APT
Association of Proprietary Traders

Discussion Paper New Prudential Regime for Investment Firms

Consultation feedback of the Association of Proprietary Traders,

the Netherlands

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Amsterdam/Gouda, 1 February 2016

Dear Madam/Sir,

The Association of Proprietary Traders of the Netherlands ("**APT**") herewith provides the European Banking Authority ("**EBA**") with its feedback and responses to the questions included in the Discussion Paper "Designing a New Prudential Regime for Investment Firms" dated 4 November 2016 (EBA/DP/2016/02), (the "**Discussion Paper**").

For the sake of completeness, we have chosen to include the responses to the various questions filled out in the electronic form of EBA in this document.

A copy of this contribution and feedback document will be shared with the Dutch authorities, being the Dutch Ministry of Finance, the Dutch Central Bank and the Dutch Authority Financial Markets. We have also contributed a copy of this document to the working group of FISMA of the European Commission.

Please do contact us should EBA wish to obtain more or other information about the subject matter of our responses to the Discussion Paper.

Sincerely yours,

H.J.G. Kruisinga
Chairman of the Board

M.E.A. Hiskes-Willemse
Secretary to the Board

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1 About APT and the Capital Adequacy regime applicable to APT-Members

APT is the representative trade association of sixteen proprietary traders established in the Netherlands. Members of APT ("**APT-Members**") are legal entities that, as their business, deal on own account and for their own risk which means that they trade against proprietary capital in the conclusion of transactions in securities and other financial instruments on regulated markets or multilateral trading facilities (MTFs). APT-Members are either holders of permits as investment firm (MiFID investment activity referred to in MiFID Annex I, Part A (3)) or members that are registered as authorised traders with a regulated market. For the avoidance of doubt, APT does not represent banking organisations.

Some of the APT-Members are larger investment firms with a global footprint, both in terms of activities on the global financial markets and group companies established on the various continents. Other APT-Members are rather locally organised and smaller firms with a workforce of between 2-20 individuals exclusively operating from the Netherlands.

The most important characteristics of the business models of the APT-Members are:

- They have no external clients and no client relationships;
- They do not hold monies or securities/financial instruments for third parties;
- Trading is always on regulated markets or in financial instruments and securities eventually made subject to central clearing;
- Trading is always made under responsibility of and subject to a guarantee issued by a clearing member which itself is member of one or more Central Counter Parties.

APT represents all licensed investment firms established in the Netherlands that exclusively deal on own account and that are subject to the supervision of the Dutch Authority Financial Markets and the Dutch Central Bank. In addition, APT represents an important number of the businesses currently not subject to MiFID authorisation requirements but that deal on own account on regulated markets by means of membership of such regulated markets, or on the basis of other trading authorities. It is expected that a significant part of the group of APT-Members currently subject to self-regulation by means of their membership with regulated exchanges will obtain authorisation as required under MiFID II in the course of 2017.

All of the APT-Members are subject to the bespoke **Risk Margin-prudential requirements regime** as established as from 1 January 2014 by the Dutch authorities. This regime requires all the firms to hold capital against the haircut amount calculated by the clearing member on a daily basis. The Risk Margin-regime constitutes a comprehensive measure of risk, taking into account volatility, liquidity, positions, concentration, etc., is independently calculated on a daily basis, using a model that is approved by the supervisory authority of the clearing members that are themselves subject to strict prudential supervision. This regime provides for a bespoke capital adequacy regime replacing the less risk sensitive CRD IV requirements with a daily marked-to-market and holistic measure as regard Value-at-Risk.

The Risk Margin-regime captures all risks to which the firms are exposed in the markets (if any and applying prudent techniques of overcollateralisaton) and allows for accurate calculation of required buffers for an orderly winding down of all positions in times of stressed market circumstances and idiosyncratic failures of individual firms. Pursuant to the arrangements between the Dutch supervisory authorities and the proprietary trading sector, APT-Members are subject to the Supervisory Review and Evaluation Process (Pillar 2, "**SREP**")). APT-Members are required to provide the Dutch authorities with Internal Capital Adequacy Assessment Process ("**ICAAP**") reporting on an annual basis.

This ICAAP reporting exercise has now been conducted for a number of years since 1 January 2014. It enables the Dutch authorities to analyse the capital adequacy of proprietary trading firms that apply the Risk Margin model for the calculation of their capital. The SREP and ICAAP process also serves as confirmation of the ability of individual firms to apply proper risk management processes within their organisations and to avoid underestimation of risks for which insufficient capital would be held. Based on the outcome of the SREP processes conducted the last years, it appears that the Risk Margin-regime for capital requirements properly addresses risks of the proprietary trading firms. Pillar 2 capital add on-discussions among the supervisory authority and the firms have not resulted in significant corrections on the initial capital adequacy assessments made by the individual firms.

All of the APT-Members are classified in the Dutch market by the national prudential supervisor as belonging to the category of small and medium sized Dutch investment firms for which a generic exemption applies from capital conservation buffers and countercyclical capital buffers within the meaning of articles 129(2) and 130(2) CRD IV.

None of the APT-Members is classified as a global systemically important institution or other systemically important institution within the meaning of article 131 CRD IV and none of the APT-Members is made subject to the discretionary systemic risk buffer of article 133 CRD IV.

None of the APT-Members is conducting a “bank like” business combining investment activities and investment services within the meaning of MiFID Annex I, Part A.

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2 Executive Summary[1]

The Association of Proprietary Traders of the Netherlands ("**APT**") supports the work of EBA towards the establishment of a bespoke and specific prudential supervision regime for investment firms.

In 2013 CRR/CRD IV amalgamated the Capital Adequacy Directive of 2006 setting forth market risk rules for banks and investment firms with the provisions of the Capital Requirements Directive of 2006 containing the banking credit and operational risk rules. As result of this process, significant out of scope, incompatibilities with business models, disproportional effects and improper alignment of the rules for investment firms occurred in supervisory practice. There is, therefore, a convincing case that the broader group of European investment firms will be made subject to an own prudential supervision regime.

EBA's Discussion Paper "Designing a New Prudential Regime for Investment Firms" proposes such separate prudential supervision regime for investment firms. APT agrees with the viewpoints of EBA as regards the alignment of risk factors to the typical business models of investment firms who operate in a different way as opposed to banks. In this manner incompatibilities of the current CRR/CRD IV regime with such business models will be removed and the risk sensitivity of the prudential supervision regime will be improved.

EBA's proposals in the Discussion Paper require to address a very broad population of investment firms active in all the EU-Member States having very different business models and propositions to the markets and customers. Although APT has not analysed the applicability of the proposed risk factors for other types of businesses in a detailed way, it appears that, in balance, the proposed bespoke regime seems to adequately address the requirements for prudential supervision of investment firms.

APT-Members are since 1 January 2014 subject to a customised, risk sensitive and strict prudential supervision regime based on a Risk Margin calculation method, replacing the CRR/CRD IV rules that have been considered largely incompatible with the business of proprietary trading firms. Based on experience with this regime in supervisory practice, there have been no occasions where significant corrections have been necessary to address capital adequacy issues. The risk management model supporting this external prudential supervision regime has been tested in a considerable long period and has proven to be resilient to significant shocks, including the shock of the extreme turbulent markets during the financial crisis of 2008/2009.

APT considers it important that a new prudential supervision regime for proprietary trading firms is proportional and takes size, complexity and business models in this area of the financial markets into account. APT proposes in this contribution to make Class 3 proprietary trading firms subject to a Fixed Overhead requirement and to impose the Risk Margin for the larger proprietary trading firms. Consequently, APT suggests that for all proprietary trading firms tailored rules on capital adequacy, liquidity, consolidated supervision, governance and remuneration will apply. With the Risk Margin regime APT builds further on the observations of EBA in point 79 of the Discussion Paper in which a margin requirements approach is left open as a possible way forward.

[1] This Feedback document has been prepared with the support of Prof. dr. Bart P.M. Joosen, holder of the chair Prudential Supervision Law at the University of Amsterdam and private practitioner associated with Regulatory Counsel Financial Services, Amsterdam.

3 Risk to Customers (RtC)

3.1 APT-Members are not servicing external customers

One of the key recommendations in the proposed new prudential regime for investment firms as appears from the Discussion Paper concerns the establishment of a capital adequacy framework for the management of risks that investment firms pose in relation to their customers. Investment firms that pose more risks to customers ("**RtC**") should be subject to higher capital requirements than firms posing less risk.

Within the perimeter of this risk area, the factors and sources of risks are particularly defined to circumstances that may have an impact on customers' rights and assets and the damaging effects that may result from the failures with the investment firm to properly manage the risks. Such factors and sources are outlined and addressed in the whole set of observable 'proxies' or factors representing the RtC.

Each factor (defined in the Discussion Paper as "**K-Factors**") related to the RtC is then subsequently subject to the applicable percentage or scalar factor to calculate the actual capital requirement for the investment firm to address the RtC.

For the APT members none of the K-Factors as comprised in the Discussion Paper Chapter 4.3.1 (points 36 and 37) on RtC will be relevant to define the levels of their required capital adequacy. APT-Members do not have external customers as a matter of a generic characteristic of the business model of such firms. In the absence of such customer relations or contractual or other exposures to external customers, APT-Members typically exclusively deal on own account and do not pose risks to external customers.

3.2 Non-relevance RtC K-Factors for APT-Members

APT therefore reiterates that none of the following K-Factors are or may be relevant for APT-Members or for any proprietary trader having a similar business model exclusively focusing on dealing on own account:

- **Assets under management (AUM)**: none of the APT-Members manages customer portfolios or implements (whether or not discretionary) investment mandates for and on behalf of customers;
- **Assets under advice (AUA)**: APT-Members do not have external relations with customers and therefore never render investment advice;
- **Assets safeguarded and administered (ASA)**: APT-Members' business operations does not require safeguarding and administration of assets of third parties. For most APT-Members being holders of MiFID permits, safeguarding and administration activities within the meaning of MiFID Annex I Part B (1) is not in scope of their authorisation. Such firms would, consequently, even not be allowed to conduct assets safeguarding and administration activities;
- **Client money held (CMH)**: Under no circumstances will APT-Members have access to third parties' money (not in the form of own balance sheet liabilities or by means of access to asset segregation structures) and consequently this important K-Factor as outlined in paragraph 38(d) of the Discussion Paper does not apply for such businesses;
- **Liabilities to customers (LTC):** APT-Members will not engage with customers to issue guarantees or indemnities to the benefit of such customers or any other arrangements (whether it be contractual, quasi-contractual or tort law type of relations) that would bring APT-Members into the position of being indebted to external customers. This K-Factor consequently does not apply for APT-Members' businesses;

- **Customer orders handled (COH)**: The trading activities of APT-Members does not involve or relate to, directly or indirectly, the processing of customer orders in whatsoever form. APT-Members have no responsibilities towards customers for the proper, timely and adequate processing of securities' orders or comparable transactions in other financial instruments. Any trading activity of APT-Members is for own account and always against their own proprietary capital. APT-Members also do not form part of a chain of intermediaries responsible for the processing of securities orders on behalf or for external customers. In this respect there is also no indirect exposure to external customers.

3.3 Conclusion as to RtC

Based on this brief display of the analysis of APT as regards the relevancy of the K-Factors in the Chapter addressing RtC, it may be concluded that the outcome of any quantification exercise in respect of this important part of the capital adequacy framework, will be that the formulae supplied by EBA will result in zero values. This is another way of expressing that APT-Members are not engaging in whatsoever form with customers and, therefore, have no risk exposures concerning their activities that may harm or otherwise prejudice the financial or other position of external customers. The Chapter on RtC and proposed calculation methods for the quantification of capital to address this part of the risks caused or borne by investment firms are not relevant for the proprietary trading firms organised in APT.

4 Risk to Markets (RtM)

4.1 The occurrences of RtM

The risk to markets ("**RtM**") Chapter of the Discussion Paper addresses circumstances which may result in impact to the financial markets caused by investment firms. Examples of such impact as provided in paragraph 4.3.1 sub paragraphs 38 to 40 of the Discussion Paper are:

- Temporary dislocation in market access;
- Temporary dislocation in market liquidity;
- Questioning of market confidence; and
- Questioning of market integrity.

The Discussion Paper notes that K-Factors to be developed to address the RtM, may particularly be important for investment firms where no RtC K-Factors might apply if they do not have external customers. The Discussion Paper highlights that the key K-Factor in the RtM Chapter is the Proprietary Trading Activity (PTA) K-Factor.

The Discussion Paper recognises on the one hand that any temporary or permanent exit from the markets of investment firms not having external customers, predominantly impacts the own finances of such firms. Consequently, the only impact is for the owners of such investment firms whose proprietary capital has been utilised for the dealing on own account activities. Proprietary capital may be impacted as a result of the temporary or permanent exit from the markets and such capital serves to absorb the losses exclusively to be borne by the shareholders and other owners of the investment firm.

On the other hand, the Discussion Paper assumes that a temporary or permanent exit of a proprietary trading firm may also impact third parties, notwithstanding that it is recognised in the Discussion Paper that such third parties are in no circumstances "own customers" of the investment firm. The Discussion Paper refers to disruption of market access or liquidity as examples of situations where third party rights may be affected, even if such third parties are not to be considered customers of the investment firm as such.

4.2 The need for evidentiary support for the RtM framework

The Discussion Paper does not explicitly refer to examples from practice demonstrating that the risks identified are relevant and became imminent in certain cases. But it must be acknowledged in general that the Discussion Paper is not explicit in identifying actual cases occurring in the European markets that support and underpin the proposed capital measures for certain investment firms. APT notes that in the past cases have appeared where proprietary traders failed, with no material effects of the financial markets or to other investment firms or other participants in the financial markets.

APT considers it of the utmost importance to analyse as to whether or not APT-Members may, as a result of the scale of the operations of APT-Members, as a result of the nature of the (contractual) relations with counterparties, as a result of the organisation of trading activities or as a result of the potential other factors determining and influencing the risks as identified by EBA indeed cause or contribute to RtM as this concept is defined by EBA.

