



Vereniging van Vermogensbeheerders & Adviseurs

European Banking Authority
One Canada Square (Floor 46)
Canary Wharf
London E14 5AA| UK

Amsterdam, 2 February 2017

Re: EBA Discussion Paper 4th November 2016

Dear Sirs,

On behalf of the Dutch Association of Asset managers and Advisors (*'Vereniging voor Vermogensbeheerders & Adviseurs'*, hereinafter "**VV&A**"), we would like to respond to the EBA Discussion Paper dated November 4, 2016 by giving our views on a new prudential regime for investment firms.



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1. Introduction

VV&A is a Dutch branch organization.

The Netherlands has two categories of investment firms: banks and non-banks. The primary objective of the VV&A is to represent and address the common interests of the non-bank investment firms. All these firms are registered as independent investment firms with the Dutch regulator the Autoriteit Financiële Markten. At present 60% of all Dutch non-bank investment firms are members of our association the VV&A.

The VV&A is authorized by her members to represent their interests in discussions and consultations with the following authorities: the Ministry of Finance, the Dutch Central Bank (DNB), and the Autoriteit Financiële Markten (AFM). The VV&A is also responsible for handling several other issues which have a specific impact on the whole sector together with other associations such as the Dutch Association of Banks (DAB) and the Dutch Fund and Asset Management Association (DUFAS).

The VV&A itself has a managing board of six professionals, all of whom in turn are managing directors of independent investment firms affiliated with the VV&A. The VV&A stimulates an active form of both face-to-face and online exchange of opinions and information with her members, gaining where necessary extra input from an expert external team of legal advisors.



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2. General remarks

We understand that EBA proposes to make a distinction between three classes of investment firms:

- (i) Systemic and bank like investment firms (Class 1);
- (ii) Investment firms that are not systemic and bank like (Class 2);
- (iii) Very small and not interconnected investment firms (Class 3).

VV&A represents in particular very small and non-interconnected investment firms. Consequently, our respond to the Discussion Paper is limited to Class 3 investment firms.

2.1 A new regime

In favor of a new prudential regime

First of all, we would like to point out that VV&A is in favor of introducing a new prudential regime for investment firms. It is our strongest believe that a new regime enables capital requirements tailored to the needs of the business models of all different type of investment firms operating in the European market. In order to achieve this, an appropriate design and calibration of all relevant aspects of the new regime is required.



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Opposed to overhead requirements only

Class 3 investment firms should not be subject to fixed overhead requirements only. Given the diversity of all business models, fixed overhead requirements are contradictory to the principle of proportionality. A clear disadvantage of fixed capital requirements is that they may be too severe to certain type of business models and too 'soft' for other type of business models.

Minimum capital requirements should apply

However, certain initial or minimum capital requirements should apply on all investment firms. Minimum capital requirements can be determined on the basis of the type of investment services – and consequently, the risks involved – rendered. Minimum capital requirements contribute to financial healthy investments firms.

2.2 MiFID

The Discussion Paper refers to several types of capital proxies or factors (called the 'k-factors'):¹

- a) *Assets under management (AUM)*
- b) *Assets under advice (AUA)*
- c) *Assets safeguarded and administered (ASA)*
- d) *Client money held (CMH)*
- e) *Liabilities to customers (LTC)*
- f) *Customer orders handled (COH)*
- g) *Proprietary trading activity (PTA)*

¹ Discussion Paper, page 18-20.



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The application of the relevant k-factors depend on the type of services rendered by the investment firm. The Discussion Paper refers to the following type of services:²

- a) *Holding client money or securities;*
- b) *Ancillary service of safekeeping and administration (B1);*
- c) *Dealing on own account (A3);*
- d) *Underwriting or placing with a firm commitment (A6);*
- e) *The granting of credits or loans to an investor (B2);*
- f) *Operating a multilateral trading facility (or MTF) (A8);*
- g) *The MiFID II activity or operating an organised trading facility (or OTF);*
- h) *Being member of a wider group;*
- i) *Using MiFID passport, and;*
- j) *Using tied agents.*

Both (i) the criteria pursuant to which investment firms are categorized in classes and (ii) the design of a single, harmonized set of requirements enable to cover the broad range of all types of investments firms, must be clear and simple.

