believe that our proposals support the Treasury's recommendations on international competitiveness of the UK, as the proposed prudential requirements are competitive with international requirements for similar activities.

Annex 4

Abbreviations used in this document

Abbreviation	Description
AT1	Additional Tier 1 Capital
BLAR	Basic Liquid Asset Requirement
CASS	Client Assets Sourcebook
CBA	Cost Benefit analysis
CET1	Common Equity Tier 1 Capital
CHF	Swiss Francs
CP	Consultation Paper
CRYPTOPRU	New Prudential Sourcebook for CryptoAsset businesses
CRR	Capital Requirements Regulation
DP	Discussion Paper
FCA	Financial Conduct Authority
FOR	Fixed Overheads Requirement
FSMA	Financial Services and Markets Act
ILAR	Issuer Liquid Asset Requirement
ICARA	Internal Capital Adequacy and Risk Assessment
KFR	K-Factor Requirement
K-QCS	K-Factor for qualifying cryptoassets safeguarded
K-SII	K-Factor for qualifying stablecoin in issuance
MiCA	Markets in Crytpo-Asset Regulation
MIFIDPRU	Prudential Sourcebook for solo regulated MIFID investment firms

Abbreviation	Description
MLRs	Money Laundering, Terrorist Financing, and Transfer of Funds (Information on the Payer) Regulations 2017 (MLRs)
MMF	Money Market Funds
OFR	Own Funds Requirement
PDCNAV MMF	Public debt constant net asset value Money market fund
PMR	Permanent Minimum Requirement
QCS	Qualifying cryptoasset safeguarded
SII	Qualifying Stablecoin in issuance
T2	Tier 2 Capital
USD	United States Dollars

Appendix 1

Draft Handbook text

COREPRU AND CRYPTOPRU INSTRUMENT 2025

Power exercised

A. The Financial Conduct Authority ("the FCA") makes this instrument in the exercise of:

(1) the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(2)

(a) section 98 (application of section 137B of the Act to backing assets for qualifying stablecoin);
(b) section 99 (application of section 137B of the Act to safeguarding qualifying cryptoassets and relevant specified investment cryptoassets)
(c) section 137A (the FCA's general rules);
(d) section 137T (General supplementary powers);
(e) section 138C (Evidential provisions);
(f) section 138D (Actions for damages); and
(g) section 139A (Power of the FCA to give guidance); and

(2) the other powers and related provisions listed in Schedule 4 (Powers exercised) to the General Provisions of the FCA's Handbook.

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

Commencement

C. This instrument comes into force on [*date*].

Amendments to the FCA Handbook

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

E. The Prudential sourcebook for Insurers (INSPRU) is moved immediately after the Interim Prudential sourcebook for Insurers (IPRU-INS).

F. The General Prudential sourcebook (GENPRU) is moved after the Interim Prudential sourcebook for Investment Businesses (IPRU-INV), so it is the last sourcebook in the Prudential Standards block within the Handbook.

Making the Core Prudential sourcebook (COREPRU) and the Prudential sourcebook for CRYPTOPRU firms (CRYPTOPRU)

G. The FCA makes the rules and gives the guidance in accordance with Annexes B (COREPRU) and C (CRYPTOPRU) to this instrument.

H. The Core Prudential sourcebook (COREPRU) is added as the first sourcebook to the Prudential Standards block within the Handbook.

I. The Prudential sourcebook for CRYPTOPRU firms (CRYPTOPRU) is added to the Prudential Standards block within the Handbook, immediately after the Core Prudential sourcebook (COREPRU).

Notes

J. In the annexes to this instrument, the notes (indicated by "**Note:**" or "*Editor's note:*") are included for the convenience of readers, but do not form part of the legislative text.

Citation

L. This instrument may be cited as the COREPRU and CRYPTOPRU Instrument 2025.

M. The sourcebook in Annex B to this instrument may be cited as the Core Prudential sourcebook (COREPRU).

N. The sourcebook in Annex C to this instrument may be cited as the Prudential sourcebook for CRYPTOPRU firms (CRYPTOPRU).

By order of the Board
[*date*]

Annex A

Amendments to the Glossary of definitions

[*Editor's note*: This Annex takes into account the proposals and legislative changes suggested in the following consultation papers as if they were made final.]

(1)	'Definition of capital for FCA investment firms' (CP25/10) in relation to the following definitions: *additional tier 1 capital* *additional tier 1 instrument* *additional tier 1 item* *additional tier 1 or comparable instrument* *common equity tier 1 capital* *common equity tier 1 instrument* *common equity tier 1 item* *common equity tier 1 or comparable instrument* *own funds* *tier 2 capital* *tier 2 instruments* *tier 2 or comparable instrument* *tier 2 item*
(2)	'Stablecoin Issuance and Cryptoasset Custody' (CP25/14) in relation to the following definitions: *core backing assets* *backing asset pool* *burning* *expanded backing assets* *issuing qualifying stablecoins* *long-term government debt instrument* *on demand deposits* *qualifying cryptoassets* *qualifying stablecoins* *qualifying stablecoin issuer* *minted* *reference currency* *short-term government debt instrument*

	safeguarding qualifying cryptoassets
(3)	'Updating the regime for Money Market Funds' (CP23/28) in relation to the following definitions: *EU MMF* *public debt CNAV MMF*

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

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

average QCS	the rolling average of a *CRYPTOPRU firm's QCS* calculated in accordance with *CRYPTOPRU* 4.4.5R.
average SII	the rolling average of a *CRYPTOPRU firm's SII* calculated in accordance with *CRYPTOPRU* 4.5.3R.
COREPRU	the Core Prudential sourcebook.
CRYPTOPRU	the Prudential sourcebook for CRYPTOPRU firms.
CRYPTOPRU activity	any of the following activities: (a) *safeguarding qualifying cryptoassets*; and (b) *issuing qualifying stablecoins*.
CRYPTOPRU firm	a *firm* with *permission* to carry on any *CRYPTOPRU activity*.
issuer liquid asset requirement	an amount of *on demand deposits* that a *CRYPTOPRU firm* must hold, in accordance with *CRYPTOPRU* 6.1.4R to *CRYPTOPRU* 6.1.11R.
K-QCS requirement	the part of the *K-factor requirement* calculated on the basis of the *QCS* of a *CRYPTOPRU firm*, in accordance with *CRYPTOPRU* 4.4.
K-SII requirement	the part of the *K-factor requirement* calculated on the basis of the *SII* of a *CRYPTOPRU firm*, in accordance with *CRYPTOPRU* 4.5.
level 1 asset	a *short-term government debt instrument* or a *long-term government debt instrument* that has been issued by: (a) Canada; (b) France; (c) Germany;

(d) Netherlands;

(e) *United Kingdom*; or

(f) United States.

level 2 asset a *short-term government debt instrument* or a *long-term government debt instrument* that has been issued by:

(a) Australia;

(b) Austria;

(c) Belgium;

(d) Denmark;

(e) Finland;

(f) Ireland;

(g) Italy;

(h) Japan;

(i) Luxembourg;

(j) New Zealand;

(k) Norway;

(l) Portugal;

(m) Spain;

(n) Sweden; or

(o) Switzerland.

level 3 asset a *short-term government debt instrument* or a *long-term government debt instrument* that has been issued by a member of the *OECD* not listed in the definition of *level 1 asset* or *level 2 asset*.

QCS the value of *qualifying cryptoassets* that a *CRYPTOPRU firm* is safeguarding.

sectoral liquidity requirement a requirement on liquidity set out in a *sectoral prudential sourcebook*.

sectoral prudential sourcebook	any of the following:	
	(a)	the Prudential sourcebook for CRYPTOPRU firms (CRYPTOPRU); or
	(b)	[to follow]
SII	the *qualifying stablecoins* that the *qualifying stablecoin issuer* is liable to redeem, excluding any amount deducted in accordance with *COREPRU* 3.3.36R.	

Amend the following definitions as shown.

additional tier 1 capital	(1)	(in *COREPRU*) has the meaning in *COREPRU* 3.4.2R.
	(2)	(in *MIFIDPRU*) has the meaning in *MIFIDPRU* 3.4A.2R.
additional tier 1 instrument	(1)	(in *COREPRU*) a capital instrument that complies with the conditions in *COREPRU* 3.4.3R to *COREPRU* 3.4.15R and that is not a *common equity tier 1 instrument*.
	(2)	(in *MIFIDPRU*) a capital instrument that complies with the conditions in *MIFIDPRU* 3.4A.3R to *MIFIDPRU* 3.4A.15R and that is not a *common equity tier 1 instrument*.
additional tier 1 item	(1)	(in *COREPRU*) has the meaning in *COREPRU* 3.4.2R.
	(2)	(in *MIFIDPRU*) has the meaning in *MIFIDPRU* 3.4A.2R.
additional tier 1 or comparable instrument	(1)	(in *COREPRU*) has the meaning in *COREPRU* 3.4.22R.
	(2)	(in *MIFIDPRU*) has the meaning in *MIFIDPRU* 3.4A.22R.
basic liquid assets requirement	the requirement to hold a minimum amount of *core liquid assets*:	
	(1)	(in *COREPRU*) as set out in *COREPRU* 6.2.1R.
	(2)	(in *MIFIDPRU*) as set out in *MIFIDPRU* 6.2.1R for a *MIFIDPRU investment firm* ~~to hold a minimum amount of *core liquid assets*~~.
common equity tier 1 capital	(1)	(in *COREPRU*) has the meaning in *COREPRU* 3.3.2R.

	(2)	(in *MIFIDPRU*) has the meaning in *MIFIDPRU* 3.3A.2R.
common equity tier 1 instrument	(1)	(in *COREPRU*) a capital instrument that complies with the conditions in *COREPRU* 3.3.3R to *COREPRU* 3.3.16R.
	(2)	(in *MIFIDPRU*) a capital instrument that complies with the conditions in *MIFIDPRU* 3.3A.3R to *MIFIDPRU* 3.3A.16R.
common equity tier 1 item	(1)	(in *COREPRU*) has the meaning in *COREPRU* 3.3.2R.
	(2)	(in *MIFIDPRU*) has the meaning in *MIFIDPRU* 3.3A.2R.
common equity tier 1 or comparable instrument	(1)	(in *COREPRU*) has the meaning in *COREPRU* 3.3.29R.
	(2)	(in *MIFIDPRU*) has the meaning in *MIFIDPRU* 3.3A.29R.
core liquid asset	(1)	(in *COREPRU*) has the meaning in *COREPRU* 6.3 (Core liquid assets).
	(2)	(in *MIFIDPRU*) has the meaning in *MIFIDPRU* 6.3 (Core liquid assets).
fixed overheads requirement	(1)	…
	(2)	(in *COREPRU*) the part of the *own funds requirement* calculated in accordance with *COREPRU* 4.3.
	~~(2)~~ (3)	(in *IPRU(INV)*) the part of the *own funds* requirement calculated in accordance with *IPRU(INV)* 11.3.3R (Fixed overheads requirement).
	~~(3)~~ (4)	(in *MIFIDPRU*) the part of the *own funds requirement* calculated in accordance with *MIFIDPRU* 4.5 (Fixed overheads requirement).

[*Editor's note*: amendments to the definitions of 'ICARA document' and ICARA process' will be consulted on in a subsequent consultation.]

K-factor average metric	(1)		(in *MIFIDPRU*) any of the following:
	~~(1)~~	(a)	*average ASA*;
	~~(2)~~	(b)	*average AUM*;
	~~(3)~~	(c)	*average CMH*;
	~~(4)~~	(d)	*average COH*;

	~~(5)~~	(e)	*average DTF*;
	~~(6)~~	(f)	TM (which, in summary, is part of the formula in *MIFIDPRU* 4.13.5R that is used to calculate the *K-CMG requirement*).
	(2)	(in *CRYPTOPRU*) any of the following:	
		(a)	*average QCS*; and
		(b)	*average SII*.
K-factor metric	(1)	(in *MIFIDPRU*) any of the following:	
	~~(1)~~	(a)	*ASA*;
	~~(2)~~	(b)	*AUM*;
	~~(3)~~	(c)	*CMG*;
	~~(4)~~	(d)	*CMH*;
	~~(5)~~	(e)	*COH*;
	~~(6)~~	(f)	*CON*;
	~~(7)~~	(g)	*DTF*;
	~~(8)~~	(h)	*NPR*; and
	~~(9)~~	(i)	*TCD*.
	(2)	(in *CRYPTOPRU*) any of the following:	
		(a)	*QCS*; and
		(b)	*SII*.
K-factor requirement	(1)	(in *MIFIDPRU*) the part of the *own funds requirement* calculated in accordance with *MIFIDPRU* 4.6.	
	(2)	(in *COREPRU* and *CRYPTOPRU*) the part of the *own funds requirement* calculated in accordance with *COREPRU* 4.4.	
overall financial adequacy rule	…		
	(2)	(in *MIFIDPRU*) the requirement in *MIFIDPRU* 7.4.7R(1) (Overall financial adequacy rule), which is the obligation for a *MIFIDPRU investment firm* to hold *own funds* and *liquid assets* which are adequate, both as to their amount and quality, to ensure that:	

		(a) it is able to remain financially viable throughout the economic cycle, with the ability to address any material potential harm that may result from its ongoing activities; and (b) its business can be wound down in an orderly manner, minimising harm to *consumers* or to other market participants.
	(3)	(in *COREPRU*) the requirement in *COREPRU* 2.3.1R.
own funds	…	
	(4A)	(in *MIFIDPRU*) has the meaning in *MIFIDPRU* 3.2A.2R.
	(4B)	(in *COREPRU* and *CRYPTOPRU*) has the meaning in *COREPRU* 3.2.2R.
	…	
own funds requirement	(1)	(in *MIFIDPRU*) the requirement for a *MIFIDPRU investment firm* to maintain a minimum level of *own funds* specified in *MIFIDPRU* 4.3.
	(2)	(in *COREPRU*) the requirement for a *firm* to maintain a minimum level of *own funds* specified in *COREPRU* 4.1.
permanent minimum capital requirement	(1)	(in *MIFIDPRU*) the part of the *own funds requirement* calculated in accordance with *MIFIDPRU* 4.4.
	(2)	(in *COREPRU* and *CRYPTOPRU*) the part of the *own funds requirement* calculated in accordance with *COREPRU* 4.2.
relevant expenditure	(1)	(in *MIFIDPRU 4*, *MIFIDPRU* 6 and *IPRU(INV)* 11) relevant expenditure as calculated under *MIFIDPRU* 4.5.3R.
	(2)	(in *COREPRU*) relevant expenditure as calculated under *COREPRU* 4.3.3R.
tier 2 capital	(1)	(in *COREPRU*) has the meaning in *COREPRU* 3.5.2R.
	(2)	(in *MIFIDPRU*) has the meaning in *MIFIDPRU* 3.5A.2R.
tier 2 instruments	(1)	(in *COREPRU*) a capital instrument that complies with the conditions in *COREPRU* 3.5.3R to *COREPRU* 3.5.11R and is not a *common equity tier 1 instrument* or an *additional tier 1 instrument*.
	(2)	(in *MIFIDPRU*) a capital instrument that complies with the conditions in *MIFIDPRU* 3.5A.3R to *MIFIDPRU* 3.5A.11R and

		is not a *common equity tier 1 instrument* or an *additional tier 1 instrument*.
tier 2 or comparable instrument	(1)	(in *COREPRU*) has the meaning in *COREPRU* 3.5.17R.
	(2)	(in *MIFIDPRU*) has the meaning in *MIFIDPRU* 3.5A.17R.
tier 2 item	(1)	(in *COREPRU*) has the meaning in *COREPRU* 3.5.2R.
	(2)	(in *MIFIDPRU*) has the meaning in *MIFIDPRU* 3.5A.2R.