Clearly, in the event there is no reason to assume that RtM may become manifest as a result of a failure of an investment firm dealing on own account, then it should be confirmed and recommended that APT-Members are neither exposed to RtC nor to RtM. This would, basically, result in the conclusion that investment firms organised in the way APT-Members are organised, should not be subject to percentage or scalar factors related to K-Factors which would simply not apply to such investment firms.

As will be explained below, APT-Members are active in very competitive markets and a failure of one of the firms would not result in significant turbulence on the markets, as the positions of the firms can be taken over without significant interruption. Furthermore, as will be explained in more detail below, proprietary trading firms are performing trades on the markets subject to a guarantee of the clearing member. This safeguards the smooth continuation of the processing and settlement of trades initiated by a proprietary trading firm that (suddenly) exits the markets or suspends its business operations.

4.3 Excluding investment firms not qualifying as systemically important

APT wishes to emphasise that none of its members would, if the methodologies would be applied to asses Global Systemically Important Institutions ("**GSIIs**") or Other Systemically Important Institutions ("**OSIIs**"), qualify as such, not on a global scale, not on a European scale and not on a domestic scale. None of the APT-Members would qualify as a firm whose distress or failure would have a systemic impact on the Dutch or the EU economy or global financial system due to size, importance (including substitutability or financial system infrastructure), complexity, cross-border activity, and interconnectedness.

It is based on the criteria developed by EBA in furtherance of the provision of article 131(3) Capital Requirements Directive IV (Directive 2013/36/EU, "**CRD IV**")) to identify other systemically important institutions that APT has concluded that none of its members would qualify as systemically important within the meaning of prevailing assessment methodologies[2].

Following the rationale and recommendations of EBA in its Opinion to the European Commission of 19 October 2016[3] in the initial and first set of responses to the Call of Advice of the European Commission of 13 June 2016, investment firms that do qualify as systemically important (whether on a global basis or on a domestic basis) should continue to be subject to

[2] See: EBA Guidelines on the criteria to determine the conditions of application of Article 131(3) of Directive 2013/36/EU (CRD) in relation to the assessment of other systemically important institutions (O-SIIs), EBA/GL/2014/10 of 16 December 2014.

[3] Opinion of the European Banking Authority on the First Part of the Call for Advice on Investment Firms, 19 October 2016, EBA-Op-2016-16

(parts of) the CRD IV and Capital Requirements Regulation ("**CRR**"). For these investment firms, there is no convincing case to consider the development of a separate and revised prudential regime.

For investment firms that may not be assessed as being systemically important, there is good reason to develop a separate prudential regime. EBA establishes its views and recommendations in the Discussion Paper on such separate and deviating prudential regime for investment firms that in any event do not qualify as systemically important.

However, some references in the RtM Chapter of the Discussion paper seems to suggest that there is a need to introduce capital requirements for firms that could pose risks to markets, although such investment firms are not to be categorised as systemically important. APT respectfully wishes to challenge this viewpoint laid out in the Discussion Paper for the following reasons.

4.4 Non-systemically important firms cannot cause systemic risk

Both from the theoretical background underpinning the prudential regime and rules applicable to address "systemic risk" as well as from the practical application of the relevant rules for "systemic risk buffers" based on the provision of article 133 CRD IV, it is evident that firms and institutions that are to be made subject to such systemic risk buffer are in most, if not all of the cases, also qualifying as "systemically important" within the meaning of the assessment methodologies for this category of institutions. Systemic risk buffers are customarily imposed in Europe for those banks (other financial institutions such as investment firms are currently not subject at all to the systemic risk buffer regime of article 133 CRD IV) for which the national competent authorities wish to impose a measure that exceeds the ordinary capital requirements for systemically important banks.

Systemic risk buffers are imposed in order to prevent and mitigate long term non-cyclical systemic or macroprudential risks not covered by CRR. These buffers form the capstone of the prudential supervision regime. Indeed, they must be placed in the context where banks, in view of their size and importance, may have impact on the financial markets and on other participants to the financial markets to the effect that failures or stressed circumstances with such banks would cause problems on a macroprudential scale. Banks subject to systemic risk buffers are all either "Too-Big-To-Fail" or they are "Too-Interconnected-To-Fail". Consequently, systemic risk buffers within the meaning of article 133 CRD IV are imposed in Europe in certain very rare circumstances and in respect of only a handful of the very largest banks in Europe for which the ordinary prudential regime for systemically important institutions is deemed to be insufficient.

Some parts of the Discussion Paper seem to suggest that, notwithstanding that investment firms may not be classified as being systemically important (which would require these firms to remain to be subject to CRD IV and CRR), that such firms may nevertheless either be performing "bank-like" activities while not being systemic or being eligible to cause systemic risk although not performing bank-like activities. EBA notes in paragraph 12(a) of the Discussion Paper:

> "It is recognized that investment firms are not 'systemic and bank-like' and therefore, in general, the purpose of a prudential regime for investment firms is not to provide the same level of assurance as is provided for firms that are systemic and bank-like. It is, however, recognised that it is possible that an investment firm may be categorised as systemic, while not being 'bank-like'; the design of an appropriate, prudential regime for investment firms will need to provide sufficiently for any such entities. Furthermore, it is also recognised that there may be some large 'bank-like' investment firms which, although not categorized as systemic, are nevertheless deemed 'significant' in terms of their trading activity and the potential for their failure to create an adverse impact upon market confidence."

APT takes the view that this reasoning is in conflict with the general principles of prudential supervision regimes as developed in Europe the last decade. Firms (whether they are banks, investment firms or other types of financial institutions) that are not to be categorised as systemically important cannot be considered as potentially causing systemic risk. Vice versa, firms that are not considered to be able to cause systemic risk, should not be subject to an extraordinary prudential supervision regime because of (perceived) significance in terms of volume of the trading activity, balance sheet size or otherwise having a potential impact on market confidence. A firm is either systemic and should then be categorised as systemically important institution, or it is not systemic. APT strongly believes that there are no grey areas of being systemic in a limited way which would justify yet another prudential supervision regime in addition to the existing frameworks for systemically important institutions.

If an investment firm that has significant trading activity, does not exceed the thresholds of the methodology of assessing whether firms are systemically important, such an investment firm should not be subject to specific and extraordinary prudential supervision rules. Such a firm is not systemically important and cannot (consequently) cause systemic risk.

Non-systemically important investment firms that are not (potential) perpetrators of systemic risk should not be subject to specific prudential supervision rules to manage their potential impact on market confidence. Market confidence must be preserved and must be managed through the comprehensive MiFID II market conduct rules and Market Abuse Regulation framework applicable to such investment firms without exceptions.

4.5 RtM not relevant for APT-Members in view of organisation of businesses

APT interprets the EBA views discussed in paragraph 4.3.1 sub paragraphs 38 to 40 of the Discussion Paper to suggest that large proprietary traders without customers, could nevertheless have an impact on market confidence, market integrity or liquidity or market access. APT refers to the point made in the previous paragraph that the preservation of integrity and orderly functioning of the financial markets is not the domain of prudential supervisory authorities, but of market conduct authorities. APT also furthermore believes that none of the APT-Members would be in the position to impact market confidence, market integrity, liquidity or market access. The following reasons explain this viewpoint.

Firstly, the subject matter of *impact on market access*. None of the APT-Members are providers of (disclosed or undisclosed) trading facilities or trading infrastructure to third parties. APT-Members are not involved in transaction or order processing structures where dealing on own account forms part and is integrated in a chain of transactions in securities and financial instruments involving third parties or customers for whom the relevant transactions are carried out, whether partially or wholly (no principal-to-principal pass through dealings).

APT-Members are not operators of (disclosed or undisclosed) access facilities or comparable securities' order processing facilities to regulated markets, MTFs or organised trading facilities ("**OTFs**") from which third parties benefit and are dependent to carry out and execute transactions. Therefore, a temporary or permanent failure of an APT-Member will not result in prejudicial circumstances or damages to third parties as regards their possibilities to access the financial markets and perform trades and transactions thereon.

Secondly, APT-Members are in none of the markets they operate fulfilling exclusive roles as regards *liquidity provision*. The legacy roles of market makers and liquidity providers on regulated markets where more or less exclusive roles were granted to single firms to provide liquidity in the markets, has the last decade been replaced with a much more dispersed, open and highly competitive market infrastructure which has proven to be very resilient under challenging circumstances.

Partly as a result of the restrictions introduced by recent Market Abuse regulations[4] and partly caused by technological developments and internationalisation, APT-Members operate in a very competitive market and none of the APT-Members is able to control, influence or manipulate liquidity provision in the financial markets or parts of those markets. The failure of one of the firms fulfilling roles as liquidity provider or market maker would not have a detrimental impact on markets.

Markets will be able to absorb the failure of a proprietary trading firm that is unable to provide liquidity in markets and as regards the financial instruments in respect of which the failing firm played a role prior to the occurrence of its distressed situation. Such event would be without significant disruption of trading abilities of third parties on the financial markets.

4.6 *Discussion Paper RtM concept of temporary dislocation*

It is important to stress that the current CRR and MiFID frameworks are, as concerns capital requirements, not addressing risk management measures or prudential requirements for during the trading day positions and trades. All global and European systems, methodologies and (clearing and settlement) infrastructure (including the central bank end-of-the-day reserve closing) is aligned to secure prudential treatment of end of the day and overnight positions. Reference can be made to the recent Delegated Regulation on Risk Management Measures for OTC-Derivatives not centrally cleared ("**DR Risk Management OTC-Derivatives**")[5].

The risk mitigation techniques developed for OTC-Derivatives not centrally cleared align the requirements for Variation Margin to a timing of the required collateral streams to the effect that cash instruments and eligible financial instruments serving as collateral are to be exchanged on a D+1 basis and if appropriate margin period of risk ("**MPOR**") measures are in place on a D+2 basis. This means that, apparently, the European Supervisory Authorities (EBA, ESMA and EIOPA) and the European legislator are satisfied with the application of a risk mitigation technique that collateralises Marked-to-Market positions with one to three business day's delays, depending on the type of agreed upon collateral-arrangements[6]. For any trades on the European regulated markets and MTFs, a comparable timing for exchange of variation margin applies for positions to be settled in the future. For trades settled immediately upon closing of the trades, currently customary D+3 settlement timing periods apply.

The Discussion Paper places the need to address RtM and raising capital requirements for such risks in the context of "sudden" exits from the markets or failures of investment firms, particularly if this concerns proprietary trading firms that fulfil a role as market maker or liquidity provider. Such capital requirements would then address the temporary dislocation in market access or market liquidity. There is, in the view of APT, a risk that an improper definition of the expression "temporary dislocation" would introduce stricter risk management and prudential requirements on proprietary traders and liquidity providers than would generally

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4 Market abuse issues could arise more quickly if the provision of liquidity or market making in certain financial instruments or securities was left to be carried out by investment firms operating on an exclusive or almost exclusive basis.

5 Commission Delegated Regulation (EU) 2016/2251 of 4 October 2016 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council on OTC derivatives, central counterparties and trade repositories with regard to regulatory technical standards for risk-mitigation techniques for OTC derivative contracts not cleared by a central counterparty.

6 Where two counterparties are located in the same time-zone, the calculation of the Marked-to-Market value of the netting set of OTC-Derivatives shall be based on the netting set of the previous business day. Where two counterparties are not located in the same time-zone, the calculation shall be based on the transactions in the netting set which are entered into before 16.00 of the previous business day of the time zone where it is first 16.00. The obligation to post Variation Margin is occurring the following business day, or two business days after the calculation being made, subject to conditions. See article 9 and 12 DR Risk Management OTC Derivatives.

apply in the European financial markets for participants in such markets, whether it concerns exchange traded or OTC-traded instruments.

If the RtM measure aims to address "during the day" settlement risks, there would be a clear deviation from the overall concepts of addressing settlement risk as outlined hereabove. Such a measure would, as concerns the activity of proprietary trading firms not address the fact that **any and all trades performed by these firms are always** (this means from whichever time perspective this is assessed) **covered by the guarantee of the clearing member**. The operation of clearing arrangements and market infrastructure already addresses the risks that in the Discussion Paper are named "temporary dislocation" in market access and market liquidity.

If the RtM measure of the Discussion Paper aims to address risks of unavailability of market quotations or liquidity provision by a proprietary trader or liquidity provider that is temporarily or permanently unable to provide such services, it inappropriately addresses the functioning of the roles of these firms in the current financial markets as these roles have evolved over time. APT acknowledges that in the past, market makers or liquidity providers have been providing their services on a (quasi-) exclusive basis and monopolistic positions existed where exchanges and issuing entities (i.e. the companies whose securities were listed and traded on such exchanges) nominated firms to fulfil a role of market maker or liquidity provider for segments of the exchanges. Such exclusive and monopolistic role required firms that obtained such nomination to continuously provide quotations and liquidity in the markets. However, such exclusive and monopolistic roles have been abolished for numerous reasons in the recent history.

Market making and liquidity provision roles are currently assigned to market participants in an open competitive market and on a voluntary basis. This resulted in the increase of the number of participants to the regulated markets in capacities of market maker and liquidity provider. Consequently, if one of the market participants is unable to provide for market making and liquidity provision, such roles can be assumed by other participants without restrictions, delays or market access barriers. This must also be assessed in view of the continuing internationalisation of the markets, where market participants from around the globe are granted access to each other's markets without restrictions.

Therefore, an RtM measure that aims at addressing the risk of unavailability of market making or liquidity provision in the financial markets, inappropriately addresses the prevailing organisation of the open and competitive global financial markets. It also would introduce a prudential supervision measure for the orderly functioning of the financial markets, for which the (European) market conduct and market abuse frameworks of MiFID and Market Abuse Regulation properly address the particular risks threatening the fair, open and orderly functioning of financial markets. From this perspective, an RtM prudential supervision measure that aims at addressing market conduct or market abuse issues, is at risk to cross the boundaries of what constitutes and is framed in the rules of market supervision by market conduct authorities in Europe and in other jurisdictions.

4.7 Size of the investment firms as inappropriate metric

Although this does not appear in a consistent and clear way from the analysis in the Discussion Paper, it is evident that RtM fundamentals in the proposed framework are framed against the background of the (perceived role played by the) size of the investment firms. APT believes that the size of the firm alone (measured against the economical balance sheet of the firm) should not be the single determining metric to establish views as to RtM.

