**Response to:**

**EBA/DP/2016/02: EBA Discussion Paper - Designing a new prudential regime for investment firms**

**Respondent details**

**Company:** TD Direct Investing (Europe) Limited

**Name:** Ben Bright

**Position:** Regulatory Affairs Manager

**Address:** Compliance Department, TD Direct Investing, Exchange Court, Duncombe Street, Leeds, LS1 4AX, United Kingdom

**Telephone:** 0113-346-2959

**Email:** [ben\_bright@tdwh.co.uk](mailto:ben_bright@tdwh.co.uk)

**Response capacity:** Representative of an authorised firm.

**Response**

TD Direct Investing (Europe) Limited (‘TDDI’) welcomes the opportunity to respond to the EBA’s consultation.

By way of background, TDDI provides (B2C) services directly to approximately 280,000 retail customers with over £13 billion in custody assets under administration.

TDDI provides clients share dealing and investment services through its website, mobile applications or over the phone in a broad range of products available for trading and investing, specifically:

* UK and International Equities (with direct access to 17 markets including North America, Europe, Asia and Australia - 15 of which are available online);
* Funds (Unit Trusts and OEICs);
* Bonds and Gilts;
* Investment Trusts;
* Initial Public Offerings (IPOs)
* Exchange Traded Products (ETPs) and Real Estate Investment Trusts (REITs);
* Trading Accounts comprising certificated and nominee services;
* Cash management;
* ‘Tax Efficient Wrappers’ comprising stocks and shares ISAs and JISAs and SIPPs (provided by AJ Bell as the pension administrator).

TDDI’s business is wholly retail and predominantly web-based, with over 97% of trading being undertaken online. The bulk of TDDI’s trading and client assets held are equity related, linked to its history as an execution-only stockbroker. Funds and ETFs are growing areas of customer activity.

**Answers to specific questions**

**Question 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?**

We recognise that large ‘systemic and bank-like’ investment firms may need to be subject to a separate regime more akin to the existing CRD. We have no further comment on this matter.

**Question 2. What are your views on the principles for the proposed prudential regime for investment firms?**

Broadly-speaking, we support the principles for the proposed prudential regime for investment firms.

**Question 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?**

We do not consider that we would be treated as a Class 3 firm, therefore we have no comment on this issue.

**Question 4.What are your views on the criteria discussed above for identifying ‘Class 3’ investment firms?**

**For the above question, it would be useful to receive detailed comments on each of the following items, which would preclude an investment firm from being in ‘Class 3’:**

**a) holding client money or securities,**

**b) ancillary service of safekeeping and administration (B1),**

**c) dealing on own account (A3),**

**d) underwriting or placing with a firm commitment (A6),**

**e) the granting of credits or loans to an investor (B2),**

**f) operating a multilateral trading facility (or MTF) (A8),**

**g) the MiFID II activity of operating an organised trading facility (or OTF),**

**h) being member of a wider group,**

**i) using a MiFID passport, and**

**j) using tied agents.**

We do not consider that we would be treated as a Class 3 firm, therefore we have no comment on this issue.

**Question 5.Do you have any comments on the approach focusing on risk to customers (RtC), risk to markets (RtM) and risk to firm (RtF)?**

Broadly-speaking, we support the proposed approach, however, in relation to the application of a scalars to the K-factors, we would question EBA’s proposal that size can equitably be used as a proxy for measuring the risk of harm an investment firm can cause to others.

As EBA itself identifies in Paragraph 31, ‘the harm an investment firm might cause to others may, in general, be expected to arise from some combination of the “size, internal organisation, nature, scope and complexity” of its business’.

It therefore follows that, simply because Firm A is, say, five times the size of Firm B, when measured by the amount of, for example, assets under administration, this does not necessarily equate to Firm A being five times more ‘risky’ than Firm B. However, if the regime incorporates the application of a strict linear scalar to the K-factors, this would not appear to reflect anything other than the size of the business.

We therefore consider that the application of the scalars should be flexible enough to reflect the other factors that the EBA has itself identified, namely: internal organisation, nature, scope and complexity of the business.

If a firm can demonstrate sound risk mitigation in relation to, for example, the assets it has under administration, this should be reflected in the scalar that is applied.

In order to enable this flexibility to be built into the regime, we would encourage EBA and ESMA publish, on an ongoing basis, ‘Level 3’ guidance on the appropriate application of the K-factor scalars.

**Question 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?**

We believe there should be separate K-factors for client money and financial instruments belonging to clients. The risk of holding client money and securities differ and the amount of client money held is not reasonable proxy for the value of securities held by clients.

**Question 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?**

We are supportive of the approach outlined in the DP.

**Question 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)?**

We do not consider that we would be treated as a Class 3 firm, therefore we have no comment on this issue.

**Question 9.Should a fixed overhead requirement (FOR) remain part of the capital regime? If so, how could it be improved?**

A fixed overhead requirement has been a feature of the UK regulatory regime for many years albeit that the cost definitions have changed from time to time. We would like clarity as to how the fixed overhead requirement should be calculated at individual cost component level and the criteria that should be applied to determine whether or not a cost is ‘fixed’.

**Question 10. What are your views on the appropriate capital requirements required for larger firms that trade financial instruments (including derivatives)?**

We have no comment – this is not applicable to our firm.

**Question 11. Do you think the K-factor approach is appropriate for any investment firms that may be systemic but are not ‘bank-like’?**

We have no comment – this is not applicable to our firm.

