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The UK Investment Firm Prudential Regime (**"IFPR"**)

IFPR Implementation Guide

June 2021

Contents

Complexity and Impact Assessment

		Business areas impacted					
Key areas	**Impact and complexity**	**Documentation**	**Operations/HR**	**Data**	**Notifications & permissions**	**Capital & funding**	**Management body sign-off**
Classification of firms	High			✓		✓	
Consolidation / Group issues	High			✓	✓	✓	✓
Capital requirements	High	✓		✓	✓	✓	✓
ICARA / SREP	High	✓	✓	✓	✓	✓	✓
Governance	Medium	✓	✓	✓	✓		✓
Remuneration	High	✓	✓	✓	✓		✓
Liquidity requirements	Medium	✓		✓	✓	✓	✓
Concentration risk	Medium	✓		✓	✓	✓	✓
Reporting	Medium	✓		✓	✓	✓	
Waivers & notifications	Medium	✓			✓	✓	✓

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Action List

TIMELINE

IFPR comes into force

01/01/2022

2021 — Q 3 | Q 4 | 2022 — Q 1 | Q 2 | Q 3 | Q 4 | 2023 — Q 1 | 2027

By 01/01/2022 to 01/01/2027	Prepare to increase regulatory capital following the IFPR transitional measure
Before 01/01/2022	Prepare remuneration changes
Beginning of the first performance year starting after 01/01/2022	Implement remuneration changes
Q 1 2022	Prepare to submit first quarterly reports in relevant FCA template forms
Q 1 2022	Create ICARA risk assessment framework and governance [note: FCA timing expectations may change]
Q 1 2022	Complete ICARA and submit summary to FCA [note: FCA timing expectations may change]
Q 3 and Q 4 2021	Notify FCA of your firm's ICARA reference date, review date and submission date [note: wait for FCA to publish guidance on timing expectations]
Q 3 and Q 4 2021	Determine and submit appropriate consolidation waiver applications (e.g. group capital test, liquid assets and/or governance waivers).
By 01/01/2022	Calculate and hold liquid assets requirement
By 01/01/2022	Submit notification to FCA that alternative instruments issued meet the remuneration requirements to qualify under IFPR
By 01/01/2022	Calculate fixed overhead requirement
By 01/02/2022	Calculate K -factor requirements
By 01/02/2022	Consider transitional application rules

Classification

ACTION 1: DETERMINE YOUR FIRM'S CLASSIFICATION

- The IFPR creates a multi-tier classification system for investment firms. The extent to which certain rules apply will depend on which tier a firm is in.
- The first step for firms is to determine which tier they are likely to fall in. These are:
  - **Class 1 Firms** – the Capital Requirements Regulation (**"CRR"**) rules apply to the exclusion of the IFPR.
  - **Larger IFPR Firms** – the IFPR applies in full.
  - **Smaller IFPR Firms** – the IFPR applies, but firms are exempt from some governance and remuneration requirements.
  - **Small and non-interconnected firms ("SNIs")** – the IFPR applies, but firms are exempt from many key IFPR requirements.
- This Implementation Guide is aimed at IFPR investment firms and not Class 1 Firms.

Determine if you are likely to exceed the Class 1 Firm balance sheet thresholds.

Determine if you are likely to be an SNI based on your permissions profile and quantitative thresholds.

Gather the data required to monitor the quantitative thresholds and have the operational capacity in place to monitor and report this information.

If you are a Non-SNI, monitor the proportionality thresholds regarding balance sheet and trading book size, to determine whether you are a Smaller or Larger IFPR Firm.

Impact

- The operational burden on SNIs will be considerably lower.
- All firms will need a data and operational build to calculate, monitor and report the activity and volume threshold requirements.
- Firms that may fluctuate close to the thresholds should consider their growth strategies and projections, how crossing thresholds will impact this, and plan accordingly.

Consolidation/Group Issues

ACTION 2: IDENTIFY CONSOLIDATION GROUP

- Prudential consolidation will generally apply as a default position at UK parent company level.

