THE
INVESTMENT
ASSOCIATION

Response to EBA consultation on prudential requirements for Investment Firms

EBA/CP/2020/07

About the Investment Association

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

Overview of questions for consultation

1. Are the instructions and templates clear to the respondents?

The calculation of own funds largely follows CRD IV, with a stricter definition of assets that must be deducted (through removal of allowable thresholds). As these are deemed not to be qualifying assets for meeting the requirements of the regime, we believe they should also not be considered in determining whether the thresholds are met. These deductions include intangible assets, deferred tax assets and material holdings.

Currently an investment firm that has a large deductible asset (e.g. Goodwill) must deduct this when considering available own funds and therefore must ensure that there are sufficient qualifying assets to ensure that the net assets are high enough to support the required available own funds. However, under the current proposal of definition of assets, the large goodwill balance could trigger the thresholds whilst also being fully deductible.

As an agency business, investment managers typically have large, offsetting, trade receivable (asset) and trade payable (liability) balances on the balance sheet. These are based on volumes of activity in and out of funds during the T+3 settlement period. These balances are subject to very large short term fluctuations in periods of high volume trades. However, they are not reflective of a significant increase in risk of harm to clients, markets or the firm. For the purposes of the definition of assets, closely aligned assets and liabilities should be permitted to be netted.

2. Is the level of detail on small and non-interconnected investment firms templates and instructions sufficient and proportionate for the level of activity of these firms?

It would be helpful if the EBA would confirm the process for returns that are not applicable. The IA would like to suggest filtering of templates to avoid the need for nil submissions. This could be achieved through a reporting platform that has the capability of filtering the

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returns available to firms based on permissions. This would involve a series of filtering questions on activities, size of firm, etc. that would then permit a firm to populate specific returns and not be permitted to populate returns not relevant to them. For example, a limited licence firm that does not trade on its own account, but is not small and non-interconnect, would not be able to populate any K-RtM/K-RtF templates or those related to small and non-interconnect firms.

3. Are the instructions and templates IF 05.00 and IF 05.01 clear to the respondents?

The IA would like the EBA to confirm that class 2 firms are not required to submit templates IF 10.01, 10.02 and 10.03 and are not required to submit template IF 05.00.

Article 54 (1)(d) of the IFR states that firms shall report on the level of activity in respect of the conditions set out in Article 12(1) for Small and non-interconnected investment firms. However, in the draft implementing technical standards paragraph 6 of the consultation paper, it states that "all investment firms regulated under IFR shall report a template to monitor their activity profile and size …. ".

Clarification is sought on whether firms that do not meet the conditions of small and non-interconnected, are required to submit this form which would result in an additional reporting burden to report threshold metrics that have no application.

Further reporting on thresholds is required in templates IF10.01, 10.02 &% 10.03. Explicit guidance on threshold reporting for class 2 firms would be beneficial and reduce confusion and the risk of incorrect reporting.

4. Do the respondents identify any discrepancies between templates IF 06.01 - IF 06.13 and instructions and the calculation of the requirements set out in the underlying regulation?

For the purpose of table 06.01 in the IF 06.00 template, can the supporting instructions be updated to clarify why data for the three most recent months is required given the IFR Art. 17 requirement to exclude the three most recent monthly values when calculating K-factors.

For the purpose of the IF 06.04 table in template IF 06.00, it is not clear what the rationale for requesting 8 months of data when the calculation only requires 6 months of data for calculating K- factors.

The requirement to include data in the reporting template which is not required in the K-factor calculation could cause confusion. The IA suggests the EBA clarify why data that is not going to be used in the K-factor calculation is requested. If this data is not required, then the templates should be updated to remove any information that is not required for the K-factor calculations.

It is the IA's understanding that the aim of the IFR is to reduce complexity in terms of reporting which we fully support. Article 54 of the IFR states that firms shall report on a quarterly basis, however template IF 06 on K-factor metrics requires monthly data including current monthly metrics that are not used to calculate the average value for the K-factor.

