FIA EPTA response to EBA Discussion Paper : A new prudential regime for investment firms	
Question	**EPTA argumentation / response**
Section 4.2.1 - 'Systemic and bank-like' investment firms	
1. Are the criteria used to identify G-SIIs/O-SIIs appropriate for the identification of systemic and bank-like investment firms?	1. We support the three recommendations of the EBA's Opinion on the first part of the Call for Advice on investment firms [**EBA/Op/2016/16**]. 2. We believe that the five categories of Article 131(2) CRD IV remain appropriate for distinguishing systemically important investment firms that ought to remain subject to the provisions of CRD IV and CRR. However, we caution as to how the categories and the EBA Guidelines on the criteria to determine the conditions of application of Article 131(3) CRD IV in relation to the assessment of other systemically important institutions (**O-SIIs**) ("O-SII Guidelines") are applied to investment firms. The O-SII Guidelines include many optional indicators, of which few are pertinent to FIA EPTA members. Any new categorisation of investment firms should neither incentivise nor compel national competent authorities (**NCAs**) to change how they assess the systemic risks posed by investment firms under their supervision.
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?	3. FIA EPTA members do not generally underwrite financial instruments or place financial instruments on a firm commitment basis per Annex I Section A(6) of Directive 2004/39/EC on markets in financial instruments (**MiFID**). 4. We do not share the view that proprietary trading may or should be considered "bank-like". A substantial number of investment firms are authorised to deal on own account per MiFID Annex I Section A(3). The O-SII Guidelines do not refer to proprietary trading. Proprietary trading is not, and never has been, the preserve of credit institutions in the European Union or elsewhere. Indeed, CRD IV, CRR and national restrictions have compelled many credit institutions to reduce or cease proprietary trading. Collectively, the proprietary trading of market makers and liquidity providers undertaken by Principal Trading Firms (**PTFs**) is important for the overall quality of Europe's capital markets. This type of proprietary trading in Europe is highly-competitive and takes place in a non-exclusive, open market structure which is characterised by the high substitutability of actors, that are easy to resolve and that have low levels of interconnectedness due to central clearing and settlement arrangements.
What aspects in the identification of 'systemic and bank-like' investment firms could be improved?	N/A
Section 4.2.2 - Investment firms that are not 'systemic and bank-like'	
2. Views on the principles for the proposed prudential regime for investment firms?	1. We support Principle (a) insofar as we believe that a new prudential regime for non-systemic investment firms should not require minimum own funds and other requirements that may provide the same level of assurance as requirements for systemically important investment firms. However, and while we recognise that the EBA must be

	mindful of changes to the G-SII and O-SII categories, it should not confuse the scope of the proposed new prudential regime. 2. We are concerned that Principle (b)(i) may be interpreted as a "recovery requirement" (i.e. that an investment firm must hold sufficient own funds to recover from a significant loss or losses). We do not support such a requirement for non-systemic investment firms. We believe that regulatory capital requirements for non-systemic investment firms should be aimed at and calculated to ensure the orderly winding down of a failed investment firm. 3. We support Principles (b)(ii) and (iii). 4. We support Principles (c) and (e). However, we believe that any new prudential regime should not ignore conduct and market regulation, particularly MiFID, and the provisions of this regulation on *inter alia* organisational requirements for investment firms, investor protection, safeguarding of client assets and investor compensation schemes. Prudential regulation should complement conduct and market regulation. It should not seek to replicate or replace such regulation. 5. We support Principle (d) and encourage the EBA to emphasise the importance of harmonised requirements for Class 2 and 3 investment firms in the technical advice. We regret that Pillar II discretions far too often lead to divergent interpretations and are used by NCAs to layer additional own funds requirements upon investment firms. This results in inconsistent requirements across Member States and undermines the approximation of laws objective of legislation based on Article 114 of the Treaty on the Functioning of the European Union (**TFEU**). While NCAs should retain supervisory discretion, we believe that any new regulatory regime should preclude NCAs from adding own fund requirements for investment firms generally and should include new conditions that should be satisfied before NCAs can instruct a Class 2 investment firm to hold additional own funds requirements as part of any supervisory review and evaluation process. 6. We agree with the principle that investment firms that are exposed to more or greater risks should be subject to relatively higher regulatory capital requirements. However and specific to Principle (f), we do not believe that balance sheet and off-balance sheet exposures ought to be the basis for assessing the "riskiness" of positions as these measures ignore the highly-liquid nature of the financial instruments held by FIA EPTA members, the hedging of positions and/or off-setting positions, the clearing arrangements for transactions in these financial instruments, the margin applied by clearing firms and central counterparties (**CCPs**), and the low interconnectedness and high levels of competition between, and substitutability of, FIA EPTA members across markets.
Section 4.2.3 - Very small, non-interconnected investment firms	
3. Views on the identification and prudential treatment of very small and non-interconnected investment firms ('Class 3')?	1. We support the proposed classification of investment firms and consider, generally, that Class 3 investment firms ought to be subject to a simple minimum own funds requirement. We believe that categorisation should not be based on the permissions of an investment firm, its structure or where it is lawfully entitled to engage in investment activity or provide investment services within the EU and European Economic Area (**EEA**). We consider that quantitative thresholds are required for Class 3 such that only investment firms that do not exceed these thresholds are classified as Class 3 investment firms for the purpose of the new prudential regime. FIA EPTA includes in its membership investment firms, and persons that will be subject to authorisation as investment firms upon the application of MiFID II, that are small in size, non-complex in activity and structure and

