



Banc Ceannais na hÉireann
Central Bank of Ireland

Eurosystem

Feedback Statement - Consultation Paper 152: Own Funds Requirements for UCITS Management Companies and AIFMs authorised to provide discretionary portfolio management

November 2023

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1. Introduction

CP152 signalled the Central Bank of Ireland's (the "Central Bank") proposed approach to the own funds requirements for management companies authorised under Regulation 16(2) of the European Communities (Undertakings for Collective Investment in Transferable Securities) Regulations 2011 (the "UCITS Regulations") ("UCITS Management Companies") and for Alternative Investment Fund Managers authorised under Regulation 7(4) of the European Union (Alternative Investment Fund Managers) Regulations 2013 (the "AIFM Regulations") ("AIFMs") to perform discretionary portfolio management and provide additional non-core services under those regulations respectively (hereafter UCITS Management Companies and AIFMs).

Stakeholders were invited to provide observations and comments on these proposals. The closing date for comments was 23 February 2023 and five responses were received. The Central Bank is grateful for the time and effort of the parties that responded to the consultation. Their responses to the consultation are available at the following address:

<https://www.centralbank.ie/publication/consultation-papers>

Having considered the submissions received, the Central Bank has taken notice of comments provided and key points of concern identified and provided further guidance, where necessary.

The Central Bank has revised the own funds requirements for UCITS Management Companies and AIFMs set out in CP152 to take account of minor amendments as set out in this statement.

As per Central Bank (Supervision and Enforcement) Act 2013 (Section 48(1)) (Undertakings for Collective Investment in Transferable Securities) (Amendment) Regulations 2023 (S.I. No. 565 of 2023) the new requirements will not apply to UCITS Management Companies authorised on or before 27 November 2023 until 27 May 2024.

The new requirements for AIFMs are included in Part B of Chapter 3, Alternative Investment Fund Manager Requirements, in the AIF Rulebook. The new requirements will not apply to AIFMs authorised on or before 27 November 2023 until 27 May 2024.

For the avoidance of doubt, the current condition of authorisation continues to apply to all relevant UCITS Management Companies and AIFMs authorised on or before 27 November 2023 pending the application of the new own funds requirements.

UCITS Management Companies and AIFMs which obtain authorisation after 27 November 2023 will be subject to these new requirements upon authorisation.

A copy of the updated Minimum Capital Report (MCR) is available on the Central Bank's website.

**Financial Risks and Governance Division
Central Bank of Ireland
27 November 2023**

2. General Response

In general respondents commented that it was difficult to respond to CP152 and provide commentary given the lack of detail in relation to the impact of the proposal. Respondents requested more detail on what harm the proposal seeks to address, the number of firms affected and the cost to them of the change.

Central Bank Feedback:

The Central Bank notes the general response received.

The proposal set out in CP152 sought to ensure that UCITS Management Companies and AIFMs operate on a sound financial basis relative to the services they provide and the resulting risks incurred. The Central Bank aims, in the policy decisions it makes, to balance the costs for authorised entities associated with any new regulatory requirement with the benefits arising from the application of appropriate and proportionate requirements.

The new requirements represent an amendment to the additional capital requirement currently imposed on UCITS Management Companies and AIFMs and seeks to retain a level playing field between UCITS Management Companies and AIFMs and investment firms authorised to provide discretionary portfolio management services under the MiFID II Regulations (S.I. No. 375 of 2017)¹.

The Risk to Client K-factors are proxies covering the business areas of UCITS Management Companies or AIFMs from which harm to clients could conceivably arise. Specifically K-AUM, the K-factor of most relevance, captures the potential risk to clients of incorrect discretionary management of client portfolios and provides reassurance and benefits to clients in terms of continuity of service of ongoing portfolio management and, where relevant, investment advice.

The Central Bank acknowledges that the new requirements will result in an initial operational cost for UCITS Management Companies and AIFMs in the development of systems and processes to allow for compliance with the new requirements.

However, the Central Bank considers that the new requirements represent a more proportionate prudential regime for UCITS Management Companies and AIFMs, which, once

¹ European Union (Markets in Financial Instruments) Regulations 2017 (S.I. No. 375 of 2017).

implemented, should result in a reduction in the on-going operational and regulatory costs for UCITS Management Companies and AIFMs:

- (i) UCITS Management Companies and AIFMs will no longer be subject to the current condition of authorisation requiring them to comply with the own funds requirements in Regulation 18(2) of the European Communities (Capital Adequacy of Investment Firms) Regulations 2006 (S.I. No. 660 of 2006) (“CRD III”).
- (ii) UCITS Management Companies and AIFMs that will be classified as small and non-interconnected will only be required to calculate the own funds requirements set out in the AIFM Regulations or UCITS Regulations, as applicable.
- (iii) UCITS Management Companies and AIFMs that do not meet the conditions to be classified as small and non-interconnected will be required to calculate a Risk to Client K-factor own funds requirement. This calculation is a more simplified and appropriate calculation relative to the requirements in Regulation 18(2) of CRD III, thereby reducing the administrative burden on impacted UCITS Management Companies and AIFMs.