APT respectfully disagrees that via the assessment of "size" as metric to validate the need to apply the K-Factor of RtM, the Discussion Paper purports to introduce a reasoning to categorise firms as representing "systemic risk" for which an additional prudential requirement would be justified. APT reiterates that in view of the existing European framework for prudential supervision addressing systemic risk and addressing the requirements for systemically important institutions, it would be inappropriate to create an additional framework for investment firms that are to be considered "systemic" whilst not qualifying as a systemically important institution. If an investment firm is to be considered systemically important, it should be moved to the level of a "Class 1" firm and be made subject to the full CRR and CRD IV requirements. Whether an investment firm qualifies as systemically important should be exclusively measured against the scoring methodology as follows from article 131(3) CRD IV.

Assessing "size" and importance of firms within the meaning of the assessment methodology for G-SIIs and O-SIIs developed and calibrated by the Basel Committee and the Financial Stability Board and as endorsed by EBA, means that the definition of what constitutes an appropriate threshold should be set at the level for firms qualifying as global systemically important firms and firms that are otherwise categorised as large institutions. This would mean that such a threshold should be calibrated against the scope of application of the leverage ratio disclosure requirements for global systemically important firms and other large institutions. These are firms having a non-risk weighted (IFRS) balance sheet of 200 billion euro[7]. From the previous notes in this Feedback and Responses document it follows that none of the APT-Members may be classified as such a large institution.

Furthermore, and as will be explained in the paragraph on Risk-to-Firm ("**RtF**"), the measurement of the size of investment firms may not be made alone against the composition of the commercial (IFRS) balance sheets of such firms. In view of the neutralising and risk mitigating effects of the permanent and daily calculation of correlated and matched positions in the trading book and the risk transfer effects of clearing arrangements, the legal positions included in the balance sheet of proprietary traders with business models as exclusively apply for APT-Members, are significantly reduced.

The daily closing balance sheet of proprietary trading firms is reduced to the effect that market positions are extinguished entirely by means of the "take-over" arrangements with the clearing member. In turn the clearing member charges the proprietary trading firm with the Risk Margin requirement for which the firm needs to hold capital. This daily process of closing the balance sheet positions by means of risk transfer to the clearing member, effectively reduces the size of the daily closing balance sheet to the level of the Risk Margin. This is notwithstanding any trading volumes, number of trades or frequency of trades made during the trading day by the individual firm.

4.8 Interconnected cluster risk related to investment firms

The Discussion Paper also addressed the topic of RtM in the context of dependency of other investment firms that have customer relations on proprietary trading firms. In the Discussion Paper it is stated:

> "[…] *One such type of firm that may have no external customers and RtC is one that trades derivatives only on a proprietary basis, and in so doing, provides liquidity to the market (and hence to firms that do operate on behalf of customers).*"[8]

APT respectfully takes the view that this particular analysis is flawed for a number of reasons. Firstly, proprietary trading firms that would constitute a role that is so important for other market participants, that a (sudden) exit from the market or temporary failure would result in contagion effects in relation to other investment firms (that may or may not act for external

7 See for the most recent list of such European institutions: http://www.eba.europa.eu/risk-analysis-and-data/global-systemically-important-institutions/2016.

8 See: Paragraph 38, page 21 Discussion Paper.

customers) should be classified as systemically important in accordance with the assessment methodology as required pursuant to article 131 CRD IV.

Such a firm is likely to raise significant scores on the scoring categories of “interconnectedness” and “substitutability” within the meaning of the assessment methodology. As explained hereabove, none of the proprietary trading firms that are APT members would raise significant scores in those categories. Roles of market makers and liquidity providers are no longer exclusive or monopolistic and the firms conduct their business in an open and highly competitive environment, which in its nature avoids the dependency on the performance of single proprietary trading firms or groups of proprietary trading firms. The (sudden) exit or temporary failure of a proprietary trader or even a number of them will be absorbed by competing parties that will be able to step in the markets and assume the roles of the exiting proprietary trader(s) without significant interruption. Neither credit institutions nor other regulated entities with comparable roles and subject to prudential supervision are exposed to add-ons in capital requirements for the risk of simultaneous failure or the exiting of multiple firms.

If the analysis in the Discussion Paper concerning this point suggests that proprietary trading firms would be able to create outstanding and open positions vis-à-vis other investment firms trading on the same markets (on behalf of their customers), this would be based on a misconception of the functioning of the legal relations that are created in the markets for exchange traded financial instruments. As has been outlined hereabove, proprietary traders operate on the exchange traded markets via clearing members. Any legal counterparty relations of the proprietary traders are consequently and without exception assumed by the clearing member. The clearing member assigns the legal positions of the proprietary trader to the central counterparty who will, acting as central counterparty to the (clearing member of the) investment firm trading for its customers (or dealing on own account) step into the mirroring leg of the transaction related to the trade initiated by the proprietary trading firm. Any trade so executed by the proprietary trading firm therefore results with none of the trading parties from both sides of the transaction having any liabilities towards each other.

In this respect, APT doubts whether the analysis contained in the above referred quote from the Discussion Paper properly addresses the correct legal relations that arise in exchange traded markets in financial instruments. Also from historical perspective there is no evidence that failure of a single firm would have impact on other firms which would mean that individual firms would be able to cause contagion. Even in extreme stressed circumstances of the recent financial crisis, proprietary trading firms participating to such stressed markets have proven to be very resilient and able to continue to provide liquidity on the markets without interruption and without creating impediments for other firms.

4.9 Number and frequency of trades as inappropriate proxy

In the Discussion paper there is also a reference to the number or frequency of trades made by proprietary firms as a suitable metric for the measuring of the RtM K-Factor. APT respectfully rejects that this metric could serve as an appropriate proxy. Proprietary traders acting in their roles as market maker and liquidity provider are required to raise frequent quotations and trades in the market in order to fulfil their fundamental role.

A metric measuring the number or frequency of transactions would be counterproductive for the roles that such market makers and liquidity providers fulfil. By penalising the trading activity of proprietary traders with capital requirements, firms will be exposed to negative incentives to fulfil their roles. It should be furthermore noted that any impact on markets as a result of number of trades or the frequency in which such trades occur is appropriately addressed in the MiFID II framework from the perspective of market conduct, operational requirements and mitigation of risks related to such activity. A prudential measure that would affect the subject matter of number or frequency of trades risks to cross the boundaries of market conduct rules for which the market conduct authorities are competent.

In addition, it must be added to this point that neither Central Counterparties (CCPs) on the basis of EMIR requirements nor clearing members (on the basis of CRR/CRD IV requirements) are subject to additional capital requirements on the basis of the number of frequency or volume of trades. Therefore, the rationale may be challenged to impose capital requirements on proprietary trading firms for the roles they fulfil in transaction processing based on volume or frequency of transactions, as such firms operate in identical environments as CCPs and clearing members when acting on the regulated or MTF markets.

4.10 Conclusions as regards RtM for proprietary firms

With the comprehensive analysis as regards the RtM K-Factor approach as contained in the Discussion paper, APT wishes to demonstrate that the proposed metrics and proxies to establish the K-Factor for this risk area are not fit for purpose. APT summarises and concludes as follows:

- Absent evidentiary support to the need to establish a complete new risk category in the prudential supervision regime for investment firms, it should be generally concluded that it should be avoided to impose the RtM measure to proprietary firms;
- Applying the assessment methodology of article 131 CRD IV for GSIIs and OSIIs and incorporating the EBA guidelines for application of the leverage ratio disclosure requirements for global systemically important firms and other large institutions, it can be concluded that, in view of size and importance (even if this is expressed in terms of the non-risk weighted balance sheets of all APT-Members) none of the APT-Members qualify as systemically important institutions or large institution, not on a domestic scale, not on a European scale and not on a global scale;
- APT also respectfully rejects the analysis that size or importance of investment firms should be measured taking the commercial (IFRS) balance sheet as focus point. The economic balance sheet of proprietary trading firms, does not represent the actual accruals of legal obligations of firms that exclusively operate on regulated markets or otherwise submit their trades to central clearing. Eventually and in any event each time as per the close of a trading day, open positions are assigned via the clearing member to the central counterparty. Settlement risk is therefore reduced to zero for all categories of financial instruments, whether it be straightforward securities, exchange traded funds, derivatives or any other product in which the APT-Members trade;
- Furthermore, and notwithstanding the zero score as regards the size or importance, if a proprietary firm would raise high scores on the scoring categories of interconnectedness or substitutability within the meaning of the GSII/OSII assessment methodology, such a firm could be considered to be “systemic” and in such case the proprietary trading firm should be made subject to the CRR/CRD IV prudential supervision regime. None of the APT-Members have high scores on either one of the scoring categories and therefore there is no need to analyse or address as to whether or not the risk of interconnectedness or cluster-risk could accrue in respect of proprietary trading firms towards other investment firms (where these firms are themselves proprietary trading firms or investment firms with customers);
- From this analysis it follows, that if a proprietary trading firm is not to be categorised as systemically important, such a firm would also not be “systemic”. APT respectfully rejects the analysis of the Discussion Paper that there is a need or rationale to assess whether firms that are not systemically important, could nevertheless qualify as being “systemic”;

- None of the APT-Members are performing “bank-like” activities, which APT interprets as the (high risk) combination of conducting investment activities (f.i. dealing on own account) with other investment services (f.i. brokerage, investment advice or portfolio management). Consequently, there is no risk of comingling of customer monies or financial instruments with those of the investment firm;
- The number and frequency of trades is an inappropriate proxy for the establishment of K-Factors for the RtM risk area. The number and frequency of trades carried out by proprietary trading firms is carried out to prevent mispricing, and is driven by market circumstances, and is therefore most important in volatile markets as a risk mitigation tool in order to be able to provide liquidity under challenging circumstances. Penalising proprietary trading firms with capital requirements that are raised depending the number or frequency of transactions, would form a significant impediment for the fulfilment of the important roles as market makers and liquidity providers. Such roles require proprietary trading firms to perform transaction with high frequency and in large numbers of transactions. APT reiterates, however, that proprietary traders never act on an exclusive basis.

APT respectfully takes the view that the proposed framework for the RtM category as laid out in paragraph 4.3.1 number (38-40) seems to be redundant and does not effectively provide for a risk sensitive measure. From the perspective of the analysis made in this paragraph and in the previous paragraph, both the RtC and RtM categories result in zero values as regards the quantification of levels of capital for proprietary firms. However, APT is not suggesting that proprietary trading firms should not be subject to capital requirements. APT will provide for a reasoned alternative in the following paragraphs, which it believes appropriately addresses risks as they may develop with proprietary trading firms.

[Further paragraphs on following page]

5 Risk to Firm (RtF)

5.1 Risk to Firm is an inappropriate risk categorisation for APT-Members

APT wishes to lay out why it believes that as a matter of principle it is inappropriate to assess whether a risk to the firm itself should result in additional capital requirements. As outlined hereabove in the previous paragraphs, neither the RtC nor the RtM as they have been analysed in the Discussion Paper are relevant to proprietary trading firms that are neither systemically important, nor systemic nor bank like.

Particularly the fact that none of the RtC K-Factors are relevant for proprietary trading firms as they are organised in the way APT-Members are, would be the most important reason why the potential damages that a firm would incur in view of its business model or firm-specific characteristics, are not impacting third parties. Therefore, there is no direct or indirect risk that the rights, assets or position of third parties could be damaged or prejudiced if it turns out that a proprietary trading firm would be inadequately capitalised. This may only be different for the risk borne by the clearing member with whom proprietary trading firms have a dependent and important relationship.

As APT will note in the following paragraphs, clearing members exposed to proprietary trading firms require the proper capitalisation of risks that may occur, notwithstanding the full assignment of positions and trades into the central clearing infrastructure. APT therefore notes, that with the exception of the role of the clearing member for which capital requirements apply, no other external party (other than ordinary trade creditors) may be affected in the event a proprietary trading firm fails or prematurely exits the markets.

5.2 Risks of the firm are to be borne by its owners

APT points out that proprietary trading firms are without exception organised as firms whose shareholders/owners are exclusively exposed to the risks borne by the firm. RtF is equal to the risk of its shareholders. There is no rationale whatsoever to be found, why prudential requirements should be imposed on firms whose shareholders are exclusively exposed to the firm's risks.

The fact that shareholders are exclusively bearing the risks of the firm does not prevent the firm being subject to capital requirements. Effectively the capital requirements which apply to the firm will further constrain the shareholders' rights vis-à-vis the firm. This is related to the qualitative requirements applicable for the firm's capital to be held, also in the regime that APT proposes for its members.

5.3 Uplift-factor inappropriately addresses the clearing model

APT respectfully disagrees with the use of a new leverage concept as a proxy for risk arising from the balance sheet and off-balance sheet exposures of the firm. The use of this proxy in relation to fully hedged positions of proprietary trading firms would result in an extreme uplift of the capital requirement for proprietary trading firms, without this measure being risk sensitive.

Proprietary trading firms might have large balance sheets in certain cases, but these balance sheet numbers do not present the actual risks of the firm. Firstly, as stated above, positions of proprietary trading firms are often to a large extent or fully hedged. Secondly, there should be a distinction made between the concept of a commercial balance sheet established for accounting purposes, and balance sheet composition after the application of the processes where trade positions of the firm are completely assigned to the clearing member that in its turn assigns these positions to the central clearing infrastructure.

If the balance sheet numbers would be assessed taking into account such central clearing processes, significant abbreviation of the balance sheet would occur, and the remaining exposures on the liabilities side of the balance sheet would comprise of capital held at the level of the Risk Margin imposed by the clearing member as explained hereabove. Such capital required to cover for the Risk Margin would be held in the form of the collateral assets pledged to the benefit of the clearing member in the system of charging the proprietary trading firm with the required capital.

In the Discussion Paper it is noted that in certain cases "risk-sensitivity can be added to the design of the "uplift", where EBA provides for the example of applying risk weights for certain types of assets or exposures. APT recommends that a simple method to address the risk sensitivity of balance sheet positions of proprietary trading firms, would be to fully take into account the effectiveness of the clearing processes and infrastructure resulting into transfer of the risks from the proprietary trading firm.

