THE INVESTMENT ASSOCIATION

Response to EBA consultation on prudential requirements for Investment Firms

EBA/CP/2020/06

About the Investment Association

The Investment Association (IA) champions UK investment management, a world-leading industry which helps millions of households save for the future while supporting businesses and economic growth in the UK and abroad. Our 250 members range from smaller, specialist UK firms to European and global investment managers with a UK base. Collectively, they manage £7.7trillion for savers and institutions, such as pension schemes and insurance companies, in the UK and beyond. 40% of this is for overseas customers. The UK asset management industry is the largest in Europe and the second largest globally.

Overview of questions for consultation

1. **Is the proposed articulation of the K-factors calculation methods, in particular between AUM and CMH and ASA, exhaustive or should any other element be considered?**

The IA welcomes the overall approach by the EBA to not provide further specification from the IFR, which in most cases are already clear. However, there are some areas where further clarity is still required in order to ensure that the RTS reflects generally accepted methods for calculating and reporting AUM and properly reflect the inclusion or exclusion of discretionary and non-discretionary services. The IA would like the EBA to amend the RTS to clarify that the valuation basis for AUM and ASA should be net asset value.

According to paragraph 3.6.1 in the CP, the relevant amount of metric (AUM) should be included within the total K-AUM of the investment firm using a tied agent. Where this 'tied agent' is also a MiFID investment firm and subject to the same regulation, clarification is sought on whether this would be deemed as a double count.

No further guidance has been provided in the consultation paper for K-NPR as market requirements are set out in the CRR and Regulation (EU) 2019/876 (CRRII). However, we believe there is still ambiguity as to whether this relates solely to firms that have permissions to deal on own account and have trading book positions. IFR article 21 (4) indicates that RtM k factor requirement shall include positions other than trading book positions where those give rise to foreign exchange risk or commodity risk. For firms that do not have permissions to trade on own account, this could potentially significantly increase the scope of reporting.

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2. **Are the requirements for notion of segregated accounts sufficient? Are there issues on segregated accounts which need to be elaborated further?**

While clarity has been added on the definition of a segregated account, it is not clear what is held in a non-segregated account. Currently in the UK, holding client money in a non-segregated account would be a regulatory breach so the IA is keen that the EBA provide further clarity on the proposed use of segregated vs. non segregated accounts.

3. **Is there any example of situations of market stress which would not been taken into account applying the proposed approach but would be relevant for the measurement of the K-DTF?**

No material comments.

4. **What would be appropriate thresholds or events that should trigger the comparison between the calculation under the K-CMG compared to the one under the K-NPR?**

No material comments.

5. **Which other conditions should be considered to avoid double counting or to prevent regulatory arbitrage in the use of the K-CMG approach?**

The IA would like further clarity on the exclusion of the 2 highest daily amounts of total margin required by the clearing member during a 3-month period as there is potential ambiguity in the where an investment firm uses multiple clearing members. For example, should it be the third highest combined daily total of margin given on a single day, or be the sum of the third highest amounts of margin given to each clearer, even if those amounts for each clearer occur on different trading days.

Article (3) of the CP clarifies that this should be done by first determining the third highest amount of total margins required on a daily basis by each clearing member separately over the preceding three months, then adding those amounts. The IA view is that it would be more consistent with the overall concept of clearing margin given for an investment firm to first add up, across all clearing members used, the margins for each day. Essentially, that is the amount that was there at the end of that day, as the margin call made at the end of the day is typically what is 'given' to the clearer the next morning. The third highest such amount across the relevant observation period would then be taken. The alternative approach of adding margins from different clearing members from different trading days could be more prudent, but this is less likely to reflect how the underlying risk is managed in practice.

6. **Do you have any comment on the elements included in this Consultation Paper for the application of the aggregation method?**

The IA do not agree with the approach taken by the EBA in defining a completely new scope of group constellations in Articles 2 to 5 of the Draft RTS, which appear to contradict the approach taken by the IFR definition of an investment firm group with reference to Article 22 of Directive 2013/34/EU. In addition, Articles 2 to 5 of the Draft RTS considerably deviate from the current regulations on own funds on a consolidated basis for groups consisting of investment firms only (i.e. without any credit institutions) as detailed in the Capital Requirements Regulation (CRR2) Article 98.

