Thistle Initiatives

Guiding you through compliance

Are you complying with the Investment Firms Prudential Regime (IFPR)?

The Investment Firms Prudential Regime (IFPR) introduced a single prudential regime for all MiFID investment firms regulated by the FCA. IFPR established a risk-based approach that focuses on capturing any risks arising from the firm's activities that could pose threats to its clients and the markets in which it operates. The regime represented a major change for these firms and the FCA considered it critical that firms adequately prepared for the regime, which came into force on 1 January 2022.

BIPRU
IFPRU
Exempt CAD

SNI (small non-inter-connected) or non-SNI

The MiFID firm types BIPRU, IFPRU and exempt CAD, have ceased to exist and all MiFID firms are now categorised as either SNI (small and non-interconnected) firms or as non-SNI, depending on the regulatory activities they carry out and the financial thresholds they meet.

Categorisation of firms

There is a series of permission-based and quantitative thresholds for firms to determine whether they are an SNI or non-SNI firm. Firms with permission to deal on own account or to carry out underwriting and/or placing on a firm commitment basis cannot be an SNI. The quantitative thresholds are below:

Quantitative criteria for being an SNI	
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
Average daily trading flow – cash trades	Zero
Average daily trading flow – derivative trades	Zero
On-and off-balance sheet total	< £100 million
Total annual gross revenue from investment services and activities	< £30 million

These thresholds, except the on- and off-balance sheet total, only relate to the MiFID activities undertaken by the firm. A firm may manage assets without undertaking portfolio management or ongoing investment advice under MiFID or holding client money or client assets in relation to non-MiFID activities. These should be excluded from the threshold measurement.

Own funds requirement

SNI	Non-SNI
Higher of:	**Higher of:**
Permanent minimum requirement (PMR)	Permanent minimum requirement (PMR)
Fixed overhead requirement (FOR)	Fixed overhead requirement (FOR)
	K-factor requirement (KFR)

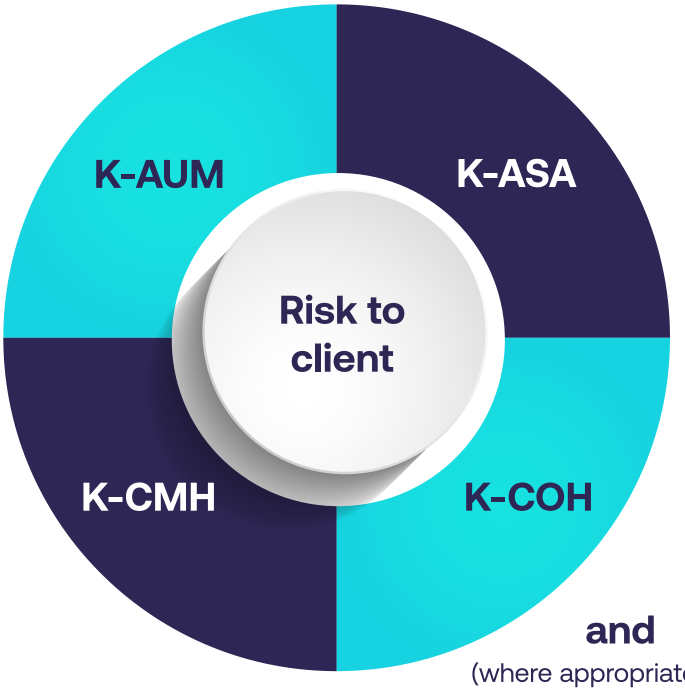
Own funds threshold requirement

SNI and Non-SNI
Higher of:
Own funds requirement
Own funds to mitigate the risk for ongoing operations
Own funds for orderly wind-down

PMR is the minimum capital requirement applicable to each firm based on its permission profile.