In the relationship with the clearing members, proprietary trading firms are charged on a daily basis with a capital charge for the risks calculated by the clearing member in respect of the positions and trades made by the firm. For this charge proprietary trading firms must post collateral to the clearing member. The aggregate margin requirements imposed by clearing members already reflect margin imposed by CCPs and are often already duplicative to a substantial extent, particularly because one leg of a transaction (long) may be lodged with one clearing member while the offsetting leg (short) may be lodged with another one for operational, prudential or commercial reasons, precluding offsetting of correlated positions and thus overcharging margin for a transaction that is factually hedged.

The risk estimated by the clearing member, furthermore takes into account the various factors that mitigate risk, such as correlation of positions in the various markets, netting effects and all other methods to assess the remaining risks. It is important to emphasise that these risk estimations are related to the daily position between the clearing member and the proprietary trading firm only. Positions in the market and of counterparties are all guaranteed by the clearing members who step in the legal leg of the trade replacing the proprietary trader, without any recourse to the proprietary trading firm by the counterparties in the market.

5.4 Conclusion as to RtF

APT cannot concur with the viewpoints included in the Discussion Paper as regards the need to impose the uplift factor for RtF to proprietary trading firms. Such firms are managed entirely at the risk of the owners/shareholders of the firm and there is no justification nor need to impose mandatory capital requirements for the RtF.

In addition, APT believed that the RtF measure as it has been designed in the Discussion Paper, does not effectively address the actual risks borne by proprietary trading firms. Those risks are towards the clearing member that requires, as part of the clearing arrangements, proprietary trading firms to cover the Risk Margin with capital. Any other risks are transferred and/or mitigated through the operation of the clearing arrangements, in which positions are assigned to the clearing member and subsequently contributed to the central counterparty.

6 Appropriate capital requirements for APT-Members

6.1 Capital requirements for orderly winding down only

None of the APT-Members have or build up exposures with external customers. Proprietary trading firms do not have access to client funds or assets, nor may these firms utilise customer funds or assets for their own trading business (for instance there is no securities lending business). Therefore, there is a strong case to consider capital requirements' objectives to only focus on the orderly winding down of the proprietary trading firm. In the event a proprietary trading firm (suddenly) exits the market and terminates its operations, the only stakeholders affected by such event would be the corporate stakeholders of the firm.

In the event that a trading firm would be wound down overnight, the effects will be that the firm will not participate in the quotation process and market making activities the following day. Its role will be assumed by other parties and there will be little (if not no) effect from the lack of presence of the firm that exited. Any open positions that the firm entered into in the previous period will be wound down via clearing and settlement, in principle, in a matter of two to three business days (depending on the timing of settlement proceedings in the applicable markets). Positions traded by proprietary trading firms prior to their exit will be contributed to clearing and settlement process that by the nature of operation of market infrastructure will effectively be resolved within a very short timeframe. Residual positions (if any) will be subject to wholesale quotation and trade processes and will be taken over also as a matter of a number of days. Effectively this means that an exiting proprietary trading firm will terminate exposure to markets within a number of days.

These positions are, to reiterate the points made earlier in this Feedback and Responses document, no direct positions of the proprietary trading firm to counterparties, as they are made subject to clearing the day before the winding down process commenced. The outstanding margin calls from the clearing member will also be wound down in a matter of a few days and this will result in a release of the proprietary trader from its obligations vis-à-vis the clearing member and a release of the capital of the proprietary trader.

In view of this fast winding down process in connection with the trade positions of the proprietary trading firm, the sole interests of stakeholders that will need to be addressed in the winding down process going forward after the closure of market positions and final settlement with the clearing member, will be the employees of the firm, the trade creditors (such as suppliers of IT-services, utilities, landlord and so forth) and the shareholders of the company. It should be considered whether serving the interests of these stakeholders should at all be an objective of prudential supervision.

In any event this point will put emphasis on the assessment how long the time horizon should be for which funding of dismantling costs should be arranged. Following from the Fixed Overhead Requirement ("**FOR**"), a three months' period is often considered to be a sufficient period in which an investment firm will be enabled to exit the market and liquidate its positions in an orderly manner. For proprietary trading firms such a three months' period would be considerably long and for these firms there is in any event little justification to extend this period beyond the three months' term.

6.2 Fixed Overhead capital requirements for proprietary trading firms

In view of the organisation of the businesses of proprietary trading firm who are member of APT, it has been established that the K-Factors designed for the RtC and RtM risk categories are not relevant weighing factors for proprietary trading firms. From this it follows that there will be no reason to apply the K-Factor prudential requirements to proprietary traders' member of APT. Consistent with this viewpoint would be to use the FOR as the absolute floor for proprietary trading firms' capital requirements, as the scoring on RtC and RtM K-Factors is likely to result in zero amounts. The FOR requirement would then serve to establish in any event a capital floor, notwithstanding the minimal impact of RtC and RtM factors.

Imposing FOR as a standard measure for proprietary trading firms would be a suitable measure to address the unwinding costs of the firm in the event of a failure or exit from the markets. The FOR would in any event cover for all fixed overhead costs for a survival period of three months. APT believes that this period is sufficient to organise an orderly winding down of the firm and to settle any claims with the corporate creditors of the firms concerned. APT reiterates its viewpoint that a proprietary trading firm that is exiting, will have no exposures to external customers or counterparties in the financial markets after two to three days after the termination of activities as trader. In any event FOR serves to wind down the firm's corporate business operations and, to a certain limited extent, it will serve to settle any claims with the clearing member(s).

From the perspective of FOR as being a dynamic capital requirement (the capital requirement will increase upon the growth of the firm as a result of the increase of the overhead costs of the firm), there will be no need to establish a regime for minimum capital requirements in the form of fixed amounts of capital to be maintained. APT believes that the original ideas of the European legislator to create a system with static minimum capital requirements and dynamic solvency capital requirements must be re-evaluated.

Minimum capital requirements could be abolished as in any event FOR capital requirements for proprietary trading firms will exceed any number that will be set for minimum capital requirements for investment firms, even if the legislator would consider to increase the 50,000-125,000-730,000 euro numbers to take inflation into account.

For market entrants an upfront FOR requirement would be a sufficient high threshold to avoid the market entrance by firms that are insufficiently capitalised. APT promotes newcomers including FinTech initiatives as it strongly believes that competition improves the resilience of the market structure. Over the last decade the monolithic market making structure requiring high dependence on a limited number of financial institutions has been successfully replaced with a highly dispersed, competitive, open, transparent environment engaged by new entrants. A FOR capital requirement promotes new entrants which is beneficial for the system as a whole.

A firm that wishes to enter the market, will be subject to severe scrutiny by the supervisory authorities in the license application process in any event. Such firms are likely to be required to properly budget costs and forecast the financial condition of the firm as a requirement to obtain the license. In line with this process it will not be too burdensome to calculate upfront a FOR for such a firm which will also serve as the "entrance" capitalisation level.

6.3 Uplift of capital requirements in the form of the Risk Margin

APT acknowledges that for the larger proprietary trading firms there may be a need to consider an uplift of the FOR capital requirement. Such an uplift should serve to address potential market participant concerns and perceptions as regards the risks that could be caused by such larger proprietary trading firms. Such market participant concern would transmit to the supervisory authorities as well, which absent a suitable mandatory requirement applicable to the larger firms, would not be constrained to use all of the available discretionary powers (such as the powers set forth in article 104 CRD IV in the context of the Supervisory review and Evaluation process). APT-Members also have an interest in legal certainty as regards the capital requirements regime that applies to all of the types of the firms.

APT therefore does not propose an alternative for the RtF, but wishes to address capital requirements in line with the proposed approach as set forth in paragraph 79 of the Discussion Paper, in which a risk margin model is considered as an alternative way forward. For this reason, APT suggests that for any of the proprietary trading firm that exceeds a certain threshold an uplift of the FOR capital requirement would be an appropriate capital requirement regime for the larger firms. Such uplift capital requirement would then be aligned to the level of the charges to the proprietary trading firms for the exposures (which would be close to a tail risk number at the end of the distribution scale of unexpected losses) existing upon assignment of all trade positions to the clearing infrastructure occurring on a daily basis. This charge would be the comprehensive assessment of the entire range of risks that may be construed in theoretical models, including settlement risk, interest rate risk, operational risk, credit valuation adjustment risk and any other relevant risk areas.

The relevant uplift numbers are comprised in the daily calculated aggregated margin numbers in the relationship between the proprietary trading firm and its clearing member. This is what is referred to by APT as the Risk Margin measure, which is quantified by applying the risk assessment models of the clearing member. An uplift of the FOR requirement for the larger proprietary trading firms would therefore result in the requirement to hold capital against the Risk Margin calculated on a daily basis.

APT suggests that this uplift of the FOR requirement should apply to the larger firms being part of its member population. The uplift factor in the form of the Risk Margin should apply to proprietary trading firms that may be considered to be perceived as being a significant participant to the markets. APT suggests that an objective and appropriate threshold should be developed to differentiate between Class 2 and Class 3 proprietary trading firms in close consultation between the legislator and the industry. APT believes that about three to four of the current APT-Members should be subject to the uplift factor in the form of the Risk Margin measure.

In order to avoid that in view of volatility swings in the financial markets, larger firms subject to the Risk Margin measure would at any time be undercapitalised depending on market circumstances, APT proposes to impose the objective capital floor of the FOR requirement as the safeguard against undercapitalisation. The capital requirement for the larger proprietary trading firms would, consequently, be displayed in the following formula:

$$\textbf{Capital requirement larger proprietary trading firms} = \textbf{MAX}[\textbf{FOR}, \textbf{Risk Margin}]$$

APT is aware and familiar with the critics concerning the dependency of proprietary trading firms on the internal model calculations by clearing members. APT respectfully disagrees that those critics are well founded. Firstly, it must be emphasised that all of the clearing members with whom the APT-Members engage in the trading business, are regulated banks/credit institutions. The Dutch clearing member with whom the APT-Members work (often in addition to the use of services from other clearing members regulated elsewhere) is fully subject to the CRR and CRD IV requirements and a “significant institution” within the meaning of the assessment criteria in the Single Supervisory Mechanism (“**SSM**”) and is therefore under direct supervision of the European Central Bank. The internal models utilised by this clearing member have therefore been subject to the strict assessment and validation processes as they stem from the CRR and CRD IV requirements involving the competent supervisory authorities. The internal model utilised by the relevant clearing member has also been exposed to historical performance tests, including the severe stressed circumstances of the volatile markets during the financial crisis of 2008-2010.

APT also suggests that firms being subject to MiFID authorisation requirements will need to comply with the requirements of article 16(5) MiFID II as concerns outsourcing of critical business functions. This MiFID requirement does not provide for an absolute prohibition to such outsourcing of certain critical business functions, but imposes a strict qualitative assessment process to support the evaluation of the outsourcing process. APT suggests that the outsourcing of the calculation of the Risk Margin as charged by the clearing member to the proprietary trading firms is to be made subject to the strict requirements of article 16(5) MiFID II. This will enable both the investment firm concerned and the competent supervisory authorities to establish a proper proceeding in which the outsourcing of this critical business function is assessed, tested and evaluated to the greatest extent.

7 Liquidity requirements

APT respectfully points out that in the current supervisory practice most (if not all) investment firms (no matter which business they conduct) are excepted from the liquidity supervision requirements as set forth in Part 6 CRR. The supervisory authorities have widely applied their discretion to exempt the investment firm sector from being subject to liquidity requirements. In this context, APT respectfully challenges that there is a convincing and evidentiary supported case to introduce a liquidity supervision scheme for investment firms.

In addition, it should be noted that the risk management model applied by clearing member firms in respect of their clients, already incorporates a stress tested liquidity and concentration risk factor in the charges of capital and requirements to post high quality liquid assets as collateral by proprietary trading firms. For example, illiquid positions held in the trading book are made subject to stricter stress tests and more severe shocks and accounted for in the Risk Margin charged to the proprietary trading firm.

If a liquidity supervision scheme is to be introduced, APT would be in favour of keeping such regime very simple. In this respect the minimum liquidity standard for investment firms should be in the form of a simple metric, for instance by imposing the requirement that a significant percentage of the capital requirement applicable to the firm is to be held in the form of liquid assets. The requirements for the assets to be maintained to fulfil the liquidity requirement should be kept simple as well. APT suggests to adapt the eligibility criteria to the standards set forth in the DR Risk Management OTC Derivatives for eligible collateral for Initial Margin and Variation Margin.

8 Consolidated supervision

APT acknowledges the need and rationale to include a chapter on supervision on consolidated basis in the future prudential supervision regime for investment firms. Such a regime should particularly enable supervisory authorities to identify any intragroup positions and intragroup transactions that may undermine or dilute the quality of the capital to be held by regulated investment firms subject to supervision of the European supervisory authorities. Any such intragroup positions and intragroup transactions affecting the quality of the regulatory capital base of regulated investment firms, should result in appropriate deduction and/or impairment rules and similar measures to enhance the quality of the regulatory capital base of the investment firms concerned.

APT does not support any rules on supervision on consolidated basis that would introduce regulatory capital requirements on a solo basis for unregulated firms. The principle to restrict capital requirements to regulated firms only also applies for the consolidated supervision regime for credit institutions (banks) and the supplementary supervision regime for insurance groups. There is no convincing reason to introduce rules for groups of investment firms that would deviate from general principles of group supervision as adopted in Europe.

Unregulated subsidiaries in the group of which an investment firm forms part, should neither be exposed to regulatory capital requirements on a solo basis nor should these requirements be created indirectly and at the level of the parent company on a consolidated basis. Unregulated subsidiaries’ values should be accounted for in the consolidated financial statements of the (European) parent, applying ordinary valuation principles and applying ordinary accounting principles (IFRS or local GAAP applicable to the parent company).

Constraints imposed on unregulated subsidiaries in the group of which one or more investment firms form part, **should be restricted to the deduction and/or impairment for the purposes of regulatory consolidation of financial indebtedness relations or cross-capital holdings** among the group members. These rules should support the avoidance of double gearing of regulatory capital and dilution of the quality of the capital of regulated investment firms in the group. Such rules should be without prejudice to the ability and permissibility of the inclusion (and therefore non-impairment) of certain intragroup debt or equity positions and values for ordinary accounting purposes if permitted under the IFRS or local-GAAP frameworks.