7. **Do you currently use the method of proportional consolidation for the consolidation of subsidiaries in accordance with Article 18(4) of Regulation (EU) No 575/2013? If proportional consolidation is used, please explain if the conditions included in this Consultation Paper are met.**

No material comments.

8. **Do you have any comments on the conditions established in this Consultation Paper to apply proportional consolidation to investment firms groups under Regulation (EU) No 2019/2033?**

Currently, the wording in Article 7 suggests that a firm is obligated to obtain permission from the competent authority if it follows the default treatment for joint control by using proportional consolidation. The IA assumes that, because it is the default treatment, firms in the first instance would apply proportional consolidation without obtaining prior approval from the group supervisor. It would then be for the competent authority to challenge the position taken by the investment group.

It is requested that the EBA provide clarification that, given it is the default treatment, proportional consolidation may be applied by the investment firm group in the first instance. The competent authority may require another accounting treatment on a case-by-case basis.

9. **The methods for calculating the K-factors in a consolidated situation may allow for further specifications. Is there any K-factor for which the calculation in the context of the consolidated basis would require further specifications? What aspects should be considered?**

It is not clear what is the correct treatment of cross-holdings between two entities within the same consolidation group or which have the same ultimate parent company where both of these entities are required to calculate an AUM-based capital requirement. Specific clarity on this point within the RTS would be welcomed.

Without further clarity, holdings that have shared ownership may not be correctly applied to the relevant entities which will impact the accuracy of the K-AUM calculation. It is recommended that the EBA clarifies the correct treatment of cross-holdings between entities that are part of the same parent group. This is just as relevant to K-COH as it is to K-AUM.

In addition, it would be helpful to clarify whether the intention of Article 11(3)(a) is to apply to all undertakings in a consolidation group. The IA understand that the overall aim is to ensure that all AUM is captured but ensure that none is captured twice. In the situation where there is a ManCo in the group then, for the purposes of the consolidated K-AUM, the full value of the ManCo AUM should be included in the calculation. However, the K-AUM calculation methodology should not be applied to the individual ManCo capital calculation under the terms of the AIFMD rules. Any other interpretation would create an unlevel playing field as an AIFM / UCITS entity could be subject to significantly higher capital requirements (via K-AUA and K-CMH in particular) than an AIFM / UCITS entity that is not within an Investment Firm Group. The IA believes the EBA should clarify that these K-factors should only apply to MiFiD business within the group in order to avoid this.

IFR article 4 (11) defines the consolidated situation as parent entity, investment firms, financial institutions, ancillary services undertakings and tied agents, however there is uncertainty around the treatment of AIFMs/UCITS that do not have additional MiFID permissions, should they be included within the scope of the consolidated K-factor? For K-factors that are relevant to both investments firms within scope of the regulation and AIFMs/UCITS/CPMs it would appear appropriate to include them, for example AUM, however where AIFMs/UCITs have specific permissions not relevant to firms in scope of this regulation, should they also be calculated? For example, where a Collective Portfolio Management firm that does not have MiFID permission but does have restricted box trading permissions, is included within the consolidated situation, this could potentially give rise to RtM K-factors such as K-DTF for the group significantly increasing the reporting burden on activities that are not undertaken by entities within scope of this regulation.

The consultation paper provides extensive detail on the 4 elements of Customer orders handled, however we would appreciate clarification on the exclusion of orders handled that, according to article 20 (IFR) ".. arise from the servicing of a client's investment portfolio where the investment firm already calculates K-AUM in respect of that client's investments." Is it the EBA's intention that for investment firm groups that have a single dealing entity within the group that this investment firm will report a K-CoH on a solo basis (for all clients within the group that are not contracted with this entity for investment management) but upon consolidation this K-factor will disappear as all orders are part of servicing a client's investment?

1. Draft RTS on the information to be provided for the authorisation of investment firms as credit institutions

No material comments.