We would question the rationale behind the request for additional underlying information from respondents and whether this is in line with the proportionate nature of the new regime.

5. Do the respondents identify any discrepancies between templates IF 07.00 – IF 08.00 and instructions and the calculation of the requirements set out in the underlying regulation?

The IA would like confirmation that a nil submission is not required for an investment firm with no trading book exposures.

In IF08.00 firms must report concentration risk of 'groups of connected counterparties'. There is no specific reference to the definition of 'connected clients' and clarification on whether the use of CRR 575/2013 article 4 (39) "group of connected clients" is appropriate would be beneficial to respondents.

6. Are the instructions and templates clear to the respondents?

No material comments.

7. Are the instructions and templates (IF 11.01, 11.02, 11.03) clear to the respondents?

The regulations appear to require reporting by each regulated entity, as well as reporting on a consolidated basis. It is not fully clear if there are reports and disclosures which are only required on a consolidated basis. The option to report on a group-wide basis would reduce the amount of reporting required under the regulations, whilst still providing supervisors with an appropriate level of oversight of the risks the group pose to their objectives. The IA requests the EBA clarified the level of application (individual / consolidated) for the various reports / disclosures required under IFR in order to reduce unnecessary submissions.

It is our understanding that this form would only be submitted upon authorisation from the competent authority of a derogation from consolidated reporting under IFR Article 8. We would request confirmation that this is to monitor compliance.

8. Do the respondents identify any discrepancies between the template and instructions and the requirements set out in the underlying regulation?

EU IF CC1 – Column E (ref b) is asking for sources based on the audited balance sheet. However, the majority of these items will not be disclosed within the balance sheet in the financial statements. The IA would like clarity that it is not mandatory for references to be completed against every line for which an amount exists on column D.

According to IFR Article 46 "Investment firms shall publicly disclose the information specified in this Part on the same date as they publish their annual financial statements." Clarification is sought as to whether, for investment firms that do not publish annual financial statements, this date can be the date annual accounts are submitted to a Government Agency such as Companies House in the UK or the National Competent Authority. This confirmation would provide clarity and reduce the risk of late disclosures.

9. Do the respondents identify any discrepancies between the template and instructions and the requirements set out in the underlying regulation?

It is stated at the top of EU IF CC2 that this is a flexible template and that "Columns shall be kept fixed, unless the investment firm has the same accounting and regulatory scope of consolidation, in which case the volumes have to be entered in column (a) only." It would be helpful to get more clarity on the definition of "accounting". For instance, "accounting" for the consolidation may only be prepared for regulatory purposes and thus is aligned with the regulatory scope by default. However, if accounting in this template refers to "statutory accounting" then there could be differences in items between solo (statutory financial statements) and consolidated positions (non-statutory financial statements prepared for regulatory purposes only).

10. Are the instructions and templates clear to the respondents?

The IA do not believe that the implementation of such a granular set of disclosure requirements under the Pillar 3 framework for relatively simple investment firm structures provide the user with additional value.

11. Is the ITS text clear to the respondents?

Clarification is required on the specific templates that firms are required to submit depending on whether they fall within class 2 or class 3. Explicit instructions for class 2 firms and class 3 firms would assist in understanding the individual reporting requirements.

12. Are the provisions of the RTS, the templates and instructions clear? In those cases where you identify issues, please provide concrete examples or detailed explanations to illustrate your doubt.

The IA understand that the monitoring of thresholds is done through forms IF10.01,2,3 and these are submitted by the parent entity and only required by relevant investment firms or parent entities where total assets (consolidated assets) of the firm /group exceed EUR5bn and do activities 3& 6.

We believe there is an inconsistency between available own funds and the determination of thresholds based on balance sheet assets. If full deductions for significant investments need to be made for own funds, the same methodology should apply when calculating threshold balance sheet size.