	are “non-interconnected”. These investment firms should be classified as Class 3 investment firms.
Advantages and disadvantages of subjecting Class 3 firms to fixed overheads only?	2. We see no obvious disadvantages as long as there are appropriate exclusions and quantitative thresholds for inclusion in Class 3.
Advantages and disadvantages of merging class 3 with other classes?	3. We do not support the ‘built-in’ approach. Such an approach would be disproportionate and overly complex for Class 3 investment firms and thus contrary to Recommendation 1 of the EBA Report on Investment Firms [**EBA/Op/2015/20**]. 4. We consider basing minimum regulatory capital requirements on fixed overhead requirements (**FOR**) to be an established and proven practice with bases in Union law.
4. Views on the criteria for identifying Class 3 firms?	1. As noted above, we believe that categorisation for the new regime should be both activities-based and size-based. We consider three-months FOR an appropriate quantitative measure and propose a FOR ceiling of EUR 3.5 million such that investment firms that do not undertake excluded activities and with FOR at or below the ceiling be classified within Class 3.
In particular views on the following criteria which would preclude being identified as Class 3:	2. We caution the EBA against trying to fit exclusions to the population of investment firms set out in the annex to EBA/Op/2015/20. Categorisation for the purposes of the new regime should, first and foremost, be risk-based. An investment firm’s permissions do not determine its risk profile, or indeed the risks it may pose to its customers or to the markets in which it participates.
a) holding client money or securities	We support this exclusion.
b) ancillary service of safekeeping and administration (B1)	We support this exclusion.
c) dealing on own account (A3)	We oppose this exclusion. FIA EPTA members, including members that ought to be classified as Class 3 investment firms, are authorised to deal on own account in financial instruments.
d) underwriting or placing with a firm commitment (A6)	We support this exclusion.
e) the granting of credits or loans to an investor (B2)	We oppose this exclusion for firms dealing with eligible counterparties. This exclusion would exclude from Class 3 investment firms that may provide credit support to counterparties for the purpose of a transaction. We do not consider this to be a sophisticated or high-risk activity *per se*.
f) operating a multilateral trading facility (or MTF) (A8)	N/A
g) the MiFID II activity of operating an organised	N/A

trading facility (or OTF)	
h) being member of a wider group	We oppose this exclusion. Consolidation requirements would effectively address the risks suggested in the EBA's analysis and we consider it unlikely that an investment firm would seek to divide its business into a number of small firms with restricted permissions to avoid minimum own funds requirements.
i) using a MiFID passport	We oppose this exclusion. The EBA's analysis at paragraph 19 discounts the purported risk of 'passporting' of regulated activities into other EU Member States.
j) using tied agents	We support this exclusion.
Section 4.3.1 - Capital requirements	
5. Comments on the approach focusing on risk to customers (RtC), risk to markets (RtM) and risk to firm (RtF)?	1. We are broadly supportive of the proposed approach and the focus on risk to customers (**RtC**) and risk to market (**RtM**), although we consider that both need some adjustment to properly address bilaterally executed transactions and the clearing and settlement arrangements prevalent in European securities and derivatives markets. 2. We are doubtful as to the utility of the risk to firm (**RtF**) factor and how this measure may affect risk to customers and risk to market. Clearing firms adjust margin requirements reflecting the risks of a clearing customer's positions and any increase or decrease in the riskiness of these positions. Increased or decreased margin requirements are already accounted for in the revised RtM calculation proposed by FIA EPTA members in our response to Question 6. Therefore, we are concerned that, as proposed, the risk to firm uplift measure (**RFUM**) would constitute double counting of risk and inappropriately applying a de-facto leverage ratio to investment firms exempted from Part VII CRR requirements. 3. We caution the EBA against any approach that would set regulatory capital requirements that would act as a barrier to entry to new market participants. We also caution the EBA against any approach that would set own funds requirements for non-systemic investment firms that are significantly higher than those applicable to alternative investment fund managers (**AIFMs**). We see no good outcome from any such divergences between regimes. 4. We believe that the proposed approach should be focussed on calculating regulatory capital sufficient to finance the orderly winding down of failed investment firms and not the ability to recover. We believe that the best way of ensuring such appropriate and proportionate calculations to use FOR as a reference for own funds requirements for Class 2 investment firms.
6. Views on the initial K-factors identified?	We are concerned generally that the EBA's analysis at paragraphs 36-37, 38-39, and 49 makes no reference whatsoever to the extensive conduct and market regulation applicable to investment firms, including the new MiFID II and MiFIR regime, as well as Regulation (EU) No 596/2014 on market abuse (**MAR**). Any K-factor analysis must consider the scope and primacy of these regulations. 1. Risk to customers (RtC)

FIA EPTA members do not generally have “customers” as the term is used in CRD IV and CRR. Nor do FIA EPTA members engage in portfolio management, provide investment advice or hold client assets or moneys. Thus, the analysis at paragraphs 36 and 37 of the DP and the six K-factors identified are, by and large, not applicable to FIA EPTA members.