Identify your UK entity and group by identifying group entities in scope of the IFPR (e.g. consolidation of UK parent and in-scope subsidiaries/connected undertakings).

Determine if groups are eligible for waivers (e.g. group capital test (**"GCT"**), liquid assets and/or governance waivers).

Prepare your applications for relevant waivers in advance of 1 January 2022. The FCA may accept draft submissions in Q3-Q4 2021.

Impact

- The capital and liquidity waivers/permissions will be substantially beneficial for many groups and will simplify burden and data calculations. The FCA has said that it supports groups using the GCT and expects many UK groups will qualify. We expect widespread uptake of the GCT, with most groups using it where possible.
- Alongside the EU's Investment Firms Regulation, the IFPR can create consolidation issues for mixed UK-EU groups, if any entities are included in both a UK and EU consolidation group.
- Consolidation requirements will also be challenging for groups which include a credit institution or PRA-designated investment firm, as these could be subject to both CRR and IFPR requirements. Such groups may consider rationalising their structure or applying for appropriate waivers.

Capital Requirements

ACTION 3: CONDUCT K-FACTOR ASSESSMENT

- Firms will need to assess their: (i) permanent minimum requirement; (ii) K-factor requirement (**"KFR"**); and (iii) fixed overhead requirement (**"FOR"**).
- The highest of the three requirements will then drive any necessary increases to a firm's capital.
- Firms must ensure that issued capital and proposed issuances are eligible as own funds under the IFR. This requires notification (in the case of existing issued capital) and prior approval from the FCA (in the case of new issuances).

Calculate your FOR (including the impact of consolidated group entities).

Assess the K-factors which are applicable to your firm's business.

Collate the data set inputs and design the operational build to calculate, monitor and report relevant K-factors and comply with your KFR.

Assess your firm's capital base, ensure capital is eligible for IFR, and plan necessary capital increases (noting the available transitional relief).

Impact

- Building the K-factor data methodology will be a material one-off undertaking for many firms, with some ongoing operational work to monitor and update the process. This also extends to the non-UK entities within scope of consolidation.
- SNIs are not required to calculate K-factors.
- For firms with substantial trading books and/or client trading facilitation activities, we expect that the K-factors will be the operative requirement and capital increases could be substantial for some.
- For firms providing advisory/management services, the FOR is likely to be the operative requirement.

Liquidity Requirements

ACTION 4: DETERMINE LIQUID ASSETS REQUIREMENT

Basic liquid asset requirement equal to one-third of the fixed overhead requirement plus 1.6% of any guarantees given to clients.

Core Assets. The FCA proposes a list of core liquid assets that FCA investment firms can use to meet the basic liquid assets requirement.

Any amount of the following can be used as core assets:

