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WORKING PAPER

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WORKING DOCUMENT

From:	DE and CZ delegations
To:	Working party on Financial Services (IFS)
Subject:	Technical issues to help clarify the application and ease the burden of the classification requirements (between class 2 and class 3)

DE - CZ NON-PAPER

Technical issues to help clarify the application and ease the burden of the classification requirements (between class 2 and class 3).

The purpose of this non-paper is to set out a series of proposed technical amendments that:

- align the IFR and IFD classification rules;
- reduce the frequency and impact of firms swinging from one class (2,3) to another (in either direction); and
- facilitate first application of K-Factor based capital requirements (when a firm moves into class 2).

While recognizing that a different (i.e. longer) deferral period may be required for an investment firm to prepare to comply with any additional requirements of the IFD (e.g. more governance or remuneration arrangements) when it moves from class 3 into class 2, in order to clarify and reduce complexity, the determination of when this occurs under Art 23 of IFD should, as far as possible be aligned with that in Art 12 of the IFR.

The requirements should be clear, appropriate and proportionate both in respect of firms moving up from class 3 to class 2 and for firms moving down from class 2 to class 3. They should allow for any such change to be more 'permanent' rather than either burden a firm or release it too soon from existing (class 2) requirements where any 'switch' might be only temporary or accidental. This requires some use of averaging. Some minor technical changes are also made to Art. 12 IFR to provide for more practical application.

Some related changes are also proposed under Arts. 17(3), 18(2), 19(2), 20(3) and 32(4) of IFR for the calculation of the relevant K-factors, to clarify what to do where a firm may not yet hold sufficient historical data (whether a new entrant growing rapidly, or for the non-zero thresholds an existing class 3 firm growing more steadily).

It is proposed that the additional clarity provided by these changes would remove the need for the Level 2 measures in the original Commission proposal.

Finally, some minor clarifications are made to the definitions in Art. 4 of IFR, as it is more appropriate here to use the text to define the metrics AUM, CMH etc. themselves, rather than the K-factors K-AUM, K-CMH etc. which are defined in Title II of Part Three of IFR.

One option, which is not covered in this paper, is the increase in the period for the calculation of K-COH, referring to each business day over the previous 6 calendar months, by applying to each business day over the previous 9 calendar months, excluding the 3 most recent calendar months. This would reduce cyclicity from the thresholds between Class 2 and Class 3 firms and the calculation of K-factors. For consistency, if chosen, this change should also apply to K-DTF (eventhough this has a zero threshold for the purpose of classification).

However, if the application of Section 2 of Chapter 2 IFD was revisited in order to apply governance requirements to all firms (proportionate and consistent with MiFID) and the

details on the assessment of risks, the drafting of Article 23 IFD could be further simplified, including the merger of paragraphs 3 and 3a of this Article.

The following pages identify proposed drafting suggestions, in double underline and double ~~strike-through~~. [Highlighted in yellow] are the comments regarding each of the proposed changes.

For completeness, the drafting also incorporates any relevant changes to these Articles from the joint CZ-DE-UK non-paper that was discussed at the June CWG meeting; such changes are shown in green (single underline and strike-through) and without repeating the justifications that can be found in the June CWG agenda paper.

Article 23 [IFD – Internal governance etc.]
~~Assessment~~Scope for the purposes of the application of this Section

1. ~~For the purposes of this Section, Member States shall ensure that investment firms assess, on an annual basis, and in accordance with points (a) and (b), whether they meet the conditions set out in Article 12(1) of [Regulation (EU) ---/---[IFR];~~ [IFD should rely upon the calculation technique of Art. 12 IFR. It should be avoided that firms are at the same time class 2 and class 3 (under IFD against IFR or vice versa), which would lead to additional complexity for firms and supervisors. As firms are expected to know in which class they fall, there is also no room for any additional legal measures by Member States.]
 - ~~(a) an investment firm shall determine whether, based on the figures from the two year period immediately preceding a given financial year, it satisfies the conditions set out in points (c) to (g) of Article 12(1) of [Regulation (EU) ---/---[IFR];~~
 - [The purpose of such a calculation is unclear: every amount above zero will, regardless of the averaging period, still be above zero. Effectively this provision would only hold firms crossing zero thresholds (possibly even by mistake) in class 2 for two years. This has a more retaining effect than the 6 months waiting period under IFR.]
 - ~~(b) an investment firm shall determine whether, based on the figures from that same period, it exceeds on average the limits laid down in points (a), (b), (h) and (i) of Article 12 (1) of [Regulation (EU) ---/---[IFR];~~ [The idea of averaging positive values for AUM and COH should be transferred to Art. 12 IFR, as should average revenues. There is no significant merit in averaging balance sheet size or annual gross revenue (as firms have possibilities of window-dressing anyway).]
2. This Section shall not apply where, on the basis of ~~the assessment referred to in paragraph 1~~Article 12(1) of [Regulation (EU) ---/---[IFR], an investment firm determines that it meets all of the conditions set out in Article 12(1) of [Regulation (EU) ---/---[IFR] therein.