Any rules on consolidated supervision requiring regulated firms to hold regulatory capital levels should be restricted to firms established in the EEA. In this respect, APT is in favour of the territorial scope of application of the mitigated consolidated supervision regime for groups of investment firms as laid out in article 15 CRR. APT therefore suggests that this territorial restriction to EEA-investment firms as this is prevailing in the article 15 CRR provision, is to be confirmed in the new prudential supervision regime as well.

APT would strongly reject any extraterritorial effect of the prudential supervision regime applicable to European investment firms beyond the borders of the EEA as a result of the application of the rules on consolidated supervision. For the avoidance of doubt with "prudential supervision regime" APT refers to all its elements: capital, liquidity, governance and remuneration.

9 Qualitative capital requirements

APT concurs with the viewpoints included in points 88 to 90 of the Discussion Paper as to the qualitative requirements for capital to be held by investment firms. The applicable system for banks pursuant to the rules of CRR is not fit for purpose for the investment firm industry in view of complexity and misalignment of the purpose of capital to be held by such firms.

Most of the APT-Members apply the capital requirements by means of the raising of fully paid in ordinary capital from its shareholders and prudent policies as regards retained earnings distribution. Retained earnings reserves are in many instances utilised to support the further growth of the firm and serve as buffer for future expansion of the business. Shareholders waive in such cases their rights for full dividend distribution.

APT does see the advantage of a second tier of capital that may qualify as regulatory capital in the form of medium term subordinated debt. Such "Tier 2" regulatory capital instrument should be properly aligned to the requirements of proprietary trading firms however. As is noted in paragraph 6, regulatory capital requirements for proprietary trading firms should serve to support the orderly winding down of the firm applying a maximum horizon of three months.

In view of the limited horizon where regulatory capital serves to wind down the firm's affairs and to liquidate the business operations, any provisions in the qualitative requirements for Tier 2 capital instruments, should take into account that restrictions on repayment of the principal amount borrowed upon the issue of the Tier 2 instrument should be sufficiently flexible to cater for a winding down of the Tier 2 instrument as well, simultaneously with the process of liquidating the firm.

As regards the subject matter of prudential filters and deductions, APT briefly notes that particularly the deductions from capital for the holding in intangible assets do restrict the possibilities for starting firms that have capitalised the development costs of software and automated platforms. Therefore, as has been the case for comparable developments in the FinTech industry, the deduction form capital as a generic measure might create impediments for the market entry of newcomers.

APT concurs that any prudential filters related to accounting values might not be relevant for the investment firm industry and in a revised prudential supervision regime, the abolishment of the larger majority of the prudential filters and deductions would contribute to the further simplification of the rules, without frustrating the general concepts of the risk sensitive approach.

10 Remuneration

10.1 Introduction

Investment firms which are "CRR-Investment firms" are made subject, through the construction of the CRR concept of "institution" to the remuneration rules as laid out in articles 92 up to and including 96 CRD IV. Investment firms that are not defined as "CRR-Investment firm" are excluded, in principle, from the aforementioned CRD IV rules. Within Europe there is therefore a different application of the remuneration rules for investment firms, depending on the type of activities they perform.

An important differentiator for the application of the remuneration rules to investment firms, concerns the inclusion of investment firms in the scope of application of articles 92 up to and including 96 CRD IV if they are qualifying as investment firm within the meaning of article 4(1)(2) CRR. Excluded from this definition are, amongst others, investment firms that are not permitted to carry out the ancillary activities of Annex I, Part B (1) MiFID (custodian activities as regards client monies and financial instruments). This example demonstrates that also in the current applicable environment, there is a differentiation in scope of applicability excluding investment firms that are less in the position (in view of their restricted activities) to cause risks to customers.

The conceptual framework of CRD IV for remuneration rules, also suggests that remuneration should be constrained in such circumstances that employee compensation would have direct effect and influence on the increase of the risks financial institutions take and eventually, the detrimental consequences for customers of this risk taking behaviour. In most instances in Europe remuneration rules are required to apply to all individuals at management board level, all individuals at the levels in the hierarchy of the institution's work force where influence on the risk profile of the firm may be exercised and all those individuals having client facing positions.

10.2 Remuneration rules in the context of proprietary trading firms

The original objectives of the European remuneration rules of the CRD IV regime particularly aimed to introduce constraints on variable remuneration paid out <u>within banking organisations</u>, particularly to introduce a level playing field between shareholders of the company and employees as regards dividend distributions. The outflow of dividends and correlated variable remuneration to executives of banking organisations had been perceived by the policymakers worldwide to be prejudicial to the ability of banks to use profits to build up capital buffers and make banking organisations more resilient.

It may be argued whether such rules should apply at all to proprietary trading firms. Typically, these firms do not act for customers and they do not pose any risk to customers. As has been outlined in the paragraph on the RtF risk factor (corporate) governance relations within proprietary trading firms differ significantly from the governance and stakeholders' model for investment firms acting for and on behalf of customers. The stakeholder model of proprietary trading firms does not require to take into account the customer's interests and the requirement to constrain the risks that a firm may develop vis-à-vis its customers.

There is also a less persuasive need to constrain dividend distribution mechanisms within proprietary trading firms. These firms need not to be capitalised to make the business resilient against internal or external negative shocks or other idiosyncratic issues in order to create a long term viability of the firm. If a proprietary trading firm fails, it should be exiting the markets as soon as practicable and any and all losses are to be borne by the shareholders of the firm only.

It is in recognition of the differences in respect of the stakeholders' models of investment firms and particularly the fact that proprietary trading firms do not act for and on behalf of customers, that the Dutch legislator has introduced a bespoke statutory regime for Dutch proprietary traders, exempting these firms from significant parts of the rules that are otherwise applicable to the Dutch financial industry.

10.3 Position APT as to remuneration

From the outset it has been understood by the Dutch proprietary trading firm industry, that to a certain extent some of the remuneration rules are useful to be applied within their internal organisations as well. Much more than any other part of the financial industry, employees and individuals working within proprietary trading firms are co-sharing the risks of the business with the owners and shareholders of the firm.

The typical organisation model of most of the Dutch proprietary trading firms discourage risk taking by traders by means of direct penalisation at personal income level. A trader not respecting the boundaries of the risk profile determined and established by the management and shareholders of the firm, will feel direct consequences in the pay out of remuneration. The levels of fixed remuneration with Dutch proprietary trading firms is also significantly lower than in other parts of the Dutch financial industry, particularly remuneration earned within banks.

Employees and individuals contracted by proprietary firms are much more exposed to the risks of the firm than in any other part of the private sector. Such individuals bear more or less the same risks as the shareholders' of the firm and therefore benefit from the prosperity of the firm at par with the shareholders, but also have to bear the negative consequences of a downturn of the firm or less profitable years jointly with the shareholders.

It is within this perimeter that APT has defended towards the authorities that a certain part of the remuneration rules as applicable for banks and other comparable financial institutions are relevant for the proprietary trading industry, but that other parts are irrelevant and even cause severe conflicts with the organisation of the risk management function and processes within the proprietary trading firms.

This particular position has been recognised and acknowledged by the Dutch legislator and authorities and has resulted in a bespoke regime for the proprietary trading industry in the Netherlands. This bespoke regime is based on the one hand on statutory law confirmation providing for a carve out of certain parts of the rules for variable remuneration for proprietary trading firms and on the other hand on application of the rules by supervisory authorities based on principles of proportionality.

As regards the latter, particularly the new to be introduced exemption rules in the proposals of the European Commission of 26 November 2016 for revision of articles 92 and 94 CRD IV as regards proportional application of remuneration principles, distribution of variable remuneration in the form of financial instruments and retention periods in fact confirm the currently applicable arrangements for Dutch proprietary trading firms.

APT recommends that if remuneration rules are to be introduced for investment firms in the new prudential supervision regime, similar carve outs and proportional application as currently exists under the currently applicable rules should be continue to apply in the future. To reiterate the position of APT in this respect the following main principles should form part of the new regime on remuneration as regards proprietary trading firms:

- Setting the **limitation on levels of variable remuneration** and payment modalities should be left **at the discretion of the proprietary trading firms** and no mandatory statutory law limits should apply. This measure allows proprietary firms to expose their employees and contractors trading on the markets to the full effects of risk management and subject such individuals fully to the upside but also downside of the business of the firm, co-sharing risks effectively and efficiently;

- Retention and vesting rules regarding variable remuneration should allow for implementing of **vesting schemes and distribution schemes with shorter time horizons and intervals**, permitting sufficient flexibility in the recruiting and employee redundancy schemes of proprietary trading firms whilst fully accommodating claw back arrangements for underperforming individuals;
- Profit **distribution and retention rules** regarding **variable remuneration should be aligned to the time horizon of the necessary survival period of proprietary trading firms**, being a briefer period to enable the orderly winding down of the firm with no need to resurrect or recover the business to serve the interests of external stakeholders. Therefore, there is in any event no convincing reason to include Pillar2-capital requirements into the calculation of maximum distributable reserves for proprietary trading firms.

11 Responses to 35 Questions contained in the Discussion Paper

APT has filled out the electronic response form made available by EBA and posted the responses by means of the electronic tool made available by EBA on its website. APT wishes to reiterate the questions and responses in this document for the sake of completeness'.

Question #	EBA Question	APT Responses
1	What are your views on the application of the same criteria, as provided for G-SIIs and O-SIIs, for the identification of 'systemic and bank-like' investment firms? What are your views on both qualitative and quantitative indicators or thresholds for 'bank-like' activities, being underwriting on a firm commitment basis and proprietary trading at a very large scale? What aspects in the identification of 'systemic and bank-like' investment firms could be improved?	**First Question**: The Dutch Association of Proprietary Traders ("**APT**") wishes to emphasise that none of its members would, if the methodologies would be applied to asses Global Systemically Important Institutions ("**GSIIs**") or Other Systemically Important Institutions ("**OSIIs**"), qualify as such, not on a global scale, not on a European scale and not on a domestic scale. None of the APT-Members would qualify as a firm whose distress or failure would have a systemic impact on the Dutch or the EU economy or global financial system due to size, importance (including substitutability or financial system infrastructure), complexity, cross-border activity, and interconnectedness. It is based on the criteria developed by EBA in furtherance of the provision of article 131(3) Capital Requirements Directive IV (Directive 2013/36/EU, "**CRD IV**")) to identify other systemically important institutions that APT has concluded that none of its members would qualify as systemically important within the meaning of prevailing assessment methodologies. Following the rationale and recommendations of EBA in its Opinion to the European Commission of 19 October 2016 (Opinion of the European Banking Authority on the First Part of the Call for Advice on Investment Firms, 19 October 2016, EBA-Op-2016-16) in the initial and first set of

Question #	EBA Question	APT Responses
		responses to the Call of Advice of the European Commission of 13 June 2016, investment firms that do qualify as systemically important (whether on a global basis or on a domestic basis) should continue to be subject to (parts of) the CRD IV and Capital Requirements Regulation ("**CRR**"). For these investment firms, there is no convincing case to consider the development of a separate and revised prudential regime. APT therefore believes that the assessment methodology for G-SIIs and O-SIIs is appropriate for the identification of systemically important institutions, but rejects the analysis that other criteria to assess whether an investment firm would perform "systemic and bank-like" activities would be a suitable method to categorise investment firms as being "systemically important" or not. **Second Question:** For investment firms that may not be assessed as being systemically important, there is good reason to develop a separate prudential regime. EBA establishes its views and recommendations in the Discussion Paper on such separate and deviating prudential regime for investment firms that in any event do not qualify as systemically important. APT is supportive to this analysis. If an investment firm that has significant trading activity, does not exceed the thresholds of the methodology of assessing whether firms are systemically important, such an investment firm should not be subject to specific and extraordinary prudential supervision rules. Such a firm is not systemically important and cannot (consequently) cause systemic risk. Non-systemically important investment firms that are not (potential) perpetrators of systemic risk should not be subject to specific prudential supervision rules to manage their potential impact on market confidence. Market confidence must be preserved and must be managed through the comprehensive MiFID II market conduct rules and Market Abuse Regulation framework applicable to such investment firms without exceptions. In summary: APT does not support the analysis that certain activities such as proprietary trading constitute a "qualitative" criterion suitable to categorise investment firms as systemically important, and consequently the mere fact of the "quantitative" criterion of scale of the activities does not conclusively assess whether an

Question #	EBA Question	APT Responses
		investment firm is to be categorised as systemically important or not. **Third Question**: APT does not support the analysis made by EBA in respect of introducing additional qualitative criteria to rank investment firms in certain categories. APT does not believe that an investment firm that is not systemically important can be systemic. APT does see a conflict between the internationally agreed upon assessment methodology for systemically important institutions (which APT believes is not an open-ended system for which additional assessment criteria can be added) and the addition of new qualitative criteria. APT believes that there is a fundamental flaw in the analysis with respect to the criterion of "bank-like". Either an investment firm is performing banking activities for which it would need to be licensed as a credit institution, or the firm is acting in accordance with the MiFID authorisation performing investment services and investment activities in accordance with the scope of its license. *Further details of the viewpoints of APT can be found in paragraph 4.3 and 4.4 of its Feedback and Responses Memorandum dated 1 February 2017.*
2	What are your views on the principles for the proposed prudential regime for investment firms?	In 2013 CRR/CRD IV amalgamated the Capital Adequacy Directive of 2006 setting forth market risk rules for banks and investment firms with the provisions of the Capital Requirements Directive of 2006 containing the banking credit and operational risk rules. As result of this process, significant out of scope, incompatibilities with business models, disproportional effects and improper alignment of the rules for investment firms occurred in supervisory practice. There is, therefore, a convincing case that the broader group of European investment firms will be made subject to an own prudential supervision regime. EBA's Discussion Paper proposes such separate prudential supervision regime for investment firms. APT agrees with the viewpoints of EBA as regards the alignment of risk factors to the typical business models of investment firms who operate in a different way as opposed to banks. In this manner incompatibilities of the current CRR/CRD IV regime with such business models will be removed and the risk sensitivity of the prudential supervision regime will be improved.