2. Draft RTS on the calculation of the threshold referred to in Article 4(1)(1b) CRR

Accounting standards to calculate the total value of assets
Article 3 (2) refers to prudential individual reporting yet this term is not clearly defined. Given that this could be the subject of local regulations, there could be variation in the reports used and potential inconsistencies in the application of this statement. Without further clarity firms may not use the same basis for calculating the total value of assets for an institution. This may have most impact for firms with a number of entities in different countries. This would appear to conflict with the principle of harmonisation that is a stated objective of the regime. It would be helpful if the EBA could define this term and clarify if the report used for the consolidating entity should be used for this calculation. This would help ensure that application of the legislation is consistent between different jurisdictions that may have pre-existing rules for individual vs. consolidated reporting.

Article 3 appears to suggest a waterfall approach is applied i.e. only if an institution cannot determine the value based on prudential reporting, audited annual accounts as prepared under IFRS should be applied, and, if that is not available, the non-statutory financial statements should be used to calculate the total value of assets. It would be helpful if the EBA could confirm if this interpretation is correct and advise if firms are at liberty to select which method from Article 3 (2-4) they wish to apply.

As an alternative to allowing differing local applications, the EBA could consider prescribing a uniform definition of assets that applies in determining the threshold amount. In order to ensure that the thresholds are risk sensitive and proportionate, the EBA should consider within the definition to allow:

1. Exclusion of assets that are deducted from own funds. Currently, an Investment firm that has a large deductible asset (e.g. Goodwill) could trigger the threshold amounts as a result. However, this would seem to “double-hit” a firm as the asset is already fully deducted for determining own funds and therefore any risk of harm is already fully addressed/ nullified. If those same assets were then to result in the firm being subject to additional requirements, this would appear counter-intuitive. The EBA should therefore consider allowing assets that are deducted from own funds to also be deducted from the Total Assets definition in determining the meeting of the thresholds.
2. Allow the netting of Assets with Liabilities that are closely related and are largely offsetting. In some regions, the legal form of the funds combined with the applicable accounting standard means that, as an agent, the asset manager temporarily holds a receivable from the client/ fund (depending on whether the transaction is a subscription or redemption) and a vice versa payable to the fund/ client. These are based on volumes of activity in and out of funds during the T+3 settlement period. This balance can be volatile during periods of large activity. However, given the mitigated nature of the risk, they should be excluded from the definition of Total Assets for the purposes of determining thresholds. This would

remove significant volatility from the determination of Total Assets of asset managers and allow a more consistent and risk sensitive application.

We recommend that the requirements utilise the same basis of calculation for all thresholds. This RTS uses “total assets” while Article 32(4)(a) on Variable Remuneration uses “value of on and off-balance sheet assets”. The IA recommend the use of Net Assets/Shareholders Funds as calculated under accepted accounting frameworks as an appropriate metric for establishing thresholds. This would have the benefit of off-setting significant creation and redemption balances, a concern for some members firms, being a well-recognised metric, being subject to disclosure on an annual basis as part of the individual firm’s disclosure requirement, and likely to be aligned to the Own Funds of the firm and therefore reflective of the risk profile of the firm.

Application of exchange rates
The IA would welcome clarity on the expectations the EBA has for the source for the spot exchange rate referred to in Article 4. Without further clarification, there may be inconsistencies in the calculation of total assets. If firms are all required to use one source, the converted value may differ between their audited accounts (where their own source is used) and the value used for this calculation. It would be helpful if the EBA confirm firms are allowed to apply exchange rates consistent with their annual accounts.

The article refers to (i) the spot exchange rate prevailing at the date the amount is recorded and (ii) the spot exchange rate prevailing at the reporting reference date. The IA would prefer that the exchange rate at the reporting reference date be the reference point as it eliminates any inconsistencies that may arise if there is a delay in recording the information.