In our opinion a clear and understandable application of the k-factors can only be achieved by connecting these factors to the type of investment and ancillary services as defined under MiFID 2.

² Discussion Paper, page 16.



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MiFID 2 defines the following type of investment services:³

- i. Reception and transmission of orders in relation to one or more financial instruments;*
- ii. Execution of orders on behalf of the clients;*
- iii. Dealing on own account;*
- iv. Portfolio management;*
- v. Investment advice;*
- vi. Underwriting of financial instruments and/or placing of financial instruments on a firm commitment basis;*
- vii. Placing of financial instruments without a firm commitment basis;*
- viii. Operation of a MTF;*
- ix. Operation of a OTF.*

In order to achieve a new prudential regime that is understandable, appropriate and proportional, each type of investment service as defined under MiFID 2 should lead to the application of a prescribed k-factors.

For instance: on a firm rendering investment advice as defined under MiFID 2 and no other investment services, only the k-factor AUA should apply. Please note that all Class 3 investment firms are regulated under MiFID 1 and in the near future MiFiD 2, and that for these firms the framework and regulation MiFID is their 'legal environment'.

We recommend to replace the categorization of investment services currently mentioned in the Discussion Paper by the MiFID definitions of investment services.

³ Regulation 2014/65/EU (MiFID II), Annex I (A).



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2.3 Particulars Dutch law

Securities depository foundation and segregation

The securities depository foundation is a typical Dutch manner of segregation of clients' assets. The manner of conducting depository services in the Netherlands differs relative to other European countries. Last year, a few alterations were made in the legal framework regarding conducting depository services. This new regulation provides in a stringent and comprehensive set of rules regarding the segregation of assets. Therefore, the interests of depositors are properly safeguarded under the Dutch framework.

Investment firms in the Netherlands are obligated to segregate clients' financial instruments and other funds. The latter does not apply to investment firms that hold a banking license. Funds and financial instruments must be kept in a segregated account. The clients' funds and financial instruments are thus protected in the event of bankruptcy and the client is exposed to a minimal risk of losing his money or instruments. It is unclear whether this segregation (and the protection it offers to clients) is taken in account with respect to the new prudential regime.

VV&A understands that not every European framework does provide in a similar segregation obligation. Failure of Class 3 Dutch investment firms will not affect the clients rights. The k-factor ASA must take this into account.



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3. Dutch markets and a few concrete examples

In order to have a better understanding of the impact of the k-factors we have calculated the capital requirements that will apply on investment firms 'Class 3' by identifying the most common business models for retail investment firms operating in the Dutch market:

- i. Rendering investment advice;
- ii. Rendering investment advice and transmission of orders;
- iii. Rendering investment advice and execution of orders;
- iv. Portfolio management and transmission of orders;
- v. Portfolio management and execution of orders; and,
- vi. Portfolio management including the aggregation of funds via a securities depository.

Based on the presentation held by the Dutch Central Bank in November 2016⁴, we have made our calculations based on the following assumptions of the k-factors:

- i. 0.1% for asset under management (AUM)
- ii. 0.02% for assets under advice (AUA)
- iii. 0.1% for assets safeguarded and administered (ASA)
- iv. 5% for client money held (CMH)
- v. 0.1% for liabilities to customers (LTC)
- vi. 1% for customer orders handled (COH)
- vii. 1.5% for proprietary trading activity (PTA)

Please note that we are aware of the fact that these assumptions are not mentioned in the Discussion Paper.

