



Consultation on Own Funds Requirements for Investment Firms based on Fixed Overheads

Public Hearing
5 September 2013 | London

EBA

BTS in the context of EU legislation

Common rulebook

Maximum harmonisation

...but proportionate to different financial institutions

EU legislators
Sectoral Directives

EU Commission
'Implementing legislation'

EBA to
provide advice

EBA developing binding technical
standards

Binding Technical Standards

The EBA regulation (EU) No 1093/2010

- > Article 8(1): one of the EBA's tasks is to develop draft regulatory (RTS) and implementing technical standards (ITS).
- > Article 10(1): The EBA shall submit draft RTS to the Commission for the endorsement and shall conduct open public consultation before submitting draft RTS to the Commission.
- > Within 3 months of receipt of a draft RTS, the Commission shall decide whether to endorse it.
- > The Commission shall not change the content of a draft RTS prepared by the EBA without prior coordination with the EBA.
- > Article 10(4). The Regulatory technical standards shall be adopted by means of regulations or decisions. They shall be published in the Official Journal of the European Union and shall enter into force on the date stated therein.

Next steps and submission

- | | |
|---|------------------------------|
| ✓ Publication CRR | June, 2013 |
| ✓ EBA publishes the Consultation Paper | July, 2013 |
| <input type="checkbox"/> End consultation period | September 30, 2013 |
| <input type="checkbox"/> Endorsement of the final draft BTS
EBA Board of Supervisors | December or February
2013 |
| <input type="checkbox"/> Submission to the Commission | Q1 2013 |
| <input type="checkbox"/> Deadline | March 31, 2014 |
| <input type="checkbox"/> Commission to review, endorse and translate | + 3 months |
| <input type="checkbox"/> Parliament to review and endorse | + 1 month |
| <input type="checkbox"/> Publication in the Official Journal of the EU | + 1 day |
| <input type="checkbox"/> Entry into force after publication in the OJ | 20 days |

Mandate

- > Article 97(4) of Regulation (EU) No 575/2013 (CRR) mandates EBA to draft these RTS in consultation with ESMA to specify:
 - Calculations of the requirement to hold eligible capital of at least $\frac{1}{4}$ of the fixed overheads of the previous year (or projected fixed overheads if a starting firm)
 - Conditions for competent authorities to make adjustments in the capital requirements in case of material change in the business activities of a firm
- > Not a new requirement, was also in Directive 2006/49/EC

Aim of this RTS

- > RTS targeted at investment firms with limited authorisation to provide investment services as set out in articles 95 and 96 of the CRR
- > Also relevant to management companies, as defined under UCITS Directive, and Alternative Investment Fund Managers (AIFMs)
- > So far different concepts used in different member states
- > Aim is to harmonise calculations of capital requirements and to provide a clear definition of fixed overheads
- > Also harmonise conditions for competent authorities to make adjustments to the capital requirements.

Approaches considered

- > Two alternatives were considered – ‘additive’ and ‘subtractive’ approach
- > The EBA proposes ‘subtractive’ approach where variable cost items would be deducted from total expenses
- > Changes to the accounting framework automatically taken into account
- > Can be used if firm does not use IFRS, appropriate for smaller firms
- > Minimises the risk of faulty classification

- > ‘Additive’ approach would consist of adding up pre-defined accounting items
- > Risk that some cost items could be wrongly re-classified
- > Problematic given different national accounting standards

Definition of fixed overheads

> Items to be deducted from total expenses:

- (a) fully discretionary staff bonuses;
- (b) employees', directors' and partners' shares in profits, to the extent that they are fully discretionary;
- (c) other appropriations of profits, to the extent that they are fully discretionary;
- (d) shared commission and fees payable which are directly related to commission and fees receivable, which are included within total revenue, and where the payment of the commission and fees payable is contingent upon the actual receipt of the commission and fees receivable;
- (e) fees, brokerage and other charges paid to clearing houses, exchanges and intermediate brokers for the purposes of executing, registering or clearing transactions;
- (f) fees to tied agents;
- (g) interest paid to customers on client money;
- (h) extraordinary non-recurring expenses.

> Tied agents to be included with 35% fixed lump sum per agent

Thresholds

- > Competent authorities shall consider that a *material* change has occurred in the business of an investment firm since the preceding year if:
 - the change in the business of the firm results in [20%] change in the firm’s projected fixed overheads;
 - the change in the business of the firm results in changes in the firm’s capital requirements that amount to [2 million EUR] or more.

- > A material change will trigger a change in the capital requirement

Contact information

Katrin Johanson

Katrin.johanson@eba.europa.eu

+44 (0)20 7997 5945

European Banking Authority

Floor 18 | Tower 42 | 25 Old Broad Street

London EC2N 1HQ | United Kingdom

t +44 (0)20 7933 9900

f +44 (0)20 7382 1771

info@eba.europa.eu

www.eba.europa.eu