THE AUTHORITY'S PRUDENTIAL MEASURES

MEASURE 1: ***Prudential measures to address issues identified either through the SREP or as part of ongoing supervision should be applied promptly***.

a. If the authority considers that a credit institution's ICAAP does not adequately reflect its overall risk profile, or does not result in the credit institution having adequate capital, then consideration will be given to applying prudential measures.

b. The measures available to the authority include:

- Requiring a credit institution to hold own funds and/or Tier 1 capital above the minimum level required by BR/04 – *Capital Requirements of Credit Institutions Authorised under the Banking Act 1994,* and/or imposing other limitations on own funds. For the purposes of determining the appropriate level of own funds on the basis of the review and evaluation carried out in accordance with article 17D of the Act, the authority shall assess whether any imposition of a specific own funds requirement in excess of the minimum level is required to capture risks to which a credit institution is or might be exposed, taking into account the following:

  (i) the quantitative and qualitative aspects of the credit institutions' assessment process referred to in article 17C of the Act;

  (ii) the credit institutions' arrangements, processes and mechanisms referred to in article 17B of the Act; and

  (iii) the outcome of the review and evaluation carried out in accordance with article 17D and this Rule.

- Requiring the credit institution to improve its internal control and risk management frameworks.

- Requiring the credit institution to apply a specific provisioning policy or treatment of assets in terms of own funds requirements.

- Restricting or limiting the business, operations or network of the credit institution.

- Requiring the credit institution to reduce the risks inherent in its activities, products and systems.

- Requiring the credit institution to limit variable remuneration as a percentage of total net revenues when it is inconsistent with the maintenance of a sound capital base.

- Requiring the credit institution to use net profits to strengthen its capital base.

c. The range of envisaged supervisory measures should be identified as one output of the SREP. The final decision on which measures to implement will be taken by the authority, taking into account the outcome of the dialogue with the credit institution.

d. The choice of prudential measures should be determined according to the severity and underlying causes of the situation and the range of measures and sanctions available to the authority. Measures can be used individually or in combination. A specific own funds requirement could, however, be imposed on any credit institution which exhibits an imbalance between its business risks and its internal control and risk frameworks, if that imbalance cannot be remedied by other prudential measures or supervisory actions within an appropriate timeframe.

e. A specific own funds' requirement may also be set where the authority judges the level of own funds held by a credit institution to be inherently inadequate for its overall risk profile. It must be acknowledged that there is no 'scientific' method for determining the amount, and that capital is not a long run substitute for remedying deficiencies in systems and controls. In practice, the process relies heavily on subjective judgement and peer group consistency to ensure a level playing field and a defence to challenge by credit institutions.

f. In the undertaking of its supervisory oversight, the authority will take into consideration the prevailing circumstances within the institution, as well as all relevant external factors prior to taking action deemed necessary in line with the available supervisory measures (as referred to in paragraph b. above).

MEASURE 2: ***Prudential measures should be communicated promptly and in sufficient detail.***

a. In communicating its decision on prudential measures, the authority would:

- Explain in sufficient detail the factors which have led to the risk assessment conclusions.

- Indicate areas of weakness and the timeframe for remedial action.

- Explain the reasons for any adjustment to the credit institution's capital requirements.

- Indicate what improvements could be made to systems and controls to make them adequate for the risks and activities of the credit institution and for this improvement to be reflected in the credit institution's capital requirements.

b. In accordance with Article 31(9) of the Banking Act 1994, it is the duty of an external auditor to inform the authority, whether through the relative institution's management or, if circumstances so warrant, directly to the authority if he becomes aware of any matter which may have serious adverse effects on depositors. The authority considers that this would include any issues relating to the adequacy and suitability of the ICAAP to cover the institution's risks. In the same manner, the authority may also deem fit to advise the external auditors accordingly in case that its SREP indicates that an institution's ICAAP is deemed inadequate for the institution's risk profile.