[*Editor's note*: amendments to the definition of 'trading book' will be consulted on in a subsequent consultation.]

Annex B

Core Prudential sourcebook (COREPRU)

[*Editor's note*: This Annex takes into account the proposals and legislative changes suggested in the following consultation papers as if they were made final:

(1) 'Definition of capital for FCA investment firms' (CP25/10); and
(2) 'Stablecoin Issuance and Cryptoasset Custody' (CP25/14).]

In this Annex, all the text is new and is not underlined. Insert the following new sourcebook, the Core Prudential sourcebook (COREPRU), as the first sourcebook in the Prudential Standards Handbook Module.

1 Application

1.1 Application and interaction with sectoral prudential sourcebooks

Application

1.1.1 R *COREPRU* applies to a *CRYPTOPRU firm*.

1.2 COREPRU and the sectoral prudential sourcebooks

1.2.1 G *COREPRU* contains the prudential requirements that apply to the *firms* listed in *COREPRU* 1.1.1R.

1.2.2 G The prudential requirements in this chapter are cross-cutting requirements that are intended to apply across multiple sectors. These cross-cutting requirements are supplemented by sector-specific requirements in the *sectoral prudential sourcebooks*, such as *CRYPTOPRU*. *COREPRU* should therefore be read alongside any *sectoral prudential sourcebooks* which apply to a *firm*.

1.2.3 G For example, a *CRYPTOPRU firm* needs to comply with the *own funds requirement* in *COREPRU* 4.1. The *own funds requirement* has a variety of components, some of which are cross-cutting and defined in *COREPRU*, whilst others are sector-specific and defined in the *sectoral prudential sourcebooks* (which, in the case of a *CRYPTOPRU firm*, would mean *CRYPTOPRU*).

1.3 Actions for damages

1.3.1 R A contravention of any *rule* in *COREPRU* does not give rise to a right of action by a *private person* under section 138D of the *Act* (and each of those *rules* is specified under section 138D(3) of the *Act* as a provision giving rise to no such right of action).

2 Overall financial adequacy

2.1 Purpose

2.1.1 G *COREPRU* contains *rules* and *guidance* which supplement the overarching requirements under:

(1) the appropriate resources *threshold condition* in Schedule 6 to the *Act* (as explained in *COND* 2.4) under which a *firm* must have appropriate resources in relation to the *regulated activities* that it carries on; and

(2) *Principle* 4 (Financial prudence) under which a *firm* must maintain adequate financial resources.

2.1.2 G The overall purpose of the requirements in *COREPRU* is to ensure that a *firm*:

(1) holds financial resources that are adequate for the business it undertakes; and

(2) has appropriate systems and controls in place to identify, monitor and, where proportionate, reduce all potential material harms that may result from the ongoing operation of its business or winding down its business.

2.1.3 G The *FCA*:

(1) recognises that there is a vast range of potential harms and it will not be possible for the *FCA* or *firms* to eliminate all potential risks and sources of harm;

(2) considers that *firms* should focus on material harms, adopting a proportionate and risk-based approach to their business and operating models; and

(3) recognises that some *firms* may still fail, but considers that *firms* should aim to ensure that any wind-down of those *firms* occurs in an orderly manner, minimising the impact on *consumers* and the wider market.

2.2 Voluntary application of stricter requirements

2.2.1 R No provision in *COREPRU* or the *sectoral prudential sourcebooks* prevents a *firm* from:

(1) holding *own funds* (or components of *own funds*) or *liquid assets* that exceed those required by an applicable *rule*; or

(2) applying other measures that are stricter than those required by an applicable *rule*.

2.2.2 G If a *firm* wishes to apply a stricter measure but is unsure of whether that measure would meet the prudential requirements applicable to it, it should discuss the proposal with the *FCA* before applying the measure.

2.3 Overall financial adequacy rule

2.3.1 R (1) A *firm* must, at all times, maintain *own funds* and *liquid assets* that are adequate in both amount and quality for the business it undertakes.

(2) The requirement in (1) is known as the *overall financial adequacy rule*.

2.3.2 R The remainder of *COREPRU* expands upon the *overall financial adequacy rule* as follows:

(1) *COREPRU* 3 explains how a *firm* must quantify its *own funds*;

(2) *COREPRU* 4 explains how a *firm* must calculate an *own funds requirement* in accordance with a quantified methodology prescribed by the *FCA*;

(3) *COREPRU* 5 contains requirements relating to concentration risk;

(4) *COREPRU* 6 explains how a *firm* must calculate its *basic liquid assets requirement* in accordance with a quantified methodology prescribed by the *FCA*;

[*Editor's note*: additional chapters of COREPRU will be consulted on in a subsequent consultation.]

3 Own funds

3.1 Purpose and interpretation

Purpose

3.1.1 G This chapter explains how a *firm* must calculate its *own funds*. *Own funds* is the term the *FCA* commonly uses to describe a *firm's* regulatory capital.

Principles underlying the definition of own funds

3.1.2 G By requiring a *firm* to maintain an appropriate level of *own funds*, the *FCA* helps ensure that:

(1) a *firm* can absorb losses whilst continuing to operate as a going concern;

(2) a *firm* can absorb losses in *liquidation* in an orderly way that minimises harm to clients, markets and the wider financial system;

(3) *own funds* are calculated in a consistent and transparent way, allowing the *FCA* and other stakeholders to assess a *firm's* loss-absorbing capacity; and

(4) the interests of a *firm's* owners are appropriately aligned with the long-term interests of the *firm* itself.

Interpretation

3.1.3 R A *firm* must categorise and value its assets and off-balance sheet items in accordance with the applicable accounting framework, unless a *rule* specifies otherwise.

3.1.4 G Every provision in the *Handbook* must be interpreted in the light of its purpose (*GEN* 2.2.1R). A *firm* must therefore look beyond the legal form of its capital arrangements and consider their economic substance. This includes considering matters not set out in the terms of a capital instrument.

Mutual societies

3.1.5 G The *FCA* recognises that a mutual society may require modification of certain requirements in this chapter. The *FCA* will generally use the *own funds* rules for mutual societies in the *PRA Rulebook* as the starting point for such modifications, but will discuss this with relevant mutual societies.

3.2 Composition of own funds

3.2.1 G The *FCA* divides *own funds* into categories, or tiers, reflecting differences in the extent to which the capital concerned meet the purposes set out in *COREPRU* 3.1.2G.

3.2.2 R The *own funds* of a *firm* are the sum of its:

(1) *common equity tier 1 capital*;

(2) *additional tier 1 capital*; and

(3) *tier 2 capital*.

3.2.3 G The *FCA* generally prefers a *firm* to hold *common equity tier 1 capital* because it provides the highest quality of loss absorption and permanence. *Common equity tier 1 capital* can be used to meet a *firm's* capital requirements without limit. Other tiers of capital are subject to limits as set out in *COREPRU* 3.2.4R.

3.2.4 R A *firm* must, at all times, have *own funds* that satisfy all the following conditions:

(1) the *firm's common equity tier 1 capital* must be equal to or greater than 56% of the *firm's own funds requirement* under *COREPRU* 4.1;

(2) the sum of the *firm's common equity tier 1 capital* and *additional tier 1 capital* must be equal to or greater than 75% of the *firm's own funds requirement* under *COREPRU* 4.1; and

(3) the *firm's own funds* must be equal to or greater than 100% of the *firm's own funds requirement* under *COREPRU* 4.1.

3.3 Common equity tier 1 capital

3.3.1 G (1) *Common equity tier 1 capital* has the following core characteristics:

(a) it is able to absorb losses as they occur;

(b) it ranks below all other claims in *liquidation*;

(c) it is permanent;

(d) there is no obligation to make a *distribution*; and

(e) the level of *distributions* is not capped.

(2) The remainder of *COREPRU* 3.3 contains the detailed *rules* and *guidance* for calculating *common equity tier 1 capital*.

3.3.2 R A *firm* must calculate its *common equity tier 1 capital* in accordance with the first column of the following table. The second column indicates where relevant *rules* and *guidance* are found.

Item	Relevant rules and guidance
Common equity tier 1 items:	
(1) *common equity tier 1 instruments*;	*COREPRU* 3.3.3R to *COREPRU* 3.3.16R
(2) share premium accounts related to the *common equity tier 1 instruments*;	
(3) *retained earnings*;	
(4) interim or provisional year-end profits;	*COREPRU* 3.3.17R and *COREPRU* 3.3.18G
(5) *accumulated other comprehensive income*;	
(6) *other reserves*;	
Note: (3) to (6) may only be recognised as *common equity tier 1 items* if they are available to the *firm* for unrestricted and immediate use to cover risks or losses as soon as these occur.	
LESS	
Deductions from *common equity tier 1 items*:	*COREPRU* 3.3.19G
(7) losses for the current financial year;	*COREPRU* 3.3.20R
(8) *intangible assets*;	*COREPRU* 3.3.21R

(9) deferred tax assets that rely on future profitability;	*COREPRU* 3.3.22R
(10) defined benefit pension fund assets;	*COREPRU* 3.3.23R
(11) direct, indirect and synthetic holdings of own *common equity tier 1 instruments*;	*COREPRU* 3.3.24R, 3.3.30R and 3.3.31G
(12) direct, indirect and synthetic holdings of *common equity tier 1 or comparable instruments* of *financial sector entities* where those entities have a *reciprocal cross-holding* with the *firm*;	*COREPRU* 3.3.25R, *COREPRU* 3.3.26G, and *COREPRU* 3.3.29R to *COREPRU* 3.3.31G
(13) direct, indirect and synthetic holdings of *common equity tier 1 or comparable instruments* of *financial sector entities* which are not held in the *trading book*;	*COREPRU* 3.3.27R to *COREPRU* 3.3.31G
(14) any excess of AT1 deductions above the *firm's additional tier 1 capital*;	*COREPRU* 3.3.32R
(15) foreseeable tax charges relating to *common equity tier 1 items*;	*COREPRU* 3.3.33R
(16) *qualifying holdings* outside the financial sector;	*COREPRU* 3.3.34R
(17) (for *partnerships* or *limited liability partnerships*) excess withdrawals;	*COREPRU* 3.3.35R
(18) direct, indirect or synthetic holdings of *qualifying cryptoassets* issued by, or where the supply is controlled by, the *firm* or a connected entity;	*COREPRU* 3.3.36R and *COREPRU* 3.3.37G
ADJUSTED FOR	
Prudential filters for *common equity tier 1 capital*:	
(19) cash flow hedges and changes in the value of own liabilities due to own credit standing; and	*COREPRU* 3.3.38R and *COREPRU* 3.3.39G

(20) additional valuation adjustment for the *trading book*.	*COREPRU* 3.3.40R

Prior permission and notification of issuances of common equity tier 1 instruments

3.3.3 R (1) A *firm* must not classify an issuance of a capital instrument as a c*ommon equity tier 1 instrument* unless:

(a) it has obtained prior permission from the *FCA*; or

(b) (i) it is issuing new instruments on terms which are substantially the same as instruments for which the *firm* has already received the *FCA's* prior permission; and

(ii) it notifies the *FCA* sufficiently far in advance of classifying the new instruments as *common equity tier 1 instruments*.

(2) The *FCA* will grant the permission in (1)(a) if it is satisfied that the capital instrument meets the criteria in *COREPRU* 3.3.5R to *COREPRU* 3.3.16R.

3.3.4 G The *FCA* generally expects to receive a notification of a new issuance of an existing form of *common equity tier 1 instrument* under *COREPRU* 3.3.3R(1)(b)(ii) at least 20 *business days* before the *firm* intends to classify that issuance as *common equity tier 1 instruments*.

Common equity tier 1 instruments: loss absorption

3.3.5 R (1) A *common equity tier 1 instrument* must be classified as equity within the meaning of the applicable accounting framework.

(2) A *firm's* obligations under the instrument must not constitute a liability (including a contingent or prospective liability) that would be relevant for the purposes of section 123(2) of the Insolvency Act 1986.

(3) The holder of the instrument must not have any right, arising from the non-payment of any sums connected to the instrument, to petition for the winding up or administration of the *firm*, or any similar procedure.

(4) The instrument must not be secured by, or subject to, a guarantee or other arrangement which enhances the legal or economic seniority of the claim.

(5) (a) The *common equity tier 1 instruments* must rank below all other claims in the event of *liquidation*, except for claims from holders of other ordinary *shares* which rank pari passu with the instruments.

(b) The *common equity tier 1 instruments* must entitle their owners to a claim on the residual assets of the *firm* which, in the event of *liquidation* and after payment of all senior claims, is proportionate to the amount of such instruments issued and is not fixed or subject

to a cap, except that a claim specified as a percentage of residual assets does not constitute a fixed or capped claim.

(c) Each *common equity tier 1 instrument* must absorb losses to the same degree as all other *common equity tier 1 instruments*, and all *common equity tier 1 instruments* must absorb losses before any other *own funds instruments* issued by the *firm*.

3.3.6 R Whilst the conditions in *COREPRU* 3.3.5R(5) require *common equity tier 1 instruments* to absorb losses before any other *own funds instruments*, the fact that an *additional tier 1 instrument* or *tier 2 instrument* may be permanently written down does not prevent these conditions from being met.

3.3.7 R (1) A *common equity tier 1 instrument* must be fully paid and the proceeds of issue immediately and fully available to the *firm*.

(2) Where an instrument is partly paid, only the paid-up portion is eligible as a *common equity tier 1 instrument*.

