JOHNSTON CARMICHAEL

Investment Firm Prudential Regime

What do you need to do?

Supporting you on your IFPR journey

As a firm, we have been tracking the development of the Investment Firm Prudential Regime ("IFPR") throughout the multiple publications by the Financial Conduct Authority. The IFPR regime aims for a more proportionate approach to the prudential regulations of investments firms in the UK. It broadly aligns with the European equivalent, which, although it followed an earlier implementation date, the FCA were heavily involved in prior to the UK's departure from the EU.

We have summarised the key changes arising from the IFPR on the remaining slides. Some of these concepts will be familiar and some will be new, we hope the content allows for a deeper understanding of how the changes apply to your firm and the different areas of change.

We are happy to take any of your questions and provide support with any challenges you face as you aim to implement the requirements.

How do the new rules apply to you?

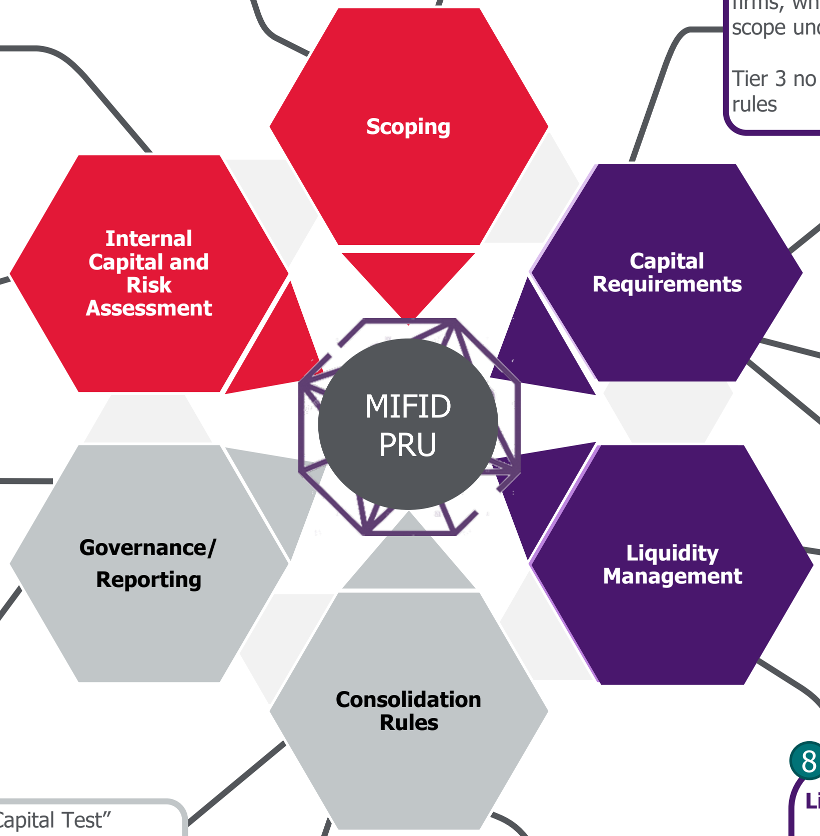
The below are the key areas of consideration as you determine your compliance requirements with IFPR…

Themes	Details
1 **Within the scope of the IFPR?**	All firms which fall under the scope of MiFID, will be required to comply with the Investment Firm Prudential Regulations, however:- • *Article 3 MIFID Exempt Firms will not be in scope* ***(unless they 'opted' into MiFid).*** • *If you did opt-in, we can help you vary your permissions to fall outside of IFPR, given there is no obvious benefit to remaining a MiFID Firm post Brexit.* For in-scope firms, your historic minimum requirement of 50k Euros will increase from 1st January 2022:- • *Firms will move from holding a minimum requirement of 50k EUR of regulatory capital to a minimum of £75k.* • *Specific transition provisions exist to allow a stepped approach to the increased capital requirements under the new MIFIDPRU handbook.*
2 **Considerations**	Considerations vary depending on your firm type, however a summary of the key ones are:- • *Upon calculation of your Permanent Minimum Requirement, you may be required to hold more than £75k.* • *As the Fixed Overhead Requirement includes salaries, the difference against your current €50k Own Funds Requirement could be significant.* • *The Internal Capital Adequacy Risk Assessment will be particularly challenging for Exempt-CAD firms, who were not in scope to do an Internal Capital Adequacy Assessment Process, given the ICARA is an extension of the ICAAP.* • *All firm types will need to calculate whether consolidation rules apply to your group. Given the rules are not straight-forward, we are able to assist if you do not have the expertise in-house, particularly if this is your first time.* • *When it comes to the extended scope of businesses subject to the consolidated supervision, groups who consider their models are not complex also have the option to apply to the regulator for an exemption from applying group consolidation, via a process known as a Group Capital Test (we can help you with this* ***given the application deadline of 31st January 2022).***
3 **Small & non-inter connected firms**	All thresholds to be met to be considered a Small & Non-Interconnected firm "SNI" (see table on right):- • *Calculation of AUM, COH, On & Off-Balance Sheet and total Gross Revenue must be calculated on a combined basis if in a group.* • *Exclusion Criteria – A firm with the ability to deal on own account means they cannot become an SNI despite meeting the criteria.* • *A number of transition provisions available for firms to gently ease in.* • *Requirement for ongoing monitoring thresholds in case firms move into 'non-SNI' which requires prompt regulatory notification.*

Measure*	Threshold
Assets under management	< £1.2 billion
Client orders handled – cash trades	< £100 million per day
Client orders handled – derivative trades	< £1 billion per day
Assets safeguarded and administered	zero
Client money held	zero
On- and off-balance sheet total	< £100 million
Total annual gross revenue from investment services and activities	< £30 million

Key challenges

What are your key areas of the IFPR?