3. Draft RTS to specify the calculation of the fixed overheads requirement and to define the notion of a material change

Materiality
The draft requirements provide that a material change in fixed overheads is either a 30% change in the firm’s projected overheads or a €2m change in the firm’s own funds requirement based on fixed overheads. When considered against the materiality levels applied by audit firms (typically ca. 5% of Profits before Taxation) applying only the €2m change in fixed overheads requirement would lead to medium/large investment managers being required to change their fixed overheads requirement for changes in their cost base that could be considered immaterial. Likewise, applying only the 30% change in the fixed overheads would lead to a number of firms not changing their fixed overhead requirement for changes that in other contexts would be considered material. The opposite would be true of smaller firms where a change of €7m and 25% in fixed overheads would not lead to a requirement for the firms to change the fixed overhead requirement for a change that would be considered material in other contexts.

The IA suggests a material change is one where there is a change in fixed overheads of greater than 20%. This would provide for an appropriate change that is proportionate for all sizes of firm.

Otherwise, the IA would like the EBA to suggest a simpler approach of a given percentage as this should be proportionate for all firms.

It would also be helpful to clarify whether firms themselves should adjust their Fixed Overhead Requirement when the materiality threshold is met or it can only be adjusted by the Competent Authority (as suggested by Article 13(2) of the IFR). Given the frequency of Competent Authority review and given that the materiality thresholds are objectively defined, the EBA should consider that Investment Firms can increase the FOR, without direction from the Competent Authority, but decreases in FOR would require permission from the Competent Authority.

UCITS/AIFMD firms
The IA would welcome further clarity on the treatment for UCITS/AIFMD firms (CPM) that need to follow IFR/IFD to calculate the fixed overhead requirement. For example, whether UCITS/AIFMD firms will be required to complete the reporting templates and how the fixed overheads requirement will sit alongside other prudential requirements on UCITS/AIFMD firms. It is the IA's understanding that the EBA intends the RTS to ensure the calculation of FOR is consistent across all entities in the group (as noted in Articles 60 and 61), but not to get firms not caught by the regulation to also report.

Bonus payments
Article 1(4) provides additional guidance on the characteristics of bonus that can be deducted when calculating fixed overheads. The IA believes that the objective of the requirement it to ensure that firms can only pay bonuses when net profits are available from which the bonus would be paid from, thereby ensuring that the payment of the bonus does not impact on the firm's capital position. However, the wording of Article 1(4)(a) does not clearly support this objective. The section states that bonuses to be deducted "have already been paid to the employees in the year preceding the year of payment". It is unclear as to firms interpret this and review remuneration policies to ensure that discretionary bonuses are settled in a way that allows the firm to deduct the expense. Furthermore, Article 1(4)(b) seems to articulate the requirement that in order to be permitted to deduct the cost a firm must not be obligated to pay a future bonus, and therefore has discretion to make future awards, but again is worded in a potentially more complex manner.

The initial assessment of Article 1(4) is that this is not expected to be an issue for firms as bonuses tend to be paid out of profits and do not tend to be paid should they lead to the firm then making a loss, thereby meeting the requirement of the second element of Article 1(4)(a).

In cases where a bonus is deferred the assumption would be that awards have been "paid for" in the year of award. Deferred awards, in the form of shares, tend to be held in trust for employees with the firm remitting cash to the trust on the award date. For accounting purposes, the cost of the deferred award is then spread to vesting date under accounting rules. There is potential that the accretion of the full cost of the award after the award date could lead to the firm making a loss in the year(s) after award. The current wording could lead to uncertainty as to whether the costs associated with the deferred element of the bonus would be allowable in the calculation of fixed overheads.

It is important to note that, although this may seem irrelevant as the FOR is normally calculated based on previous years expenses, what is being proposed can have a knock-on impact for the calculations of material changes in FOR, that would lead to a recalculation of requirements.

Based on the current drafting, the normal calculation of FOR would, in most cases, include a deduction of bonuses. However, the calculation of a projected FOR would not. This means that the calculation of previous years and current year are technically different. In addition, because of this, firms may breach the thresholds in Article 3 of the delegated regulation and have to calculate a FOR based on these projected figures.

A full list of permissible deductions in a single document
The full list of deductions is not included in any of the documents (regulation and delegated regulation). In the delegated regulation, the additional items to deduct are referenced as being added to the items already included in the regulation. This means although the reference to 'net profits' for the bonus is included in the regulation, all the items in the regulation have been stated as items to be considered. This means that they can be changed if a complete list is included in the delegated regulation, making it even more important to have a full list of deductions, with potential amendments to the text in the IFR, in the delegated regulation. The IA recommends that the RTS includes a full list of the permissible deductions.