3.3.8 G *COREPRU* 3.3.7R requires that the full amount of capital has been irrevocably received by the *firm*, is fully under the *firm's* control, and does not directly or indirectly expose the *firm* to the credit risk of the investor. This condition is stricter than the definition of fully paid in the Companies Act 2006, which may be met by an undertaking to pay.

3.3.9 R (1) A *common equity tier 1 instrument* must not be funded directly or indirectly by the *firm* itself.

(2) (1) does not apply if the funding is provided in the ordinary course of the *firm's* business.

3.3.10 G (1) *COREPRU* 3.3.9R prevents the artificial inflation of a *firm's own funds* by prohibiting a *firm* from funding its own capital instruments. This includes situations where:

(a) a *firm* grants a loan or other funding to an investor that is used to purchase the *firm's* own capital instruments;

(b) a *firm* grants any funding to an existing investor in its capital instruments;

(c) a *firm* provides a guarantee, enters into a credit derivative, or enters into some other form of arrangement so that the credit risk in a capital instrument is or may be transferred to the *firm*; or

(d) the funding in (a), (b) or (c) is provided to an external investor indirectly, for example by a member of the *firm's group* or via another intermediary.

(2) However, there is an exception for funding that is provided in the ordinary course of a *firm's* business. This covers situations where:

(a) funding is provided as part of a *firm's* normal trading or business operations;

(b) the terms are comparable to the terms the *firm* offers for third-party instruments; and

(c) the funding is not designed to support the *firm's* capital position.

(3) For example, a market maker providing standard margin lending that happens to involve the market maker's own capital instruments is likely to qualify for the exception. However, a structured arrangement specifically designed to fund purchases of the *firm's* capital instruments would not qualify.

Common equity tier 1 instruments: perpetuity

3.3.11 R (1) A *common equity tier 1 instrument* must be perpetual, with a *reduction of capital* only permissible where:

(a) the *firm* is in *liquidation*; or

(b) the *firm* carries out a *reduction of capital* which complies with *COREPRU* 3.6.4R or *COREPRU* 3.6.6R.

(2) A *firm* must not do anything to create an expectation that it will or might carry out a *reduction of capital* under (1)(b) when it issues the instrument, and the statutory or contractual terms of the instrument must not contain any feature which would or might give rise to such an expectation.

3.3.12 G (1) A *firm* generally has the right to carry out a *reduction of capital* under company law. However, *COREPRU* 3.6.4R requires that any *reduction of capital* is generally first approved by the *FCA*.

(2) The *FCA* recognises that relevant documentation may acknowledge the fact that a *firm* is able to carry out a *reduction of capital*. However, the *firm* must not create an expectation that it would or might carry out a *reduction of capital* when it issues the relevant instrument.

(3) An expectation that a *firm* would or might carry out a *reduction of capital* may be created by:

(a) a term which creates an economic incentive for the *firm* to carry out a *reduction of capital* at a particular point in time;

(b) a term which suggests that a *reduction of capital* may be carried out at a particular point in time, or at the initiative of any *person* other than the *firm*, even if this is conditional upon the approval of the *firm's management body* and the *FCA*; or

(c) any other contractual or non-contractual indication that the *firm* would or might carry out a *reduction of capital* on a particular date, or in particular circumstances.

Common equity tier 1 instruments: perpetuity, partnerships and limited liability partnerships

3.3.13 R (1) This *rule* applies to:

(a) a *partner's* account in a *firm* that is a *partnership*; and

(b) a member's account in a *firm* that is a *limited liability partnership*.

(2) References to a *partner* or a *partnership* in this *rule* include a member and a *limited liability partnership* respectively.

(3) A *partner's* account satisfies the conditions in *COREPRU* 3.3.11R if:

(a) capital contributed by *partners* is paid into the account; and

(b) the terms of the partnership agreement ensure that (otherwise than with prior *FCA* consent under *COREPRU* 3.6.4R or in the circumstances set out in *COREPRU* 3.6.6R) capital may only be withdrawn from the account by a *partner* ('A') if:

(i) A ceases to be a *partner* and an equal amount is contributed to another *partner's* account by A's former *partners* or any *person* replacing A as their *partner*;

(ii) any reduction in the capital credited to A's account is immediately offset by an equal contribution to other *partner* accounts by one or more of A's *partners* (including any *person* becoming a *partner* of A at the time that the additional contribution is made);

(iii) the *partnership* is wound up or dissolved; or

(iv) the *firm* ceases to be *authorised* or no longer has a *Part 4A permission*.

Common equity tier 1 instruments: distributions

3.3.14 R A *common equity tier 1 instrument* must meet the following conditions regarding *distributions* (subject to *COREPRU* 3.3.16R):

(1) the instrument must not provide or allow for the payment of preferential *distributions* over other *common equity tier 1 instruments* or any other capital instruments;

(2) the instrument must not include a cap on *distributions* or any other restriction on the maximum amount payable;

(3) the level of *distributions* must not be linked to the amount for which the instrument was purchased at issuance;

(4) there must be no circumstances in which *distributions* are obligatory, including where non-payment triggers some other obligation (for example, to make payments in kind); and

(5) failure to make *distributions* must not constitute an event of default.

3.3.15 G (1) *COREPRU* 3.3.14R(1) prohibits differentiated levels of *distributions*, or preferences in factors such as the order or timing of *distributions*, subject to the exception for instruments with fewer or no voting rights in *COREPRU* 3.3.16R.

(2) *COREPRU* 3.3.14R(5) means that a failure to make *distributions* must not have contractual or other consequences associated with an event of default, such as by engaging rights of termination, early repayment, additional voting rights, or other similar consequences.

Common equity tier 1 instruments: dividend multiples on instruments with fewer or no voting rights

3.3.16 R A *common equity tier 1 instrument* may pay a dividend multiple relative to another *common equity tier 1 instrument* if:

(1) the higher dividend multiple applies to *common equity tier 1 instruments* with fewer or no voting rights;

(2) the dividend multiple is set contractually or under the *firm's* constitution;

(3) the dividend multiple is not revisable;

(4) the same dividend multiple applies to all instruments with a dividend multiple;

(5) the dividend multiple is no more than 125% of the *distribution* on one voting *common equity tier 1 instrument*; and

(6) the total amount of *distributions* paid on all *common equity tier 1 instruments* during a 1-year period does not exceed 105% of the amount that would have been paid if instruments with fewer or no voting rights received the same *distributions* as voting instruments.

Inclusion of interim profits or provisional year-end profits in common equity tier 1 capital

3.3.17 R A *firm* must not include interim profits or year-end profits in its *common equity tier 1 capital* before its formal decision confirming final profit or loss for the year, unless:

(1) those profits have been verified by a *person* who is independent of the *firm* and is responsible for the auditing of the accounts of that *firm*;

(2) the verification provides an adequate level of assurance that those profits have been evaluated in accordance with the principles set out in the applicable accounting framework;

(3) the *firm* is satisfied that any foreseeable charge or dividend has been deducted from the amount of those profits on a prudent and conservative basis; and

(4) the *firm* notifies the *FCA* as soon as reasonably practicable after including the profits in its *common equity tier 1 capital*.

3.3.18 G (1) When deducting foreseeable dividends under *COREPRU* 3.3.17R(3), a *firm* should consider:

(a) any formal decisions about dividends that have been taken by the *firm's management body*;

(b) the upper end of any dividend policy;

(c) the ratio of dividends to income paid out in previous years; and

(d) any other factors that might reasonably affect the *firm's* approach to *distributions* for the relevant period.

(2) When deducting foreseeable charges under *COREPRU* 3.3.17R(3), a *firm* should consider:

(a) any tax charges attributable to the profits being verified;

(b) any other charges that are attributable to the relevant period but have not yet been reflected in the *firm's common equity tier 1 capital* calculation; and

(c) any other factors that might reasonably be expected to affect the final profit or loss figure for the period.

Deductions and filters for common equity tier 1 capital

3.3.19 G (1) Deductions and filters help to ensure that a *firm* measures its *own funds* in a way that reflects its ability to absorb losses in stressed conditions or *liquidation*.

(2) They achieve this by adjusting accounting values, for example because those values:

(a) are subject to significant valuation uncertainty;

(b) may not reflect realisable values in stressed conditions;

(c) include unrealised or market-value gains and losses that may reverse with changing market conditions; or

(d) are only realisable if the *firm* continues to operate as a going concern.

Deduction of losses for the current financial year

3.3.20 R (1) A *firm* must deduct losses for the current financial year, save where the losses have already resulted in a reduction in its *common equity tier 1 items*.

(2) For the purposes of (1), a *firm* must:

(a) apply the same accounting policies and standards as used for the year-end financial report;

(b) prudently estimate and assign income and expenses to the interim period in which they are incurred;

(c) recognise material or non-recurrent events in full and without delay in the interim period during which they arise; and

(d) determine profits, gains and losses, and deduct any resulting losses, as they arise.

Deduction of intangible assets

3.3.21 R (1) A *firm* must deduct *intangible assets*.

(2) For the purposes of (1):

(a) a *firm* must also deduct any *intangible assets* included in the valuation of its *qualifying holdings*;

(b) where the *qualifying holding* in (2)(a) is not wholly owned or controlled by the *firm*, the *firm* must only deduct the portion of *intangible assets* corresponding to its percentage of ownership or control; and

(c) a *firm* must reduce the amount to be deducted by the amount of associated deferred tax liabilities that would be extinguished if the *intangible assets* became impaired or were derecognised, under the applicable accounting framework.

Deduction of deferred tax assets that rely on future profitability

3.3.22 R (1) A *firm* must deduct deferred tax assets that rely on future profitability.

(2) For the purposes of (1):

(a) a *firm* may offset deferred tax liabilities against associated deferred tax assets if:

(i) the *firm* has a legally enforceable right to set off those current tax assets against current tax liabilities;

(ii) the deferred tax assets and the deferred tax liabilities arise from the same tax authority and for the same taxable entity; and

(iii) the deferred tax liabilities do not reduce the amount of *intangible assets* or defined pension fund assets deductible under *COREPRU* 3.3.21R or *COREPRU* 3.3.23R; and

(b) for the calculation of deferred tax assets and liabilities at consolidated level, a taxable entity includes any number of entities which are members of the same tax group, fiscal consolidation, fiscal unity or consolidated tax return.

Deduction of defined benefit pension fund assets on the firm's balance sheet

3.3.23 R (1) A *firm* must deduct the value of any defined benefit pension fund assets on its balance sheet.

(2) For the purposes of (1):

(a) a *firm* must net off pension fund assets against its obligations under the fund; and

(b) a *firm* must reduce the amount to be deducted by the amount of associated deferred tax liabilities which would be extinguished if the assets became impaired or were derecognised, under the applicable accounting framework.

Deduction of holdings of own common equity tier 1 instruments

3.3.24 R (1) A *firm* must deduct direct, indirect and synthetic holdings of its own *common equity tier 1 instruments*.

(2) For the purposes of (1):

(a) a *firm* must also apply the deduction where it could be obliged to purchase its own *common equity tier 1 instrument* as a result of an existing contractual obligation;

(b) a *firm* must deduct its gross long position unless (2)(c) applies; and

(c) a *firm* may deduct its net long position if:

(i) the long and short positions are in the same underlying exposure;

(ii) the short positions are cleared through an *authorised central counterparty* or subject to appropriate margining requirements; and

(iii) the long and short positions are both held in the *trading book* or are both held outside the *trading book*.

Deduction of holdings of common equity tier 1 or comparable instruments where a firm has a reciprocal cross-holding designed to inflate own funds artificially

3.3.25 R (1) A *firm* must deduct direct, indirect and synthetic holdings of the *common equity tier 1 or comparable instruments* of *financial sector entities* where those entities have a *reciprocal cross-holding* with the *firm* that is designed to inflate the *own funds* of the *firm* artificially.

(2) For the purposes of (1), a *firm* must deduct holdings based on its gross long position.

3.3.26 G The following factors indicate a *reciprocal cross-holding* designed to inflate *own funds* artificially:

(1) the cross-holding does not serve a genuine business purpose;

(2) the timing and circumstances of the cross-holding suggest an intention to boost regulatory capital; or

(3) other connections between relevant entities which might indicate coordinated capital management.

Deduction of holdings of common equity tier 1 or comparable instruments of financial sector entities

3.3.27 R (1) A *firm* must deduct direct, indirect and synthetic holdings of *common equity tier 1 or comparable instruments* of *financial sector entities* which are held outside of the *trading book*, unless *COREPRU* 3.3.28R applies.

(2) A *firm* must calculate holdings based on its gross long position unless (3) applies.

(3) A *firm* may calculate holdings based on its net long position where:

(a) (i) the maturity date of the short position is the same as, or longer than, the maturity date of the long position; or

(ii) the residual maturity of the short position is at least one year; and

(b) the long and short positions are held outside of the *trading book*.

Holdings of common equity tier 1 instruments issued by a financial sector entity within an investment firm group

3.3.28 R A *MIFIDPRU investment firm* is not required to deduct holdings of *common equity tier 1 instruments* of a *financial sector entity* under *COREPRU* 3.3.27R if all of the conditions in *MIFIDPRU* 3.3A.27R are met.

Common equity tier 1 or comparable instruments

3.3.29 R A *common equity tier 1 or comparable instrument* means:

(1) (for an entity subject to *COREPRU* or *MIFIDPRU*) a *common equity tier 1 instrument*;

(2) (for an *insurer* subject to the Solvency II Firms part of the *PRA Rulebook*) 'Tier 1 own funds' as defined in the Own Funds (Solvency II Firms) part of the *PRA Rulebook*, the inclusion of which is not restricted by Own Funds 4A.3 in the Solvency II Firms part of the *PRA Rulebook*; and

(3) (for a *financial sector entity* not subject to (1) or (2)) any capital instrument that ranks below all other claims in *liquidation*.

Identifying and valuing indirect and synthetic holdings

3.3.30 R For the purposes of *COREPRU* 3.3.24R, *COREPRU* 3.3.25R and *COREPRU* 3.3.27R:

(1) An indirect holding means an economic exposure through an intermediate entity such as a holding company or special purpose vehicle.

(2) A *firm* must calculate the amount to be deducted for indirect holdings by:

(a) identifying any intermediate entities or structures through which it may be exposed to a deductible *common equity tier 1 instrument*;

(b) making a prudent estimate of the full economic exposure of the intermediate entities or structures to deductible instruments; and

(c) deducting the proportion of economic exposure that is attributable to the *firm*.

(3) A *firm* is not required to treat a holding in a *fund* as an indirect holding.