2a. Where an investment firm which has not met all of the conditions set out in Article 12(1) of [Regulation (EU) ---/---[IFR] subsequently meets those conditions, this Section shall only cease to apply after a period of 6 months from the date when those conditions are met.

3. ~~Where An investment firm that, on the basis of the assessment referred to in paragraph 1, determines that it does not longer meets all of the conditions set out in Article 12(1) of [Regulation (EU) ---/---[IFR], it shall comply with this Section as of the financial year following the financial year in which that assessment took place.~~

[There may be no 'correct' or single answer as to how much time will be needed by a class 3 firm to make arrangements to fulfil the additional requirements of IFD that apply to a class 2 firm; a year may be too generous for governance arrangements and at the same time at least that period may be required to change staff contracts to comply with any additional remuneration rules. But there may be good reason to apply a different deferral period in IFD than in IFR and on balance a year seems appropriate. However, as the change in class could be triggered by any of the thresholds in Art. 12 of IFR, and 'the financial year following the financial year' could lead to different periods, for consistency and clarity firms should be given up to '12 months' (i.e. 'within 12 months') from the date of assessment.]

3a. By way of derogation from paragraph [3], Member States shall require investment firms to apply the provisions laid down in Article 30 to remuneration awarded for services provided or performance ~~following~~ of the financial year of following the financial year in which the determination referred to in paragraph takes place [2].

[**This is simply moving Art. 30(5) forward** in order to have all deferral rules for the IFD here in one place. In this instance it is appropriate to keep reference to financial year. However, the text is also amended to provide more clarity.]

4. Where this Section applies, Member States shall ensure that ~~this Section~~ it is applied to investment firms on an individual basis and at group level.

[Provides more clarity.]

Where Article 8 of [Regulation (EU) ---/---[IFR] is applied, Member States shall ensure that ~~investment firms subject to this Section~~ the Union parent undertaking implements the requirements of this Section in their subsidiaries that are financial institutions as defined in Article 4(13) of [Regulation (EU) ---/---[IFR] ~~all group entities that are included within the scope of the K-factor consolidation, including those established in third countries, unless the parent undertaking in the Union can demonstrate to the competent authorities that the application of this Section is unlawful under the laws of the third country where those subsidiaries are established.~~

[It is disproportionate that a class 3 firm may find itself indirectly subject to the requirements of this section only in regard of its parent company. Instead group entities other than class 2 investment firms should only be caught where a K-factor consolidation is applied under Art. 8 of IFR.]

5. ~~Competent authorities may set a shorter period than the two years referred in paragraph 1 of this Article where both of the following conditions are met:~~

~~(a) the business of the investment firm has been subject to a material change; and~~

~~(b) as a result of point (a), the investment firm meets the conditions set out in Article 12(1) of [Regulation (EU) / [IFR].~~

[Competent authority discretion is not seen as necessary in light of the fact that the calculation/waiting period will be set to shorter than 2 years. Therefore any effect of a shrunken business size will become effective at an earlier point in time anyway.]

6. ~~EBA, in consultation with ESMA, shall develop draft regulatory technical standards to specify the method for calculating the average referred to in paragraph 1(b) of this Article. EBA shall submit those draft regulatory technical standards to the Commission by [date of entry into force of this Directive].~~

~~Power is delegated to the Commission to adopt the regulatory technical standards referred to in the first subparagraph in accordance with Articles 10 to 14 of Regulation (EU) No 1093/2010.~~

[Classification is too central to not provide sufficient clarity in Level 1 text.]

