

Getting the balance right: Calibrating capital to support growth, stability and homeownership

Response to the FPC's assessment of capital requirements

About the Building Societies Association

The Building Societies Association (BSA) represents all 42 UK building societies, including both mutual-owned banks, as well as 7 of the largest credit unions. Building societies and mutual-owned banks have total assets of almost £650 billion. They hold residential mortgages of over £485 billion, 29% of the total outstanding in the UK. They are also helping 23 million people build their financial resilience, holding over £485 billion of retail deposits, accounting for 23% of all such deposits in the UK. Building societies and mutual-owned banks account for 47% of all cash ISA balances. With all their headquarters outside London, building societies employ around 52,300 full and part-time staff. In addition to digital services, they operate through approximately 1,300 branches, holding a 30% share of branches across the UK.

Executive summary

The BSA welcomes the FPC's review of the overall capital framework in the UK. We support the decision to reduce the target level of tier 1 capital in the system from 14% to 13%. We agree that capital levels should neither be too high nor too low in order to optimise economic growth while minimising the risk (and cost to GDP) of future crises. Building societies were established 250 years ago for the purpose of supporting home-ownership for ordinary people which is a driver of economic growth. Research shows that the mortgage market adds £26bn in direct GVA (£20bn mortgage lending and £6bn spending by first-time buyers and homeowners) with an additional £21bn generated through indirect and induced effects. For every property purchase made, buyers contribute around an additional c£10k to GDP¹ through spending associated with moving home. We therefore welcome that the FPC is considering these important trade-offs between capital held by banks and building societies and the impact on GDP and growth.

The mortgage market in the UK is of particular relevance to the BSA, and capital requirements have a direct impact on the level of building society lending. In the last five years, the UK has experienced the COVID pandemic and a cost-of-living crisis, coupled with the market dislocation and volatility caused by the September 2023 mini-budget. Throughout this period, building societies and credit unions have continued to support their members, while not observing any material increase in mortgage credit losses. While it is right to be pleased by the absence of mortgage losses, this also begs the question of whether lenders have been able to take enough risk? Or whether too much capital allocated to low-risk mortgage lending is crowding out lending to businesses and other economic growth priorities. We acknowledge the significant government support for mortgage borrowers during the same period, which cannot be relied upon in any future crisis. However, the level of capital now held against low-risk mortgages through pillar 1 IRB hybrid model

¹ See [Economic benefits of housing market activity](#), Nov 2020

adjustments², the IRB floor, pillar 2a, MREL, leverage ratio and buffers – **around ten times the pillar 1 requirements** - is arguably disproportionate to the underlying risks of unexpected losses (expected losses being captured by IFRS9 provisions which also include layers of conservatism). Stress testing outcomes also demonstrate the forward-looking resilience of mortgage portfolios of BSA members. Building societies were set up to support home-ownership for ordinary people, but our data shows that it is becoming increasingly difficult for first-time buyers to purchase their own homes.³ These factors suggest that any gradual and well-controlled easing of capital requirements to allow more mortgage lending would be strongly welcome and beneficial to supporting home ownership and growth in GDP.

The BSA welcomes the changes that the FPC has already made, including easing the LTI flow limit to ensure it genuinely applies only at the macro-prudential level. When the 15% cap was applied at the individual firm-level this was overly penal to certain business models such as building societies.

We welcome that the FPC is now reviewing the components and calibration of the overall capital framework. We are particularly keen that the FPC considers how the various components interact as these requirements do not exist in isolation. Capital buffers are a key consideration here. Usability of buffers must include a review of all of the components of the buffers to really understand the dynamics and incentives at play. The FPC has set a positive neutral rate for the countercyclical buffer of 2%, and said that this is not open to review. However, research has indicated that banks are more likely to use the countercyclical buffer than other components of the buffers. Therefore, it feels important to include a review of this aspect of the buffer framework – and whether the positive neutral rate is effectively double-counting the purpose of the capital conservation buffer? These are fundamental questions to ask given that any perception that the countercyclical buffer is more 'usable' can undermine whether the capital conservation buffer is usable given it is not releasable.