Costs associated with items already deducted from capital
From the deductions listed in Article 13(4) and Article 1(6), and the principles behind the ability to deduct them from total expenses, there is at least one type of deduction that is not included and should be added to the list. These relate to a 'deduction of expenses related to items that have already been deducted from own funds'.

The current drafting of the requirements, while consistent with the CRR definition of FOR leads to items such as charges on intangible assets are included when the asset has been fully deducted from Own Funds. Any further charges or accelerated write down of these assets would have no impact on own funds as the corresponding reduction in profit would be offset by the reduction in the deduction required under Article 36 of the CRR. Following the same principle as being used for the deduction of bonuses.

The IA would recommend the inclusion of an additional permitted deduction in the list of deductions available when calculating the fixed overheads, this would be 'deduction of expenses related to items that have already been deducted from own funds'. These items would include, but not be limited to:

- Charges related to Intangible Assets,
- Charges related to Deferred Tax Assets
- Losses related to Investments classed as holdings under Article 36 of the CRR

While this change would increase the deductions available, thereby lowering the fixed overheads of firms with certain assets on their balance sheet it would provide greater consistency in relation to those costs that would cause the capital of the firm to be impacted in the event of a decrease in the scale of the business and resulting profits. Additionally, the inclusion of Deferred Tax Assets would remove any potential for charges relating to deferred tax assets being included in the calculation of fixed overheads as they fall outside the deduction permitted by Article 1(6)(c) of the RTS.

Starting point for calculation of the fixed overheads
The IFR and draft RTS both state that firms should calculate Fixed Overhead Requirements from figures "resulting from the applicable accounting framework". This does not provide a clear starting point from which firms should then deduction those costs permitted by the texts. There is potential for firms to use different figures to base their calculations on

resulting in the potential for erroneous calculations and firms not holding the correct amount of Own Funds against the requirement.

It is recommended that a clear starting point is articulated. The IA suggests this be all expenditure incurred by the firm as disclosed in the audited financial statements, to arrive at the net profit for the financial year. This would provide clarity on the starting point of the calculation and should provide a greater level of consistency in the application of the requirements.

Other points

The IA would welcome additional clarification on the terms used in the deductible expenses. In particular:

- "Staff Bonus" – the IA suggests that all discretionary bonus charges should be included in the deduction;
- "Other remuneration" to the extent that it is discretionary;
- Bonus charge is deductible if charged on current year's net profit – clarification needed to understand how to apply the deductions when a firm makes a loss and when staff bonuses are based on a firms activities or Group performance rather than firm profits;
- Expenditures from 'taxes'- additional guidance on whether 'taxes' include corporation tax, and deferred tax; and
- Shared commission and fees payable – additional guidance on whether marketing commission and marketing fees paid are included in the deduction.

The RTS provide some more information on the permitted deductions, but there are some areas where further clarity is sought. The IA recommends that the EBA finalisation of the drafting include:

- Amending the materiality thresholds to try to ensure that only truly material changes in fixed overheads drive a change in the requirement
- Clarifying the starting point of the calculation of fixed overheads
- Including a complete list of permitted deductions in the RTS
- Amending the list of permitted deductions to include expenses associated with items deducted from Own Funds
- Amending the wording around the deduction on bonuses by reverting to "fully discretionary" rather than the proposed draft wording.

4. Draft RTS to specify the methods for measuring the K-factors

Measurement of AUM

The EBA consultation paper mentions that to properly capture the value of AUM, no offset should be taken into account, including the instruments that might have a negative value (i.e. Gross Asset Value). The IA does not agree with this approach as the Net Asset Value of AUM is based on the value of assets a firm manages on behalf of its clients, and the amount it would have to return in case a client decides to close its account. This means it would return the NAV. Clients are also normally charged fees based on the net value of the assets being managed by investment firms.