1
Existing MIFID framework alignment to new framework not straightforward

2
Three new categories:-

i. Credit Institutions
ii. Non – SNI*
iii. SNI*

Firms need to ensure they have checked criteria appropriately

**Small and non-interconnected investment firms*

SIZE

3
Enhanced requirements for certain firms, which may not have been in-scope under old rules.

Tier 3 no longer allowable under new rules

4
Permanent Minimum Requirement:-

SNI Firm
i. £75,000

Non SNI Firm (dependant on activities)
i. £75,000
ii. £150,000
iii. £750,000

5
Fixed Overheads Requirement:-

25% of overheads, less specific items:-

- Bonuses,
- Expenses directly related to income,
- non-recurring,
- non-ordinary items.

6
Sum of K-factor requirements from ICARA (Only applies to Credit Institutions & Non-SNI firms)

i. Risk to Consumer
ii. Risk to Market
iii. Risk to Firm

Own Funds Requirement – Highest of 4, 5 or 6

7
Liquid Assets Definitions:-

i) Cash at UK Banks (no limit)
ii) Receivable within 30 days

Limited to 50% of FOR after 50% reduction on absolute amount

8
Liquidity Requirement:-

Sum of:-

i. At least one third of FOR required to be held in liquid assets
ii. 1.6% guarantee to clients

9
- Rules on whether your group structure falls under group consolidation are complex.
- If yes, all entities under a UK parent are treated as one entity.

10
"Consolidated" Groups must comply with multiple obligations

11
"Group Capital Test" Firms can apply to FCA to disapply prudential consolidation

12
- Reporting requirements have been simplified
- Given the number of new forms and variation in reporting frequency, detailed analysis is still required

13
Governance & Remuneration requirements apply to all firms; complexity scales-up as firm size increases:-

- SNI Firms require compliance with "MIFIDPRU Remuneration Code" only.
- Non-SNI firms will need to establish risk, remuneration & nomination committees.

Ultimate responsibility lies with SMF holders

14
- Fundamental changes, particularly for those not subject to ICAAP previously.
- Annual assessment may lead to increased capital requirements and/or liquid assets based on firm risks
- SNI firms can tailor down requirements

15
- Replaces the 'ICAAP'
- Can be performed on a consolidated basis, except for Windown Planning & Overall Financial Adequacy

Source: Johnston Carmichael Chartered Accounts and Business Advisors

Investment Firm Prudential Regime

What is ICARA and does it apply to us…?

ICARA stands for **I**nternal **C**apital & **A**dequacy **R**isk **A**ssessment and aims to replace the ICAAP and is the new approach to determining a firms own fund requirements:-

- It applies to all firms within the Scope of the IFPR and required to be performed at least annually although SNI firms can be 'proportionate' in their approach.
- Integral to the firm's Risk Management framework, will require linking to existing Risk & Control Matrixes in order to ensure appropriate identification and monitoring of risk of Harm to Consumers, Markets & the Firm.
- Applicability of Risk Factors are dependant on each firms business model.
- ICARA will need to be a continuous end to end process, demonstrate the controls, risk management and governance processes of the firm.
- Firms will need to review the adequacy of their ICARA process annually and report outputs to the FCA via a questionnaire.
- If there is a material change, an updated questionnaire requires to be sent to the governing body with 20 Business Days.
- Firm's will require to complete an ICARA document which will require governing body approval.

SREPS stands for **S**upervisory **R**eview and **E**valuation **P**rocess and is the process by which the regulator will monitor investments firms compliance with IFPR:-

- The regulator is moving away from minimum cycles to a more regular supervisory approach, supported through data collection of a number of key documents.
- The regulator will likely make their own assessment of the validity and accuracy of your approach within onward intervention if current calculations are not sufficient.

Our team are here to help with any questions

Scott Holmes

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Scott has over 30 years' experience in financial services audit and assurance assignments and currently acts for a wide variety of financial institutions, including investment managers, funds, corporate financiers, brokerages and IFAs.

Scott's background is in audit with a big 4 practice, where he also worked with banks, listed groups and building societies.

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Zabe is an experienced Risk & Regulatory specialist focusing on the provision of regulatory and controls assurance services to clients including asset management, wealth management, platforms and custodian banks. He has worked within the regulatory space for over 15 years including holding leadership positions within industry and the 'Big 4'.

He has worked on a variety of assignments from traditional CASS audits to internal control reviews (SAS70s, ISAE3402 reports) as well as s166 FCA engagements. His experience covers a wide range of disciplines including regulatory reporting, client money protection, product suitability, AML/Financial Crime, risk/control mapping, internal audit, operational resilience and regulatory due diligence.

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Jack Elliott

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Jack Elliot is a Senior Manager in Johnston Carmichael's Financial Services Audit and Assurance team. He is dedicated to working with FCA regulated firms and his particular focus is on Risk and Compliance.

Prior to joining Johnston Carmichael, Jack was a manager in Deloitte's Risk Advisory Team. He is a Chartered Accountant and holds a first-class law degree from the University of Edinburgh.

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