PMR	£75,000	£150,000	£750,000
MiFID activities undertaken	Reception and transmission of orders Execution of orders on behalf of clients Portfolio management Investment advice Placing without a firm commitment basis	All other investment firms	Dealing on own account Underwriting and/or placing on a firm commitment basis Operating an OTF without a limitation that prevents matched principal trading and dealing on own account

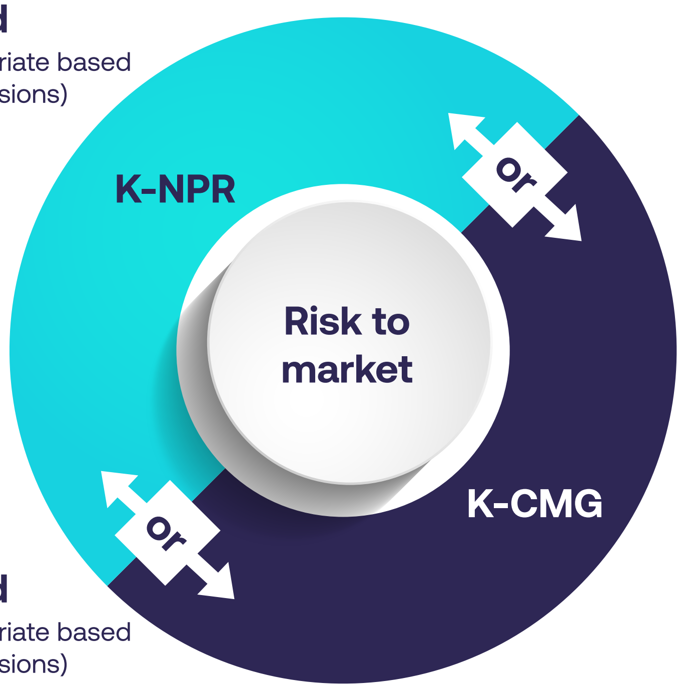
K-factors



Sum of:

K-AUM - Assets Under Discretionary/Advisory Management
K-ASA - Client Assets Safeguarded and Administered
K-CMH - Client Money Held
K-COH - Client Orders Handled

and
(where appropriate based on permissions)



Either:

K-NPR - Net Position Risk; or
K-CMG - Clearing Margin Given

and
(where appropriate based on permissions)

Sum of:

K-TCD - Exposure to Trading Counterparties Default
K-CON - Concentration risk based on large exposures to specific counterparties
K-DTF - Operational risks from Daily Trading Flow

K-factors explained

K-AUM

K-factor requirement for the amount of own funds investment firms are required to hold against risks associated with managing assets for clients. It covers both assets managed on a discretionary portfolio management basis and assets under an ongoing non-discretionary advisory arrangement.

K-ASA

K-factor own funds requirement assigned against the risk of harm associated with the safeguarding and administering of a client's financial instruments.

K-CMH

K-factor own funds requirement for the amount of client money an investment firm may hold.

K-COH

K-factor own funds requirement designed to cover potential risks from both the execution of orders in the name of the client and the reception and transmission of client orders.

K-NPR

Value of transactions recorded in firm's trading book or which give rise to foreign exchange or commodities risk.

K-CMG

Only applies to investment firms that deal on own account and is an alternative to K-NPR to provide for market risk, that builds upon the systemic resilience created by EMIR and use of a clearing member.

K-TCD

K-factor own funds requirement that aims to capture risks from trading counterparties failing to meet their obligations to the investment firm.

K-CON

Is a further own funds requirement that only applies to exposures in the trading book for investment firms that deal on own account.

K-DTF

Is designed to capture operational risks related to the value of trading activity an investment firm conducts in its own name either for itself or on behalf of a client throughout each business day.

Matched principal trading

There is no matched principal exemption under IFPR, so former €50,000 matched principal brokers will move to a PMR of £750,000 (over five years). While there is no longer the benefit of a lower capital requirement, the FCA believes it is helpful for such firms to 'limit' their activity of dealing in investments as principal, in order to clarify how they trade and to demonstrate they are a lower risk principal dealer.