The extent to which a UCITS Management Company or AIFM will be required to hold additional own funds going forward will depend on:

- (i) the level of assets under discretionary portfolio management held; and
- (ii) the level of net qualifying expenditure incurred.

3. Specific Responses

Proposal to update the Own Funds Requirements

Question 1:

Do you agree with the proposal to update the own funds requirements applicable to UCITS Management Companies and AIFMs given the application of the IFR² to MiFID portfolio managers?

Response:

Two respondents considered the proposal as reasonable and proportionate as it will ensure regulatory and prudential alignment for entities conducting MiFID type activities and will simplify the ICAAP return process. However, one of these respondents queried the extent to which the Central Bank has carefully considered the costs and benefits (to both firms and clients) of increasing the regulatory overhead for firms that are not systemically important.

One respondent, while supportive of ensuring a level playing field and reducing complexity, considered the proposal could reduce the desired simplicity and standardisation of requirements. Additionally concerns were identified regarding the introduction of a new regime in advance of an EU-wide approach, with one respondent stating that this could potentially impose an undue cost on investors. Two respondents considered that the current requirements are sufficient to address the risks arising from the services provided by UCITS Management Companies and AIFMs.

One respondent called for a harmonisation of other inconsistencies between the own funds regime applicable to investment firms authorised under MiFID and that applicable to UCITS Management Companies and AIFMs in relation to 'eligible assets' and the higher liquidity requirements applicable to UCITS Management Companies and AIFMs relative to MiFID investment firms. This respondent also called for the Central Bank to engage and consult with industry to develop a guidance note in relation to the interpretation and implementation of the new requirements and for a 12-month implementation period prior to the application of the new requirements.

² Regulation (EU) No. 2019/2033 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 27 November 2019 on the prudential requirements of investment firms and amending Regulations (EU) No 1093/2010, (EU) No 575/2013, (EU) No 600/2014 and (EU) No 806/2014).

One respondent was unable to agree with this proposal stating that it appeared to impose an un-specified level of cost on an unquantified number of AIFMs and UCITS Management Companies.

Central Bank Feedback:

The proposal set out in CP 152 represents an amendment of the own funds requirements on UCITS Management Companies and AIFMs. UCITS Management Companies and AIFMs will no longer be subject to a condition of authorisation requiring them to comply with the own funds requirements set out in CRD III which do not fully address the specific risks inherent to the provision of portfolio management and other non-core services by UCITS Management Companies and AIFMs.

UCITS Management Companies and AIFMs that meet the conditions to be classified a “small and non-interconnected firm” will not be required to calculate any additional own funds requirement in excess of that applicable under the UCITS Regulations or the AIFM Regulations, as applicable. For the remaining UCITS Management Companies and AIFMs, the calculation of the K-AUM, which is expected to be the K-factor most relevant to this cohort of UCITS Management Companies and AIFMs, is a more streamlined calculation relative to the own funds requirements applicable under CRD III. Therefore, once implemented, the Central Bank expects the new requirements to result in a reduction in the operational and regulatory burden on UCITS Management Companies and AIFMs.

The Central Bank recognises that UCITS Management Companies and AIFMs will require time to prepare for the application of the new own funds requirements. Therefore, the new requirements will not apply to UCITS Management Companies or AIFMs authorised on or before 27 November 2023 until 27 May 2024.

UCITS Management Companies and AIFMs which obtain authorisation after 27 November 2023 will be subject to these requirements upon authorisation.

The Central Bank will continue to work with our domestic and EU colleagues to progress the development of an EU wide solution to address risks relating to the provision of discretionary portfolio services and related non-core services by UCITS Management Companies and AIFMs on a consistent EU-wide basis.

The amendment of the liquidity requirements applicable to all UCITS Management Companies and AIFMs, including the amendment of the definition of “eligible assets”, is beyond the scope of this consultation.

Any individual firm-specific risks that remain post the introduction of these requirements will continue to be dealt with through the ICAAP and SREP process.

The development of a guidance note is beyond the scope of the current consultation. UCITS Management Companies' and AIFMs' attention is directed to the [relevant documents produced by the EBA](#) and to relevant [EBA Q&As](#).