⁴ Presentation Dutch Central Bank 'Seminar Beleggingsondernemingen' d.d. 15 November 2016.



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Example 1

1. Investment advice without transmission or execution of client orders:

AUM	€ 125,000,000
Number of portfolios	250
Average portfolio value	€ 500,000
Total number of orders under advice a year	5,000

Business model I:



Explanatory notes:

The investment services are limited to investment advice only. The firm does not transmit or execute client orders. The client must refer to another investment firm for the execution of orders.

Outcome calculation:

Advised capital:	€ 125,000,000
AUA =	€ 25,000
(< ICR and < FOR)	
Outcome:	€ 25,000



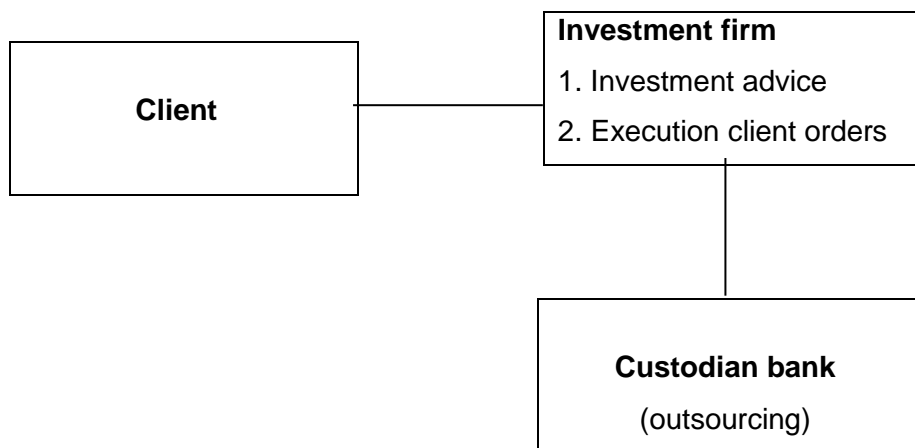
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Example 2

2. Investment advice with execution of client orders:

AUM	€ 125,000,000
Number of portfolios	250
Average portfolio value	€ 500,000
Total number of orders under advice a year	5,000

Business model II:



Explanatory notes:

The investment services include investment advice and the execution of client orders. The execution of client orders is outsourced by the investment firm to the custodian bank.

Outcome calculation:

Advised capital:	€ 125,000,000
AUA =	€ 25,000
COH =	€ 50
(< ICR and < FOR)	
Outcome:	€ 25,050



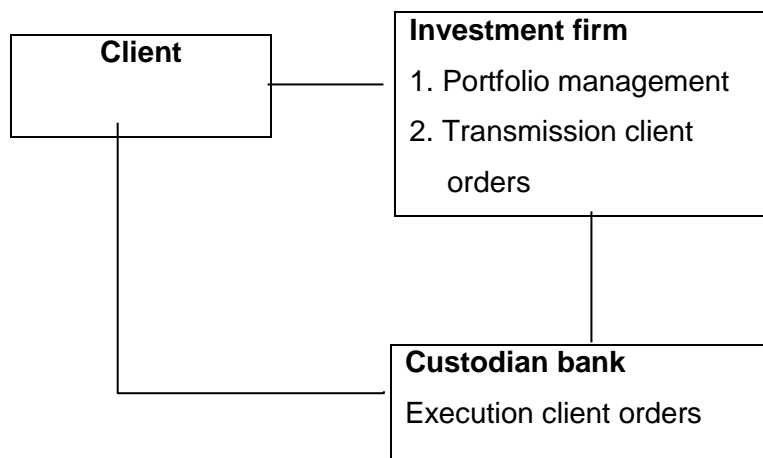
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Example 3

3. Portfolio management and transmission of client orders:

AUM	€ 125,000,000
Number of portfolios	250
Average portfolio value	€ 500,000
Total number of orders under advice a year	5,000

Business model III:



Explanatory notes:

The services include portfolio management and transmission of client orders. The custodian bank has a legal obligation towards the client (and not the investment firm) for execution of orders.