We would also encourage the FPC to ensure that it deploys its macroprudential tools in a way that is proportionate to the risks posed by firms or groups of firms, such as mutuals. The current one-size-fits-all application of banking standards to building societies are particularly penal to the mutual business model. Prudential regulations are being tailored to be more proportionate for smaller firms and we strongly welcome the new Strong & Simple requirements under SDDT. However, for non-SDDT firms the requirements for banks and building societies are identical even though the business models, incentives and therefore risks are significantly different. Through this review we hope that the FPC will consider how requirements that are penal to certain business models might then constrain growth in that sector thereby reducing business model diversity over time and the negative impact that might have on financial stability.

Mutuals contribution to financial stability

² All but one of the IRB societies are awaiting final approval of their hybrid IRB models. This is another reason why they are holding excess capital to cover the uncertainty around any increase in IRB capital requirements under the hybrid model approach. This uncertainty in pillar 1 requirements multiplies up through the capital stack.

³ See [First-time buyers: The missing missions](#), April 2025

Our analysis of the research⁴ shows that diversity of business models and ownership structure is beneficial for financial stability, as well a range of other positive social consequences. As one type of firm is impacted by shocks, other types of firms can continue to support the economy. For example, building societies accounted for significantly more net lending than banks in the period following the global financial crisis, sometimes accounting for >100% of net lending when shareholder banks were repairing their balance sheets.⁵

We encourage the FPC to consider more closely the impact of its policies on mutuals and whether the deployment of its macroprudential tools can drive a reduction in business model diversity by favouring policies designed and calibrated for shareholder-owned banks. The FPC could consider measuring, monitoring and reporting business model diversity to better understand how it varies over time and in response to its interventions.

Leverage ratio framework

The BSA has previously set out in detail its objections to the UK- specific leverage ratio framework in its response to CP2/25.⁶ While that consultation was focused on the threshold at which the leverage ratio framework applies, we included analysis of Pillar 3 disclosures that clearly demonstrated the penal nature of the framework on the building society mutual model, and called for a more fundamental review. We argued that different structures and incentives exist for mutuals such as in the Building Societies Act nature limits⁷, which ensure that mutuals remain true to their principle purpose of accepting deposits for the purpose of mortgage lending. Mutual societies have a more limited ability to raise growth capital compared to banks, and the absence of external investors at the Board mean very different incentives drive risk-taking. These features together mean that the risks of excessive growth – which the leverage ratio aims to contain⁸ - are far lower for a mutual than for a shareholder-owned bank.

The UK leverage ratio threshold increase to £75bn means that only Nationwide Building Society is captured by the full UK leverage ratio framework. The UK leverage ratio buffers are particularly penal to a low-risk mortgage lender like Nationwide and are not part of the Basel framework. So while we are supportive of the threshold excluding almost all building societies we would also question whether leverage

⁴ [“Harnessing the mutuals sector potential for growth”](#), WPI Economics, 2025

[“The origin of financial instability and systemic risk: Do bank business models matter?”](#), Barbara Casu, Rym Ayadi, Paola Bongini, Doriana Cucinelli, Journal of Financial Stability, 2025

[“Systemic risk in banking ecosystems”](#), Haldane, A and May, R, Nature, 2011

[“Regulators should encourage more diversity in the financial system”](#), Wagner, W & Goodhart, C, CEPR, 2012

[“Measuring corporate diversity in financial services: a diversity index”](#) Michie, J & Oughton, C, International Review of Applied Economics, 2022

⁵ Building societies accounted for >100% net lending during 2012 and 2013, and again in 2023, which was very significantly more than their market share

⁶ See [BSA Response to CP2/25](#)

⁷ The Building Societies Act requires that a minimum of 75% of assets must be loans secured on residential property and 50% of funds must come from member shares. As such, the low-risk and stable balance sheet is assured by statute. No comparable constraints apply to banks.

⁸ See CP2/25, paragraph 1.2 “Its objective is to guard against – as a backstop measure – the risk of errors and uncertainties in assigning risk weights. It can also limit excessive balance sheet growth or act as a constraint to such excess before it occurs.”

ratio buffers are the right tool for the right purpose when applied to any building society, including Nationwide. If the purpose of a buffer on risk-weighted capital requirements is to mitigate the risk of RWA variability, then the same logic does not apply with the leverage ratio which is designed to be more stable over time. Our BSA members have demonstrated through their stress testing that the leverage ratio is stable through a severe but plausible scenario. As such, an additional leverage ratio buffer is not required in order to ensure ongoing compliance with the leverage ratio through a severe but plausible stress scenario.⁹ This appears to be the same conclusion that other Basel Committee member jurisdictions have made as leverage ratio buffers do not form part of the Basel framework and have not been applied outside of the UK. Nationwide alone could increase lending by c£30bn if the leverage ratio buffers were removed. Such a change would allow additional lending but without a meaningful shift up the risk curve, nor impacting broader financial stability. This would help more people to own their own homes and could also enable more lending to business customers to grow and thrive.