Some FIA EPTA members deal bilaterally in financial instruments with eligible counterparties as defined in Article 24(2) MIFID. Such transactions are not subject to MiFID requirements including the obligation to provide ‘best execution’. Investment firm positions arising from such transactions, or any other transactions not subject to best execution requirements, should be excluded from the assessment of any RtC K-factor. Instead, such positions should be included in the assessment of RtM K-factors in accordance with the revised approach proposed by FIA EPTA (see below).

2. Risk to market (RtM)

We are sceptical that FIA EPTA members pose risk to market as described in the EBA analysis at paragraphs 38-40. Simply put, FIA EPTA members, were one or more to fail, would not deny third parties access to markets in financial instruments, would not materially reduce liquidity and would not inordinately harm market confidence. The reasons for this are as follows:

(1) FIA EPTA members are mainly active on exchange-traded markets that are today closely supervised, highly-competitive and transparent. Exclusive market making arrangements in a financial instrument in these markets are extremely rare. These markets bear little resemblance to the fixed income and OTC derivatives markets of yesteryear, which were controlled by a small number of large credit institutions and systemically-important investment firms. In today’s exchange-traded markets market making is diffuse and there are many liquidity providers competing for business. These markets will not miss one or more failed market makers or liquidity providers, whose remaining business will be quickly taken on by another.

(2) FIA EPTA members’ transactions are generally cleared and subject to margin requirements imposed by clearing firms. These clearing arrangements ensure that were a FIA EPTA member to fail, its positions could be quickly liquidated without loss to the clearing firm or the CCP. Similar clearing arrangements are used by FIA EPTA members for bilaterally executed transactions, which may also be margined. These clearing arrangements ensure that counterparty credit risk is appropriately managed and that effects of an investment firm failure do not spread risk in wholesale markets.

(3) FIA EPTA members typically trade highly-liquid financial instruments. The positions of a FIA EPTA member, were it to fail, would generally be settled in a regular manner or sold off to other market participants within two working days.

The above arguments notwithstanding, were the EBA to propose a revised ‘proprietary trading activity’ (**PTA**) K-factor we believe it should be calculated on the basis of the aggregate margin applied by clearing firms (or CCPs directly) to the investment firm’s positions in financial instruments. We do not believe that balance sheet and off-balance sheet exposures are the appropriate basis for any PTA K-factor because these accounting measures do not reflect off-setting or hedged positions in financial instruments typically held by FIA EPTA members. We consider the margin model applied by clearing firms to be the most appropriate basis for the calculation of the risk of a position in financial instruments held by FIA EPTA members for the following reasons:

(1) Clearing firms act as de-facto gatekeepers to the markets, both on an initial and ongoing basis. When on-boarding clearing clients, clearing firms assess both the risk profile as well as the trading strategy of the customer and apply an initial margin on this basis. The clearing firm monitors, on a real-time, intraday basis, the activities of the clearing client and adjusts the margin requirement when pre-set risk limits are breached. The clearing firm will also, if circumstances so require, step in to forcefully close or net out the clearing client's trading position (at the client's cost). Additionally, clearing clients are subject to holistic review on a frequent basis to ensure that the client's internal controls and trading strategy are still appropriate and pose no risk to the clearing firm and the wider market.

(2) The margin requirement provides the most accurate picture of the risk of an investment firm's positions as it accounts for *inter alia* price volatility, liquidity, collateralisation, concentration and size of relevant positions and therefore, by extension, what may be considered any measure of RtM were that investment firm to fail.

(3) Clearing firms are credit institutions and systemically important investment firms subject to the requirements of CRD IV, CRR, and, by extension, Regulation 648/2012 on OTC derivatives, central counterparties and trade repositories (**EMIR**) where these clearing firms are members of a CCP.

(4) These institutions must hold own funds requirements in accordance with Article 92 CRR, which must account for the positions they hold on behalf of their clearing clients. These institutions devise clearing models reflecting their Part III CRR obligations and use these models to calculate the margin of their clearing clients, including FIA EPTA members.

Therefore, we believe that RtM calculated on the basis of aggregate margin requirements imposed by clearing firms on non-systemic investment firms offers EU policy makers the 'best of both worlds' – a new and simplified prudential regime for principal trading firms, which at the same time is firmly grounded in CRD IV and CRR.