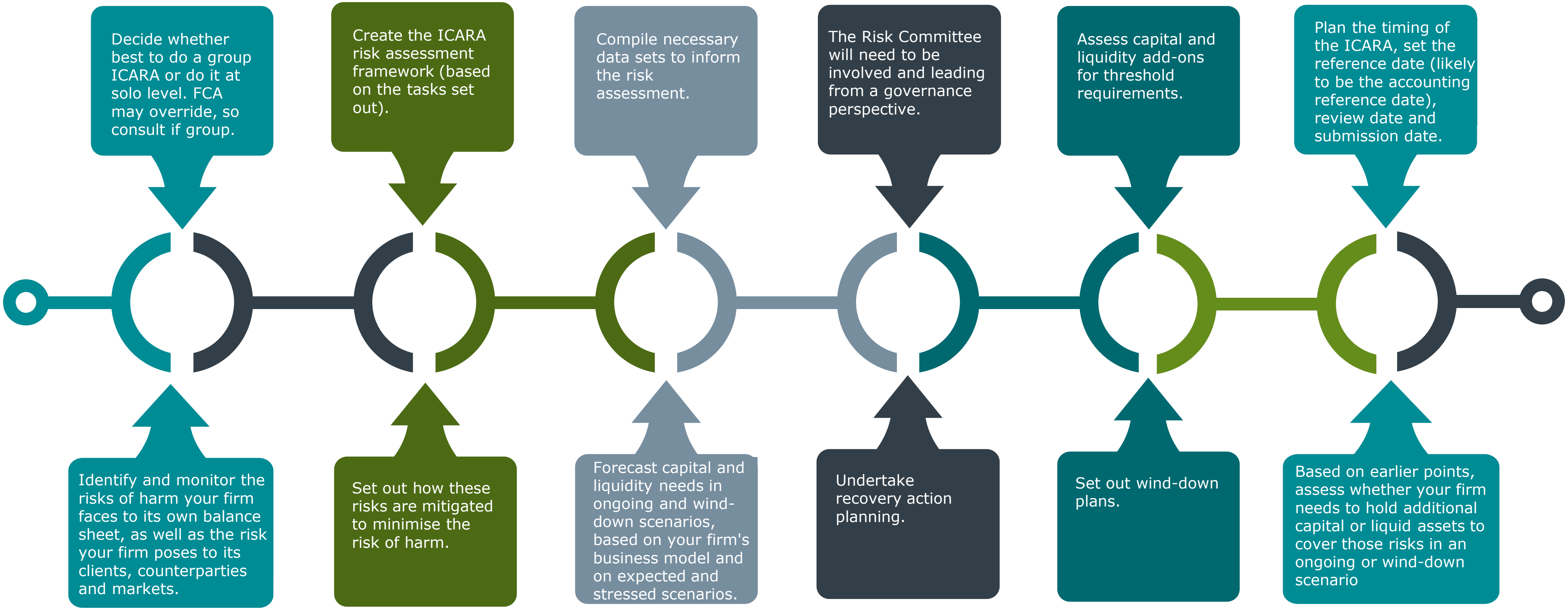
- coins and banknotes;
- short-term deposits at a UK bank;
- assets representing claims on or guaranteed by the UK government or the Bank of England (e.g. UK gilts and Treasury bonds); and
- units or shares in a short-term regulated money market fund, or in a comparable third country fund.

Impact

- Firms that are part of complex/international groups may need to consider the location of liquid assets, as overseas group entities may contribute to the FOR, but liquid assets held outside the UK will not count towards the liquid asset requirement.
- Firms may need to consider their group liquidity management/governance and available waivers.

ICARA

ACTION 5: CREATE ICARA PROCESS



IMPACT

- In assessing harms, firms need to take into account FCA’s finalised guidance (FG 20/1).
- Creating the ICARA framework and the required inputs will require material initial and ongoing work for most firms.
- Input will need to be coordinated from across the firm, and is not simply a Finance department exercise.
- The complexity of the ICARA will increase relative to the complexity of a firm’s activities and business model.
- Time is of the essence – in the absence of relief, firms with calendar-year reference dates will need to undertake their first ICARA in Q1-Q2 2022.

Governance

ACTION 6: ADJUST GOVERNANCE STRUCTURES

1

Large Non-SNI Firms must have:
- risk committee;
- remuneration committee; and
- nomination committee.

Generally at solo investment firm level (waivers available to allow group committees).

Committees must have at least 50% NED members (and chair should be a NED).

2

Regular Non-SNI Firms do not require the committees. They must observe high-level requirements:
- clear organisational structure;
- effective risk management processes; and
- adequate internal controls.

3

Remuneration: even if there is no remuneration committee, remuneration will be subject to considerable governance requirements:
- management body must regularly review the policy and oversee any implementation action;
- remuneration for control functions should be independently set; and
- remuneration must align risk and reward.

Impact

- Many firms (which were not significant IFPRU firms previously) will need to create committees for the first time and there will be extensive non-executive director recruitment in the industry.
- Firms should consider available governance waivers to avoid the need to duplicate committees and functions.