Enhancing buffer usability

Much has been written about the lack of usability of capital buffers. The FPC report notes that firms are reluctant to breach buffers, and this reflects an IMF working paper published in 2022.¹⁰ Firms often hold management buffers over and above regulatory minima and regulatory buffers according to their capital (and regulatory) risk appetite. Minimum distribution amounts (MDAs) act as a clear economic incentive for firms not to use buffers. As such, it can be argued that capital buffers are not achieving the policy intent they were designed to achieve.¹¹

The FPC goes on to note that firms are more likely to view releasable buffers such as the countercyclical buffer (CCyB) as more usable than other elements of the buffer. As such, we were disappointed to read in the FPC capital review report that the positive neutral CCyB rate set at 2% is not in the scope of this review. We do not understand how the BoE can conduct this review on buffer usability without taking the CCyB into account, particularly given that the UK CCyB is currently set higher than any other major jurisdiction in the world and this could be overlapping with the purpose of the capital conservation buffer.¹²

There are two distinct reasons why a firm may not meet regulatory capital buffers:

- Losses occur that reduce capital such that the buffers are not met. While sound risk management should protect against this scenario occurring, if it does occur then a firm does not have a choice as to whether or not to dip into the buffer.
- A firm wants to continue to grow its RWAs quicker than its capital such as through lending during an economic downturn and therefore chooses to not meet buffers to support this growth.

⁹ If using the same methodology as the PRA buffer for risk-weighted requirements, very little additional buffer would be required because of the more static nature of the leverage ratio through a downturn

¹⁰ See [Usability of Bank Capital Buffers: The Role of Market Expectations](#), January 2022

¹¹ The Basel buffers are designed to “promote the conservation of capital and the build-up of adequate buffers above the minimum that can be drawn down in periods of stress”

¹² See [BIS CCyB dashboard](#) showing that the UK CCyB at 2% is the highest of any G20 jurisdiction and significantly higher than the US, Switzerland, Japan, China, Italy or Canada that are currently set at zero.

While sound risk management processes and control frameworks will reduce the probability of the first situation from occurring, if those controls have not been sufficiently effective to prevent e.g. a cyber attack causing operational losses, then the firm doesn't have a choice about whether or not to meet the buffers. The loss has already occurred or is occurring and losses always deplete capital levels. So, the debate on buffer usability is really about the second situation. Here a firm has a choice of whether to continue to lend and grow or whether to slow down lending to repair capital and avoid dipping into the buffers. This is essentially a risk appetite question and a decision for the Board. The Board will need to consider the views of other stakeholders such as market investors and rating agencies, as well as its fiduciary duty to act in the best interests of building society members. For mutuals this decision will also be influenced by the longer time it takes to repair the buffers either through retained earnings or issuance. As such, these differing incentives must be taken into account.

Taking these factors together, its not surprising that mid-tier building societies typically set their risk appetite in a way that they do not breach capital buffers. Our data analysis shows that **the largest five societies hold excess capital above reg cap + MREL + buffer requirements in a range of 3.3-23.7%RWAs.**¹³ Nationwide is leverage ratio constrained, so the 5.6%RWA equivalent excess is over the leverage ratio. **This compares to the average across the UK major banks of 2%RWAs.** It is also important to note that building societies tend to meet a greater share of their MREL requirements through CET1 resources as demonstrated by the even larger gap between TCR and buffers and available regulatory capital resources. This means that for a building society subject to MREL requirements, the capital mix is quite different with higher levels of CET1 than a shareholder-owned bank.