**Question 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)?**

We have no comment on this issue.

**Question 13. Are the cases described above a real concern for the investment firms? How can those aspects be addressed while properly safeguarding applicable objectives of the permanence principle?**

We have no comment on this issue.

**Question 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?**

We have no comment on this issue.

**Question 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?**

We have no comment on this issue.

**Question 16. What are your views overall on the options for the best way forward for the definition and quality of capital for investment firms?**

We strongly support the second option to introduce new standards on what is regulatory capital specifically for investment firms; simplifying the area of definition and quality of capital consistent with a new framework for determining regulatory capital.

**Question 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?**

We agree with the statement in the DP that an on-going obligation is retained and clarified as such, so that the minimum level(s) for authorisation in effect act as a further ’floor’ to the minimum level of capital an investment firm must continue to hold in order to keep its authorisation to conduct MiFID investment services. We support the recommendation that the definition of capital used for the purposes of meeting the minimum level(s) required as a condition for (on-going) authorisation of an investment firm under MiFID should also be aligned with whatever definition of capital (i.e. own funds) is decided to be used for the purposes of meeting the capital adequacy requirements of investment firms.

**Question 18.What aspects should be taken into account when requiring different levels of initial capital for different firms? Is there any undesirable consequence or incentive that should be considered?**

We believe the current arrangements whereby the initial capital is set by reference to the activities to be undertaken by the investment firm should continue.

**Question 19. What are your views on whether there is a need to have a separate concept of eligible capital, or whether there is potential for simplification through aligning this concept with the definition of regulatory capital used for meeting capital requirements?**

We would support the concept of eligible capital should being aligned, such that there is only one, single, definition of regulatory capital (i.e. own funds) to work with for investment firms, for whatever prudential purpose.

**Question 20. Do you see any common stress scenario for liquidity as necessary for investment firms? If so, how could that stress be defined?**

We have no comment on this issue.

**Question 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?**

We would support a 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.

**Question 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).**

We have no comment on this issue.

**Question 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?**

We have no comment on this issue.

**Question 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?**

We would counter against adding layers of complexity in the rules governing liquidity risk management. Issues around operational requirements should rest with the NCA and be addressed as part of the supervisory engagement with the individual firm.

**Question 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?**

We have no comment on this issue.

**Question 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 that could be applied, and if so, why?**

We are supportive of the approach illustrated in Figure 6 of the DP.

**Question 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?**

We have no comment on this issue.

**Question 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?**

We would encourage the development of a simpler, more streamlined supervisory review processes for NCAs that is part of a wider discussion about the activities of the firm as a whole and is less focussed on technical minutia.

**Question 29. What examples do you have of any excessive burden for investment firms arising from the current regulatory reporting regime?**

We would draw your attention the UK Wealth Management Association (‘WMA’) response to this question:

Firms have had to incur costs in acquiring systems to meet COREP requirements and have to pay ongoing maintenance costs. The reporting requirements are exceedingly complex and the reporting requirements focus upon the needs of major banks. In most cases investment firms are only completing a very few number of data fields. The complex nature of the reporting requirements means that many small and medium investment firms have to seek ongoing external advice to ensure they meet their obligations. The data reported is meaningless for most investment firms and does not reflect the typical management information maintained by investment firms. We believe the data is of limited use to NCAs.

Consequently, we would favour a significantly simplified and more relevant reporting regime.

**Question 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?**

We have no comment on this issue.

**Question 31.What are your views on the relevance of CRD governance requirements to investment firms, and what evidence do you have to support this?**

Our view is that the MIFID governance and remuneration requirements are sufficient.

**Question 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?**

We have no comment on this issue.

**Question 33.What is your view on a prudential remuneration framework for other than ‘systemic and bank-like’ investment firms that should mainly aim to counteract against conduct related operational risks and would aim at the protection of consumers?**

Our view is that the existing MIFID remuneration requirements are sufficient. In particular, the ‘material risk takers’ regime in CRD IV is materially disproportionate to the risk to the financial system presented by firms dealing in an agency capacity.

**Question 34.What are your views on having a separate prudential regime for investment firms? Alternatively, should the CRR be amended instead to take into account a higher degree of proportionality? Which type of investment firms, if any, apart from systemic and bank-like investment firms, would be better suited under a simplified CRR regime?**

In our view, a separate regime for investment firms reflecting their particular activities and not those of banks is very desirable.

Broadly-speaking, the proposals in the DP represent a good starting-point for the development of the regime.

We would strongly oppose a solution for investment firms that is based upon amendments to the existing CRD regime.

**Question 35.What are the main problems from an investment firm perspective with the current regime? Please list the main problems with the current regime.**

The principle problem with the current regime is that it has essentially been designed in response to the global banking crisis and its primary objective is to address the risks posed to the financial system by systemically significant and large, globally active, banks.

Consequently, investment firms with very simple business models find themselves having to expend a significant amount of energy (and therefore cost) firstly on assessing the extent to which the regime is applicable to them and secondly on establishing and maintaining the systems, controls and processes required to comply with a regime that is administratively disproportionate to the risk they pose to global markets.

In practice, most investment firms pose no material risk to the financial system, rather the key risk they pose is to consumer confidence, particularly in relation to misconduct in the areas of advice, sales and safeguarding of client assets and client money. The current prudential regime for investment firms is not adequately reflective of this reality.