3. Risk to firm (RtF)

We do not support the proposed RFUM. We do not believe that the EBA's analysis at paragraph 47 identifies any risk that would not be captured by the revised RtM calculation proposed by FIA EPTA above. Nor do we believe that the risks described by the EBA under the RtC and RtM K-factors would increase significantly in circumstances where the failure of an investment firm becomes more likely. The EBA's analysis at paragraph 49 assumes that a failing investment firm may be "more susceptible to poor behaviour, weaker controls and greater risk-taking" without considering the relevant conduct and market regulation, the role of clearing firms and their monitoring and enforcement actions to restrict the trading activities and/or liquidate the trading positions of clearing clients, the ongoing supervision of investment firms by NCAs and the powers of NCAs to restrict the actions of investment firms or to order an investment firm to cease trading. We are concerned that, as proposed, the RFUM would constitute the double counting of risk for the purposes of setting own funds requirements.

Furthermore, we do not believe that leverage as described at paragraph 52 is an appropriate proxy for investment firm risk. Applied to balance sheet and/or off-balance sheet exposures, the proposed measure would not reflect offsetting or hedged positions held by an investment firm nor would the measure account in any way for increasing margin requirements set by clearing firms. We are concerned that applying the RFUM as proposed would, in effect, apply the CRR leverage ratio to investment firms expressly excluded from Article 429 CRR were it to be amended in accordance with the European Commission's proposal. We consider that FIA EPTA members, as customers of

	clearing firms that will be subject to a binding leverage ratio, are already subject indirectly to the leverage ratio. We recognise, however, that the K-factors approach may need an uplift measure to adjust minimum own funds requirements for Class 2 investment firms which may be engaging in more risky trading activity. Indeed, we accept that winding down such investment firms should they fail may take longer and may be more costly, and thus higher own funds requirements are warranted. With this in mind, we propose a revised approach to the uplift measure and believe that an amended RFUM be set at "1" for all positions of a Class 2 investment firm that are subject to clearing arrangements or that are subject to other margining arrangements. In exceptional circumstances, and reflecting only those positions which are not subject to clearing arrangements or are not otherwise margined, NCAs should be permitted to apply a RFUM greater than 1 to reflect the elevated risk. NCAs must be able to justify any increase to own funds requirements on an ongoing basis. 4. FOR v (RtC + RtM) We are broadly supportive of the EBA's proposal that minimum regulatory capital requirements for Class 2 investment firms be the larger of FOR or the sum of applicable K-factors. We believe that FOR must remain the key reference for own funds requirements for Class 2 investment firms under any new prudential regime.
Should there be separate K-factors for client money and financial instruments belonging to clients?	N/A
Should there be an RtM for securitisation risk-retentions?	N/A
Suggestions for additional K-factors that can be both easily observable and risk sensitive?	N/A
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?	No. Please see section 2 of our answer to Question 6 above.
If not, what alternative approach to addressing risk to firm (RtF) would you suggest?	N/A
8. Views on the 'built-in' approach to delivering simpler, proportionate capital requirements for Class 3 investment firms?	We do not consider the 'built-in' approach to be appropriate for Class 3 investment firms. Please see our answers to Questions 3 and 4 above.
9. Should a fixed overhead requirement (FOR) remain part of the capital regime? If so, how	We consider the current secondary legislation on fixed overheads to be appropriate.

could it be improved?	
10. Views on the appropriate capital requirements required for larger firms that trade financial instruments (including derivatives)?	We believe that regulatory capital requirements sufficient to finance the orderly winding down on a failed investment firm are appropriate.
11. Is the K-factor approach appropriate for investment firms that may be systemic but are not 'bank-like'?	No. We believe that all systemically-important investment firms ought to remain subject to the provisions of CRD IV and CRR as well as other relevant regimes (e.g. Directive 2014/59/EU on establishing a framework for the recovery and resolution of credit institutions and investment firms (**BRRD**)). We also believe that investment firm subsidiaries of credit institutions or with credit institutions in their group ought to remain subject to the provisions of CRD IV, CRR and other relevant regimes.
Section 4.3.2 - Definition and quality of capital for investment firms	
12. Does the definition of capital in the CRR appropriately cater for all the cases of investment firms that are not joint stock companies?	We do not believe that the CRR definition of capital poses material problems for investment firms that are not joint stock companies.
13. Are the cases described a real concern for the investment firms? How can these aspects be addressed while properly safeguarding applicable objectives of the permanence principle?	N/A
14. Views on the need to simply the range of items that qualify as regulatory capital and how the different tiers of capital operate? How could this be achieved?	1. Given the way in which investment firms capitalise their businesses, FIA EPTA members would welcome any attempt to simplify the definition of eligible capital and the tiering mechanism. 2. We propose maintaining two distinct tiers of capital with any distributable reserves and share capital, including preference shares, comprising Tier 1 and any long-term subordinated debt being included in Tier 2 only.
15. In which areas is it possible to simplify the current CRR approach whilst maintaining the same level of quality in the capital definition?	1. We are of the view that the existing regime for deductions and prudential filters set out in CRR would have to be simplified in a new prudential regime for investment firms and could do so without jeopardising the quality of capital. 2. In particular, the deduction of financial services entity (**FSE**) investments is a challenge for FIA EPTA members where these investment firms may be holding positions in such securities for only 1-2 days on their trading book. Any new prudential regime should require FSE deductions only where the position is not on the investment firm's trading book and is held for speculative purposes. 3. We do not believe that all existing deductions are inapplicable. We agree with the EBA's assertion at paragraph 91 that some deductions in CRR remain relevant for investment firms. The deduction of assets such as intangible assets and deferred tax apply across any type of regulated entity and ought to apply to investment firms under any