(4) A synthetic holding means an economic exposure through a derivative instrument, guarantee, credit protection, or other similar arrangement.

(5) A *firm* must calculate the amount to be deducted for synthetic holdings by determining the maximum potential loss that would arise if the underlying deductible *common equity tier 1 instrument* or equivalent economic exposure had zero value, taking into account:

(a) all contractual obligations relating to the position; and

(b) any other features that could increase the *firm's* economic exposure.

3.3.31 G (1) *COREPRU* 3.3.30R explains how a *firm* should identify and value any indirect or synthetic holdings for the purposes of *COREPRU* 3.3.24R, *COREPRU* 3.3.25R and *COREPRU* 3.3.27R.

(2) The *FCA* generally considers it disproportionate to require a *firm* to look through a *fund* for these purposes, given the limited exposures to a *firm's* own capital instruments and those of other *financial sector entities* that are likely to arise through most *funds*.

(3) However, *COREPRU* 3.1.4G reminds *firms* to consider the economic substance of its capital arrangements. The *FCA* does not expect to see *firms* entering into arrangements intended to arbitrage this or other such concessions. Where a *fund* has a purpose or mandate to invest mainly in the capital instruments of *financial sector entities*, a *firm* should apply the relevant capital deductions accordingly.

Deduction of excess AT1 deductions

3.3.32 R A *firm* must deduct from *common equity tier 1 items* the amount by which any items required to be deducted from *additional tier 1 capital* under *COREPRU* 3.4.2R exceed *additional tier 1 items*.

Deduction of foreseeable tax charges relating to common equity tier 1 items

3.3.33 R (1) This deduction applies if a *firm* does not calculate its *own funds* in accordance with *UK-adopted international accounting standards*.

(2) Where this deduction applies, a *firm* must:

(a) deduct any foreseeable current and deferred tax charges relating to *common equity tier 1 items* that are not yet accounted for in its *common equity tier 1 capital*;

(b) calculate the amount to be deducted using the approach in *UK-adopted international accounting standards*; and

(c) deduct the amount of foreseeable current and deferred tax charges without netting off against any unrecognised deferred tax assets.

Deduction of qualifying holdings outside the financial sector

3.3.34 R (1) A *firm* must deduct any amounts in excess of the following limits:

(a) a *qualifying holding* in a *non-financial sector entity* which exceeds 15% of the *firm's own funds*; and

(b) the total of all the *qualifying holdings* of the *firm* in *non-financial sector entities* which exceeds 60% of the *firm's own funds*.

(2) When calculating the amounts in (1), a *firm* must treat a *fund* as a *non-financial sector entity*.

(3) When calculating the amounts in (1), a *firm* must exclude:

(a) shares held in the name of the *firm* on behalf of others; and

(b) shares held in the *trading book*.

Deduction of excess partnership withdrawals

3.3.35 R A *firm* that is a *partnership* or a *limited liability partnership* must deduct the amount by which the aggregate of any amounts withdrawn by its *partners* or members exceeds the profits of the *firm*, except to the extent that the amount:

(1) has already been deducted from the *firm's own funds* as a loss under *COREPRU* 3.3.20R;

(2) was repaid in accordance with *COREPRU* 3.3.13R(3); or

(3) is already reflected in a reduction of the *firm's own funds* that was permitted under *COREPRU* 3.6.4R or *COREPRU* 3.6.6R.

3.3.36 R (1) A *firm* must deduct any direct, indirect or synthetic holding of a *qualifying cryptoasset* issued by, or where supply is controlled by:

(a) the *firm*;

(b) a member of the same *group* as the *firm*;

(c) a *controller*, shareholder or member of the *firm*;

(d) a *director*, other *officer* or *employee* of the *firm*, or any member of the same *group* as the *firm*; or

(e) a *close relative* of a *person* falling within (c) or (d).

(2) (1) does not apply if:

(a) the *qualifying cryptoasset* is a *qualifying stablecoin* that is compliant with the requirements in *CASS* 16; or

(b) the *qualifying cryptoasset* is deducted in accordance with another *rule* in *COREPRU* 3.3.

3.3.37 G When considering whether it has control of supply of a *qualifying cryptoasset*, a *firm* should consider factors such as:

(1) any contractual or non-contractual arrangements which give the *firm* control of supply; and

(2) whether the *firm* holds a position in the relevant *qualifying cryptoasset* that enables it to behave independently of other market participants to control supply.

Adjustment for cash flow hedges and changes in the value of own liabilities

3.3.38 R A *firm* must exclude the following from its *common equity tier 1 items*:

(1) any unrealised gain or loss on cash flow hedges of financial instruments that are not measured at fair value, except where:

(a) the hedged item itself is measured at fair value; or

(b) the unrealised gain or loss represents effective net investment hedges of foreign operations; and

(2) any gain or loss arising from changes in the value of its liabilities that are due to changes in the *firm's* own credit standing.

3.3.39 G (1) *COREPRU* 3.3.38R(1) prevents unrealised gains or losses that arise from cash flow hedges from being included in *common equity tier 1 capital* where the hedged financial instruments are not measured at fair value. This filter is necessary because these hedge-related gains or losses may reverse over time, while not being matched by corresponding changes in the value of the hedged item in the regulatory capital calculation.

(2) *COREPRU* 3.3.38R(2) ensures that a deterioration in a *firm's* own creditworthiness does not increase its *common equity tier 1 capital*. For example, if a *firm's* creditworthiness deteriorates, this could result in the fair value of its liabilities decreasing, resulting in an accounting gain. This gain is counterproductive from a prudential perspective because the *firm's* financial condition is actually worsening. *COREPRU* 3.3.38R(2) filters this out to ensure capital reflects true loss-absorbing capacity.

Additional value adjustment for the trading book

3.3.40 R (1) A *firm* with a *trading book* must deduct the additional valuation adjustment in (2) from its *common equity tier 1 items*.

(2) A *firm* must calculate the additional valuation adjustment as 0.1% of the base value of positions in the *trading book*.

(3) The base value of positions in the *trading book* is the sum of the absolute value of fair-valued assets and liabilities stated in its financial statements under the applicable accounting framework, except that:

(a) exactly matching offsetting fair-valued assets and liabilities must be excluded;

(b) where a change in the accounting valuation of fair-valued assets and liabilities would only partially be reflected in *common equity*

tier 1 capital, the value of those assets or liabilities must only be included in proportion to the impact of the relevant valuation change on *common equity tier 1 capital*; and

(c) where a change in the accounting valuation of fair-valued assets and liabilities would have no impact on *common equity tier 1 capital*, the value of those assets or liabilities must be excluded.

3.4 Additional tier 1 capital

3.4.1 G (1) *Additional tier 1 capital* has the following core characteristics:

(a) it converts into *common equity tier 1 capital*, or is written down, upon the occurrence of one or more trigger events;

(b) it has no fixed maturity;

(c) there is no inescapable obligation to make a *distribution*; and

(d) *distributions* do not accelerate when the *firm* experiences stress.

(2) The remainder of *COREPRU* 3.4 contains the detailed *rules* and *guidance* for calculating *additional tier 1 capital*.

3.4.2 R A *firm* must calculate its *additional tier 1 capital* in accordance with the first column of the following table. The second column indicates where relevant *rules* and *guidance* are found.

Item	Relevant rules and guidance
Additional tier 1 items:	
(1) *additional tier 1 instruments*;	*COREPRU* 3.4.3R to *COREPRU* 3.4.16G
(2) share premium accounts related to the *additional tier 1 instruments*;	
LESS	
Deductions from *additional tier 1 items*:	
(3) direct, indirect and synthetic holdings of own *additional tier 1 instruments*;	*COREPRU* 3.4.17R and *COREPRU* 3.4.23R
(4) direct, indirect and synthetic holdings of *additional tier 1 or comparable instruments* of *financial sector entities* where those entities have a *reciprocal cross-holding* with the *firm*;	*COREPRU* 3.4.18R, *COREPRU* 3.4.19G, *COREPRU* 3.4.22R and *COREPRU* 3.4.23R

(5) direct, indirect and synthetic holdings of *additional tier 1 or comparable instruments* of *financial sector entities* which are not held in the *trading book*;	*COREPRU* 3.4.20R to *COREPRU* 3.4.23R
(6) any excess of tier 2 deductions above the *firm's tier 2 capital*; and	*COREPRU* 3.4.24R
(7) foreseeable tax charges relating to *additional tier 1 items*.	*COREPRU* 3.4.25R

Additional tier 1 instruments: loss absorption

3.4.3 R (1) If one or more trigger events occurs, the full principal amount of the *additional tier 1 instrument* must be written down on a permanent or temporary basis, or the instrument converted into a *common equity tier 1 instrument*, in accordance with the requirements of *COREPRU* 3.4.9R to *COREPRU* 3.4.12R.

(2) A *firm's* obligations under the instrument must not constitute a liability (including a contingent or prospective liability) that would be relevant for the purposes of section 123(2) of the Insolvency Act 1986.

(3) An *additional tier 1 instrument* must not be secured or subject to a guarantee or other arrangement which enhances the legal or economic seniority of the claim.

(4) The instrument must rank below any *tier 2 instrument* in *liquidation*.

(5) The instrument must not be subject to set-off or netting arrangements that would undermine its capacity to absorb losses.

(6) The provisions governing the instrument must not include any feature that could hinder the recapitalisation of the *firm*.

3.4.4 G For the purposes of *COREPRU* 3.4.3R(6), a feature that could hinder the recapitalisation of the *firm* includes:

(1) a provision that requires the *firm* to compensate existing holders of capital instruments where a new capital instrument is issued; and

(2) other terms that could discourage the *firm* from issuing new capital instruments for recapitalisation.

3.4.5 R (1) An *additional tier 1 instrument* must be fully paid and the proceeds of issue must be immediately and fully available to the *firm*.

(2) Where an instrument is partly paid, only the paid-up portion is eligible as an *additional tier 1 instrument*.

3.4.6 G *COREPRU* 3.3.8G applies to *additional tier 1 instruments* as it applies to *common equity tier 1 instruments*.

3.4.7 R (1) An *additional tier 1 instrument* must not be funded directly or indirectly by the *firm* itself.

(2) (1) does not apply if the funding is provided in the ordinary course of the *firm's* business.

3.4.8 G *COREPRU* 3.3.10G applies to *additional tier 1 instruments* as it applies to *common equity tier 1 instruments*.

Additional tier 1 instruments: Trigger events

3.4.9 R (1) A *firm* must specify one or more trigger events in the terms of an *additional tier 1 instrument*.

(2) The trigger events specified under (1) must include a trigger event that occurs where the *common equity tier 1 capital* of the *firm* falls below a level specified by the *firm* that is no lower than 64% of the *firm's own funds requirement*.

(3) The full principal amount of an *additional tier 1 instrument* must be written down or converted when a trigger event occurs.

(4) The amount recognised for *additional tier 1 instruments* and any associated share premium accounts must not exceed the amount of *common equity tier 1 items* that would be generated if there was a write down or conversion.

(5) Where a trigger event occurs, a *firm* must:

(a) convene the *management body* or other *relevant body* without delay to determinate that a trigger event has occurred;

(b) immediately inform the *FCA*;

(c) inform the holders of the *additional tier 1 instruments*; and

(d) write down or convert the instruments without delay, and within 1 *month*.

3.4.10 G (1) *COREPRU* 3.4.9R requires that the principal amount of an *additional tier 1 instrument* converts into *common equity tier 1 instruments* or is written down if the *firm's common equity tier capital* falls below a specified level.

(2) This level must be set at no lower than 64% of the *firm's own funds requirement* but a *firm* may set the relevant trigger at a higher level (such as 70% of its *own funds requirement*) if it wishes.

(3) A *firm* may also specify additional trigger events alongside the required trigger event in *COREPRU* 3.4.9R(2).

Additional tier 1 instruments: write down

3.4.11 R Where a *firm* issues *additional tier 1 instruments* that write down:

(1) the write-down must extinguish:

(a) the claim of the holder in *liquidation*;

(b) any amount required to be paid in the event of call or redemption of the instrument; and

(c) any *distribution* on the instrument;

(2) the write-down must apply to all holders of *additional tier 1 instruments* that include the same trigger; and

(3) in the case of a write-up after temporary write-down:

(a) any write-up must be based on profits after the *firm* has taken a formal decision confirming the final profits;

(b) any write-up must be at the full discretion of the *firm* (subject to (3)(c) to (3)(e) below), and there must be no obligation on the *firm* to operate or accelerate a write-up under specific circumstances;

(c) write-up must be operated on a pro rata basis among *additional tier 1 instruments* with the same trigger that was subject to write-down;

(d) the maximum amount that can be written up must be calculated using the formula:

M = P * A/T

where:

- M = the maximum amount that can be written up;
- P = the profit of the *firm*;
- A = the aggregate nominal value (before write-down) of all *additional tier 1 instruments* that were subject to a write-down; and
- T = the sum of the *common equity tier 1 capital* and *additional tier 1 capital* of the *firm*; and

(e) any write-up amount must be treated as a payment that reduces the *firm's common equity tier 1 capital*.

Additional tier 1 instruments: conversion into common equity tier 1

3.4.12 R Where a *firm* issues *additional tier 1 instruments* that convert into *common equity tier 1 instruments*, it must:

(1) specify in the provisions governing the *additional tier 1 instruments* either:

(a) the rate of such conversion; or

(b) a range within which the instruments will convert into *common equity tier 1 instruments*;

(2) retain all necessary authorisations for converting all of its *additional tier 1 instruments* into *common equity tier 1 instruments*; and

(3) ensure there are no procedural impediments to conversion under its constitutional or contractual arrangements.

Additional tier 1 instruments: perpetuity

3.4.13 R (1) An *additional tier 1 instrument* must be perpetual, with a *reduction of capital* only permissible where:

(a) the *firm* is in *liquidation*; or

(b) the *firm* carries out a *reduction of capital* which:

(i) complies with *COREPRU* 3.6.4R or *COREPRU* 3.6.6R; and

(ii) does not take place before 5 years after the date of issuance, unless the conditions in *COREPRU* 3.6.6R(1) or (2) are met.

(2) The *additional tier 1 instrument* must not include any incentive for the *firm* to carry out a *reduction of capital*.

(3) A *firm* must not explicitly or implicitly indicate that the *additional tier 1 instrument* would be redeemed or repaid other than in *liquidation*, and the terms of the instrument must not provide such an indication.

(4) Where the *additional tier 1 instrument* includes one or more early redemption options including call options, the options must be exercisable at the sole discretion of the *firm*.

