



## EUROPEAN COMMISSION

Directorate General Financial Stability, Financial Services and Capital Markets Union

### Call for advice to the EBA for the purposes of the report on the prudential requirements applicable to investment firms

#### Context

In accordance with Articles 493(2), 498(2) and 508(2) and (3) of Regulation (EU) No 575/2013<sup>1</sup> (henceforth ‘the Capital Requirements Regulation’ or ‘CRR’) the Commission is required to submit, by 31 December 2015, three reports to the European Parliament and the Council.

In preparing these reports the Commission is required to consult with the EBA and ESMA and discuss the matter with competent authorities.

In consideration of these mandates, the Commission sought technical advice from the EBA and ESMA in December 2014 to assess whether the current prudential requirements applicable to investment firms (including exemptions therefrom) laid down in the CRR and in Directive 2013/36/EU (henceforth ‘the Capital Requirements Directive’ or ‘CRD’)<sup>2</sup> are appropriate or whether they should be modified and if so, how.

In its response, sent to the Commission on 15 December 2015 (hereafter referred to as ‘the Response’), the EBA described the current status quo by discussing the current categorisations framework for investment firms, it then attempted to analyse the risks investment firms are exposed to and the existing prudential regime, and broadly concluded that the current regime is not fit for purpose for investment firms.

The key output of the Response, was its recommendations, of which there are three:

- **Recommendation 1** proposed that there should be three classes for investment firms: 1) systemic, ‘bank-like’ firms which should remain within the scope of the current CRR; 2) a middle category for the majority of firms – these will not be systemic but do pose risks and should be subject to a less-complex prudential regime calibrated to address specific risks; and 3) small firms which are not interconnected which should be subject to a very simple regime to cater for wind-down, if appropriate.
- **Recommendation 2** suggests that there needs to be more work done to design the regime for classes 2 and 3 and that there will need to be additional data collections and policy development for both classes.
- **Recommendation 3** points out that the exemptions provided in Articles 493 and 498 of the CRR need to be extended until 2020 to avoid any unintended burdens on certain firms that fall under MiFID.

<sup>1</sup> Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012.

<sup>2</sup> Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC

## **Scope and need for further technical advice**

The EBA is asked to consider and provide detailed technical advice on the first two recommendations in its report.

In particular, on the first recommendation, the Commission would like the EBA to develop, for each of the three proposed classes of firms, the exact criteria/indicators and thresholds for determining which firm falls in each class. The reason for the selection of each criterion should be clearly substantiated.

The EBA should provide clear definitions for quantitative indicators (e.g. size). In calibrating those indicators, the EBA should take into account that there may be differences between Member States, and as such it should consider expressing the indicators not only in absolute but also relative terms. For qualitative indicators, clear definitions should be provided and should, to the extent possible, rely on existing definitions contained in Union law. If the EBA considers that alternative definitions are more suitable, it should clearly articulate why existing ones are not adequate.

In relation to the second recommendation, the Commission would like the EBA to report on the following:

a) for class one investment firms:

- The EBA should provide advice on whether class 1 firms should simply be subjected to the same rules as banks or if there is a need for any derogations for these firms;
- Further to this, the EBA should provide a clear rationale for the position taken as well as any modifications to existing derogations or calibrations for any new derogations;

b) for class two and three investment firms:

- the appropriate design and calibration of all relevant aspects of a new prudential regime, which should be clear to operate, specifically tailored to the needs of the business models of those firms and the risks that their operations present. It should also be proportionate, and take account of both quantitative and qualitative aspects and regulatory tools that may form part of an overall regime. It should include, but not necessarily be limited to, capital requirements;
- the appropriate initial capital requirements for both categories of investment firms;
- the impact of the new regime compared to the existing regime;
- the extent to which the new regime would also be - or could be adapted to be - suitable for specialised commodity derivatives firms. In case this is not possible, to provide advice on an alternative new regime for these firms;
- whether class 2 and 3 firms should be subject to liquidity requirements and, if so, which ones (in analysing this issue the EBA should consider the appropriateness of any existing requirements).

Moreover the Commission would like the EBA to also clearly articulate a mapping of the new prudential rules to the current ones, highlighting any significant deviations from the current rules and the rationale behind these deviations.

## **Remuneration and corporate governance**

The Commission takes note of the EBA's remarks on remuneration contained in the Response, in particular that investment firms commonly have different risk profiles, business models and pay structures compared to credit institutions, due to which specific challenges could arise from the full application of the CRD/CRR remuneration requirements to investment firms.

The Commission would therefore like to ask the EBA to provide advice in relation to the application of the CRD/CRR remuneration requirements to the investment firm population distinguishing, where relevant, between the recommended treatment for each of the proposed investment firm classes.

Moreover, the EBA is kindly invited to signal whether and to what extent, in the EBA's view, the proposed new classification of investment firms would affect the applicability of the CRD/CRR corporate governance rules.

### **Data collection**

In addition, the Commission would like the EBA to collect all data and information that it deems necessary in order to formulate its advice to include sufficient evidence in its advice in order to underpin its recommendations. The information collected by the EBA should cover, among others:

- statistical evidence which corroborates any quantitative elements of the EBA's proposals;
- data on the extent to which liquidity provisions apply to investment firms in each Member State. This should include data on the number of firms to whom the liquidity regime may apply and the number of exempted firms per member state;
- data on the total number of investment firms which are part of a wider banking group;
- data in order to assess the impact of the proposed regime.

### **Final considerations**

The Commission would like the EBA to also report on any other issues or inconsistencies that competent authorities in the EU may have identified in the implementation of the rules related to investment firms. In particular, any suggestions on how to rectify the identified issues and inconsistencies or how to clarify the terminology used would be welcomed.

In preparing its advice the EBA should also consult with the ESMA staff on the substantive aspects of its advice.

The deadlines for this call for advice are the following:

- By 31 September 2016, the analysis relating to class one firms, both the criteria to identify this class and the rules which should apply to them.
- By 30 June 2017, the final report, for the substantive content and calibration of the proposed regimes.

It is recalled that the analysis provided will not prejudice the Commission's final decision. Moreover, in accordance with the established practices of the Commission Expert Group on Banking, Payments and Insurance, the Commission will continue, where appropriate, to consult the experts appointed by the Member States in the preparation of its report.