1. Draft ITS on reporting requirements for investment firms under Article 54(3) and on disclosures requirements under Article 49(2) of IFR

Resubmission
Art 3 (titled "Reporting remittance dates") requires that "where audited figures deviate from submitted unaudited figures, the revised, audited figures shall be submitted without undue delay". It is not clear if a resubmission will be required for every deviation or only for material deviation. The IA would request that the EBA state whether a resubmission would be required only for material deviations. Where this is the case, it would also be worth specifying whether the EBA would determine and define the word "material change" or can each firm through its policies and procedures define the level of materiality.

The IA suggest that the EBA consider the submission of any annual return be linked to the date that audited accounts are approved by its management body as this would likely address this issue.

Group applicability – individual vs. consolidated reporting and disclosures
The regulations appear to require reporting by each regulated entity, as well as reporting on a consolidated basis. It is not fully clear if there are reports and disclosures which are only required on a consolidated basis. The option to report on a group-wide basis would reduce the amount of reporting required under the regulations, whilst still providing supervisors with an appropriate level of oversight of the risks the group pose to their objectives. The IA requests the EBA clarified the level of application (individual / consolidated) for the various reports / disclosures required under IFR in order to reduce unnecessary submissions.

Publication date
IFR Article 46 states that 'Investment firms … shall publicly disclose the information specified in this Part on the same date as they publish their annual financial statements.' The IA propose that for entities where the accounts are not published (e.g. consolidating entity), firms use the date of submission of the annual accounts to Companies House (or equivalent) as the date by which they need to publish the disclosures required in IFR Part Six.

Completion of nil returns
Where a firm has concluded that any of the K-factors are not applicable, the IA suggests that a nil return submission would not be required. For example, if a firm concludes that they are not required to calculate K-CON, the firm should not need to submit a nil return for the IF 07.00 template.

The IA would like the EBA to confirm that class 2 firms are not required to submit templates IF 10.01, 10.02 and 10.03 and are not required to submit template IF 05.00.

It would be helpful if the EBA would confirm the process for returns that are not applicable. The IA would like to suggest filtering of templates to avoid the need for nil submissions.

Inconsistencies in data requests
For the purpose of table 06.01 in the IF 06.00 template, can the supporting instructions be updated to clarify why data for the three most recent months is required given the IFR Art.

17 requirement to exclude the three most recent monthly values when calculating K-factors.

For the purpose of the IF 06.04 table in template IF 06.00, it is not clear what the rationale for requesting 8 months of data when the calculation only requires 6 months of data for calculating K- factors.

The requirement to include data in the reporting template which is not required in the K-factor calculation could cause confusion. The IA suggests the EBA clarify why data for that is not going to be used in the K-factor calculation is requested. If this data is not required, then the templates should be updated to remove any information that is not required for the K-factor calculations.

Clarification between execution of client orders and reception and transmission of client orders

Calculating K-COH on cash trades will be at execution (point at which price is known). There may not be a specific methodology for capturing and calculating transmission of the order if this was subsequently cancelled (e.g. there is a mistake when processing the order). Without clarification of the methodology to be applied, there could be potential confusion over how to calculate client orders that are subsequently cancelled. It would be helpful if the EBA could clarify the distinction between execution of client orders and reception/transmission of orders.

Fixed Overhead Requirement template

There is potential confusion over the completion of the Fixed Overhead Requirement template. The IA propose that the EBA update the templates / instructions to address the following queries:

(1) For the purpose of the IF 03.00 template, what is the definition of 'Distribution of profits' to be used for row 0060 of the IF 03.00 template, and how is this distinct from the value to be reported on rows 0090 and 0100?
(2) For the purpose of IF 03.00, can explicit confirmation be provided that discretionary dividend payments should never be included in the Fixed Overhead Requirement calculation?
(3) Why do the instructions of the IF 03.00 template mandate that row 0060 (Distributions of profit) will be lower than 0050 (Total expenses before distribution of profits)?
(4) Why do the instructions of the IF 03.00 template require row 0030 to be the difference between rows 0050 and 0060, rather than the sum of those rows?