	new prudential regime. 4. Additionally, any new prudential regime should reconsider the discretion on deductions available to NCAs. Experience shows that this discretion is prone to divergent use, which results in extraordinary differences in CRR requirements across Member States contrary to CRR policy objectives.
16. Overall views on the best way forward for the definition and quality of capital for investment firms?	1. FIA EPTA members strongly support any simplification of the definition of regulatory capital. 2. That said, we believe that the Tier 1 capital definition should reflect how investment firms report equity and debt per applicable financial reporting standards. Whilst we support limits on the use of Tier 2 capital to prevent capital gearing, we believe that the requirements around the distinction between Tier 1 and Tier 2 capital should be appropriate for investment firms. Simply importing the requirements provided for in CRR would not be appropriate or proportionate for non-systemic and non-bank like investment firms.
Section 4.3.3 - Initial capital requirements	
17. Views on the definition of initial capital and the potential for simplification?	We consider the definition of initial capital to be sufficiently simple and do not believe that further revisions are necessary.
To what extent should the definition of initial capital be aligned with that of regulatory capital used for meeting capital requirements?	N/A
18. What aspects should be taken into account when requiring different levels of initial capital for different firms?	1. We would suggest adjusting the levels of initial capital to take account of inflation as the figures have remained the same for over 20 years. 2. We would strongly agree that the definition of initial capital under any resulting prudential regime should be aligned with the definition under MIFID, and subsequently MIFID II, and CRD IV. We also agree that insurance should not be considered to be a substitute for any aspect of regulatory capital.
Is there any undesirable consequence or incentive that should be considered?	3. As stated in the discussion paper, there is also a EUR 50,000 initial capital regime which is applicable to ‘local firms’. However, this is based upon a national discretion which has not been exercised by all Member States. We would advocate limiting the national discretion in this respect and making the EUR 50 000 initial capital regime directly applicable to avoid creating the conditions for regulatory arbitrage and an uneven playing field within the Union.
Section 4.3.4 - Eligible Capital	
19. Views on the need to have a separate concept of eligible capital, or whether there is potential for simplification through alignment with the definition of regulatory capital used for meeting capital	We believe it would be better to align the definitions of eligible capital and regulatory capital. Maintaining a separate eligible capital solely for the purposes of the FOR, the large exposure regime and for qualifying holdings outside the financial sector seems to be unnecessarily complex.

requirements?	
Section 4.3.5 - Liquidity requirements for investment firms	
20. Are there any common stress scenario for liquidity as necessary for investment firms? If so, how could that stress be defined?	1. Given the large number of business models of investment firms, it is unlikely that there is a common stress test that would be appropriate for all investment firms. We also consider that key stress tests are already included in clearing firm margin models. 2. Class 2 investment firms should be permitted to rely upon the margin models applied by clearing firms. These investment firms could be encouraged to develop their own stress scenarios as part of a minimum liquidity standard, provided that the requirement is proportional to the complexity and size of the firm.
21. Views on whether holding an amount of liquid assets set by reference to a percentage of the amount of obligations reflected in regulatory capital requirements would provide an appropriate basis and floor for liquidity requirements for 'non systemic' investment firms?	1. FIA EPTA members would, of course, welcome a liquidity regime which is both simple to understand and to implement. 2. Linking the liquidity requirement to the K-factors seems a sensible idea in that liquidity requirements and risks are different depending on the type of investment activity and services that FIA EPTA members undertake or provide. 3. We emphasise that the objective of any such liquidity regime should be to ensure that an investment firm has sufficiently liquid funds to facilitate an orderly wind down in the event that it should default. The calibration of the liquidity requirements must reflect this objective. 4. Whether the calculation results in an appropriate measure for determining minimum liquidity amounts is dependent on both the calibration of the factors and the assets that are available to meet the requirement. 5. As described below in Question 22, we emphasise that cash (and cash-like assets) and all trading assets should be available to meet liquidity requirements. 6. Additionally, clearing members also incorporate liquidity risk into their margin calculation. They measure concentration risk, do larger shocks for illiquid positions and perform stress events, for example. Having illiquid positions already leads to higher margin at the request of clearing members. Therefore any liquidity regime should ensure against the double counting of risk.
Could you provide any evidence or counterexamples 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?	N/A
22. What types of items should count as liquid assets to meet any regulatory liquidity requirements, and why?	1. FIA EPTA members are of the opinion that all trading book assets should be eligible for liquidity purposes. 2. It should be recognised that reducing trading positions can improve an investment firm's liquidity position both by a direct cash flow from selling securities or by reducing margin requirements at a clearing firm by closing out positions