| | TCR | TCR + combined buffer | Capital resources | Resources in excess of combined buffer | MREL + combined buffer | Total resources (capital & MREL) | Resources in excess of MREL+combined buffer |
|-----------------------------------|-----------------|-----------------------|-------------------|----------------------------------------|------------------------|----------------------------------|----------------------------------------------|
| Nationwide Group RWA (March 2025) | 12.7% 10,422 | 18.2% 14,901 | 23.8% 19,489 | 5.6% 4,588 | n/a | 37.5% 30,733 | n/a leverage equivalent of 5.6%RWA |
| Nationwide leverage | 3.25% | 4.3% | 5.2% 17,732 | 0.9% 2,939 | 7.55% 26,082 | 8.9% 30,733 | 1.35% 4,651 |
| Coventry (Dec 24) | 10.6% 990 | 15.1% 1,411 | 35.5% 3,320 | 20.4% 1,909 | 25.7% 2,401 | 49.4% 4,615 | 23.7%RWA 2,214 |
| Yorkshire (Dec 25) | 8.0% 1,789 | 12.5% 2,796 | 19.4% 4,338 | 6.9% 1,542 | 20.5% 4,584 | 23.8% 5,324.4 | 3.3%RWA 704 |
| Skipton (2025) | 10.6% 969 | 14.9% 1,362 | 28.3% 2,590 | 13.4% 1,228 | 25.5% 2,331 | 32.2% 2,940 | 6.7%RWA 609 |
| Leeds (2024) | 11.06% 683 | 15.56% 960 | 25.85% 1,595 | 10.26% 635 | 26.6% 1,646 | 31.5% ¹⁴ 1,946 | 4.9%RWA |

As above, we request that the FPC conducts this important analysis in a way that explores whether mutuals and shareholder-banks have the same or different approaches to the usability of buffers, given the different incentives at play. This can

¹³ The largest surplus of 23.7%RWAs is a point-in-time number just ahead of the Coventry building society's purchase of CoOp Bank. This was before the PRA increase in the threshold for application of the leverage ratio framework so included pre-funding of MREL leverage requirements.

¹⁴ These figures relate to YE2024. Leeds Building Society is now partial transfer.

then help the FPC to demonstrate that it is being mindful of the FSMA requirement to have regards for business model diversity and the impact of regulatory policies on mutuals.

We propose that the FPC in thinking about the usability of buffers, asks itself the following questions:

- What incentives are at play for firms to choose to utilise buffers and how does this feed into the size of any management buffer? How is this different for a mutual vs a shareholder-owned bank?
- What are the realistic scenarios where firms might operate within their buffers? As such, are buffers ever truly usable?
- What are the mechanisms to reduce incentives for firms to hold large management buffers in excess of regulatory buffers? We believe the options include: removal of the positive neutral CCyB; clearer communication of how any increase in the CCyB will be implemented e.g. a cap of say 0.5% as the maximum upwards increase that might be applied during the one year implementation period; removal of the capital conservation buffer in favour of a larger overall CCyB to ensure the whole buffer is considered releasable/usable; removing the link between buffers and restrictions on distributions (MDA) in line with the approach for SDDTs

Interactions between capital requirements for domestic exposures

The BSA is strongly supportive of the FPC reviewing the interactions between different capital requirements. While we understand that there are different risks associated to mortgages – credit risk, operational risk, concentration risk, risk of excess leverage – capital requirements need to be mindful of the layering effect that can result in capital that is dis-proportionate to the overall risk of losses that may occur across the portfolio. As one example of the excessively prudent nature of capital requirements, Coventry Building Society as at end 2024 held reserves equivalent to 900 years worth of credit losses experienced this century, including the credit crisis period.¹⁵

The standardised approach risk-weights for residential mortgages have been decreased by the Basel Committee over time from 50% (Basel I) to 35% (Basel II) to 20% (Basel 3.1) in recognition of the low-risk nature coupled with the much lower risk-weights generated by IRB models. This leaves regulators with a dilemma of applying prudence to protect against future housing market crises – which may be different from past crises – versus the clear social and economic benefits of facilitating home-ownership when compared to large sections of the population remaining trapped in the private rental market. This means that a re-assessment and potential re-calibration of the overall UK framework is timely and appreciated, while still adhering to international standards in the Basel framework. Our suggestions therefore focus on the elements that are UK-specific or gold-plating versus international standards.