Section I: Calculation of the Risk to Client K-factor Requirement

Question 2:

Do you agree with the manner in which the Risk to Client K-factors are to be calculated and that the Risk to Client K-factor requirement is not subject to a limit?

Response:

In general, respondents agreed with the manner in which the Central Bank proposed to calculate the Risk to Client K-factors.

However, one respondent called for clear and measurable guidelines on what constitutes a material change in the business model. Additionally the respondent sought guidance on the scope of AUM to be included and on relevant definitions. Clarification was also sought as to why K-COH is only applicable to AIFMs.

Two respondents called for the use of net asset values in the calculation of the AUM and stated that gross values would not generally be available. However, one respondent stated the use of gross values would standardise calculations for firms undertaking MiFID activities.

Concerns were also raised regarding the uncapped nature of the proposed calculation.

One respondent requested clarification on the coefficient to be used in the calculation of K-COH for cash trades.

Central Bank Feedback:

The calculation of the K-factor own funds requirement proposed in CP152 mirrored the manner in which the Risk to Client K-factors are calculated under the IFR. [Commission Delegated Regulation \(EU\) No. 2022/25³](#), specifying the methods for measuring the K-factors under the IFR regime, requires the use of absolute values notwithstanding similar feedback to [the relevant EBA consultation](#) calling for the use of gross values. Therefore, in the interest of ensuring a level playing field between two cohorts of firms providing similar services, absolute values are used in the determination of the K-AUM additional own funds requirement.

Similarly, given that no limit applies to the own funds requirement applicable to MiFID investment firms, the introduction of a limit on the K-factor own funds requirement for UCITS

³ Commission Delegated Regulation (EU) 2022/25 of 22 September 2021 supplementing Regulation (EU) 2019/2033 of the European Parliament and of the Council with regard to regulatory technical standards specifying the methods for measuring the K-factors referred to in Article 15 of that Regulation.

Management Companies and AIFMs would lead to an un-level playing field vis-à-vis MiFID investment firms. Therefore, the Central Bank has not introduced such a limit.

The Central Bank considers that provision of domestic guidance or clarifications could give rise to a risk of divergence of application of the own funds requirements between the two cohorts of firms. Therefore, the Central Bank does not propose to develop additional bespoke guidance for UCITS Management Companies and AIFMs and impacted firms' attention is directed to relevant EBA publications.

K-COH only applies where a firm is authorised to receive and transmit or execute transactions. Only AIFMs can be authorised for the provision of such services.

The coefficient for the calculation of K-COH for cash trades has been amended to 0.1%.

Section II: Transitional Arrangements

Question 3: Do you agree that UCITS Management Companies and AIFMs should be able to benefit from transitional arrangements up to the period ending 30 June 2026?

Response:

In general, respondents agreed that UCITS Management Companies and AIFMs should be able to benefit from transitional arrangements up to end June 2026 to facilitate the transition between the two methodologies. However, one respondent noted that firms are concerned that the adoption of the new methodology may become a cumbersome process for them going forward.

Another respondent called for a transitional arrangement with regard to the K-factor metrics such that a firm does not need to rely on data relating to a period in advance of issuance of CP152. Another respondent called for a longer transitional period given the burden that compliance with IFR entails.

Additionally clarification was requested on the proposed implementation date for the requirements with an implementation period of at least 12 months sought by one respondent to allow firms to update their internal reporting procedures and IT systems and/or to engage with board and shareholders to arrange receipt of any additional capital required. One respondent called out that, as the approach is not consistent with that applying to similarly regulated firms in other EU Member States, firms will not be able to avail of group IT initiatives and will have to seek additional budget approval to develop Ireland-specific processes and reports.

Two respondents requested additional clarity on the calculation of the fixed overhead requirement.

Central Bank Feedback:

CP 152 set out the Central Bank's intention to mirror the transitional arrangements for MiFID portfolio managers as set out in Article 57(3) of the IFR. Therefore any increase in own funds arising from the application of the new requirements is limited to twice the fixed overhead requirement until 26 June 2026.

The Central Bank notes that in general respondents agreed with this proposal although there was a concern raised regarding the need for adequate time to develop new systems and processes.

The Central Bank recognises the need for UCITS Management Companies and AIFMs to be given adequate time to develop systems, policies and processes. Therefore, as set out above, the new requirements will not apply to UCITS Management Companies or AIFMs authorised on or before 27 November 2023 until 27 May 2024.

However UCITS Management Companies and AIFMs which obtain authorisation after 27 November 2023 will be subject to these requirements upon authorisation.

A clarification has been added to the new requirements to ensure that, notwithstanding these transitional arrangements, the own funds held by UCITS Management Companies and AIFMs can never be less than that required under the UCITS Regulations or AIFM Regulations, as relevant.