	(including exchange traded derivatives and OTC derivative contracts). This can be done in a matter of days. 3. In principle, FIA EPTA members consider all assets in their trading book to be available to meet liquidity needs. This is particularly true where those assets are cash or cash-like (money market funds, short-dated government bonds), quickly and easily liquidated or where the positions are relatively small compared to normal trading volumes. 4. Even where securities may be less liquid or positions large relative to normal trading volumes, an investment firm will still be able to realise those assets over time. All assets are for sale at some price and, to the extent possible, the level of any requirements should reflect how much time a firm has to meet a liquidity requirement. 5. It should also be noted that clearing firm margin calls do not have to be met with cash, but can be met with any assets after taking into account the clearing firm's margin requirement on those assets. Thus trading book assets are as valuable as cash (after adjusting for margin requirements) in meeting liquidity needs.
23. 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?	1. We are of the view that if the liquidity requirements are properly calibrated, then there should be no need to provide additional or supplementary measures for larger, more complex firms. 2. While NCAs should retain supervisory discretion, we believe that any new regulatory regime should preclude NCAs from adding liquidity requirements for Class 3 investment firms and should include new conditions that should be satisfied before NCAs can instruct a Class 2 investment firm to do so as part of any supervisory review and evaluation process. 3. Moreover, the application of additional liquidity requirements should be limited as they have the potential to put firms at a competitive disadvantage and distort the level playing field in the EU market.
24. 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?	1. We agree that investment firms should have appropriate operational controls in place to manage their liquidity. Those controls should be proportionate to the nature and complexity of the firm. We understand regulators’ concerns but we do not see the merit of prescribing additional strict operational requirements. Regulators must recognise that firms have in place existing risk management practices tailored to their business models and activities, including those prescribed in detail in MiFID II, as well as being subject to the margin arrangements imposed by clearing firms which take account of the liquidity risks. 2. As an alternative, we suggest establishing a set of minimum standards and principles to which firms should adhere. Any shortcomings can be addressed as part of a supervisory review process.
Section 4.4.1 - Concentration risk	
25. Views on the relevance of large exposures risk to investment firms?	1. Credit institutions and systemic investment firms play a significant role in Europe’s capital markets. In order to minimise contagion and to protect the system as a whole it would be prudent to continue to require such institutions to be subject to comparable CRR large exposure (**LE**) requirements. 2. Whilst the majority of investment firms that are not ‘systemic and bank-like’ will not be subject to LE requirements, FIA EPTA members recognise that some firms may be subject to the requirements on account of the MiFID investment services and ancillary services they provide. 3. Firms that provide the ancillary services of the safekeeping and administration of financial instruments for the

	account of clients or services relating to underwriting should be subject to LE requirements. These firms exhibit a higher RtC profile than other firms and accordingly it is prudent to mitigate the likelihood of contagion arising in the event of a defaulting firm, as well as the impact on their underlying clients, by limiting their exposures to third parties. 4. Non-systemic and non-bank like firms that do not provide such ancillary services and have lower RtC profiles do not represent similar default or contagion risks to clients. Therefore the LE requirements should be waived. Such an approach is already provided for in the existing CRR regime (CRR Art 388 in respect to CRR 95 and 96 firms).
Would a basic reporting scheme for identifying concentration risk be appropriate for some investment firms, including Class 3 firms?	5. In line with our thinking set out above, it is logical that investment firms subject to LE requirements are subject to a reporting regime similar to the existing regime (in line with COREP Large Exposures Individual and Consolidated) under CRR/ CRD IV. This will enable prudential regulators to (i) verify firms' continued compliance with their LE requirements, (ii) at a macro-prudential level assist the identification of the build-up of systemic credit risks, and (iii) provide early warnings for the variation of additional prudential capital buffers. 6. It is not unreasonable to require investment firms that are not 'systemic and bank-like' (Class 2) to provide metrics on their exposures. This would enable prudential regulators to monitor at a macro-prudential level the build-up of systemic credit risks. 7. However, we would urge the EBA to caution NCAs against using reporting requirements as an excuse to use their Pillar 2 discretions to layer on additional capital requirements. 8. With regard to Class 3 firms, considering the nature, small size and low complexity of these investment firms which are not subject to the LE requirements, it would be overly excessive and burdensome to require such firms to provide detailed reporting on exposures. Moreover, it would burden prudential regulators with additional non-material metrics for validation and assessment with limited macro-supervisory benefit.
Section 4.4.2 - Consolidated supervision	
26. Views on the proposed approach to addressing group risk within investment firm-only groups?	1. We broadly agree with applying consolidated supervision as it serves to supplement the supervision of an individual authorised entity, providing a view of the wider risks that a firm may be exposed to by virtue of its membership of a group. However, its application should not result in the imposition of capital requirements which exceed the sum of the requirements of each individual EEA entity within the group. According to figure 6 of the discussion paper this is not the intention of consolidation and in fact would penalise firms for being part of a group. 2. For other regulated entities the EBA suggests using the intra-group supplied capital. These entities are already regulated with their own local regulatory capital requirement. The suggested consolidated method could lead to higher capital requirements if the intra-group supplied capital is higher than the locally required regulatory capital. 3. We would question the value of including very small and non-complex affiliates within the scope of consolidation given their negligent impact on the risk of the group as a whole. Consequently, we would propose establishing a threshold for a 'material subsidiary' greater than that provided for in Article 19(1) CRR. Moreover, as noted above in Question 4, we do not consider there to be a genuine risk that a firm would separate itself into several very small firms to circumvent consolidation requirements. 4. For unregulated entities the EBA suggests using the book value. Unregulated entities have no local regulatory