The BSA has developed a stylised example loan based on typical observed data. This demonstrates the layering effect of capital requirements for domestic mortgage exposures. The example loan is for a £100k loan at 55% LTV. The items shaded blue are at the discretion of the PRA and not part of the Basel framework international standards. This example shows that the **total loss absorbing capacity (including MREL**

¹⁵ See also [written evidence to House of Lords Financial Regulation Committee](#), Jan 2025

and buffers) that is required for a low LTV mortgage is almost ten times higher than the pillar 1 requirement at £7,200 compared to £792.

| Capital held on prime residential mortgage | £ |
|--------------------------------------------------------------------|----------|
| Loan size | £100k |
| Property value (as origination) | £182k |
| Pillar 1 IRB RW (using PRA IRB benchmark) | 9.9% |
| Pillar 1 SA RW | 20% |
| Pillar 1 capital charge (IRB) | £792 |
| IRB floor @ 72.5% standardised approach (high level proxy) | £1,160 |
| Pillar 2a capital for credit concentration risk (1.4% for UK-only) | £138.6 |
| CRR buffers (CCoB+CCyB) | £652.5 |
| PRA buffer (from severe but plausible scenario) | varies |
| | |
| Leverage ratio (3.25% min) | £3,250 |
| Leverage ratio buffer | £700 |
| Total leverage + buffers | £3,950 |
| | |
| Total capital held against mortgage | £3,950 |
| | |
| MREL @ 2x binding minimum i.e. leverage | £6,500 |
| Total MREL + buffers held against mortgage | £7,200 |

These numbers refer to capital held for unexpected losses. By comparison, expected losses are captured through mortgage pricing and provisions under IFRS9, which also include levels of conservatism.¹⁶

Reviewing credit concentration risk

The UK FSA first set capital add-ons for credit concentration risk under Pillar 2a when they implemented Basel II in 2006/2007. Credit concentration risk reflects the risk that loans can be correlated and hence more vulnerable to shocks at the portfolio level in the event of a crisis. This has been applied in the UK to domestic-only lenders to reflect the lack of international diversification. For a UK building society, this means there are several ways of being penalised both for being domestic and for not being international e.g. the IRB floor is calibrated for a diversified firm given the floor applies across portfolios and hence the floor is more likely to bind for a low-risk monoline mortgage lender. Then at the same time, a pillar 2a capital add-on is applied to societies on the grounds of lending being UK-only – so extra capital for being domestic and further extra capital for not being international!

Pillar 2 of the Basel framework does not prescribe capital add-ons in the way they have been used in the UK. Many other jurisdictions do not apply capital add-ons

¹⁶ The move to IFRS9 provisioning models includes the need to take a more forward-looking view of credit risk losses

over and above the Pillar 1 minimum and a broad range of practices exist across the world.¹⁷

The BSA welcomes that the FPC and PRA intend to now review the approach to Pillar 2 more broadly and credit concentration risk specifically.

Thresholds that mitigate 'prudential drag'

The BSA welcomes that the PRA has re-set a number of regulatory thresholds during 2025. This ensures that thresholds remain fit for purpose over time and additional firms aren't captured purely due to average levels of growth and inflation. However, we would prefer in the future for the PRA to take a more holistic approach to thresholds to give firms a greater ability to anticipate future likely reviews, coupled with appropriate transitional periods to avoid cliff-edge implementation. The system could include the following elements:

- Defined timelines for reviews, such as every two years or more regularly in periods of higher inflation
- A published set of principles that the PRA will consider in its periodic review e.g. inflation, GDP, market share etc.
- The ability to review thresholds from first principles to reflect changes in the environment and risk appetite of the regulators, in line with the FSMA rule review requirements
- Careful consideration of cliff edge effects, and mitigation using transitional periods for implementation after crossing a threshold (so firms don't have to build up capacity too far in advance of crossing a threshold)
- Greater streamlining and simplification between different thresholds – fewer simpler thresholds capturing multiple requirements
- Automated indexation

PRA review of IRB modelling for mortgages (DP1/25)

The BSA is strongly supportive of the work that the PRA is conducting to try to address the current road blockages with existing IRB hybrid modelling approaches and also to introduce a more proportionate and accessible approach for medium-sized firms. We have responded in full to DP1/25 and engaged in other outreach with the PRA.¹⁸

¹⁷ See [Overview of Pillar 2 supervisory review practices and approaches](#), June 2019

¹⁸ See [BSA Response to DP1/25](#), October 2025