Remuneration

ACTION 7: REVIEW REMUNERATION POLICY AND ARRANGEMENTS

Identify your firm's classification and Remuneration Code

Basic

Review remuneration policy

Standard

- Review remuneration policy
- Map your firm's MRTs
- Implement changes to employment contracts and other remuneration arrangements
- Malus and clawback

Extended

- Review remuneration policy
- Map your firm's MRTs
- Implement changes to employment contracts and other remuneration arrangements
- Malus and clawback
- Deferral
- Payout instruments

Impact

- The most material impacts will be felt by larger Non-SNIs, which will potentially include operational work to facilitate payment in instruments (particularly for partnerships), significant employee communications and possibly various stakeholder consents.
- Some firms will have to consider various Remuneration Code(es), not just the IFPR Code and there may be international issues too.

Concentration Risk

ACTION 8: MONITOR AND CONTROL CONCENTRATION RISK

Assess all concentration risk items.

Create monitoring framework and prepare to report top five exposures quarterly (using MIF004):

- trading book exposures;
- non trading book assets;
- off balance sheet items;
- location of client assets/money; and
- source of earnings.

Consider waiver applications for any large intra-group exposures.

Trading Book Exposures

1. Monitor against the soft limit (25% of own funds).
2. Create methodology for exposure value to calculate K-CON when exceeding the soft limit (and consequent capital increase).
3. Monitor against the hard limits (500% or 600% of own funds).
4. Build FCA notification process in the event that the limits are exceeded.

Impact

- Change in methodology and data collation for all firms.
- Firms with trading book to consider concentration limits and projected impact for the first 18 months.

Reporting

ACTION 9: PREPARE FOR SINGLE SUITE OF FCA REPORTING FORMS

Quarterly	Annual
Capital (MIF001) • Includes capital held, FOR and K-factors • SNIs do not need to calculate K-factors	**ICARA Questionnaire (MIF007)**
Liquidity (MIF002)	**Remuneration Report (MIF008)** • Basic form for SNIs, more detail for larger firms
Monitoring metrics (MIF003) • The quantitative metrics relevant to the SNI thresholds	
GCT reporting (MIF006) • If using GCT	
Non-SNIs only	
Non-K-CON concentration risk (MIF004) • Regarding the location of a firm's client money and securities	
K-CON concentration risk where soft limit exceeded (MIF005) • Soft limit is 25% of own fund	

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Permissions & Notifications

ACTION 10: PREPARE REQUIRED PERMISSIONS & NOTIFICATIONS

Common waivers/permissions

- Exemption from liquidity requirements on a consolidated basis.
- Permission to apply the GCT to avoid consolidation.
- Permission to use advanced internal models for the calculation of K-NPR.
- Modification to risk committee, remuneration committee or nomination committee at group level rather than individual basis.
- Modification to the rule on pay-out in shares and other instruments to accommodate alternative arrangements.
- Permission to count CET1 items for an instrument not previously approved.

Common notifications

- Notification of ICARA reference date, review date and submission date for ICARA questionnaire (MIF007).
- Notification of issuance of additional capital instruments in a class that has already been approved as CET1 instruments.
- Notification of the intended reduction in own funds instruments where either of the conditions in MIFIDPRU 3.6.4R apply.
- Notification of the intention to issue AT1 or T2 instruments.

Impact

- Identify relevant items and plan for submission, including supporting materials, legal approvals and management approvals, where relevant.

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Key Contacts

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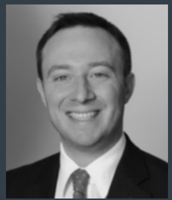

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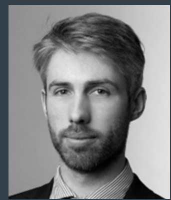

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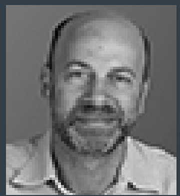

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Note: this briefing is for general guidance only and is not legal advice.