Outcome calculation:

Managed capital:	€ 125,000,000
AUM =	€ 125,000
COH =	€ 50
Outcome:	€ 125,050



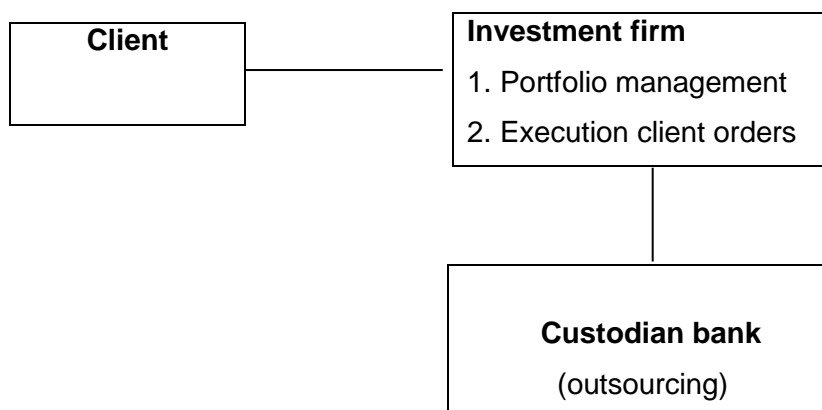
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Example 4

4. Portfolio management and execution of client orders:

AUM	€ 125,000,000
Number of portfolios	250
Average portfolio value	€ 500,000
Total number of orders under advice a year	5,000

Business model IV:



Explanatory notes:

The services include portfolio management and the execution of client orders. The execution of client orders is outsourced by the investment firm to the custodian bank.

Outcome calculation:

Managed capital:	€ 125,000,000
AUM =	€ 125,000
COH =	€ 50
Outcome:	€ 125,050



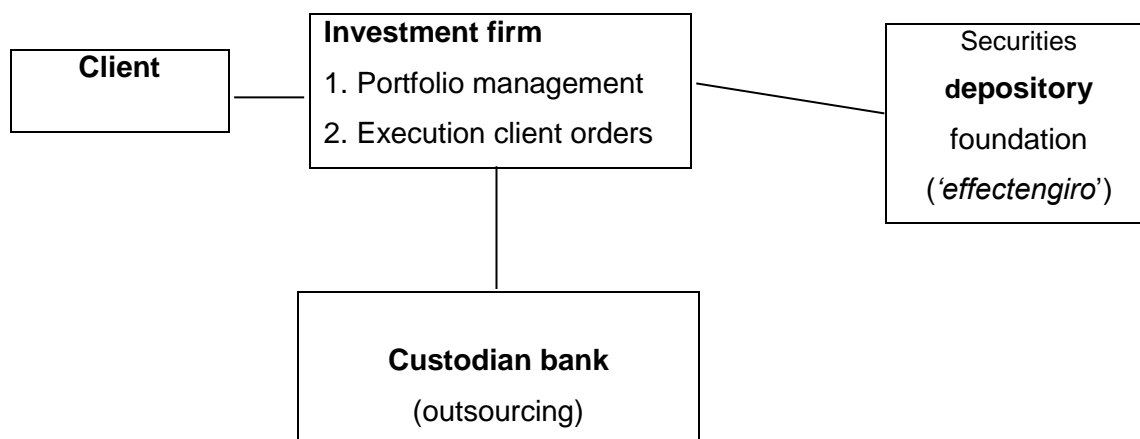
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Example 5

5. Portfolio management with depository:

AUM	€ 1,500,000,000
Number of portfolios	250
Average portfolio value	€ 500,000
Total number of orders under advice a year	5,000
Whereof the maximum of 'client money held'	€ 1,000,000

Business model V:



Explanatory notes:

The investment services include portfolio management and execution of client orders. The execution of client orders is outsourced by the investment firm to the custodian bank. The depository is responsible for safekeeping and administration of the various assets of the investment firm.