(5) A *firm* must not indicate explicitly or implicitly that the *FCA* would consent to a *reduction of capital*.

3.4.14 G (1) An incentive to carry out a *reduction of capital* in *COREPRU* 3.4.13R(2) includes any feature that provides, at the date of issuance of a capital instrument, an expectation that the capital instrument is likely to be redeemed.

(2) Examples of (1) include:

(a) a term which creates an economic incentive for the *firm* to carry out a *reduction of capital* at a particular point in time; and

(b) marketing of the instrument in a way which suggests to investors that the instrument will be called.

Additional tier 1 instruments: distributions

3.4.15 R An *additional tier 1 instrument* must meet the following conditions regarding *distributions*:

(1) the *firm* must at all times have full discretion to cancel *distributions* on the instruments for an unlimited period and on a non-cumulative basis;

(2) the *firm* must be able to use cancelled *distributions* to meet its obligations as they fall due, without restriction;

(3) failure to make *distributions* must not constitute an event of default;

(4) the *additional tier 1 instrument* must not include a requirement:

(a) to make a *distribution* in the event of a *distribution* being made on another instrument that ranks the same or more junior;

(b) that, if a *distribution* is not made on that instrument, a *distribution* cannot be made on another capital instrument; or

(c) substituting the obligation to make a *distribution* with any other obligation to make payment in any other form; and

(5) the level of *distribution* must not change in a way that is linked to the credit standing of the *firm* or any member of the *firm's group*;

3.4.16 G *COREPRU* 3.4.15R(3) means that a failure to make *distributions* must not have contractual or other consequences associated with an event of default, such as by engaging rights of termination, early repayment, additional voting rights, or other similar consequences.

Deduction of holdings of own additional tier 1 instruments

3.4.17 R (1) A *firm* must deduct direct, indirect and synthetic holdings of its own *additional tier 1 instruments*.

(2) For the purposes of (1):

(a) a *firm* must also apply the deduction where it could be obliged to purchase the *additional tier 1 instrument* as a result of an existing contractual obligation;

(b) a *firm* must deduct its gross long position unless (2)(c) applies; and

(c) a *firm* may deduct its net long position if:

(i) the long and short positions are in the same underlying exposure;

(ii) the short positions are cleared through an *authorised central counterparty* or subject to appropriate margining requirements; and

(iii) the long and short positions are both held in the *trading book* or are both held outside of the *trading book*.

Deduction of holdings of additional tier 1 or comparable instruments where a firm has a reciprocal cross-holding designed to inflate own funds artificially

3.4.18 R (1) A *firm* must deduct direct, indirect and synthetic holdings of the *additional tier 1 or comparable instruments* of *financial sector entities* where those entities have a *reciprocal cross-holding* with the *firm* designed to inflate the *own funds* of the *firm* artificially.

(2) For the purposes of (1), a *firm* must calculate holdings based on its gross long position.

3.4.19 G The factors in *COREPRU* 3.3.26G indicate a *reciprocal cross-holding* designed to inflate *own funds* artificially.

Deduction of holdings of additional tier 1 or comparable instruments of financial sector entities

3.4.20 R (1) A *firm* must deduct direct, indirect and synthetic holdings of *additional tier 1 or comparable instruments* of *financial sector entities* which are held outside of the *trading book*, unless *COREPRU* 3.4.21R applies.

(2) A *firm* must calculate holdings based on its gross long position unless (3) applies.

(3) A *firm* may calculate holdings based on its net long position where:

(a) (i) the maturity date of the short position is the same or later than the maturity date of the long position; or

(ii) the residual maturity of the short position is at least one year; and

(b) the long and short positions are held outside of the *trading book*.

Holdings of additional tier 1 instruments issued by a financial sector entity within an investment firm group

3.4.21 R A *MIFIDPRU investment firm* is not required to deduct holdings of *additional tier 1 instruments* of a *financial sector entity* under *COREPRU* 3.4.20R if all of the conditions in *MIFIDPRU* 3.4A.21R are met.

Additional tier 1 or comparable instruments

3.4.22 R An *additional tier 1 or comparable instrument* means:

(1) (for an entity subject to *COREPRU* or *MIFIDPRU*) an *additional tier 1 instrument*;

(2) (for an *insurer* subject to the Solvency II Firms part of the *PRA Rulebook*) 'Tier 1 own funds' as defined in the Own Funds (Solvency II) part of the *PRA Rulebook*, the inclusion of which is restricted by Own Funds 4A.3 in the Solvency II Firms part of the *PRA Rulebook*; and

(3) (for a *financial sector entity* not subject to (1) or (2)) any capital instrument that does not rank below all other claims in *liquidation* but absorbs losses on a going concern basis.

Identifying and valuing indirect and synthetic holdings

3.4.23 R *COREPRU* 3.3.30R (Identifying and valuing indirect and synthetic holdings) applies to holdings of *additional tier 1 instruments* as it applies to holdings of *common equity tier 1 instruments*.

Deduction of excess T2 deductions

3.4.24 R A *firm* must deduct from *additional tier 1 items* the amount by which any items required to be deducted from *tier 2 items* under *COREPRU* 3.5.2R exceed *tier 2 items*.

Deduction of foreseeable tax charges relating to additional tier 1 items

3.4.25 R (1) This deduction applies if a *firm* does not calculate its *own funds* in accordance with *UK-adopted international accounting standards*.

(2) Where this deduction applies, a *firm* must:

(a) deduct any current and deferred tax charges relating to *additional tier 1 items* that are not yet accounted for in its *common equity tier 1 capital*;

(b) calculate the amount to be deducted using the approach in *UK-adopted international accounting standards*; and

(c) deduct the amount of foreseeable current and deferred tax charges without netting off against any unrecognised deferred tax assets.

3.5 Tier 2 capital

3.5.1 G (1) *Tier 2 capital* has the following core characteristics:

(a) it ranks below ordinary creditors in *liquidation*;

(b) it has an original maturity of at least 5 years;

(c) it amortises over the final 5 years; and

(d) *distributions* do not accelerate when the *firm* experiences stress.

(2) The remainder of *COREPRU* 3.5 contains detailed *rules* and *guidance* for calculating *tier 2 capital*.

3.5.2 R A *firm* must calculate its *tier 2 capital* in accordance with the first column of the following table. The second column indicates where relevant *rules* and *guidance* are found.

Item	**Relevant rules and guidance**
Tier 2 items:	
(1) *tier 2 instruments*;	*COREPRU* 3.5.3R to *COREPRU* 3.5.11R
(2) share premium accounts related to the *tier 2 instruments*;	
LESS	
Deductions from *tier 2 items*:	
(3) direct, indirect and synthetic holdings of own *tier 2 instruments*;	*COREPRU* 3.5.12R and *COREPRU* 3.5.18R
(4) direct, indirect and synthetic holdings of *tier 2 or comparable instruments* of *financial sector entities* where those entities have a *reciprocal cross-holding* with the *firm*; and	*COREPRU* 3.5.13R, *COREPRU* 3.5.14G, *COREPRU* 3.5.17R and *COREPRU* 3.5.18R
(5) direct, indirect and synthetic holdings of *tier 2 or comparable instruments* of *financial sector entities* which are not held in the *trading book*.	*COREPRU* 3.5.15R to *COREPRU* 3.5.18R

Tier 2 instruments: loss absorption

3.5.3 R (1) The claim on the principal amount of a *tier 2 instrument* must be wholly subordinated to the claims of all non-subordinated creditors.

(2) A *tier 2 instrument* must not be secured or subject to a guarantee or other arrangement which enhances the legal or economic seniority of the claim.

(3) A *tier 2 instrument* must not be subject to set-off or netting arrangements that would undermine its capacity to absorb losses.

3.5.4 R (1) A *tier 2 instrument* must be fully paid and the proceeds of issue immediately and fully available to the *firm*.

(2) Where an instrument is partly paid, only the paid-up portion is eligible as a *tier 2 instrument*.

3.5.5 G *COREPRU* 3.3.8G applies to *tier 2 instruments* as it applies to *common equity tier 1 instruments*.

3.5.6 R (1) A *tier 2 instrument* must not be funded directly or indirectly by the *firm* itself.

(2) (1) does not apply if the funding is provided in the ordinary course of the *firm's* business.

3.5.7 G *COREPRU* 3.3.10G applies to *tier 2 instruments* as it applies to *common equity tier 1 instruments*.

Tier 2 instruments: duration

3.5.8 R (1) A *tier 2 instrument* must have an original maturity of at least 5 years, with a *reduction of capital* prior to maturity only permissible where:

(a) the *firm* is in *liquidation*; or

(b) the *firm* carries out a *reduction of capital* which:

(i) has been approved by the *FCA* under *COREPRU* 3.6.4R; and

(ii) does not take place before 5 years after the date of issuance, unless the conditions in *COREPRU* 3.6.6R(1) or (2) are met.

(2) A *tier 2 instrument* must not include any incentive for the principal amount to be redeemed or repaid prior to maturity, or a right to accelerate early redemption or repayment.

(3) A *firm* must not explicitly or implicitly indicate that the *tier 2 instrument* would be redeemed or repaid prior to maturity other than in *liquidation*, and the terms of the instrument must not provide such an indication.

(4) Where the *tier 2 instrument* includes one or more early redemption options including call options, the options must be exercisable at the sole discretion of the *firm*.

3.5.9 G (1) An incentive for the principal amount to be redeemed or repaid in *COREPRU* 3.5.8R(2) includes any feature that provides, at the date of issuance of a capital instrument, an expectation that the capital instrument is likely to be redeemed before its stated maturity date.

(2) An incentive under (1) includes:

(a) a term which creates an economic incentive for the *firm* to reduce or repay the principal before maturity; and

(b) marketing of the instrument in a way which suggests to investors that the instrument will be called before maturity.

Tier 2 instruments: amortisation

3.5.10 R Where a *tier 2 instrument* has a residual maturity of 5 years or less, the proportion of the instrument which qualifies as a *tier 2 item* must be calculated by multiplying A and B, where:

- A is the notional amount of the instrument on the first day of the final 5-year period of their contractual maturity divided by the number of *days* in that period; and
- B is the number of remaining *days* of contractual maturity of the instrument.

Tier 2 instruments: distributions

3.5.11 R A *tier 2 instrument* must meet the following conditions regarding *distributions*:

(1) the holder of the instrument must have no right to accelerate the future scheduled payment of *distributions*, other than in *liquidation*; and

(2) the level of *distribution* must not change in a way that is linked to the credit standing of the *firm* or any member of the *firm's group*.

Deduction of holdings of own tier 2 instruments

3.5.12 R (1) A *firm* must deduct direct, indirect and synthetic holdings of its own *tier 2 instruments*.

(2) For the purposes of (1):

(a) a *firm* must also apply the deduction where it could be obliged to purchase the *tier 2 instrument* as a result of an existing contractual obligation;

(b) a *firm* must deduct its gross long position unless (2)(c) applies; and

(c) a *firm* may deduct its net long position if:

(i) the long and short positions are in the same underlying exposure;

(ii) the short positions are cleared through an *authorised central counterparty* or subject to appropriate margining requirements; and

(iii) the long and short positions are both held in the *trading book* or are both held outside of the *trading book*.

Deduction of holdings of tier 2 or comparable instruments where a firm has a reciprocal cross-holding designed to inflate own funds artificially

3.5.13 R (1) A *firm* must deduct direct, indirect and synthetic holdings of the *tier 2 or comparable instruments* of *financial sector entities* where those entities have a *reciprocal cross-holding* with the *firm* designed to inflate the *own funds* of the *firm* artificially.

(2) For the purposes of (1), a *firm* must calculate holdings based on its gross long position.

3.5.14 G The factors in *COREPRU* 3.3.26G indicate a *reciprocal cross-holding* designed to inflate *own funds* artificially.

Deduction of holdings of tier 2 or comparable instruments of financial sector entities

3.5.15 R (1) A *firm* must deduct direct, indirect and synthetic holdings of *tier 2 or comparable instruments* of *financial sector entities* which are held outside of the *trading book*, unless *COREPRU* 3.5.16R applies.

(2) A *firm* must calculate holdings based on its the gross long position unless (3) applies.

(3) A *firm* may calculate holdings based on its net long positions where:

(a) (i) the maturity date of the short position is the same or later than the maturity date of the long position; or

(ii) the residual maturity of the short position is at least 1 year; and

(b) the long and short positions are held outside of the *trading book*.

Holdings of tier 2 instruments issued by a financial sector entity within an investment firm group

3.5.16 R A *MIFIDPRU investment firm* is not required to deduct holdings of *tier 2 instruments* of a *financial sector entity* under *COREPRU* 3.5.15R if all of the conditions in *MIFIDPRU* 3.5A.16R are met.

Tier 2 or comparable instruments

3.5.17 R A *tier 2 or comparable instruments* means:

(1) (for an entity subject to *COREPRU* or *MIFIDPRU*) a *tier 2 instrument*;

(2) (for an *insurer* subject to the Solvency II Firms part of the *PRA Rulebook*):

(a) 'Tier 2 basic own funds' as defined in the Own Funds (Solvency II Firms) part of the *PRA Rulebook*; and

(b) 'Tier 3 own funds' that are 'basic own funds' as those terms are defined in the Own Funds (Solvency II Firms) part of the *PRA Rulebook*; and

(3) (for a *financial sector entity* not subject to (1) or (2)) any subordinated instrument that does not absorb losses on a going-concern basis.

Identifying and valuing indirect and synthetic holdings

3.5.18 R *COREPRU* 3.3.30R (Identifying and valuing indirect and synthetic holdings) applies to holdings of *tier 2 instruments* as it applies to holdings of *common equity tier 1 instruments*.

3.6 General requirements for own funds instruments

3.6.1 R An *own funds instrument* must not provide or allow for the payment of *distributions* in a form other than cash or *own funds instruments*.

3.6.2 R For the purposes of the deductions in *COREPRU* 3.3.24R, *COREPRU* 3.3.27R, *COREPRU* 3.4.17R, *COREPRU* 3.4.20R, *COREPRU* 3.5.12R and *COREPRU* 3.5.15R, a *firm* may reduce the amount of a long position in a capital instrument by the portion of a short position in an index that is made up of the same underlying exposure, provided that:

(1) the positions are either both held in the *trading book*, or are both held outside of the *trading book*; and

(2) the positions are held at fair value on the *firm's* balance sheet.

3.6.3 R An *own funds instrument* and any associated share premium account immediately ceases to count towards *own funds* if it ceases to meet any applicable requirement in *COREPRU* 3.