Question #	EBA Question	APT Responses
		EBA's proposals in the Discussion Paper require to address a very broad population of investment firms active in all the EU-Member States having very different business models and propositions to the markets and customers. Although APT has not analysed the applicability of the proposed risk factors for other types of businesses in a detailed way, it appears that, in balance, the proposed bespoke regime seems to adequately address the requirements for prudential supervision of investment firms. None of the APT-Members have or build up exposures with external customers. Proprietary trading firms do not have access to client funds or assets, nor may these firms utilise customer funds or assets for their own trading business (for instance there is no securities lending business). Therefore, there is a strong case to consider capital requirements' objectives to only focus on the orderly winding down of the proprietary trading firm. In the event a proprietary trading firm (suddenly) exits the market and terminates its operations, the only stakeholders affected by such event would be the corporate stakeholders of the firm. *Further details of the viewpoints of APT can be found in paragraph 4.3 and 4.4 of its Feedback and Responses Memorandum dated 1 February 2017.*
3	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 overheads 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 regime with 'built-in' proportionality have?	In view of the organisation of the businesses of proprietary trading firm who are member of APT, APT establishes that the K-Factors designed for the RtC and RtM risk categories are not relevant weighing factors for proprietary trading firms. From this it follows that there will be no reason to apply the K-Factor prudential requirements to proprietary traders' member of APT. Consistent with this viewpoint would be to use the FOR as the absolute floor for proprietary trading firms' capital requirements, as the scoring on RtC and RtM K-Factors is likely to result in zero amounts. The FOR requirement would then serve to establish in any event a capital floor, notwithstanding the minimal impact of RtC and RtM factors. <u>This prudential regime would be suitable for proprietary trading firms that fall in Class 3.</u> APT acknowledges that for the larger proprietary trading firms there may be a need to consider an uplift of the FOR capital requirement. <u>These firms would classify as Class 2 proprietary trading firms.</u> Such an uplift should serve to address potential

Question #	EBA Question	APT Responses
		market participant concerns and perceptions as regards the risks that could be caused by such larger proprietary trading firms. Such market participant concern would transmit to the supervisory authorities as well, which absent a suitable mandatory requirement applicable to the larger firms, would not be constrained to use all of the available discretionary powers (such as the powers set forth in article 104 CRD IV in the context of the Supervisory review and Evaluation process). APT-Members also have an interest in legal certainty as regards the capital requirements regime that applies to all of the types of the firms. For this reason, APT suggests that for any of the proprietary trading firm that exceeds a certain threshold an uplift of the FOR capital requirement would be an appropriate capital requirement regime for the larger firms. Such uplift capital requirement would then be aligned to the level of the charges to the proprietary trading firms for the exposures (which would be close to a tail risk number at the end of the distribution scale of unexpected losses) existing upon assignment of all trade positions to the clearing infrastructure occurring on a daily basis. This charge would be the comprehensive assessment of the entire range of risks that may be construed in theoretical models, including settlement risk, interest rate risk, operational risk, credit valuation adjustment risk and any other relevant risk areas. The relevant uplift numbers could be derived from the daily calculated aggregated margin numbers in the relationship between the proprietary trading firm and its clearing member. This is what is referred to by APT as the Risk Margin measure, which is quantified by applying the risk assessment models of the clearing member. An uplift of the FOR requirement for the larger proprietary trading firms would therefore result in the requirement to hold capital against the Risk Margin calculated on a daily basis. APT suggests that this uplift of the FOR requirement should apply to the larger firms being part of its member population. In order to establish a sufficiently objective and strong threshold number that is not subject to discretion or interpretation issues, APT proposes to use a threshold based on the FOR-numbers calculated in four quarters on an average basis in the relevant measurement year.

Question #	**EBA Question**	**APT Responses**
		The uplift factor in the form of the Risk Margin should apply to proprietary trading firms that may be considered to be perceived as being a significant participant to the markets. We expect that an appropriate threshold would lead to three to four of the current APT-Members to be subject to the uplift factor in the form of the Risk Margin measure. In order to avoid that in view of volatility swings in the financial markets, larger firms subject to the Risk Margin measure would at any time be undercapitalised depending on market circumstances, APT proposes to impose the objective capital floor of the FOR requirement as the safeguard against undercapitalisation. *Further details of the viewpoints of APT can be found in paragraph 4.3 and 4.4 of its Feedback and Responses Memorandum dated 1 February 2017.*
4	What are your views on the criteria discussed above for identifying 'Class 3' investment firms?	APT respectfully wishes to propose an alternative for the categorisation of Class 3 firms deviating from the proposals in the Discussion Paper that it believes are not suitable for proprietary trading firms. APT disagrees with the observation that investment firms that are conducting the investment activity of dealing on own account should be precluded from being categorised as a Class 3 firm as a general principle. APT proposes for the categorisation to become a Class 3 proprietary trading firms, to use an objective quantitative threshold to be developed in close discussion between the legislator and the industry. *Further details of the viewpoints of APT can be found in paragraph 6 of its Feedback and Responses Memorandum dated 1 February 2017.*
5	Do you have any comments on the approach focusing on risk to customers (RtC), risk to markets (RtM) and risk to firm (RtF)?	APT believes that neither the RtC nor the RtM as they have been analysed in the Discussion Paper are relevant to proprietary trading firms that are neither systemically important, nor systemic nor bank like. Particularly the fact that none of the RtC K-Factors are relevant for proprietary trading firms as they are organised in the way APT-Members are, would be the most important reason why the potential damages that a firm would incur in view of its business model or firm-specific characteristics, are not impacting third parties. Therefore, there is no direct or indirect risk that the rights, assets or position of third parties could be damaged or prejudiced if it turns out that a

Question #	**EBA Question**	**APT Responses**
		proprietary trading firm would be inadequately capitalised. This may only be different for the risk borne by the clearing member with whom proprietary trading firms have a dependent and important relationship. APT points out that proprietary trading firms are without exception organised as firms whose shareholders/owners are exclusively exposed to the risks borne by the firm. RtF is equal to the risk of its shareholders. There is no rationale whatsoever to be found, why prudential requirements should be imposed on firms whose shareholders are exclusively exposed to the firm's risks. The fact that shareholders are exclusively bearing the risks of the firm does not prevent the firm being subject to capital requirements. Effectively the capital requirements which apply to the firm will further constrain the shareholders' rights vis-à-vis the firm. This is related to the qualitative requirements applicable for the firm's capital to be held, also in the regime that APT proposes for its members. *Further details of the viewpoints of APT can be found in paragraph 3, 5 and 5 of its Feedback and Responses Memorandum dated 1 February 2017.*
6	What are your views on the initial K-factors identified? For example, should there be separate K-factors for client money and financial instruments belonging to clients? And should there be an RtM for securitisation risk-retentions? Do you have any suggestions for additional K-factors that can be both easily observable and risk sensitive?	APT has assessed that none of the following K-Factors for **the RtC risk category** are or may be relevant for APT-Members or for any proprietary trader having a similar business model exclusively focusing on dealing on own account and not having external customers: — Assets under management (AUM): none of the APT-Members manages customer portfolios or implements (whether or not discretionary) investment mandates for and on behalf of customers; — Assets under advice (AUA): APT-Members do not have external relations with customers and therefore never render investment advice; — Assets safeguarded and administered (ASA): APT-Members' business operations does not require safeguarding and administration of assets of third parties. For most APT-Members being holders of MiFID permits, safeguarding and administration activities within the meaning of MiFID Annex I Part B (1) is not in scope of their authorisation. Such firms would, consequently, even not be allowed to conduct assets safeguarding and administration activities;

Question #	EBA Question	APT Responses
		— Client money held (CMH): Under no circumstances will APT-Members have access to third parties' money (not in the form of own balance sheet liabilities or by means of access to asset segregation structures) and consequently this important K-Factor as outlined in paragraph 38(d) of the Discussion Paper does not apply for such businesses; — Liabilities to customers (LTC): APT-Members will not engage with customers to issue guarantees or indemnities to the benefit of such customers or any other arrangements (whether it be contractual, quasi-contractual or tort law type of relations) that would bring APT-Members into the position of being indebted to external customers. This K-Factor consequently does not apply for APT-Members' businesses; — Customer orders handled (COH): The trading activities of APT-Members does not involve or relate to, directly or indirectly, the processing of customer orders in whatsoever form. APT-Members have no responsibilities towards customers for the proper, timely and adequate processing of securities' orders or comparable transactions in other financial instruments. Any trading activity of APT-Members is for own account and always against their own proprietary capital. APT-Members also do not form part of a chain of intermediaries responsible for the processing of securities orders on behalf or for external customers. In this respect there is also no indirect exposure to external customers. With its comprehensive analysis as regards the **RtM K-Factor approach** as contained in the Discussion Paper, APT wishes to demonstrate that the proposed metrics and proxies to establish the K-Factor for this risk area are not fit for purpose. APT concludes as follows: — Absent evidentiary support to the need to establish a complete new risk category in the prudential supervision regime for investment firms, it should be generally concluded that it should be avoided to impose the RtM measure to proprietary firms; — Applying the assessment methodology of article 131 CRD IV for GSIIs and OSIIs and incorporating the EBA guidelines for application of the leverage ratio disclosure requirements for global systemically

Question #	EBA Question	APT Responses
		important firms and other large institutions, it can be concluded that, in view of size and importance (even if this is expressed in terms of the non-risk weighted balance sheets of all APT-Members) none of the APT-Members qualify as systemically important institutions or large institution, not on a domestic scale, not on a European scale and not on a global scale; — APT also respectfully rejects the analysis that size or importance of investment firms should be measured taking the commercial (IFRS) balance sheet as focus point. The economic balance sheet of proprietary trading firms, does not represent the actual accruals of legal obligations of firms that exclusively operate on regulated markets or otherwise submit their trades to central clearing. Eventually and in any event each time as per the close of a trading day, open positions are assigned via the clearing member to the central counterparty. Settlement risk is therefore reduced to zero for all categories of financial instruments, whether it be straightforward securities, exchange traded funds, derivatives or any other product in which the APT-Members trade; — Furthermore, and notwithstanding the zero score as regards the size or importance, if a proprietary firm would raise high scores on the scoring categories of interconnectedness or substitutability within the meaning of the GSII/OSII assessment methodology, such a firm could be considered to be “systemic” and in such case the proprietary trading firm should be made subject to the CRR/CRD IV prudential supervision regime. None of the APT-Members have high scores on either one of the scoring categories and therefore there is no need to analyse or address as to whether or not the risk of interconnectedness or cluster-risk could accrue in respect of proprietary trading firms towards other investment firms (where these firms are themselves proprietary trading firms or investment firms with customers); — From this analysis it follows, that if a proprietary trading firm is not to be categorised as systemically important, such a firm would also not be “systemic”. APT respectfully rejects the analysis of the Discussion Paper that there is a need or rationale to assess whether firms that are

Question #	EBA Question	APT Responses
		not systemically important, could nevertheless qualify as being "systemic"; — None of the APT-Members are performing "bank-like" activities, which APT interprets as the (high risk) combination of conducting investment activities (f.i. dealing on own account) with other investment services (f.i. brokerage, investment advice or portfolio management). Consequently, there is no risk of comingling of customer monies or financial instruments with those of the investment firm; — The number and frequency of trades is an inappropriate proxy for the establishment of K-Factors for the RtM risk area. The number and frequency of trades carried out by proprietary trading firms is carried out to prevent mispricing, and is driven by market circumstances, and is therefore most important in volatile markets as a risk mitigation tool in order to be able to provide liquidity under challenging circumstances. Penalising proprietary trading firms with capital requirements that are raised depending the number or frequency of transactions, would form a significant impediment for the fulfilment of the important roles as market makers and liquidity providers. Such roles require proprietary trading forms to perform transaction with high frequency and in large numbers of transactions. APT reiterates, however, that proprietary traders never act on an exclusive basis. APT cannot concur with the viewpoints included in the Discussion Paper as regards the need to impose **the uplift factor for RtF** to proprietary trading firms. Such firms are managed entirely at the risk of the owners/shareholders of the firm and there is no justification nor need to impose mandatory capital requirements for the RtF. In addition, APT believed that the RtF measure as it has been designed in the Discussion Paper, does not effectively address the actual risks borne by proprietary trading firms. Those risks are towards the clearing member that requires, as part of the clearing arrangements, proprietary trading firms to cover the Risk Margin with capital. Any other risks are transferred and/or mitigated through the operation of the clearing arrangements, in which positions are assigned to the clearing member and subsequently contributed to the central counterparty.

