

# DISCUSSION PAPER ON A NEW PRUDENTIAL REGIME FOR INVESTMENT FIRMS

Thank you for the opportunity to provide our thoughts on this topic. JP Morgan Asset Management supports the creation of a new regime for investment firms that are not bank-like. However, there should not be distinct Category 2 and Category 3 regimes because size alone is not sufficient to determine the level of risk that a firm poses. We support a level playing field for firms undertaking similar activity and competing for the same customers and staff.

Asset managers act as agents for underlying clients and not as principal. They do not bear their clients' market risk or credit risk on their own balance sheet. This demonstrates that asset managers are not bank-like under the EBA's definition (undertaking bank-like intermediation and underwriting risks on a significant scale). Furthermore, if, as is typically the case, client money and assets are segregated in separate accounts with a custodian or depositary, asset managers are not vulnerable to run risk in the way that banks are. This is because clients will have access to their segregated assets even in the event of the asset manager's failure, and will not need to compete with others to claim their share of remaining assets, as with a bank. A more appropriate prudential regime is justified.

Certain requirements such as the Fixed Overheads Requirement will rightly differ for firms based on their scale. However, a quantitative threshold for investment firms of different sizes would be counterproductive. Such an approach could distract from the actual risks that a firm runs, such as the role of leverage and concentration risk. The Discussion Paper also stresses the need to ensure that small firms are not dis-incentivised from making infrastructure investments, for example. But consideration must also be given to not creating artificial incentives to operate businesses below arbitrary thresholds to avoid prudential requirements. A better approach would be to distinguish between the inherent (pre-mitigation) risk and residual risk once systems and controls are taken into account. Capital should be applied to the residual risk. This would incentivise all firms to invest in their systems and controls; and should be feasible because the distinction is already embedded in firms' risk assessment methodologies.

We agree that regulation needs to ensure that client assets and money are properly managed. In reference to question 6, we do not believe that capital requirements are the right approach if client assets are required to be segregated in a separate account. The requirement to segregate varies across Member States and there is a case for a consistent approach across the EU. Additional capital should only be considered where segregation does not apply.

In reference to question 25, we do not think that traditional bank-like large exposure limits and reporting are appropriate for limited license investment firms, which typically have large cash balances to hand. Managing these balances as large exposures would unnecessarily complicate these firms' operating models and potentially add operational risk. Concentration risk is relevant to firms in the context of reliance on single products or clients.

Adequate resources must be maintained to ensure that a wind down of a firm can be executed without detriment to the market or customers.

Within investment-firm only groups, we find that the approach referenced in question 26 could be problematic. Group risk requirements could be applied to the parent company of regulated entities but this would mean creating a new category of regulated firms. It would also be necessary to determine what capital deductions would apply in the capital calculation for this new category of regulated firm.

As suggested in question 27, we believe that it will be possible to apply the new regime on a solo basis to asset managers that are part of a banking group, ensuring a level playing field between asset managers competing for the same customers. Similar to insurers, which are excluded from a banking group consolidation even when part of the statutory group, asset management activity poses little spill-over risk to the banking activities and asset managers within such a group structure could possibly be carved out from the regulatory consolidation group of the bank in the same way that insurers currently are.

Beyond our comments on the points above we have provided in the consultation form for those specific questions. We support the Investment Association's feedback in their response. We would be happy to further discuss our comments with you.