Reduction of own funds instruments

3.6.4 R Save in the circumstances set out in *COREPRU* 3.6.6R, a *firm* must obtain the prior permission of the *FCA* to:

(1) carry out a *reduction of capital* in relation to any of its *common equity tier 1 instruments*;

(2) reduce, distribute or reclassify as another *own funds* item the share premium accounts related to any of its *own funds instruments*;

(3) carry out a *reduction of capital* in relation to an *additional tier 1 instrument*, whether on a call date or otherwise; or

(4) carry out a *reduction of capital* in relation to a *tier 2 instrument* prior to maturity.

3.6.5 R The *FCA* will grant the permission in *COREPRU* 3.6.4R if it is satisfied that the *firm* will continue to exceed its *own funds threshold requirement* by a margin sufficient to ensure adequate financial resilience for the foreseeable future.

3.6.6 R A *firm* is not required to obtain the permission in *COREPRU* 3.6.4R if:

(1) the instrument is being repurchased for market making purposes; or

(2) all of the following conditions are met:

(a) either of the conditions in *COREPRU* 3.6.7R are met;

(b) at least 20 *business days* before the *day* on which the *reduction of capital* is proposed to occur, the *firm* has notified the *FCA* of:

(i) the proposed *reduction of capital*; and

(ii) the basis on which the *firm* has concluded that either condition in (2)(a) is satisfied; and

(c) the *FCA* has not notified the *firm* of any objection to the proposal before the *day* on which the *reduction of capital* is proposed to occur.

3.6.7 R The conditions referred to in *COREPRU* 3.6.6R(2)(a) are that:

(1) before or at the same time as the *reduction of capital*, the *firm* replaces the relevant *own funds instruments* with *own funds instruments* of equal or higher quality on terms that are sustainable for the income capacity of the *firm*, so that:

(a) the profitability of the *firm* will continue to be sound and will not see any negative change in the foreseeable future after the replacement of the original *own funds instruments* with *own funds instruments* of equal or higher quality; and

(b) the assessment of profitability in the foreseeable future in (1)(a) takes into account the *firm's* profitability in stressed situations; or

(2) the *firm* is redeeming *additional tier 1 instruments* or *tier 2 instruments* within 5 years of their date of issue and either:

(a) there is a change in the regulatory classification of the instruments that is likely to result in their exclusion from *own funds* or reclassification as a lower quality form of *own funds*, and both the following conditions are met:

(i) there are reasonable grounds to conclude that the change is sufficiently certain; and

(ii) the regulatory reclassification of the instruments was not reasonably foreseeable at the time of their issuance; or

(b) there is a change in the applicable tax treatment of those instruments which is material and was not reasonably foreseeable at the time of their issuance.

Notification of issuance of additional tier 1 and tier 2 instruments

3.6.8 R (1) A *firm* must notify the *FCA* at least 20 *business days* before the intended issuance date of the *firm's* intention to issue:

(a) *additional tier 1 instruments*; or

(b) *tier 2 instruments*.

(2) The notification requirement in (1) does not apply if:

(a) the *firm* has previously notified the *FCA* of an issuance of the same class of *additional tier 1 instruments* or *tier 2 instruments*; and

(b) the terms of the new instruments are identical in all material respects to the terms of the instruments in the issuance previously notified to the *FCA*.

(3) The notification under (1) must include the following:

(a) confirmation of whether the instruments are intended to be classified as *additional tier 1 instruments* or *tier 2 instruments*;

(b) confirmation of whether the instruments are intended to be issued to external investors or only to other members of the *firm's group* or connected parties;

(c) a copy of the term sheet and details of any features of the capital instrument which are novel, unusual or different from a capital instrument of a similar nature previously issued by the *firm* or widely available in the market;

(d) confirmation from a member of the *firm's senior management* or *governing body* who has oversight of the intended issuance that the instrument meets the conditions in *COREPRU* 3.4 or

COREPRU 3.5 (as applicable) to be classified as *additional tier 1 instruments* or *tier 2 instruments*; and

(e) a properly reasoned legal opinion from an appropriately qualified *individual*, confirming that the capital instruments meet the conditions in (3)(d).

3.6.9 G *Firms* that are proposing to classify an issuance of capital instruments as *common equity tier 1 capital* should refer to the obligations and *guidance* in *COREPRU* 3.3.3R and *COREPRU* 3.3.4G. In particular, *firms* must obtain the *FCA's* prior permission for the first issuance of a class of instruments that is intended to comprise *common equity tier 1 capital*.

3.6.10 G Submitting a notification in accordance with *COREPRU* 3.6.8R does not guarantee that the relevant instruments meet the required conditions in *COREPRU* 3.4 or *COREPRU* 3.5 to qualify as *own funds*. The *firm* or *parent undertaking* must ensure that an instrument continues to meet the conditions to be counted as *own funds*, including if its terms are varied on a later date.

4 Own funds requirements

4.1 Own funds requirement

4.1.1 R A *firm* must at all times maintain *own funds* that are at least equal to its *own funds requirement*.

4.1.2 R The *own funds requirement* is the highest of:

(1) the *permanent minimum capital requirement*;

(2) the *fixed overheads requirement*; or

(3) the *K-factor requirement*.

4.1.3 G *Authorised payment institutions* and *electronic money institutions* who are also subject to *COREPRU* should note that they need to meet any capital requirements imposed under the *Payment Services Regulations* and the *Electronic Money Regulations* separately and in addition to any applicable *own funds requirement*.

4.2 Permanent minimum capital requirement

4.2.1 R The *permanent minimum capital requirement* is the highest of the applicable requirements in the following table:

Category of firm	Applicable requirement
A *CRYPTOPRU firm*	The applicable requirement in *CRYPTOPRU* 4.2.1R (Permanent minimum capital requirement)

A *MIFIDPRU investment firm*	The applicable requirement in *MIFIDPRU* 4.4 (Permanent minimum capital requirement)

4.3 Fixed overheads requirement

4.3.1 R (1) The *fixed overheads requirement* is an amount equal to one quarter of a *firm's relevant expenditure* during the preceding year.

(2) When calculating its *fixed overheads requirement* in (1), a *firm* must use the figures resulting from the accounting framework applied in accordance with *COREPRU* 4.3.2R.

(3) This *rule* is subject to *COREPRU* 4.3.5R and *COREPRU* 4.3.7R.

4.3.2 R (1) For the purposes of the calculation in *COREPRU* 4.3.1R, a *firm* must use the figures in its most recent:

(a) audited *annual financial statements*; or

(b) unaudited *annual financial statements*, where audited *annual financial statements* are not available.

(2) If a *firm* has used unaudited *annual financial statements* in accordance with (1)(b) and audited *annual financial statements* subsequently become available, the *firm* must update the calculation in *COREPRU* 4.3.1R using the audited figures.

(3) Where the financial statements in (1) do not cover a 12-*month* period, the *firm* must:

(a) divide the amounts included in those statements by the number of *months* the financial statements cover; and

(b) multiply the result of the calculation in (3)(a) by 12 to produce an equivalent annual amount.

4.3.3 R (1) For the purpose of *COREPRU* 4.3.1R(1), a *firm* must calculate its *relevant expenditure* by:

(a) calculating the *firm's* total expenditure before distribution of profits; and

(b) deducting any of the items in (2) from the total expenditure in (1)(a) to the extent that those items have been included in the expenditure.

(2) The items that a *firm* may deduct from its total expenditure are:

(a) any of the following, if they are fully discretionary:

(i) staff bonuses and other variable *remuneration*;

(ii) *employees'*, *directors'*, *partners'* and *limited liability partnership* members' shares in profits; and

(iii) other appropriations of profits;

(b) shared commission and fees payable that meet all of the following conditions:

(i) they are directly related to commission and fees receivable;

(ii) the commission and fees receivable are included within total revenue; and

(iii) the payment of the commission and fees payable is contingent on receipt of the commission and fees receivable;

(c) non-recurring expenses from non-ordinary activities;

(d) taxes where they fall due in relation to the annual profits of the *firm*;

(e) payments related to contract-based profit and loss transfer agreements according to which the *firm* is obliged to transfer its annual profit to the *parent undertaking* following the preparation of the *firm's annual financial statements*;

(f) other expenses, to the extent that their value has already been reflected in a deduction from *own funds* under *COREPRU* 3; and

(g) (for a *MIFIDPRU investment firm*) any other deductions permissible under *MIFIDPRU* 4.5.3R and *MIFIDPRU* 4.5.4R.

Expenses incurred on behalf of the firm by third parties

4.3.4 R (1) A *firm* must add any fixed expenses that have been incurred on its behalf by a third party to the *firm's* total expenditure for the purposes of *COREPRU* 4.3.3R in accordance with this *rule*.

(2) A *firm* is not required to add fixed expenses which are already included in the figures resulting from *COREPRU* 4.3.3R.

(3) Where a breakdown of the third party's expenses is available, the *firm* must add its share of the third party's expenses.

(4) Where a breakdown of the third party's expenses is not available, the *firm* must:

(a) add its share of the third party's expenses as projected in the *firm's* business plan; or

(b) (if the *firm* does not have a business plan that projects the third party's expenses) reasonably estimate the share of those expenses that are attributable to the *firm's* business and add that estimated share of expenses to the *firm's* total expenditure.

Material change to projected relevant expenditure during the year

4.3.5 R (1) This *rule* applies where:

(a) there is an increase of 30% or more in the *firm's* projected *relevant expenditure* for the current year; or

(b) there would be an increase of £2 million or more in the *firm's fixed overheads requirement* based on projected *relevant expenditure* for the current year.

(2) Where this *rule* applies, a *firm* must:

(a) immediately recalculate its *fixed overheads requirement* by applying the methodology in *COREPRU* 4.3.3R to the projected *relevant expenditure*, taking into account the increase in (1);

(b) immediately substitute the revised *fixed overheads requirement* that results from the calculation in (2)(a) for the *firm's* previous *fixed overheads requirement* under *COREPRU* 4.3.1R(1); and

(c) immediately recalculate its *basic liquid assets requirement* using the revised *fixed overheads requirement* in (2)(b) and substitute the updated amount for its previous *basic liquid assets requirement*.

4.3.6 G (1) Where there is a material increase in the *firm's* projected *relevant expenditure* that triggers the obligation in *COREPRU* 4.3.5R, a *firm* should also consider the potential impact on its *ICARA process* and the conclusions documented in its last *ICARA document*.

(2) The review in (1) is particularly important if the *firm's own funds requirement* was determined by the *fixed overheads requirement* immediately before the change occurred.

4.3.7 R (1) This *rule* applies where:

(a) there is a decrease of 30% or more in the *firm's* projected *relevant expenditure* for the current year; or

(b) there would be a decrease of £2 million or more in the *firm's fixed overheads requirement* based on projected *relevant expenditure* for the current year.

(2) Where this *rule* applies, a *firm* may:

(a) recalculate its *fixed overheads requirement* by applying the methodology in *COREPRU* 4.3.3R to the projected *relevant expenditure*, taking into account the decrease in (1); and

(b) if it has obtained prior permission from the *FCA*, substitute the revised *fixed overheads requirement* that results from the calculation in (2)(a) for the *firm's* original *fixed overheads requirement*.

(3) To obtain the permission in (2), a *firm* must demonstrate all of the following:

(a) that one of the conditions in (1)(a) or (1)(b) is met and the projected reduction in the *firm's relevant expenditure* is a reasonable projection;

(b) that the *firm* has adequately considered the impact of the reduction on the *firm*'s *ICARA process* and the conclusions documented in the *firm's* last *ICARA document*; and

(c) that there is a reasonable basis to conclude that, following the reduction in the *firm's fixed overheads requirement*, the *firm* will continue to hold sufficient *own funds* and *liquid assets* to comply with its obligations under [*Editor's note*: the ICARA process will be consulted on in a subsequent consultation, and a reference to the relevant provision(s) will be added here.]

4.3.8 G (1) Under *COREPRU* 4.3.1R, a *firm* is required to calculate its *fixed overheads requirement* based on its *relevant expenditure* as set out in its *annual financial statement* for the previous year.

(2) Under *COREPRU* 4.3.5R, if there is a material increase in the *firm's* projected *relevant expenditure* for the current year, the *firm* must recalculate its *fixed overheads requirement* on the basis of the projected increased *relevant expenditure*, taking into account the impact of that change.

(3) However, under *COREPRU* 4.3.7R, if there is a material change that results in a decrease in the *firm's* projected *relevant expenditure* for the current year, the *firm* must obtain permission from the *FCA* before substituting a reduced *fixed overheads requirement* calculated based on the projected decrease.

(4) In many cases, a material change of the type specified in *COREPRU* 4.3.5R(1) or *COREPRU* 4.3.7R(1) would result from planned changes to the *firm's* business. Examples of these changes may include:

(a) starting or ceasing a major business line;

(b) acquiring or disposing of a major business; or

(c) undertaking a significant investment, upgrade or restructuring programme.

(5) A *firm* that is planning to implement a material change to its business should calculate the anticipated impact of that change on its *fixed overheads requirement* (and its broader *own funds requirement*) before executing the relevant change. This should include considering the potential impact on its *ICARA process*.

Firms in business for less than 1 year

4.3.9 R (1) This *rule* applies where a *firm* has been in business for less than 1 year.

(2) For the purposes of the calculation in *COREPRU* 4.3.1R, a *firm* must use the *relevant expenditure* included in its projections for the first 12 *months'* trading, as submitted in its application for *authorisation*.

4.4 Overall K-factor requirement

4.4.1 The *K-factor requirement* is the sum of all the applicable requirements in the following table:

Type of firm	Applicable requirements
A *CRYPTOPRU firm*	The requirements in *CRYPTOPRU* 4.3.1R.
A *MIFIDPRU firm*	The requirements in *MIFIDPRU* 4.6.1R.

4.4.2 G (1) The *sectoral prudential sourcebooks* contain specific *K-factor requirements* for a variety of activities.

(2) A *firm* is only required to consider *K-factor requirements* which are applicable to it. The application of each *K-factor requirement* is explained in the relevant *sectoral prudential sourcebook*.

(3) If a *firm* is subject to multiple *sectoral prudential sourcebooks*, it must sum the applicable *K-factor requirements* from each sourcebook.

5 Concentration risk

5.1 Monitoring obligation

5.1.1 R A *firm* must monitor and control its concentration risk using sound administrative and accounting procedures and robust internal control mechanisms.

5.1.2 G *COREPRU* 5.1.1R requires a *firm* to monitor and control all sources of concentration risk. It includes any concentration risk that may arise from the following:

(1) the location of any assets safeguarded in accordance with the Client Asset sourcebook (*CASS*);

(2) a *firm's* own cash deposits; and

(3) earnings.