	capital as their activities are not regulated. The suggested consolidated method could lead to higher capital requirements if the book value suddenly needed to be taken as regulatory capital. 5. Given that unregulated entities undertake activities which are not regulated, we are of the view that no additional capital is required. In the event that these firms would require capital we would suggest maintaining the use of FOR. 6. We would also advocate that consolidation should only extend to the capital requirements of EEA group affiliates. To capture non-EEA entities in this calculation would be an extra-territorial reach of the legislation.
Any other suggested treatments that could be applied, and if so, why?	7. We agree with taking the consolidated equity on a group level, although for calculating the required capital we would suggest using the regulatory capital on an individual basis for EEA entities as required by the different local regulators.
27. In the case of an investment firm which is a subsidiary of a banking consolidation group, are there any difficulties in the implementation of the proposed capital requirements on an individual firm basis?	N/A
Any suggestions to address these?	
Section 4.4.3 - Additional requirements on an individual firm basis	
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?	1. FIA EPTA members welcome the EBA's efforts to develop a proportionate application of prudential measures which takes into account the existing 'additional requirements' investment firms are subject to under MIFID I and MIFID II as well as the supervisory and evaluation process (**SREP**), as referred to in paragraphs 159 and 160. 2. In order to ensure the proportionate application of prudential measures, we would like to reiterate that the EBA should consider limiting the NCAs' Pillar 2 discretion. As Pillar 1 becomes more extensive under the new regime for investment firms, the diverging interpretations and use of the national discretion under Pillar 2 will undermine the effectiveness of Pillar 1 requirements and the efforts to ensure their proportionate application.
4.4.5 Reporting and any other prudential tools	
29. Examples of excessive burdens for investment firms arising from the current regulatory reporting regime?	1. The breadth and onerous nature of the public disclosure requirement for investment firms, including under the CRR, has been well documented in responses to the Commission's Call for Evidence. 2. For example: – The disclosure of remuneration information is unnecessary and potentially places investment firms at a competitive disadvantage to their peers. – The asset encumbrance reporting is similarly burdensome for investment firms and its design is wholly unsuitable for firms' business models.

	– The countercyclical capital buffer is designed with credit institutions in mind and is not suitable for investment firms given the quick settlement of trading positions and absence of a maturity mismatch. – The FSE monitoring and reporting regime is onerous and poorly implemented. The degree of off-set permitted between long and short positions is inadequate. The exposure levels to financial sector entities should be determined on a net economic value basis as the current specification is punitive on market-makers and misleading for competent authorities. Basel III permits more off-set between long and short positions than is the case in the CRR. 3. This list is not exhaustive and should be considered indicative of the need for a simple and proportionate reporting regime which is aligned with the objectives of the new prudential regime as a whole.
30. Views on the need for any other prudential tools as part of the new prudential regime for investment firms?	
How could the tools be made more appropriate and in particular, is there a need for requirements on public disclosure of prudential information?	1. We would challenge the inclusion of Pillar 3 disclosure requirements in a new prudential regime for investment firms. We consider it to be unnecessary, as explained below, and can potentially place a firm at a competitive disadvantage vis-à-vis its competitors who are not subject to this requirement. 2. We agree that public disclosure of a limited amount of information to provide reassurance to market participants seems reasonable if those firms deal with retail clients. 3. However, we disagree with the EBA's anecdotal evidence in paragraph 168. It is our experience that Pillar 3 statements exhibit limited utility to investment firms when assessing professional counterparties. Typically due diligence will rely on credit assessments (ECAI ratings or detailed financial statements) and a review of regulatory status and not on Pillar 3 statements. 4. Therefore it is our recommendation that there should be no requirement to prepare or provide a Pillar 3 disclosure as other information - whether it be terms of business or financial statements - is more efficient and appropriate for the communication of key information.
Is there a need for requirements on recovery and resolution?	5. We do not believe that EU tools for recovery and resolution such as the BRRD are appropriate for either Class 2 or Class 3 investment firms. As noted above in our response to Question 11, if investment firms fall out of the scope of CRD IV/ CRR then interconnected regimes, including BRRD, should not be applicable. 6. The BRRD was created to provide authorities with harmonised procedures for resolving, at a Union level, institutions which could cause systemic damage to financial stability institutions. As such, it should only be applicable to credit institutions and a limited number of systemic investment firms as only the default of these types of firms would cause financial instability to such an extent that BRRD measures would be required. It would be disproportionate to require all other investment firms to comply with the BRRD requirements. 7. Moreover, the BRRD requires investment firms to contribute to a resolution fund to which it would have no claim were it to be subject to an orderly wind down. This requirement places a significant financial burden on non-systemic investment firms. It is not equitable that such firms should be required to contribute their own capital to a fund for