Question #	EBA Question	APT Responses
		Further details of the viewpoints of APT can be found in paragraphs 3, 4 and 5 of its Feedback and Responses Memorandum dated 1 February 2017.
7	Is the proposed risk to firm 'up-lift' measure an appropriate way to address the indirect impact of the exposure risk a firm poses to customers and markets? If not, what alternative approach to addressing risk to firm (RtF) would you suggest?	**First question:** APT points out that proprietary trading firms are without exception organised as firms whose shareholders/owners are exclusively exposed to the risks borne by the firm. RtF is equal to the risk of its shareholders. There is no rationale whatsoever to be found, why prudential requirements should be imposed on firms whose shareholders are exclusively exposed to the firm's risks. APT therefore recommends that the RtF uplift factor should not apply to proprietary trading firms. **Second question:** APT therefore does not propose an alternative for the RtF, but wishes to address capital requirements in line with the proposed approach as set forth in paragraph 79 of the Discussion Paper, in which a risk margin model is considered as al alternative way forward. *Further details of the viewpoints of APT can be found in paragraph 6 of its Feedback and Responses Memorandum dated 1 February 2017.*
8	What are your views on the 'built-in' approach to delivering simpler, proportionate capital requirements for Class 3 investment firms, (compared to having a separate regime for such firms)?	APT believes that the Categorisation of firms in Class 2 and Class 3 firms is a sensible approach. In its proposals in this feedback, APT suggests that for Class 3 firms FOR should serve as the capital adequacy floor. For larger firms an uplift is recommended in the form of a Risk Margin measure, where the FOR requirement would serve as absolute floor for those firms. *Further details of the viewpoints of APT can be found in paragraph 6 of its Feedback and Responses Memorandum dated 1 February 2017.*
9	Should a fixed overhead requirement (FOR) remain part of the capital regime? If so, how could it be improved?	Imposing FOR as a standard measure for Class 3 proprietary trading firms would be a suitable measure to address the unwinding costs of the firm in the event of a failure or exit from the markets. The FOR would in any event cover for all fixed overhead costs for a survival period of three months. APT believes that this period is sufficient to organise an orderly winding down of the firm and to settle any claims with the corporate creditors of the firms concerned. APT reiterates its viewpoint that a proprietary trading firm that is exiting, will have no exposures to external customers or counterparties in the financial

Question #	EBA Question	APT Responses
		markets after two to three days after the termination of activities as trader. In any event FOR serves to wind down the firm's corporate business operations and, to a certain limited extent, it will serve to settle any claims with the clearing member(s). APT therefore does not recommend any changes to the capital measure of FOR. *Further details of the viewpoints of APT can be found in paragraph 6 of its Feedback and Responses Memorandum dated 1 February 2017.*
10	What are your views on the appropriate capital requirements required for larger firms that trade financial instruments (including derivatives)?	APT acknowledges that for the larger proprietary trading firms there may be a need to consider an uplift of the FOR capital requirement. <u>These firms would classify as Class 2 proprietary trading firms.</u> Such an uplift should serve to address potential market participant concerns and perceptions as regards the risks that could be caused by such larger proprietary trading firms. Such market participant concern would transmit to the supervisory authorities as well, which absent a suitable mandatory requirement applicable to the larger firms, would not be constrained to use all of the available discretionary powers (such as the powers set forth in article 104 CRD IV in the context of the Supervisory review and Evaluation process). APT-Members also have an interest in legal certainty as regards the capital requirements regime that applies to all of the types of the firms. For this reason, APT suggests that for any of the proprietary trading firm that exceeds a certain threshold an uplift of the FOR capital requirement would be an appropriate capital requirement regime for the larger firms. Such uplift capital requirement would then be aligned to the level of the charges to the proprietary trading firms for the exposures (which would be close to a tail risk number at the end of the distribution scale of unexpected losses) existing upon assignment of all trade positions to the clearing infrastructure occurring on a daily basis. This charge would be the comprehensive assessment of the entire range of risks that may be construed in theoretical models, including settlement risk, interest rate risk, operational risk, credit valuation adjustment risk and any other relevant risk areas. The relevant uplift numbers could be derived from the daily calculated aggregated margin numbers in the relationship between the proprietary trading firm and its clearing member.

Question #	EBA Question	APT Responses
		This is what is referred to by APT as the Risk Margin measure, which is quantified by applying the risk assessment models of the clearing member. An uplift of the FOR requirement for the larger proprietary trading firms would therefore result in the requirement to hold capital against the Risk Margin calculated on a daily basis. APT suggests that this uplift of the FOR requirement should apply to the larger firms being part of its member population. The uplift factor in the form of the Risk Margin should apply to proprietary trading firms that may be considered to be perceived as being a significant participant to the markets. APT suggests that an objective threshold should be developed to differentiate between Class 2 and Class 3 proprietary trading firms in close consultation between the legislator and the industry. APT believes that when the appropriate metric would be applied that about three to four of the current APT-Members will be subject to the uplift factor in the form of the Risk Margin measure. *Further details of the viewpoints of APT can be found in paragraph 6 of its Feedback and Responses Memorandum dated 1 February 2017.*
11	Do you think the K-factor approach is appropriate for any investment firms that may be systemic but are not 'bank-like'?	If an investment firm that has significant trading activity, does not exceed the thresholds of the methodology of assessing whether firms are systemically important, such an investment firm should not be subject to specific and extraordinary prudential supervision rules. Such a firm is not systemically important and cannot (consequently) cause systemic risk. *Further details of the viewpoints of APT can be found in paragraph 4.3 and 4.4 of its Feedback and Responses Memorandum dated 1 February 2017.*
12	Does the definition of capital in the CRR appropriately cater for all the cases of investment firms that are not joint stock companies (such as partnerships, LLPs and sole-traders)?	APT concurs with the viewpoints included in points 88 to 90 of the Discussion Paper as to the qualitative requirements for capital to be held by investment firms. The applicable system for banks pursuant to the rules of CRR is not fit for purpose for the investment firm industry in view of complexity and misalignment of the purpose of capital to be held by such firms. *Further details of the viewpoints of APT can be found in paragraph 9 of its Feedback and Responses Memorandum dated 1 February 2017.*
13	Are the cases described above a real concern for the investment	APT does not have members that are organised in other legal form than limited liability companies

Question #	EBA Question	APT Responses
	firms? How can those aspects be addressed while properly safeguarding applicable objectives of the permanence principle?	(joint stock companies). The LLP or partnership model is not utilised in the recent history of the Dutch proprietary trading firm industry. APT therefore responds to this question that it does not believe it is relevant. *Further details of the viewpoints of APT can be found in paragraph 9 of its Feedback and Responses Memorandum dated 1 February 2017.*
14	What are your views on whether or not simplification in the range of items that qualify as regulatory capital and how the different 'tiers' of capital operate for investment firms would be appropriate? If so, how could this be achieved?	In balance, APT proposes a significant simplification of the qualitative capital requirements regime that should apply to proprietary traders and concurs with the viewpoints in the Discussion Paper that such a simplified regime would be appropriate for the industry. Most of the APT-Members apply the capital requirements by means of the raising of fully paid in ordinary capital from its shareholders and prudent policies as regards retained earnings distribution. Retained earnings reserves are in many instances utilised to support the further growth of the firm and serve as buffer for future expansion of the business. Shareholders waive in such cases their rights for full dividend distribution. APT does see the advantage of a second tier of capital that may qualify as regulatory capital in the form of medium term subordinated debt. Such "Tier 2" regulatory capital instrument should be properly aligned to the requirements of proprietary trading firms however. APT notes that regulatory capital requirements for proprietary trading firms should serve to support the orderly winding down of the firm applying a maximum horizon of three months. In view of the limited horizon where regulatory capital serves to wind down the firm's affairs and to liquidate the business operations, any provisions in the qualitative requirements for Tier 2 capital instruments, should take into account that restrictions on repayment of the principal amount borrowed upon the issue of the Tier 2 instrument should be sufficiently flexible to cater for a winding down of the Tier 2 instrument as well, simultaneously with the process of liquidating the firm. *Further details of the viewpoints of APT can be found in paragraph 9 of its Feedback and Responses Memorandum dated 1 February 2017.*

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15	In the context of deductions and prudential filters, in which areas is it possible to simplify the current CRR approach, whilst maintaining the same level of quality in the capital definition?	As regards the subject matter of prudential filters and deductions, APT briefly notes that particularly the deductions from capital for the holding in intangible assets do restrict the possibilities for starting firms that have capitalised the development costs of software and automated platforms. Therefore, as has been the case for comparable developments in the FinTech industry, the deduction form capital as a generic measure might create impediments for the market entry of newcomers. APT concurs that any prudential filters related to accounting values might not be relevant for the investment firm industry and in a revised prudential supervision regime, the abolishment of the larger majority of the prudential filters and deductions would contribute to the further simplification of the rules, without frustrating the general concepts of the risk sensitive approach. *Further details of the viewpoints of APT can be found in paragraph 9 of its Feedback and Responses Memorandum dated 1 February 2017.*
16	What are your views overall on the options for the best way forward for the definition and quality of capital for investment firms?	In balance, APT proposes a significant simplification of the qualitative capital requirements regime that should apply to proprietary traders and concurs with the viewpoints in the Discussion Paper that such a simplified regime would be appropriate for the industry. Most of the APT-Members apply the capital requirements by means of the raising of fully paid in ordinary capital from its shareholders and prudent policies as regards retained earnings distribution. Retained earnings reserves are in many instances utilised to support the further growth of the firm and serve as buffer for future expansion of the business. Shareholders waive in such cases their rights for full dividend distribution. APT does see the advantage of a second tier of capital that may qualify as regulatory capital in the form of medium term subordinated debt. Such “Tier 2” regulatory capital instrument should be properly aligned to the requirements of proprietary trading firms however. APT notes that regulatory capital requirements for proprietary trading firms should serve to support the orderly winding down of the firm applying a maximum horizon of three months. In view of the limited horizon where regulatory capital serves to wind down the firm’s affairs and

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		to liquidate the business operations, any provisions in the qualitative requirements for Tier 2 capital instruments, should take into account that restrictions on repayment of the principal amount borrowed upon the issue of the Tier 2 instrument should be sufficiently flexible to cater for a winding down of the Tier 2 instrument as well, simultaneously with the process of liquidating the firm. *Further details of the viewpoints of APT can be found in paragraph 9 of its Feedback and Responses Memorandum dated 1 February 2017.*
17	What are your views on the definition of initial capital and the potential for simplification? To what extent should the definition of initial capital be aligned with that of regulatory capital used for meeting capital requirements?	Minimum capital requirements could be abolished as in any event FOR capital requirements for proprietary trading firms will exceed any number that will be set for minimum capital requirements for investment firms, even if the legislator would consider to increase the 50,000-125,000-730,000 euro numbers to take inflation into account. For market entrants an upfront FOR requirement would be a sufficient high threshold to avoid the market entrance by firms insufficiently capitalised. A firm that wishes to enter the market, will be subject to severe scrutiny by the supervisory authorities in the license application process in any event. Such firms are likely to be required to properly budget costs and forecast the financial condition of the firm as a requirement to obtain the license. In line with this process it will not be too burdensome to calculate upfront a FOR for such a firm which will also serve as the “entrance” capitalisation level. *Further details of the viewpoints of APT can be found in paragraph 9 of its Feedback and Responses Memorandum dated 1 February 2017.*
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?	Minimum capital requirements could be abolished as in any event FOR capital requirements for proprietary trading firms will exceed any number that will be set for minimum capital requirements for investment firms, even if the legislator would consider to increase the 50,000-125,000-730,000 euro numbers to take inflation into account. For market entrants an upfront FOR requirement would be a sufficient high threshold to avoid the market entrance by firms insufficiently capitalised. A firm that wishes to enter the market, will be subject to severe scrutiny by the supervisory authorities in the license application process in any event. Such firms are likely to be

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		required to properly budget costs and forecast the financial condition of the firm as a requirement to obtain the license. In line with this process it will not be too burdensome to calculate upfront a FOR for such a firm which will also serve as the "entrance" capitalisation level. *Further details of the viewpoints of APT can be found in paragraph 4.3 and 4.4 of its Feedback and Responses Memorandum dated 1 February 2017.*
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?	In balance, APT proposes a significant simplification of the qualitative capital requirements regime that should apply to proprietary traders and concurs with the viewpoints in the Discussion Paper that such a simplified regime would be appropriate for the industry. Most of the APT-Members apply the capital requirements by means of the raising of fully paid in ordinary capital from its shareholders and prudent policies as regards retained earnings distribution. Retained earnings reserves are in many instances utilised to support the further growth of the firm and serve as buffer for future expansion of the business. Shareholders waive in such cases their rights for full dividend distribution. APT does see the advantage of a second tier of capital that may qualify as regulatory capital in the form of medium term subordinated debt. Such "Tier 2" regulatory capital instrument should be properly aligned to the requirements of proprietary trading firms however. APT notes that regulatory capital requirements for proprietary trading firms should serve to support the orderly winding down of the firm applying a maximum horizon of three months. In view of the limited horizon where regulatory capital serves to wind down the firm's affairs and to liquidate the business operations, any provisions in the qualitative requirements for Tier 2 capital instruments, should take into account that restrictions on repayment of the principal amount borrowed upon the issue of the Tier 2 instrument should be sufficiently flexible to cater for a winding down of the Tier 2 instrument as well, simultaneously with the process of liquidating the firm. *Further details of the viewpoints of APT can be found in paragraph 9 of its Feedback and Responses Memorandum dated 1 February 2017.*

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20	Do you see any common stress scenario for liquidity as necessary for investment firms? If so, how could that stress be defined?	APT respectfully points out that in the current supervisory practice most (if not all) investment firms (no matter which business they conduct) are excepted from the liquidity supervision requirements as set forth in Part 6 CRR. The supervisory authorities have widely applied their discretion to exempt the investment firm sector from being subject to liquidity requirements. In this context, APT respectfully challenges that there is a convincing and evidentiary supported case to introduce a liquidity supervision scheme for investment firms. In addition, it should be noted that the risk management model applied by clearing member firms in respect of their clients, already incorporates a stress tested liquidity and concentration risk factor in the charges of capital and requirements to post high quality liquid assets as collateral by proprietary trading firms. For example, illiquid positions held in the trading book are made subject to stricter stress tests and more severe shocks and accounted for in the Risk Margin charged to the proprietary trading firm. Introducing a supplemental regime to manage liquidity risk for proprietary trading firms utilising the Risk Margin model would result in double counting of liquidity measures and should be avoided. *Further details of the viewpoints of APT can be found in paragraph 7 of its Feedback and Responses Memorandum dated 1 February 2017.*
21	What is your view on whether holding an amount of liquid assets set by reference to a percentage of the amount of obligations reflected in regulatory capital requirements such as the FOR would provide an appropriate basis and floor for liquidity requirements for 'non-systemic' investment firms? More specifically, could you provide any evidence or counter-examples where holding an amount of liquid assets equivalent to a percentage of the FOR may not provide an appropriate basis for a liquidity regime for very small and 'non-interconnected' investment firms?	Introducing a supplemental regime to manage liquidity risk for proprietary trading firms utilising the Risk Margin model would result in double counting of liquidity measures and should be avoided. If a liquidity supervision scheme is to be introduced, APT would be in favour of keeping such regime very simple. In this respect the minimum liquidity standard for investment firms should be in the form of a simple metric, for instance by imposing the requirement that a significant percentage of the capital requirement applicable to the firm is to be held in the form of liquid assets. *Further details of the viewpoints of APT can be found in paragraph 7 of its Feedback and Responses Memorandum dated 1 February 2017.*