Given this implementation period the need for a transitional period relating to the collection of data to support the calculation of the K-factors does not arise.

The calculation of the Fixed Overhead Requirement by UCITS Management Companies and AIFMs is dealt with Under Section III Reporting, below.

Section III: Reporting

Question 4: Do you agree that

- a) the frequency of submission of the Minimum Capital Requirement Report should remain as that currently in place; and
- b) the format of the Minimum Capital Requirement Report should be amended to allow for reporting of compliance with the updated own funds requirements?

Response

All respondents agreed that the frequency of reporting should remain as that currently in place and that the Minimum Capital Requirement Report should be amended to allow for reporting of compliance with the updated own funds requirements. However, one respondent raised operating and efficiency challenges arising from the application of different reporting cycles to different entity types within the same financial group.

Additionally one respondent called for clarification regarding which fixed overhead requirement calculation should be used in the Minimum Capital Requirement Report.

It was also noted that it is difficult to quantify the cost of compliance and the time it will take to amend systems until such time as the final reporting template has been shared with industry.

While agreeing with the proposal in the consultation paper one respondent called for a review of other reporting requirements to remove any overlapping reporting requirements that may become redundant once this new reporting comes into effect. This respondent also called for a comprehensive testing regime for the reporting system to ensure the system is both efficient and resilient for firms.

Central Bank Feedback

CP152 set out the Central Bank's intention to require UCITS Management Companies and AIFMs to continue to submit a Minimum Capital Requirement Report (MCR), amended to allow for reporting of compliance with the updated own funds requirements, on the same frequency as that currently in place.

While the Central Bank recognises the operational and efficiency challenges arising where financial groups comprised of firms regulated under different regimes are subject to two different reporting cycles the new requirements do not give rise to new challenges in this regard.

The Central Bank notes that, as per Regulation 17(6) of the UCITS Regulations (as amended) and Regulation 10(5) of the AIFM Regulations (as amended) the own funds of a UCITS Management Company and AIFM respectively shall never be less than the amount prescribed in Article 13 of the IFR, the Fixed Overhead Requirement. Therefore, all UCITS Management Companies and AIFMs are required to comply with the IFR Fixed Overhead Requirement.

The Minimum Capital Report (MCR) has been amended to reflect the Fixed Overhead Requirement (FOR) set out in Article 13 of the IFR. A copy of this MCR is available on the Central Bank website and will be applicable for all UCITS Management Companies and AIFMs, including those not authorised to provide discretionary portfolio management services, from 27 May 2024.

The Central Bank recognises that UCITS Management Companies and AIFMs will need time to amend systems and implement the new reporting requirements including associated testing. As set out above, the new requirements will not apply to UCITS Management Companies or AIFMs authorised on or before 27 November 2023 until 27 May 2024.

A review of other reporting requirements is out of scope of the current consultation.

Section IV: Requirement to perform an assessment of internal capital

Question 5: Do you agree that the requirement to undertake an assessment of internal capital be set out in the Central Bank UCITS Regulations and the AIF Rulebook?

Response

Overall respondents agreed with this proposal.

However, one respondent called for the assessment of internal capital (“ICAAP”) only to be applied to “non-small and non-interconnected” firms and for firms that are part of a group producing a consolidated ICAAP to be exempt from the requirement. Another respondent noted that the requirement to produce an ICAAP goes beyond the EU requirements and requested further engagement with the Central Bank to understand the rationale for the requirement. It was also stated that the introduction of an either/or approach for the own funds requirement could subject firms to constant flux in assessing the additional risks not covered by the base requirement.

A query was raised regarding proposed changes to the ICAAP questionnaire and further guidance on how firms will undertake an ICAAP was requested.

Finally, one respondent considered that the requirement for AIFMs should sit in Part 2 of Paragraph 10 of the AIFM Regulations.

Central Bank Feedback

CP152 relates to the manner in which the requirement to undertake an ICAAP is imposed on UCITS Management Companies and AIFMs and aims to ensure that current and future UCITS Management Companies and AIFMs will undertake this ICAAP in a consistent and comparable manner.

Therefore, the rationale and scope of the requirement to undertake an ICAAP and the development of associated guidance is beyond the remit of the current consultation.

A copy of the updated ICAAP questionnaire is available on the Central Bank website.

The Central Bank notes the concern that the either/or approach may result in a fluctuation in assessing additional risks. However, given that the K-factor is based on rolling average over 15 months (excluding the last 3 months) it is not expected that this will fluctuate excessively.

The Central Bank is not empowered to amend the AIFM Regulations.



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