6 Basic liquid assets requirement

6.1 Purpose

6.1.1 G This chapter contains *rules* and *guidance* about a *firm's* liquidity. It contains:

(1) a *basic liquid assets requirement* for a *firm* (*COREPRU* 6.2);

(2) *rules* and *guidance* on which assets count as *core liquid assets* for the purposes of the *basic liquid assets requirement* (*COREPRU* 6.3); and

(3) a *rule* excluding double counting of *core liquid assets* (*COREPRU* 6.3.7R).

6.1.2 G A *firm's basic liquid assets requirement* provides a minimum level of *core liquid assets* that the *firm* must maintain at all times. The purpose of the *basic liquid assets requirement* is to ensure that the *firm* always has a minimum stock of *liquid assets* to fund the initial stages of its wind-down process if wind-down becomes necessary. The *firm* cannot, therefore, use the value of the *core liquid assets* that it holds to meet the *basic liquid assets requirement* as *liquid assets* for any supplementary *sectoral liquidity requirement* or the liquidity needs of its ongoing business.

6.1.3 G A *firm* should also refer to the *rules* and *guidance* on any supplementary *sectoral liquidity requirement* that applies to it.

6.1.4 G [*Editor's note*: This provision, relating to the ICARA process, will be consulted on in a subsequent consultation.]

6.1.5 G [*Editor's note*: This provision, relating to the ICARA process, will be consulted on in a subsequent consultation.]

6.2 Basic liquid assets requirement

6.2.1 R A *firm* must hold an amount of *core liquid assets* equal to the sum of:

(1) one third of the amount of its *fixed overheads requirement*; and

(2) 1.6% of the total amount of any guarantees provided to *clients*.

6.2.2 R Where a *firm* calculates a total amount for guarantees under *COREPRU* 6.2.1R(2), it must calculate:

(1) the total value of guarantees that the *firm* has outstanding at the end of each *business day*; or

(2) an average value for the guarantees that the *firm* has had outstanding over an appropriate time period, which must be updated at regular, appropriate intervals.

6.2.3 G (1) *COREPRU* 6.2.2R(2) is intended to allow a *firm* to smooth out its liquidity requirement for guarantees, where the value of its outstanding guarantees fluctuates on a daily basis.

(2) An appropriate time period for calculating and updating this amount is likely to be a period that produces an average value that is representative of the overall liquidity risk arising out of the provision of guarantees to *clients*.

6.3 Core liquid assets

6.3.1 R Subject to *COREPRU* 6.3.3R to *COREPRU* 6.3.5R, a *core liquid asset* means any of the following, when denominated in pound sterling:

(1) coins and banknotes;

(2) short-term deposits at a *UK-authorised credit institution*;

(3) assets representing claims on, or guaranteed by, the UK government or the Bank of England;

(4) units or shares in a *short-term MMF*; and

(5) units or shares in a *third country* fund that is comparable to a *short-term MMF*.

6.3.2 G When assessing whether a *third country* fund is comparable to a *short-term MMF*, a *firm* should consider factors such as:

(1) whether the restrictions on instruments eligible for inclusion in the fund are comparable to the restrictions on instruments in article 10(1) of the *Money Market Funds Regulation*; and

(2) whether the fund is subject to requirements concerning portfolio diversification and risk management which are comparable to the requirements applicable to *short-term MMFs* in the *Money Market Funds Regulation*.

6.3.3 R (1) If a *firm's relevant expenditure* is incurred in a currency other than pound sterling, the *firm* may also treat the following assets as *liquid assets*, when denominated in that currency:

(a) coins and banknotes;

(b) short-term deposits at a *credit institution*;

(c) assets representing claims on, or guaranteed by, a central bank or government in a *third country*;

(d) units or shares in a *short-term MMF*; and

(e) units or shares in a *third country* fund that is comparable to a *short-term MMF*.

(2) The proportion of *core liquid assets* denominated in any currency other than pound sterling that a *firm* can rely upon to meet its *basic liquid assets requirement* must be no greater than:

(a) for the requirement in *COREPRU* 6.2.1R(1), the proportion of *relevant expenditure* incurred in that currency; and

(b) for the requirement in *COREPRU* 6.2.1R(2), the proportion of *guarantees* provided in that currency.

(3) This *rule* is subject to *COREPRU* 6.3.5R.

6.3.4 G The effect of *COREPRU* 6.3.3R(2) is illustrated by the following example:

(1) A *firm* has *relevant expenditure* with a value of £1,200,000, of which:

(a) 20%, equivalent to £240,000, is incurred in US dollars (USD); and

(b) 5%, equivalent to £60,000, is incurred in Swiss francs (CHF).

(2) In addition, the *firm* has provided total guarantees to *clients* with a value of £10,000,000, of which 50%, equivalent to £5,000,000, is denominated in USD.

(3) The *firm's fixed overheads requirement* (one quarter of its *relevant expenditure* calculated in accordance with *COREPRU* 4.3) is £300,000.

(4) Under *COREPRU* 6.2.1R, the *firm's basic liquid assets requirement* is £260,000, which reflects:

(a) £100,000 in respect of the requirement in *COREPRU* 6.2.1R(1) (one third of the amount of its *fixed overheads requirement*); and

(b) £160,000 in respect of the requirement in *COREPRU* 6.2.1R(2) (1.6% of the total amount of any guarantees provided to *clients*).

(5) To meet its requirement in *COREPRU* 6.2.1R, a *firm* may choose to use *liquid assets* listed in *COREPRU* 6.3.3R denominated in a currency other than pound sterling, up to a maximum equivalent to £105,000 in accordance with *COREPRU* 6.3.3R(2), as follows:

(a) for the requirement in *COREPRU* 6.2.1R(1), up to the equivalent of:

(i) £20,000 may be held in USD denominated *liquid assets* (20% of 100,000 = 20,000); and

(ii) £5,000 may be held in CHF denominated *liquid assets* (5% of 100,000 = 5,000); and

(b) for the requirement in *COREPRU* 6.2.1R(2), up to the equivalent of £80,000 (50% of 160,000 = 80,000) may be held in USD denominated *liquid assets*.

6.3.5 R A *firm* must not treat any of the following as a *core liquid asset*:

(1) any asset that belongs to a *client*; and

(2) any other asset that is encumbered.

6.3.6 G (1) For the purposes of *COREPRU* 6.3.5R(1), an asset may belong to a *client* even if the asset is held in the *firm's* own name. Examples of assets belonging to a *client* include money or other assets held under the *FCA's client asset rules*.

(2) For the purposes of *COREPRU* 6.3.5R(2), an asset may be encumbered if it is pledged as security or collateral, or subject to some other legal restriction (for example, due to regulatory or contractual requirements) which affects the *firm's* ability to liquidate, sell, transfer or assign the asset.

Requirement to exclude double counting of core liquid assets

6.3.7 R A *firm* must not use the same *core liquid assets* to meet the *basic liquid assets requirement* in *COREPRU* 6.2.1R and any supplementary *sectoral liquidity requirement*.

Interaction between COREPRU and MIFIDPRU

6.3.8 G Where a *firm* is subject to the Core Prudential Sourcebook (*COREPRU*) and the Prudential Sourcebook for MiFID Investment Firms (*MIFIDPRU*), a *firm* can use the same *core liquid assets* to meet the *basic liquid assets requirement* in *COREPRU* 6.2.1R and *MIFIDPRU* 6.2.1R.

Sch 1 Record keeping requirements

Sch 1.1 G (1) There are no record keeping requirements in *COREPRU*.

(2) *Firms* are reminded of the general record keeping obligations that apply under *SYSC* 9 (Record keeping).

Sch 2 Notification requirements

Sch 2.1 G (1) The aim of the *guidance* in the following table is to provide an overview of the relevant notification requirements in *COREPRU*.

(2) It is not a complete statement of those requirements and should not be relied on as if it were.

Handbook reference	Subject of notification	Trigger events	Time allowed
COREPRU 3.3.3R(1)	Notification of subsequent issuance of capital instruments qualifying as *common equity tier 1 instruments*	Proposed issuance of capital instruments of an existing class of *common equity tier 1 instruments*	No fewer than 20 *business days* before the issuance
COREPRU 3.3.17R(4)	Notification of inclusion of interim profits or year-end profits in the *firm's common equity tier 1 capital* where the conditions in *COREPRU* 3.3.17R are met	Inclusion of the interim profits or year-end profits in the *firm's common equity tier 1 capital* where the conditions in *COREPRU* 3.3.17R are met	Prompt notification
COREPRU 3.6.6R	Notification of proposed *reduction of capital* where the conditions in *COREPRU* 3.6.6R(2) are met	Proposed *reduction of capital* where the conditions in *COREPRU* 3.6.6R(2) are met	No later than the 20th *business day* before the *day* on which the *reduction of capital* will occur
COREPRU 3.6.8R	Notification of proposed issuance of *additional tier 1 instruments* or *tier 2 instruments*	Proposed issuance of *additional tier 1 instruments* or *tier 2 instruments*	At least 20 *business days* before the intended issuance date

Sch 3 Fees and other payment requirements

Sch 3.1 G *COREPRU* does not contain any *rules* that directly impose fees or other payments.

Sch 4 Rights of action for damages

Sch 4.1 G (1) The table below sets out the *rules* in *COREPRU*, contravention of which by an *authorised person* may be actionable under section 138D of the *Act* (Actions for damages) by a *person* who suffers loss a result of the contravention.

(2) If 'Yes' appears in the column headed 'For private person', the *rule* may be actionable by a *private person* under section 138D (or, in certain circumstances, that *person's* fiduciary or representative: see regulation 6(2) and 6(3)(c) of the Financial Services and Markets Act 2000 (Rights of Action) Regulations 2001 (SI 2001/2256)). If 'Yes' appears in the column headed 'Removed', this indicates that the *FCA* has removed the right of action under section 138D(3) of the *Act*. If so, a reference to the *rule* in which the right of action is removed is also given.

(3) The column headed 'For other person' indicates whether the *rule* may be actionable by a *person* other than a *private person* (or that *person's* fiduciary or representative) under article 6(2) and (3) of those Regulations. If so, an indication of the type of *person* by whom the *rule* may be actionable is given.

Chapter/Appendix	**Rights of action under section 138D of the Act**		
	For private person	**Removed**	**For other person**
All *rules* in *COREPRU*	No	Yes – *COREPRU* 1.3.1R	No

Sch 5 Rules that can be waived or modified

Sch 5.1 G The *rules* in *COREPRU* may be waived or modified by the *FCA* under section 138A of the *Act* (Modification or waiver of rules) where the conditions in that section are met.

Annex C

Prudential sourcebook for CRYPTOPRU firms (CRYPTOPRU)

[*Editor's note*: This Annex takes into account the proposals and legislative changes suggested in the following consultation papers as if they were made final:

(1) 'Stablecoin Issuance and Cryptoasset Custody' (CP25/14); and
(2) 'Updating the regime for Money Market Funds' (CP23/28).]

In this Annex, all the text is new and is not underlined.

Insert the following new sourcebook, the Prudential sourcebook for CRYPTOPRU firms (CRYPTOPRU), directly after the Core Prudential sourcebook (COREPRU).

1 Application

1.1 Application and purpose

Application

1.1.1 G Each chapter of *CRYPTOPRU* explains which *CRYPTOPRU firms* it applies to.

Purpose

1.1.2 G The purpose of *CRYPTOPRU* is to set out sectoral prudential requirements for *CRYPTOPRU firms*.

1.1.3 G *CRYPTOPRU* supplements the core requirements in *COREPRU* and should be read in conjunction with the prudential requirements set out there.

1.1.4 G Generally, the *rules* in *CRYPTOPRU* are intended to cover the *CRYPTOPRU activities* undertaken by a *CRYPTOPRU firm*, but certain requirements apply to a *firm* as a whole.

1.1.5 G The requirements in *CRYPTOPRU* expand upon the basic requirements under the appropriate resources *threshold condition* (referred to in *COND* 2.4) and the requirement in *Principle* 4 for a *firm* to maintain adequate financial resources.

1.2 Actions for damages

1.2.1 R A contravention of any *rule* in *CRYPTOPRU* does not give rise to a right of action by a *private person* under section 138D of the *Act* (and each of those *rules* is specified under section 138D(3) of the *Act* as a provision giving rise to no such right of action).

2 Overall financial adequacy for CRYPTOPRU firms

2.1 Guidance

2.1.1 G *CRYPTOPRU firms* are required to comply with the requirements on overall financial adequacy that are set out in *COREPRU* 2. There are no sectoral *rules* on overall financial adequacy for these *firms*.

3 Own funds for CRYPTOPRU firms

3.1 Guidance

3.1.1 G *CRYPTOPRU firms* are required to comply with the requirements on *own funds* that are set out in *COREPRU* 3. There are no sectoral *rules* on *own funds* for these *firms*.

4 Sectoral own funds requirement for CRYPTOPRU firms

4.1 Application

4.1.1 R This chapter applies to a *CRYPTOPRU firm*.

4.2 Permanent minimum requirement

4.2.1 R The *permanent minimum capital requirement* is the highest of the applicable requirements in the following table:

Category of firm	Permanent minimum requirement
A *firm* with *permission* for *issuing qualifying stablecoins*	£350,000
A *firm* with *permission* for *safeguarding qualifying cryptoassets*	£150,000

4.3 CRYPTOPRU K-factor requirement

4.3.1 R The *K-factor requirements* in *CRYPTOPRU* are:

(1) the *K-QCS requirement*; and

(2) the *K-SII requirement*.

4.4 K-factor requirement for qualifying cryptoassets that are safeguarded (K-QCS)

4.4.1 R The *K-QCS requirement* of a *firm* that is *safeguarding qualifying cryptoassets* is equal to 0.04% of its *average QCS*.

4.4.2 G (1) The definition of *QCS* only includes the *qualifying cryptoassets* that a *firm* is safeguarding. Any other *qualifying cryptoassets* do not

therefore need to be included in a *firm's* calculation of the *K-QCS requirement* (except to the extent that *CRYPTOPRU* 4.4.3R applies).

(2) A *firm* should still consider any potential material harms that may arise in connection with those *qualifying cryptoassets*, as part of its *ICARA process*. [*Editor's note*: details of the ICARA process will be consulted on in a subsequent consultation paper.]

4.4.3 R If a *firm* is unsure whether *qualifying cryptoassets* are held in the course of *safeguarding qualifying cryptoassets*, it must treat those *qualifying cryptoassets* as held in the course of *safeguarding qualifying cryptoassets* for the purposes of calculating *K-QCS*.