Outcome calculation:

Managed capital:	€ 1,500,000,000
AUM =	€ 1,500,000
ASA =	€ 1,500,000
COH =	€ 50
Outcome:	€ 3,000,050



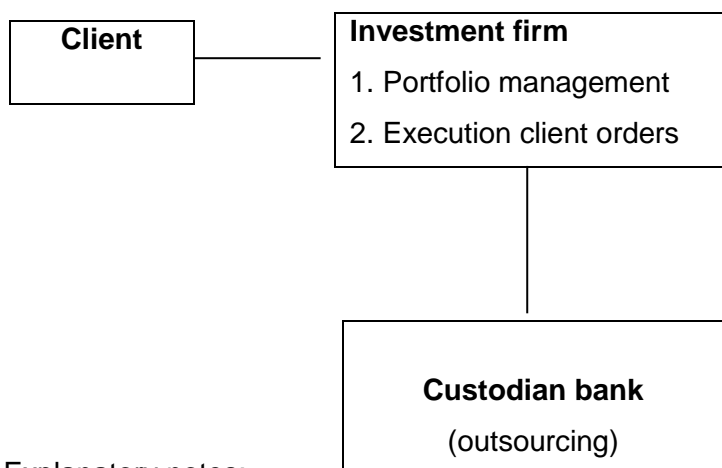
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Example 6

6. Portfolio management and execution of client orders:

AUM	€ 1,500,000,000
Number of portfolios	3,000
Average portfolio value	€ 500,000
Total number of orders under advice a year	60,000

Business model VI:



Explanatory notes:

Please note, this business model is the same as business model IV. Only the assets under management differs.

The services include portfolio management and the execution of client orders. The execution of client orders is outsourced by the investment firm to the custodian bank.

Outcome calculation:

Managed capital:	€ 1,500,000,000
AUM =	€ 1,500,000
COH =	€ 600
Outcome:	€ 1,500,600



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4. Response to specific questions

4.1 Very small, non-interconnected investment firms:

Questions 3 and 4.

What are your views on the identification and prudential treatment of very small and non-interconnected investment firms ('Class 3')? If, for example, such class was subject to fixed overhead requirements only, what advantages and drawbacks would have introducing such a Class 3? Conversely, what advantages and drawbacks could merging Class 3 with other investment firms under one single prudential 'built-in' proportionality have?

What are your views on the criteria discussed above for identifying 'Class 3' investment firms?

Response

We understand that Class 3 comprises of different types of investment firms. The investment firms belonging to the aforementioned 'Class 3' vary between large, sophisticated firms that hold a banking license and firms with relatively simple business models.

VV&A represents investment firms that have a relatively simple business model. We expect that these small investment firms will not exceed the FOR.



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Currently, investment firms in the Netherlands must report four times annually. We propose that small investment firms must report their data under the CRD IV annually. Given that the FOR is the only relevant factor for the smaller investment firms, all administrative costs to be made in the calculation of k-factors are not proportionate with respect to the modest size of investment firms that do not exceed the FOR.

We therefore propose, to develop a less stringent regime within Class 3 designed for the smallest investment firms. This regime may for example provide in less comprehensive reporting obligations compared to the larger, more sophisticated Class 3 investment firms that do exceed the FOR.

The distinction between larger firms (that would not qualify for the less stringent regime) and smaller firms (which would qualify for the less stringent regime) may be made by looking at the scale of operations (AUM/AUA), the complexity of the business and whether or not the firm holds a banking license.

Or more specifically:

- i. A balance sheet total of less than € 10,000,000;
- ii. Annual turnover of less than € 10,000,000;
- iii. Less than 50 FTE's.



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4.2 K-factors:

Question 5.