Fixed overheads requirement	¼ of the firm's relevant expenditure in the previous year

The FOR is intended to determine the level of own funds a firm needs to have (its 'own funds requirement'). It is an amount equal to one quarter of the firm's relevant expenditure during the preceding year. Ensuring a firm has own funds reflecting at least its FOR plays an important role in making sure it can exit the market in an orderly way.

Basic liquid assets requirement

Under IFPR, all investment firms are to hold liquid assets equal to at least one-third of their FOR (plus, if relevant, 1.6% of the total amount of any guarantees provided to clients). This is based on meeting at least one month's overheads, with the FOR representing three months' overheads.

The FCA expects firms to satisfy their basic liquid assets requirements using a specified list of "core liquid assets," including (but not limited to) cash, units or shares in short-term regulated money market funds and short-term deposits at UK credit institutions. Such assets are expected to be held by (i.e. in the name of) the relevant FCA investment firm.

In its second IFPR policy statement, the FCA clarified that where a firm benefits from transitional relief limiting its FOR, it will also have its basic liquid assets requirement correspondingly reduced. For a former exempt CAD firm, this means the basic liquid assets requirement is equal to its transitional PMR in the first year, and 1/3 of the reduced FOR (10%) in year two (see next section for the transitional provisions).

Liquid assets threshold requirement

A firm's basic liquid assets requirement provides a minimum level of core liquid assets that the firm must maintain at all times. The basic liquid assets requirement may, however, be insufficient to provide the liquid assets that the firm has assessed would be necessary. Therefore, the firm may identify that it needs to hold an additional amount of liquid assets, which becomes the liquid assets threshold requirement.

The liquid assets threshold requirement is the sum of the basic liquid asset requirement ('BLAR') and the higher of the liquid assets required from the following assessments: (a) to fund ongoing business operations during each quarter over the next 12 months or (b) to ensure the firm can be wound down in an orderly manner.

Transitional arrangements

Transitional provisions (TPs) are available to help investment firms adjust to the minimum capital requirements of the IFPR.

The table below demonstrates how the base capital requirement increases gradually for firms that, after the commencement of IFPR, had a PMR of £75,000.

Timeline	BIPRU / IFPRU €50K – PMR/FOR	Exempt CAD - PMR/FOR
Before 1 January 2022	The greater of €50,000 or the FOR	€50,000 (or at least £5k + PII)
Year 1	The greater of £50,000 or the FOR	£50,000
Year 2	The greater of £55,000 or the FOR	The greater of £55,000 or 10% of the FOR
Year 3	The greater of £60,000 or the FOR	The greater of £60,000 or 25% of the FOR
Year 4	The greater of £65,000 or the FOR	The greater of £65,000 or 45% of the FOR
Year 5	The greater of £70,000 or the FOR	The greater of £70,000 or 70% of the FOR

On 1 January 2027, five years after MIFIDPRU began to apply, the transitional period will be over and the capital requirement, for SNI firms, will be the greater of the PMR of £75,000 and the FOR. Transitional provisions also apply to former BIPRU and IFPRU €50k Matched Principal firms and IFPRU €125k and €730k firms.

Note: There is no transitional relief with regard to the ICARA requirements, so in practice, firms may be required to hold capital in excess of that required under the transitional provisions.

Exempt CAD

The exempt CAD category disappeared under the IFPR and, if these firms plan to remain as MiFID firms, they will need to consider key issues including:

- Increase in capital requirements
- Need to calculate variable capital such as the FOR [and in some cases K-factors also]
- Whether they will be in a consolidation group
- Requirement to produce a risk-based capital assessment, known as an ICARA
- Being subject to the Remuneration Code for the first time

Former exempt CAD firms may well wish to review whether they need to remain a MiFID firm and, if not, whether they will be able to, or will wish to, opt out of MiFID via a Variation of Permission.

ICARA

All MiFID investment firms are required to establish an ICARA process. The ICARA process replaces the ICAAP that BIPRU and IFPRU firms were required to carry out, and includes recovery planning and wind-down planning.