4.4.4 R A *firm* must calculate its *K-QCS requirement*:

(1) on the first *business day* on which *CRYPTOPRU* applies to the *firm*; and

(2) thereafter, on the first *business day* of each *month*.

4.4.5 R A *firm* must calculate its *average QCS* by:

(1) taking the total *QCS* as measured at the end of each *business day* for the previous 9 *months*;

(2) excluding the values for the most recent 3 *months*; and

(3) calculating the arithmetic mean of the daily values for the remaining 6 *months*.

4.4.6 R A *firm* must include the value of the relevant *qualifying cryptoassets* in its measurement of *QCS* in both of the following situations:

(1) the *firm* has appointed a third party to carry out the activity of *safeguarding qualifying cryptoassets* which the *firm* has undertaken to its *client* to safeguard; or

(2) a third party has appointed the *firm* to carry out the activity of *safeguarding qualifying cryptoassets*.

4.4.7 G The effect of *CRYPTOPRU* 4.4.6R is that a *firm* will not reduce its level of *QCS* by appointing a third party to carry out the activity of *safeguarding qualifying cryptoassets*. However, a *firm* will increase the level of its *QCS* by accepting the appointment from a third party to carry out the activity of *safeguarding qualifying cryptoassets*. This reflects the harm that may result from a breach of the *firm's* direct safeguarding responsibilities or the *firm's* responsibilities in relation to the selection, appointment and periodic review of any third party which the *firm* has appointed to carry out the activity of *safeguarding qualifying cryptoassets*.

4.4.8 R When measuring *QCS*, a *firm* must:

(1) use the market value of the *qualifying cryptoassets*; or

(2) where a market value is not available for a *qualifying cryptoasset*, use an alternative measure of fair value, which may include an estimated value calculated on a best-efforts basis.

4.4.9 G The values used by a *firm* under *CRYPTOPRU* 4.4.8R should be consistent with the information on *qualifying cryptoassets* in any relevant regulatory data reported by the *firm* to the *FCA*, and in any internal or external reconciliations and records maintained in accordance with *CASS* 17.5 (Records of qualifying cryptoassets and reconciliations) unless a *rule* or relevant *guidance* requires the *firm* to take a different approach.

4.4.10 R Where a *firm* has been *safeguarding qualifying cryptoassets* for less than 9 *months*, it must calculate its *average QCS* as follows:

(1) During the first *month* in which it is *safeguarding qualifying cryptoassets*, the *firm* must:

(a) make a best-efforts estimate of expected *QCS* for that *month*; and

(b) use that estimate as its *average QCS*.

(2) During the subsequent 8 *months*, the *firm's average QCS* must be calculated in accordance with *CRYPTOPRU* 4.6.1R(2).

4.5 K-factor requirement for stablecoins in issuance (K-SII)

4.5.1 R The *K-SII requirement* of a *firm* that is *issuing qualifying stablecoins* is equal to 2% of its *average SII*.

4.5.2 R A *firm* must calculate its *K-SII requirement*:

(1) on the first *business day* on which *CRYPTOPRU* applies to the *firm*; and

(2) thereafter, on the first *business day* of each *month*.

4.5.3 R A *firm* must calculate its *average SII* by:

(1) taking the total *SII* as measured at the end of each *business day* for the previous 9 *months*;

(2) excluding the values for the most recent 3 *months*; and

(3) calculating the arithmetic mean of the daily values for the remaining 6 *months*.

4.5.4 R (1) When measuring the value of *SII* for a particular *business day*, a *firm* must convert any amounts in foreign currencies into the *firm's* functional currency.

(2) For the purposes of the currency conversion in (1), a *firm* must:

(a) determine the conversion rate by reference to an appropriate market rate; and

(b) record the rate used.

4.5.5 G (1) *CRYPTOPRU* 4.5.4R(1) addresses the situation where a *firm* issues a *qualifying stablecoin products* that references a fiat currency other than its functional currency.

(2) It does so by requiring the *firm* to convert its *SII* for each such stablecoin into sterling before calculating its *average SII*.

(3) The relevant daily spot exchange rate against sterling that the Bank of England publishes is an example of an appropriate market rate which a *firm* for could use the purpose of this currency conversion.

4.5.6 G (1) As the definition of *SII* includes any *qualifying stablecoin* that the *qualifying stablecoin issuer* is liable to redeem, this:

(a) includes *qualifying stablecoins* that were *minted* at any time, including before *CRYPTOPRU* came into force;

(b) includes *qualifying stablecoins* that have been *minted* by a *person* other than the *qualifying stablecoin issuer* (which could include *qualifying stablecoins minted* outside the *UK*) if they are fungible with the relevant *qualifying stablecoins*; but

(c) excludes *qualifying stablecoins* that have been *burned*.

(2) The definition of *SII* excludes *qualifying stablecoins* the value of which have been deducted from the *qualifying stablecoin issuer's own funds*, in accordance with *COREPRU* 3.3.36R. Such *qualifying stablecoins* will not therefore be included in the calculation of *average SII*.

4.5.7 R Where a *firm* has been *issuing qualifying stablecoins* for less than 9 *months*, it must calculate its *average SII* as follows:

(1) during the first *month* in which it is *issuing qualifying stablecoins*, the *firm* must:

(a) make a best efforts estimate of expected *SII* for that *month*; and

(b) use that estimate as its *average SII*; and

(2) during the subsequent 8 *months*, the *firm's average SII* must be calculated in accordance with *CRYPTOPRU* 4.6.1R(2).

4.6 Modified calculation for CRYPTOPRU firms performing CRYPTOPRU activities for less than 9 months

4.6.1 R (1) This provision applies to the calculation of:

(a) *average QCS* (for the purpose of *CRYPTOPRU* 4.4.10R(2)); and

(b) *average SII* (for the purpose of *CRYPTOPRU* 4.5.7R(2)).

(2) For the purpose of calculating the values in (1), a *firm* must calculate the arithmetic mean of the daily values over the previous *n months - y months*.

Where:

- *n* = the number of *months* that have elapsed since *CRYPTOPRU* began to apply (with the *month* during which *CRYPROPRU* begins to apply being counted as *month* 1); and
- y = the greater of 0 and (*n* - 6) *months*.

5 Sectoral concentration risk requirements for CRYPTOPRU firms

[*Editor's note*: this chapter will be consulted on in a subsequent consultation paper.]

6 Sectoral liquidity requirement

6.1 Application and purpose

Application

6.1.1 R This chapter applies to a *CRYPTOPRU firm* that is carrying out the activity of *issuing qualifying stablecoins*.

Purpose

6.1.2 G This chapter contains *rules* and *guidance* on the amount of *on demand deposits* that a *qualifying stablecoin issuer* must hold to ensure it has adequate financial resources and can comply with the requirement in *CASS* 16.2.1R(3) at all times (its '*issuer liquid asset requirement*').

6.1.3 G The *issuer liquid asset requirement* supplements the *basic liquid assets requirement* that *COREPRU* 6 requires all *CRYPTOPRU firms* to meet.

Issuer liquid asset requirement

6.1.4 R A *qualifying stablecoin issuer* must calculate its *issuer liquid asset requirement* based on the following assets in its *backing asset pool*:

(1) *core backing assets*, excluding *on demand deposits*; and

(2) *expanded backing assets*.

6.1.5 G Where a *firm* issues multiple *qualifying stablecoins*, it must calculate its *issuer liquid asset requirement* based on the *backing asset pool* for each *qualifying stablecoin*.

6.1.6 R (1) For a unit in a *public debt CNAV MMF* or an *EU MMF*, a *qualifying stablecoin issuer* that is aware of the underlying investments on a daily basis may look through and calculate its *issuer liquid asset requirement* based on the underlying government debt securities.

(2) For the purpose of (1), where the underlying investments include a *repurchase transaction*, the *qualifying stablecoin issuer* must calculate its *issuer liquid asset requirement* in accordance with *CRYPTOPRU* 6.1.7R.

(3) If a *qualifying stablecoin issuer* cannot look through in accordance with (1) and (2), or chooses not to do so, it must (instead of performing the calculation in *CRYPTOPRU* 6.1.9R) calculate its *issuer liquid asset requirement* by multiplying the notional value of the unit by 5%.

6.1.7 R For a *repurchase transaction*, a *qualifying stablecoin issuer* must calculate its *issuer liquid asset requirement* based on any government debt securities that have been exchanged for the duration of the contract.

6.1.8 G The effect of *CRYPTOPRU* 6.1.7R is that a *qualifying stablecoin issuer* must calculate its *issuer liquid asset requirement* based on any government debt securities that have been exchanged as part of a *repurchase transaction*, irrespective of whether it is a *repurchase transaction* or a reverse *repurchase transaction*.

6.1.9 R A *firm* must calculate its *issuer liquid asset requirement* by:

(1) determining whether an asset is a *level 1 asset*, a *level 2 asset* or a *level 3 asset*;

(2) determining the charge for each asset, in accordance with the table in *CRYPTOPRU* 6.1.11R;

(3) multiplying the notional value of each asset by the relevant charge; and

(4) adding together the output from step (3) for all the assets to which *CRYPTOPRU* 6.1.4R applies.

6.1.10 G (1) The calculation of the *issuer liquid asset requirement* in *CRYPTOPRU* 6.1.4R is illustrated by the following example.

(2) In accordance with *CASS* 16.2.1R, a *qualifying stablecoin issuer* holds the following *core backing assets* and *expanded backing assets* in its *backing asset pool* for the *qualifying stablecoin* that it has issued:

(a) £30,000 in *long-term government debt instruments* issued by the *UK* (a *level 1 asset*) with a residual maturity of 5 years and a coupon of 4%;

(b) £50,000 in *short-term government debt instruments* issued by the *UK* (a *level 1 asset*) with a residual maturity of 3 *months* and a coupon of 5%; and

(c) £20,000 in *on demand deposits*.

(3) The *issuer liquid asset requirement* should be calculated by multiplying the notional value of the *long-term government debt instrument*s and the *short-term government debt instruments* by the charge found in the table in *CRYPTOPRU* 6.1.11R as follows:

£30,000 x 3.50% = £1,050

£50,000 x 0.20% = £100

(4) *On demand deposits* are not included in the calculation (this reflects the fact that the aim of the *issuer liquid asset requirement* is to capture price risk).

(5) The *issuer liquid asset requirement* is £1,150.

6.1.11 R This table belong to *CRYPTOPRU* 6.1.9R(2):

Asset charge					
Maturity bands	**Level 1 - Coupon ≤ 3%**	**Level 1 - Coupon >3%**	**Level 2 - Coupon ≤ 3%**	**Level 2 - Coupon >3%**	**Level 3 (No coupon)**
0 ≤ 1 *month*	0.00%	0.00%	0.50%	0.50%	3.0%
> 1 ≤ 3 *months*	0.20%	0.20%	0.50%	0.50%	3.0%
> 3 ≤ 6 *months*	0.40%	0.40%	0.50%	0.50%	3.0%
> 6 ≤ 12 *months*	0.70%	0.70%	0.70%	0.70%	3.0%
> 1 ≤ 2 years	1.50%	1.50%	1.50%	2.00%	5.0%
> 2 ≤ 3 years	1.75%	2.25%	2.25%	2.75%	5.0%
> 3 ≤ 4 years	2.25%	2.75%	2.75%	3.25%	6.0%

> 4 ≤ 5 years	2.75%	3.50%	3.25%	4.00%	6.0%
> 5 ≤ 7 years	3.50%	3.75%	3.75%	5.00%	8.0%
> 7 ≤ 10 years	3.75%	6.00%	4.50%	7.00%	8.0%
> 10 ≤ 15 years	6.00%	8.50%	7.00%	10.00%	12.0%
> 15 ≤ 20 years	6.00%	8.50%	7.00%	13.00%	15.0%
> 20 ≤ 25 years	8.50%	12.50%	10.00%	16.00%	20.0%
> 25 ≤ 30 years	8.50%	15.00%	10.00%	18.00%	25.0%
>30 years	12.50%	20.00%	15.00%	25.00%	30.0%

Permissible assets

6.1.12 R For the purposes of meeting the *issuer liquid asset requirement*, the *on demand deposits* must:

(1) be held at a *UK-authorised credit institution*, except where the *reference currency* of the *qualifying stablecoin* is not in pound sterling, in which case it may be held at a *credit institution*; and

(2) be denominated in the *reference currency* of each relevant *qualifying stablecoin*.

6.1.13 G A *firm* must not use the same *on demand deposits* to meet the *basic liquid assets requirement* in *COREPRU* 6.2.1R and the *issuer liquid asset requirement*.

Sch 1 Record keeping requirements

Sch 1.1 G (1) There are no record keeping requirements in *CRYPTOPRU*.

(2) *CRYPTOPRU firms* are reminded of the general record keeping obligations that apply under *SYSC* 9 (Record keeping).

Sch 2 Notification requirements

Sch 2.1 G There are no notification requirements in *CRYPTOPRU*.

Sch 3 Fees and other payment requirements

Sch 3.1 G *CRYPTOPRU* does not contain any *rules* that directly impose fees or other payments.

Sch 4 Rights of action for damages

Sch 4.1 G (1) The table below sets out the *rules* in *CRYPTOPRU*, contravention of which by an *authorised person* may be actionable under section 138D of the *Act* (Actions for damages) by a *person* who suffers loss a result of the contravention.

(2) If 'Yes' appears in the column headed 'For private person', the *rule* may be actionable by a *private person* under section 138D (or, in certain circumstances, that *person's* fiduciary or representative: see regulation 6(2) and 6(3)(c) of the Financial Services and Markets Act 2000 (Rights of Action) Regulations 2001 (SI 2001/2256)). If 'Yes' appears in the column headed 'Removed', this indicates that the *FCA* has removed the right of action under section 138D(3) of the *Act*. If so, a reference to the *rule* in which the right of action is removed is also given.

(3) The column headed 'For other person' indicates whether the *rule* may be actionable by a *person* other than a *private person* (or that *person's* fiduciary or representative) under article 6(2) and (3) of those Regulations. If so, an indication of the type of *person* by whom the *rule* may be actionable is given.

Chapter/Appendix	**Rights of action under section 138D of the *Act***		
	For private person	**Removed**	**For other person**
All *rules* in *CRYPTOPRU*	No	Yes – *CRYPTOPRU* 1.2.1R	No

Sch 5 Rules that can be waived or modified

Sch 5.1 G The *rules* in *CRYPTOPRU* may be waived or modified by the *FCA* under section 138A of the *Act* (Modification or waiver of rules) where the conditions in that section are met.

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