Other templates

EU IF CC1 – Column E (ref b) is asking for sources based on the audited balance sheet. However, the majority of these items will not be disclosed within the balance sheet in the financial statements. The IA would like clarity that it is not mandatory for references to be completed against every line for which an amount exists on column D.

It is stated at the top of EU IF CC2 that this is a flexible template and that “Columns shall be kept fixed, unless the investment firm has the same accounting and regulatory scope of consolidation, in which case the volumes have to be entered in column (a) only.” It would be helpful to get more clarity on the definition of “accounting”. For instance, “accounting” for the consolidation may only be prepared for regulatory purposes and thus is aligned with the regulatory scope by default. However, if accounting in this template refers to

“statutory accounting” then there could be differences in items between solo (statutory financial statements) and consolidated positions (non-statutory financial statements prepared for regulatory purposes only).

Feedback on IF 09.00 template and instructions:

- For row 0030 we think the list of cells which are to be aggregated to arrive at the total is incorrect and needs to be updated. We think it should be the sum of rows 0040, 0050, 0060, 0170, 0230, 0290 and 0300.
- For row 0170, the instructions say this should be the sum of rows 0170 to 0210. We think this should be 0180 – 0220.
- For row 0230, the instructions say this should be the sum of rows 0230 – 0270. We think this should be 0240 – 0280.

It is currently unclear between Article 21(1) and 21(4) of the IFR whether firms that do not trade on own account will be required to calculate K-NPR for FX positions. If it is clarified that this is required, these firms would need to submit a significant amount of null values for RtM to show just this requirement. If this is required, these firms should be exempted from the RtM returns and only show the requirement on IF 04.00

Annual reporting date

The ITS proposes the 11 Feb for submission of the Annual report. This is the same day as the quarterly submission. The annual report will therefore not likely be based on Audited financial statements. The annual position will be subject to material change post submission and may require a high volume of resubmissions. This means many firms will likely have to resubmit in accordance with Article 3(4). This in effect creates 2 sets of annual returns.

By having it the same day as the quarterly submission, it is unclear what additional value the report adds, as we believe the intention would be that the annual report should reflect the finalised approved accounts.

The quarterly reporting deadline for 31 December should allow the competent authority a timely unaudited position prior to the submission of the Annual report.

The IA propose that the annual report should be due on a set number of working days after the approval of the annual accounts by the management body of the firm rather than a set number of days after the reference date. This would ensure better consistency between the regulatory returns and the financial statements of the investment firm. By setting this based on a set number of days post the approval of the financial statements also allows the requirements to be more flexible to firms with year-end accounting dates other than the 31 December.

We believe that aligning the annual report with the accounting reference date of the firm will allow for greater challenge by the management body of the contents as it will allow for greater challenge and understanding of discrepancies if it is aligned with the accounting reference date, which the management body will already be challenging in line with their duties under local company law.

Disclosures – consolidation group

The IA would like the EBA to clarify whether investment firms that form part of an investment firm group need to disclose on a solo basis or whether they can rely on the

group disclosure. If so, could it be on a reduced scope (i.e. Quantitative components only) to reduce excessive duplication of describing the qualitative arrangements.

2. DRAFT RTS ON THE MONITORING OF INFORMATION RELATED TO THE THRESHOLDS FOR CREDIT INSTITUTIONS REPORTING REQUIREMENTS FOR INVESTMENT FIRMS UNDER POINT (5) OF ARTICLE 55 OF IFR

Definition of assets

The calculation of own funds largely follows CRD IV, with a stricter definition of assets that must be deducted (through removal of allowable thresholds). As these are deemed not to be qualifying assets for meeting the requirements of the regime, we believe they should also not be considered in determining whether the thresholds are met. These deductions include intangible assets, deferred tax assets and material holdings.

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