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22	What types of items do you think should count as liquid assets to meet any regulatory liquidity requirements, and why? (Please refer to Annex 4 for some considerations in determining what may be a liquid asset).	The requirements for the assets to be maintained to fulfil the liquidity requirement should be kept simple as well. APT suggests to adapt the eligibility criteria to the standards set forth in the DR Risk Management OTC Derivatives for eligible collateral for Initial Margin and Variation Margin. *Further details of the viewpoints of APT can be found in paragraph 7 of its Feedback and Responses Memorandum dated 1 February 2017.*
23	Could you provide your views on the need to support a minimum liquidity standard for investment firms with the ability for competent authorities to apply "supplementary" qualitative requirements to individual firms, where justified by the risk of the firm's business?	Introducing a supplemental regime to manage liquidity risk for proprietary trading firms utilising the Risk Margin model would result in double counting of liquidity measures and should be avoided. *Further details of the viewpoints of APT can be found in paragraph 7 of its Feedback and Responses Memorandum dated 1 February 2017.*
24	Do you have any comment on the need for additional operational requirements for liquidity risk management, which would be applied according to the individual nature, scale and complexity of the investment firm's business?	Introducing a supplemental regime to manage liquidity risk for proprietary trading firms utilising the Risk Margin model would result in double counting of liquidity measures and should be avoided. *Further details of the viewpoints of APT can be found in paragraph 7 of its Feedback and Responses Memorandum dated 1 February 2017.*
25	What are your views on the relevance of large exposures risk to investment firms? Do you consider that a basic reporting scheme for identifying concentration risk would be appropriate for some investment firms, including Class 3 firms?	APT notes that the risk management model applied by clearing member firms in respect of their clients, already incorporates a stress tested liquidity and concentration risk factor in the charges of capital and requirements to post high quality liquid assets as collateral by proprietary trading firms. For example, illiquid positions held in the trading book are made subject to stricter stress tests and more severe shocks and accounted for in the Risk Margin charged to the proprietary trading firm. Therefore, APT does not recommend that there is a rationale to impose additional rules to address concentration risk for proprietary trading firms. *Further details of the viewpoints of APT can be found in paragraph 6 of its Feedback and Responses Memorandum dated 1 February 2017.*
26	What are your views on the proposed approach to addressing group risk within investment firm-only groups? Do you have any other suggested treatments	APT acknowledges the need and rationale to include a chapter on supervision on consolidated basis in the future prudential supervision regime for investment firms. Such a regime should particularly enable supervisory authorities to

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	that could be applied, and if so, why?	identify any intragroup positions and intragroup transactions that may undermine or dilute the quality of the capital to be held by regulated investment firms subject to supervision of the European supervisory authorities. Any such intragroup positions and intragroup transactions affecting the quality of the regulatory capital base of regulated investment firms, should result in appropriate deduction and/or impairment rules and similar measures to enhance the quality of the regulatory capital base of the investment firms concerned. APT does not support any rules on supervision on consolidated basis that would introduce regulatory capital requirements on a solo basis for unregulated firms. The principle to restrict capital requirements to regulated firms only also applies for the consolidated supervision regime for credit institutions (banks) and the supplementary supervision regime for insurance groups. There is no convincing reason to introduce rules for groups of investment firms that would deviate from general principles of group supervision as adopted in Europe. Unregulated subsidiaries in the group of which an investment firm forms part, should neither be exposed to regulatory capital requirements on a solo basis nor should these requirements be created indirectly and at the level of the parent company on a consolidated basis. Unregulated subsidiaries' values should be accounted for in the consolidated financial statements of the (European) parent, applying ordinary valuation principles and applying ordinary accounting principles (IFRS or local GAAP applicable to the parent company). Constraints imposed on unregulated subsidiaries in the group of which one or more investment firms form part, should be restricted to the deduction and/or impairment for the purposes of regulatory consolidation of financial indebtedness relations or cross-capital holdings among the group members. These rules should support the avoidance of double gearing of regulatory capital and dilution of the quality of the capital of regulated investment firms in the group. Such rules should be without prejudice to the ability and permissibility of the inclusion (and therefore non-impairment) of certain intragroup debt or equity positions and values for ordinary accounting purposes if permitted under the IFRS or local-GAAP frameworks.

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		Any rules on consolidated supervision requiring regulated firms to hold regulatory capital levels should be restricted to firms established in the EEA. In this respect, APT is in favour of the territorial scope of application of the mitigated consolidated supervision regime for groups of investment firms as laid out in article 15 CRR. APT therefore suggests that this territorial restriction to EEA-investment firms as this is prevailing in the article 15 CRR provision, is to be confirmed in the new prudential supervision regime as well. *Further details of the viewpoints of APT can be found in paragraph 8 of its Feedback and Responses Memorandum dated 1 February 2017.*
27	In the case of an investment firm which is a subsidiary of a banking consolidation group, do you see any difficulty in the implementation of the proposed capital requirements on an individual firm basis? If so, do you have any suggestion on how to address any such difficulties?	APT does not see impediments to combine solo capital requirements imposed on proprietary traders with the consolidated supervision rules for heterogeneous groups. APT notes, however, that none of the proprietary traders which are its members, form part of a banking group. *Further details of the viewpoints of APT can be found in paragraph 8 of its Feedback and Responses Memorandum dated 1 February 2017.*
28	What other aspects should the competent authorities take into account when addressing the additional prudential measures on an individual firm basis under the prudential regime for investment firms?	In 2013 CRR/CRD IV amalgamated the Capital Adequacy Directive of 2006 setting forth market risk rules for banks and investment firms with the provisions of the Capital Requirements Directive of 2006 containing the banking credit and operational risk rules. As result of this process, significant out of scope, incompatibilities with business models, disproportional effects and improper alignment of the rules for investment firms occurred in supervisory practice. There is, therefore, a convincing case that the broader group of European investment firms will be made subject to an own prudential supervision regime. EBA's Discussion Paper proposes such separate prudential supervision regime for investment firms. APT agrees with the viewpoints of EBA as regards the alignment of risk factors to the typical business models of investment firms who operate in a different way as opposed to banks. In this manner incompatibilities of the current CRR/CRD IV regime with such business models will be removed and the risk sensitivity of the prudential supervision regime will be improved. EBA's proposals in the Discussion Paper require to address a very broad population of investment firms active in all the EU-Member States having very different business models and propositions to the markets and customers. Although APT has

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		not analysed the applicability of the proposed risk factors for other types of businesses in a detailed way, it appears that, in balance, the proposed bespoke regime seems to adequately address the requirements for prudential supervision of investment firms. None of the APT-Members have or build up exposures with external customers. Proprietary trading firms do not have access to client funds or assets, nor may these firms utilise customer funds or assets for their own trading business (for instance there is no securities lending business). Therefore, there is a strong case to consider capital requirements' objectives to only focus on the orderly winding down of the proprietary trading firm. In the event a proprietary trading firm (suddenly) exits the market and terminates its operations, the only stakeholders affected by such event would be the corporate stakeholders of the firm. *Further details of the viewpoints of APT can be found in paragraph 4.3 and 4.4 of its Feedback and Responses Memorandum dated 1 February 2017.*
29	What examples do you have of any excessive burden for investment firms arising from the current regulatory reporting regime?	One example that poses an excessive burden concerns the format and composition of the prudential reporting (COREP) for investment firms. Most templates for such reporting are designed for banks and banking groups and a very significant part of such templates are inappropriately addressing the business (models) of investment firms generally, and proprietary trading firms specifically. The workload concerned with completing these COREP supervisory reporting is considerable and would be reduced if solvency supervisory reporting could be made based on tailored templates. *Further details of the viewpoints of APT can be found in its Feedback and Responses Memorandum dated 1 February 2017.*
30	What are your views on the need for any other prudential tools as part of the new prudential regime for investment firms? And if required, how could they be made more appropriate? In particular, is there a need for requirements on public disclosure of prudential information? And what about recovery and resolution?	In 2013 CRR/CRD IV amalgamated the Capital Adequacy Directive of 2006 setting forth market risk rules for banks and investment firms with the provisions of the Capital Requirements Directive of 2006 containing the banking credit and operational risk rules. As result of this process, significant out of scope, incompatibilities with business models, disproportional effects and improper alignment of the rules for investment firms occurred in supervisory practice. There is, therefore, a convincing case that the broader

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		group of European investment firms will be made subject to an own prudential supervision regime. EBA's Discussion Paper proposes such separate prudential supervision regime for investment firms. APT agrees with the viewpoints of EBA as regards the alignment of risk factors to the typical business models of investment firms who operate in a different way as opposed to banks. In this manner incompatibilities of the current CRR/CRD IV regime with such business models will be removed and the risk sensitivity of the prudential supervision regime will be improved. EBA's proposals in the Discussion Paper require to address a very broad population of investment firms active in all the EU-Member States having very different business models and propositions to the markets and customers. Although APT has not analysed the applicability of the proposed risk factors for other types of businesses in a detailed way, it appears that, in balance, the proposed bespoke regime seems to adequately address the requirements for prudential supervision of investment firms. None of the APT-Members have or build up exposures with external customers. Proprietary trading firms do not have access to client funds or assets, nor may these firms utilise customer funds or assets for their own trading business (for instance there is no securities lending business). Therefore, there is a strong case to consider capital requirements' objectives to only focus on the orderly winding down of the proprietary trading firm. In the event a proprietary trading firm (suddenly) exits the market and terminates its operations, the only stakeholders affected by such event would be the corporate stakeholders of the firm. APT does not concur that there is a convincing need to introduce a separate and bespoke recovery and resolution regime for proprietary trading firms, in view of the very limited relevance of such a regime in the event a proprietary exits the markets or fails. As has been established in more detail in its Feedback and Responses Memorandum dated 1 February 2017, APT takes the position that an exiting or failing proprietary trading firm should and can be dissolved in a very short time period, without damages to external stakeholders. In such an event, positions of the firm will be wound down in a number of days as a result of the running clearing and settlement processes. Such positions are furthermore fully secured by a guarantee of the clearing member.

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		In turn, the clearing member or clearing members would have an appropriate coverage for the risks it or they run on the exiting or failing proprietary trading firm. Clearing member(s) are not exposed in such circumstances to risks that may impact their own business. The exiting or failing proprietary trading firm will be resolved and only claims from its corporate stakeholders will need to be settled. APT does not believe that there is a rationale for a prudential supervision regime to address recovery or resolution.
31	What are your views on the relevance of CRD governance requirements to investment firms, and what evidence do you have to support this?	None of the APT-Members have or build up exposures with external customers. Proprietary trading firms do not have access to client funds or assets, nor may these firms utilise customer funds or assets for their own trading business (for instance there is no securities lending business). Therefore, there is a strong case to consider capital requirements' objectives to only focus on the orderly winding down of the proprietary trading firm. In the event a proprietary trading firm (suddenly) exits the market and terminates its operations, the only stakeholders affected by such event would be the corporate stakeholders of the firm. With a view on this perspective, no reasons or rationale exists to introduce specific governance arrangements akin to the CRD IV banking governance chapter to proprietary trading firms. *Further details of the viewpoints of APT can be found in its Feedback and Responses Memorandum dated 1 February 2017.*
32	As regards 'systemic and bank-like' investment firms, do you envisage any challenges arising from the full application of the CRD/CRR remuneration requirements, and if so, what evidence do you have to support this? For all other investment firms, what are your views on the type of remuneration requirements that should be applied to them, given their risk profiles, business models and pay structures?	Non-systemically important investment firms that are not (potential) perpetrators of systemic risk should not be subject to specific prudential supervision rules. There is no convincing rationale to introduce specific remuneration rules for investment firms that are not to be considered systemically important. *Further details of the viewpoints of APT can be found in paragraph 10 of its Feedback and Responses Memorandum dated 1 February 2017.*
33	What is your view on a prudential remuneration framework for other than 'systemic and bank-like' investment firms that should	APT recommends that if remuneration rules are to be introduced for investment firms in the new prudential supervision regime, similar carve outs and proportional application as currently exists

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	mainly aim to counteract against conduct related operational risks and would aim at the protection of consumers?	under the currently applicable rules should be continue to apply in the future. To reiterate the position of APT in this respect the following main principles should form part of the new regime on remuneration as regards proprietary trading firms: — Setting the limitation on levels of variable remuneration should be left at the discretion of the proprietary trading firms and no mandatory statutory law limits should apply. This measure allows proprietary firms to expose their employees and contractors trading on the markets to the full effects of risk management and subject such individuals fully to the upside but also downside of the business of the firm, co-sharing risks as if the individuals are shareholders; — Retention and vesting rules regarding variable remuneration should allow for implementing of vesting schemes and distribution schemes with shorter time horizons and intervals, permitting sufficient flexibility in the recruiting and employee redundancy schemes of proprietary trading firms whilst fully accommodating claw back arrangements for underperforming individuals; — Profit distribution and retention rules regarding variable remuneration should be aligned to the time horizon of the necessary survival period of proprietary trading firms, being a briefer period to enable the orderly winding down of the firm with no need to resurrect or recover the business to serve the interests of external stakeholders. Therefore, there is in any event no convincing reason to include Pillar2-capital requirements into the calculation of maximum distributable reserves for proprietary trading firms. *Further details of the viewpoints of APT can be found in paragraph 10 of its Feedback and Responses Memorandum dated 1 February 2017.*
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,	In 2013 CRR/CRD IV amalgamated the Capital Adequacy Directive of 2006 setting forth market risk rules for banks and investment firms with the provisions of the Capital Requirements Directive of 2006 containing the banking credit and operational risk rules. As result of this process, significant out of scope, incompatibilities with business models, disproportional effects and improper alignment of the rules for investment

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	would be better suited under a simplified CRR regime?	firms occurred in supervisory practice. There is, therefore, a convincing case that the broader group of European investment firms will be made subject to an own prudential supervision regime. *Further details of the viewpoints of APT can be found in its Feedback and Responses Memorandum dated 1 February 2017.*
35	What are the main problems from an investment firm perspective with the current regime? Please list the main problems with the current regime.	*Further details of the viewpoints of APT can be found in its Feedback and Responses Memorandum dated 1 February 2017.*

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