The IFPR introduced an overall financial adequacy rule (OFAR) designed to determine whether a firm has sufficient financial resources to fund its operations. Through the ICARA process, firms will determine what level of own funds and liquid assets they need to maintain to meet their regulatory requirements.

The ICARA process is designed to allow a firm to identify, monitor, and, if relevant, mitigate all material potential harms that could result from a) ongoing operations or b) winding down of its business.

Frequency: A firm must review the adequacy of its ICARA process at least once every 12 months, and also following any material change in the firm's business model or operating model.

The FCA has confirmed that an investment firm group will not normally be required to operate an ICARA process on a consolidated basis, even if the group is subject to prudential consolidation under MIFIDPRU.

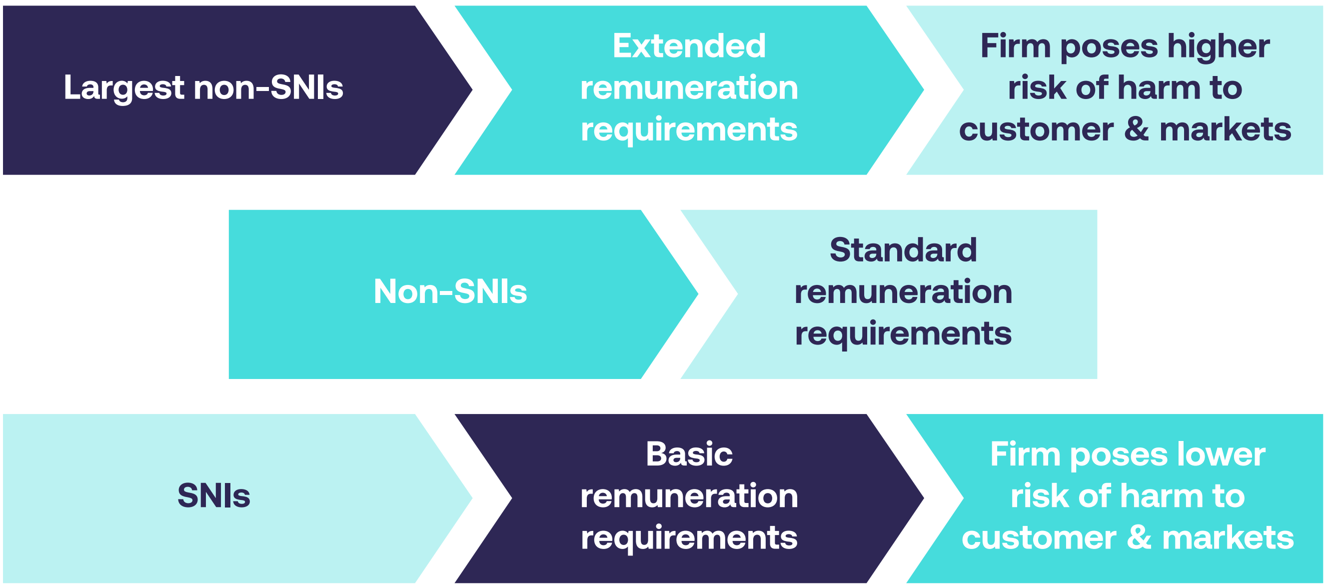
Remuneration

The FCA has removed the IFPRU and BIPRU Remuneration Codes and replaced them with Basic, Standard and Extended requirements under the MIFIDPRU Remuneration Code.

Former exempt CAD firms are caught by a remuneration code for the first time. Basic remuneration requirements include:

- A remuneration policy to cover all staff
- Responsibility of the management body for overseeing its implementation
- Fixed and variable components of remuneration must be appropriately balanced
- Variable pay must not affect the firm's ability to ensure a sound capital base

Overview of application of remuneration requirements



Get in touch

We've already supported hundreds of firms to understand and navigate the IFPR regime, and we continue to assist those with work still to do – or who simply want to verify they've got it right.

020 7436 0630 | info@thistleinitiatives.co.uk

Part of the Thistle Group