Do you have any comments on the approach focusing on risk to customers (RtC), risk to markets (RtM) and risk to firm (RtF)?

Response

Chapter 3 of this memo provides six examples that clearly indicate a linear graduated scale if the percentages provided by DNB are used. Currently, no regression in the graduated scale can be seen. Therefore, highly coveted economies of scale are not rewarded. A regression in the graduated scale is highly recommendable.

Besides, there is an overlap in k-factors between asset management and depository activities. Example 5 in chapter 3 clearly shows. Please note that we assume that the k-factor CMH does not apply in this example and that no cash is held within the depository, but all invested (possible in money market funds).

Example 5 is a clear example of double counting. The portfolio manager is subject to a factor AUM of € 1,500,000 and (possibly) a factor ASA of € 1,500,000. In the current prudential regime, the same portfolio manager is subject to a capital requirement of € 125,000. This example demonstrates the effect of double counting (AUM/ASA) and also shows the absence of 'economies of scale' in the envisaged system.

V&A proposes to provide national supervisory authorities (for example DNB in the Netherlands) with the option to set certain k-factors to 0 if the national legal framework provides in regulation aiming to diminish potential risks with respect to depository services.



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Investment firms are usually insured against liability risks. Insurance diminishes the risks with respect to clients. This should be a relevant factor in the calculation of the relevant k-factors.

The reference date for the calculation of the relevant k-factors is unclear to VV&A. In the current Dutch legal framework, the capital requirements are calculated on a quarterly basis based upon the k-factors of the previous year. In the Dutch framework, certain exceptions/deductions may apply (for example if marketing expenses were made). The k-factors would be higher compared to the calculation of the k-factor with the actual costs of the upcoming year.

Question 9.

Should a fixed overhead requirement (FOR) remain part of the capital regime? If so, how could it be improved?

Response

VV&A is an advocate of maintaining the FOR. The current FOR is not forward looking. In the Netherlands, the calculation of the FOR is based on the previous year. The FOR reflects only the costs of the previous year and hence shows no clear image. Calculating the FOR based on the previous year will impede businesses in their growth. VV&A believes that the FOR should be more flexible by having possible deductions.



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An example can be given when marketing costs occur. For instance, an investment firm has marketing costs in 2016 and will not have these in 2017. The FOR will be calculated on the basis of the costs incurred in 2016. In 2017, additional capital is required to be held due to the high costs in 2016. This shows no realistic image and impede businesses in their growth.

Contractual obligations must always be included in the calculation of the FOR. If there is a contractual obligation, then it should be calculated into your FOR. Deductible costs are the costs which have no contractual basis, and ended in the previous year. This may include marketing costs and/or flexible labor, provided that there is evidence that these costs are no longer a contractual obligation.

4.3 Definition and quality of capital for investment firms:

Question 18.

What aspects should be taken into account when requiring different levels of initial capital for different firms? Is there any undesirable consequence or incentive that should be considered?

Response

VV&A believes that the initial capital must be determined by the nature of the investment service.



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A distinction should be made between advice and management. Similarly a distinction between the investment firm that safeguards and administers client money, and an investment firm that makes use of a custodian bank. The place of execution of orders should also be relevant for determining the initial capital.

Question 19.

What are your views on whether there is a need to have a separate concept of eligible capital, or whether there is potential for simplification through aligning this concept with the definition of regulatory capital used for meeting capital requirements?

Response

VV&A calls for designing a simpler model in which one kind of capital must be maintained as standard capital.

DNB provides a license to the investment firms that do not exceed the threshold of € 50,000 of eligible capital. This license does not have any additional value, because most investment firms exceed the € 50,000 threshold. Thereby these investment firms still meet the many capital requirements, which makes it complicate to calculate. The model should be simplified for the smallest investment firms within Class 3.



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4.4 Corporate governance and remuneration:

Questions 31 and 33.