It is true the use of leverage can expose clients to additional risk. However, negative value instruments, such as derivatives, can also be used to hedge risks as part of proper discretionary portfolio management, where risks are reduced rather than increased. This means that the risks related to the use of leverage would be better captured in the 'Pillar 2' assessment rather than as a 'one size fits all' approach under the minimum K-factors capital requirements.

The EBA calibration of K-factor coefficients was based on information provided by firms, which was likely to be based on a NAV approach to measure the AUM. Based on the methodology applied by the EBA to calibrate the coefficients, if the measurement of AUM was to include negative value of liabilities, this would likely result in a lower coefficient for K-AUM. This analysis should be captured as part of an impact assessment and an amendment considered, if impacts are material.

The IA recommends the use of NAV in the calculation of K-AUM and K-ASA. NAV is a generally accepted term in the industry and is currently calculated by firms for internal and external reporting purpose. Utilisation of this basis would not add to the firm's cost of regulatory compliance.

Non-discretionary advisory definition
The IA would welcome clarity on the advisory services which should be considered in scope of "non-discretionary advisory services" to ensure assets are included correctly. It is recommended that the EBA provide examples of the advisory services which should be considered in scope of "non-discretionary advisory services". Further, it would be useful for the EBA to be explicit about what is meant by non-discretionary advisory arrangement "of an ongoing nature". It is assumed that it means the provision of "regulated advice", but could it also potentially refer to advice that does not meet the MiFID definition.

Treatment of assets where discretionary and non-discretionary services are provided
Art.2(2) clarifies the treatment of assets where both discretionary portfolio management and non-discretionary advisory services are provided by different entities. However, in the instance that both discretionary portfolio management and non-discretionary advisory services are provided by different entities within the same consolidation group, this would result in double-counting. For example, in the scenario where assets are delegated from ManCo to an investment firm within the group, but then a sleeve of the portfolio is further sub-delegated the IA suggests that this should not be included in the AUM calculation.

It makes sense not to include assets that are delegated from an entity that is already subject to an equivalent AUM-based capital requirement or otherwise subject to an appropriate prudential regime locally. The IA would welcome this being extended to third country delegations to ensure fair treatment across jurisdictions.

It is recommended that the EBA clarifies the correct treatment of assets when (1) there is delegation and sub-delegation and (2) both discretionary portfolio management and non-discretionary advisory services are provided by different entities within the same consolidation group.

Greater clarity is sought on non-discretionary advisory arrangements including where assets are delegated / sub-delegated.

Impact of new requirements on CAD Exempt firms
Our interpretation of the new requirements is that firms that only provide advisory services and are currently subject to a requirement of €50k, would, under the new requirements be subject to a K-AUM of 0.02% of the value of the assets of the advisory mandates.

As an example, a firm with €5bn of advisory assets would be required to hold capital as follows:

	Current regime	IFR
Basis	€50k initial capital	2bps of AUM
AUM	€5bn	€5bn
Capital requirement	€50k	€1m

We understood that the stated aim of the new regime was not to significantly increase capital requirements, we would request confirmation that the assessment of the impact on the above noted firm is correct.

Treatment of cross-holdings
It is not clear what is the correct treatment of cross-holdings between two entities within the same consolidation group or which have the same ultimate parent company where both of these entities are required to calculate an AUM-based capital requirement. Specific clarity on this point within the RTS would be welcomed.

Without further clarity, holdings that have shared ownership may not be correctly applied to the relevant entities which will impact the accuracy of the K-AUM calculation. It is recommended that the EBA clarifies the correct treatment of cross-holdings between entities that are part of the same parent group

Definition of investment firms and financial entities
Section 3.6.4 (Para. 49) and the IFR Art. 17 refer to instances where an investment firm "delegates management of assets to another financial entity" but distinction between investment firms and financial entities is not clear.

Section 3.6.4 also confirms that the delegation provisions apply equally to (i) delegation between IFD / IFR firms and an AIFMD / UCITS management company and (ii) delegation between two firms which are both in-scope of the IFD / IFR however it would be helpful if this is explicitly stated in the final RTS.