	credit institutions whose risk controls have failed and yet not be able to rely on such a fund themselves. It should be noted that investment firms are required to contribute to client money default funds at a national level whether they hold client money or not but credit institutions are not required to contribute to these funds.
Section 4.5 - Corporate governance and remuneration	
31. Views on the relevance of CRD governance requirements to investment firms, and any evidence to support this?	1. We would like to reiterate, as stated in our response to Question 2, the envisaged prudential regime should complement and not duplicate the existing market and conduct regulation. 2. From January 2018 all investment firms will be subject to MiFIR / MiFID II. MiFID II introduces very prescriptive and detailed requirements on governance requirements which are specifically tailored to investment firms and scaled according to the nature and activities of that investment firm. 3. Furthermore, we believe that it is opportune for ESMA, which retains subject-matter expertise on the nature of investment firm activities, to retain ownership of the assessment of governance arrangement supervision by NCAs and to provide additional guidelines or Q&As to investment firms under the MiFID II remit. 4. Introducing additional governance requirements under the prudential regime would result in duplicative requirements and unnecessary complexity which would run counter to the objectives of this regime.
32. As regards 'systemic and bank-like' investment firms, are there any potential challenges arising from the full application of the CRD/CRR remuneration requirements, any evidence to support this?	N/A
For all other investment firms, views on the type of remuneration requirements that should be applied to them, given their risk profiles, business models and pay structures?	1. The rules on remuneration were devised at a global level and implemented at a European and then national level. At each stage it was highlighted that these should be applied proportionately and should take into account a number of factors including the size, the international organisation, and the nature and complexity of activities. 2. Consequently, we would agree that systemic and bank-like investment firms should remain subject to the remuneration requirements under CRD IV. 3. However, we would challenge the appropriateness and proportionality of these requirements for Class 2 and 3 firms and would advocate for the establishment of a new principles-based approach to remuneration policies without the inclusion of definitive limitations similar to those in Article 94 CRD IV. 4. We believe that stringent limitations on remuneration policies, such as a bonus cap, would have a detrimental effect on the competitiveness of FIA EPTA members vis-à-vis other market participants who would not be not subject to such requirements, including alternative investment fund managers (AIFMs) and third country firms. We are concerned that with such limitations investment firms will no longer be able to attract and retain the most skilled personnel. 5. It has been asserted that remuneration caps contribute to financial stability. However, we would challenge this justification for remuneration caps in respect of non-systemic and non-bank like investment firms. As we have

	explained throughout our response, principal trading firms' activities pose no systemic risk and the societal impact of failure is minimal to none. Therefore we consider the costs of imposing such caps to greatly outweigh any conceivable financial stability benefit or other public policy interest. 6. Moreover, we are concerned that there is a lack of understanding of the business models, trading strategies and risk management procedures of FIA EPTA members which could be compromised by any remuneration rules which resemble those in Article 94(1) CRD IV. Variable remuneration policies promote prudent risk management amongst employees by allowing the alignment of an individual's behaviour with the risk appetite, values and long term interests of the business. Moreover, discretionary payments allow FIA EPTA members to maintain a level of flexibility in the cost base so that it can be strengthened in periods of stress and to cope with fluctuating profit levels. Thus, variable remuneration serves as an effective risk mitigation tool. 7. Finally, we would make reference to the EBA's Guidelines Compliance Table [**EBA/GL/2015/22 Appendix 1**], published in August 2016 and updated in October 2016, in which no less than seven Member States express that they do not intend to comply with the EBA's Guidelines on sound remuneration policies [**EBA/GL/2015/22**]. We consider this to be clear evidence that the regime in CRD IV is not fit for purpose for non-systemic and non-bank like investment firms. 8. With this in mind, we would propose that a principles based approach includes four key principles, namely that variable remuneration should be: – based on sharing profits of the investment firm; – paid in cash as opposed to equities; – subject to deferral above a *de minimis* threshold; and – subject to malus and claw back provisions.
33. Views on a prudential remuneration framework for investment firms other than 'systemic and bank-like' that should mainly aim to counteract against conduct related operational risks and the protection of consumers?	N/A
Section 4.6 - Alternative approach to a new regime	
34. Views on having a separate prudential regime for investment firms?	N/A
Alternatively, should the CRR be amended instead to take into account a higher degree of proportionality?	N/A

	Which type of investment firms, if any, apart from systemic and bank-like investment firms, would be better suited under a simplified CRR regime?	N/A
35.	What are the main problems from an investment firm perspective with the current regime? Please list the main problems with the current regime.	N/A