What are your views on the relevance of CRD governance requirements to investment firms, and what evidence do you have to support this?

What is your view on a prudential remuneration framework for other than 'systemic and bank-like' investment firms that should mainly aim to counteract against conduct related operational risks and would aim at the protection of consumers?

Response

To minimize the risks to consumers, a certain degree of financial requirements are needed in the remuneration system of investment firms.

The Netherlands has a more stringent remuneration policy compared to other European countries. This more stringent remuneration policy is a burden on the amount of FOR. This Dutch policy impedes the level playing field for the Dutch investment firms. Equality between Member States is essential for competitiveness. VV&A is in favor of designing a harmonized remuneration policy in Europe. To minimize the risks to consumers, a certain degree of financial requirements are needed in the remuneration system of investment firms.



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VV&A is in favor of the use of a distinction between different types of firms. A clear distinction should be made between privately held companies and for instance, listed companies. Privately held companies handle their remuneration more carefully and thus entail fewer risks to consumers. The shareholder of a privately held company will be rather affected.

4.5 Alternative approach to a new regime:

Question 34.

What are your views on having a separate prudential regime for investment firms? Alternatively, should the CRR be amended instead to take into account a higher degree of proportionality? Which type of investment firms, if any, apart from systemic and bank-like investment firms, would be better suited under a simplified CRR regime?

Response

In light of proportionality, VV&A recommends to make a distinction between (a) privately held companies and (b) public and/or listed companies, since shareholders in privately held companies do not (generally) cause the same negative effects as shareholders in public or listed companies (may) do.

Given the extent shareholders can experience negative effects, VV&A suggests that a privately held company should be eligible for a simplified CRR regime since the risk posted to customers is generally minimal considered the above.



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Question 35.

What are the main problems from an investment firm perspective with the current regime? Please list the main problems with the current regime.

Response

VV&A identified two problems with regard to the current regime.

The first problem VV&A identifies is that certain variable costs are taken into account while calculating the FOR and hence the FOR is calculated too high.

The FOR is not forward looking. The outcome of the FOR may be too high and can impede a growth situation. The FOR should be more realistic and aimed at the future.

Therefore, VV&A proposes to calculate the FOR by taking only the contractual obligations into account, and not just the obligations that existed in the previous year. This allows the FOR to be more realistic. For example, it would be prudent to exclude the costs of flexible workers from the calculation of the FOR of 2017, if these flexible workers will no longer work for the company in 2017.

The second problem of the current regime is that the frequency of reporting is too high. Currently investment firms are obliged to report quarterly. The small investment firms experience reporting on a quarterly basis as a very heavy administrative burden. VV&A is in favor of an annual reporting obligation for small investment firms in order to diminish the administrative burden and costs'



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5. Conclusion

1. VV&A is proponent of a new prudential regime. However, an appropriate design and calibration of all relevant aspects of the new regime is required.
2. VV&A is an advocate of maintaining the FOR. However, VV&A believes that the FOR should be more flexible by having possible deductions. Deductible costs are the costs which have no contractual basis or a contractual basis less than twelve months.
3. Within Class 3 a lighter regime should be introduced for very small investment firms with a relatively simple business model. VV&A proposes that small investment firms must report their data under the CRD IV annually.
4. Economies of scale should be rewarded by having regression in the graduated scale.
5. The interests of depositors are properly safeguarded under the Dutch framework. It would not be sensible to impose additional capital requirements to depositories governed by Dutch law.

We propose to provide national supervisory authorities (for example DNB in the Netherlands) with the option to set certain k-factors to 0 if the national legal framework provides in regulation aiming to diminish potential risks with respect to depository services.

6. VV&A advocates equality between Member States. This Dutch remuneration policy impedes the level playing field for the Dutch investment firms. VV&A is a proponent to harmonization of the remuneration policies within Europe.

Yours sincerely,

Mr. T. Andringa

Chairman VV&A