The intention behind the delegation provisions is to avoid double counting. Without further clarity, both entities may include delegated assets in the K-AUM calculation and therefore the assets could be double counted. It is recommended that the EBA clarifies the distinction between investment firms and financial entities in the final RTS and confirms how AIFMD / UCITS management companies should be treated. This would help avoid double counting and ensure that application of the legislation is consistent

K-COH
It is not clear whether internal trades (i.e. buys/sells between funds that are not traded in the market) should be excluded or included in the calculation. It is recommended that the EBA clarifies that firms may exclude internal trades because they can easily be reversed and corrected internally with minimal impact (i.e. there is no external execution or transmission of orders).

It is further recommended that trades captured in the K-AUM calculation also be excluded from the K-COH calculation to ensure risks are appropriately allocated.

Our understanding of the requirements is that to avoid double counting in the calculation of the K-RtC K-COH does not include orders relating to servicing client AUM (which would be included in K-AUM) and is includes orders on non-client servicing activities. Our interpretation is that for a group structure with a single dealing entity, which only handles orders for clients of the group, no K-COH would be calculated at the consolidated level. The IA would request that the EBA confirm the accuracy of this interpretation.

5. Draft RTS on the definition of segregated account

While clarity has been added on the definition of a segregated account, it is not clear what is held in a non-segregated account. Currently in the UK, holding client money in a non-segregated account would be a regulatory breach so the IA is keen that the EBA provide further clarity on the proposed use of segregated vs. non segregated accounts.

6. Draft RTS to specify adjustments to the K-DTF coefficients

No material concerns.

7. Draft RTS to specify the calculation of the amount of the total margin for the calculation of K-CMG

The IA would like further clarity on the exclusion of the 2 highest daily amounts of total margin required by the clearing member during a 3-month period as there is potential ambiguity in the where an investment firm uses multiple clearing members. For example, should it be the third highest combined daily total of margin given on a single day, or be the sum of the third highest amounts of margin given to each clearer, even if those amounts for each clearer occur on different trading days.

Article (3) of the CP clarifies that this should be done by first determining the third highest amount of total margins required on a daily basis by each clearing member separately over the preceding three months, then adding those amounts. The IA view is that it would be more consistent with the overall concept of clearing margin given for an investment firm to first add up, across all clearing members used, the margins for each day. Essentially, that is the amount that was there at the end of that day, as the margin call made at the end of the day is typically what is 'given' to the clearer the next morning. The third highest such amount across the relevant observation period would then be taken. The alternative approach of adding margins from different clearing members from different trading days could be more prudent, but this is less likely to reflect how the underlying risk is managed in practice.

8. Draft RTS on the criteria for subjecting certain investment firms to the CRR

No material concerns.

9. Draft RTS on prudential consolidation of investment firms groups

Article 2 (2) of the proposed delegated regulation on consolidation proposes that the union parent undertaking, where there are investment firms authorised in different member states, is the one with the largest balance sheet. This appears to be a banking approach. Considering investment firms' different business models, where some are balance sheet intensive, while others are off-balance sheet intensive, there should be additional metrics to make this decision. An approach similar to the alternative test in FICOD should be considered, where the decision is made based on a combination of on-balance sheet, off-balance sheet and income metrics.

Paragraph 3 of this Article provides for a waiver granted by common agreement between competent authorities. However, for investment firms, the combination of on-balance sheet, off-balance sheet and income metrics should be considered as the primary approach.

Currently, the wording in Article 7 suggests that a firm is obligated to obtain permission from the competent authority if it follows the default treatment for joint control by using proportional consolidation. The IA assumes that, because it is the default treatment, firms in the first instance would apply proportional consolidation without obtaining prior approval from the group supervisor. It would then be for the competent authority to challenge the position taken by the investment group.

It is requested that the EBA provide clarification that, given it is the default treatment, proportional consolidation may be applied by the investment firm group in the first instance. The competent authority may require another accounting treatment on a case-by-case basis.

Where consolidation groups have a parent entity within the UK and subsidiaries both in the UK and the EU, the IA requests the continuation of the current approach to consolidated supervision by the parent entity's competent authority. Solo reporting to the relevant EU national authority would be required for all EU regulated subsidiary entities of a UK group.