*Article 12 [IFR – classification of investment firms]
Small and non-interconnected investment firms*

1. An investment firm shall be deemed a small and non-interconnected investment firm for the purposes of this Regulation where it meets all of the following conditions:

- (a) AUM (or assets under management) calculated in accordance with Article 17 is less than EUR 1.2 billion;
- (b) COH (or client orders handled) calculated in accordance with Article 20 is less than either:
 - i) EUR 100 million/day for cash trades or
 - ii) EUR 1 billion/day for derivatives.
- (c) ASA (or assets safeguarded and administered) calculated in accordance with Article 19 is zero;
- (d) CMH (or client money held) calculated in accordance with Article 18 is zero;
- (e) DTF (daily trading flow) calculated in accordance with Article 32 is zero;
- (f) NPR (net position risk) or CMG (clearing ~~member guarantee~~margin given), of positions held with trading intent, calculated in accordance with Articles 22 and 23 is zero;

[To capture net positions in FX and commodities within NPR, where held with trading intent. On ‘clearing margin given’, see Non-paper on the RtM K-factors, which is also on the CWG agenda of 3 September 2018.]

- (g) TCD (trading counterparty default) calculated in accordance with Article 26 is zero;

- (h) the ~~balance-sheet~~ total assets of the investment firm is less than EUR 100 million;

[More meaningful description that aligns the terminology with the new definition of credit institution. As balance sheet total equals total asset, there is no reason to use different measurements for the same things.]

- (i) the total annual gross revenue from investment services and activities of by the investment firm is less than EUR 30 million calculated as an average on the basis of the annual figures from the two-year period immediately preceding the given financial year.

[The idea of averaging (with just two data points) is taken from the IFD.]

By way of derogation of the provisions in Title II, for the purposes of points (a), (b), (c), (e), (f) in so far as this relates to NPR, and (g), end-of day levels shall apply.

[To clarify that unless the methods under Title II are used, the relevant thresholds for classification purposes are to be monitored on end-of day basis.]

By way of derogation of the provisions in Title II, for the purposes of point (d), and (f) in so far as this relates to CMG, intra-day levels shall apply.

[To clarify that, unlike under Title II where end of business day figures are used for CMH, the threshold for classification purposes is to be monitored on an intra-day basis.]

For the purposes of points (h) and (i), the levels ~~applicable~~ at the end of the last financial year for which accounts have been finalised and approved by the management body shall apply. Where accounts have not been finalised and approved after 6 months have elapsed since the last financial year-end an investment firm shall use provisional accounts.

[To clarify that figures should be taken once year-end accounts have been finalised and approved by the management body. A 'back-stop' to use provisional accounts after 6 months is also added.]

An investment firm may calculate the factors under points (a) and (b) with the methods under Title II of this Part with the modification that the 3 most recent monthly values will not be excluded, but the calculation period will be 3 months shorter. An investment firm that exercises this calculation method shall do so for a continuous period of no less than twelve consecutive calendar months.

[The idea of averaging AUM and COH is taken from IFD. For AUM and COH the calculation can be done on the same basis as the methods applicable for determining the K-factor based capital requirements.]

This average calculation should be discretionary, because this method brings additional burden of calculation for the firm. But by switching to this method larger class 3 firms can make use of averaging in order not to 'flip' into class 2 by pure chance. This makes the regulatory set-up more

stable to all parties involved. In the case of AUM this implies that any intra-month-perspective for classification purposes will fall away. However as there is little potential for any window dressing by the firms, this does not raise concerns.

The “modification” part is necessary, because IFD makes its own determination of the length of the deferral period. Therefore the inbuilt deferral period of 3 months for the K-factor capital requirements (Arts. 17 and 20 IFR) has to be neutralised. The calculation technique will be the same, but the data-set is taken from a period 3 months earlier than for the purpose of Title II. These will then be the exact figures which determine the K-factor based capital requirements of the firm when it has to initially comply with them after the 3 months deferral period.

In order to provide some consistency and so prevent persistent ‘switching’ between methods, an investment firm shall only use the modified method for a period of at least 12 months at a time.

If required, an obligation upon the investment firm to notify the competent authority when using this approach, could also be added.]

2. The conditions set out in points (a), (b), (h) and (i) of paragraph 1 shall apply on a combined basis for all investment firms that are part of a group. For the purposes of measuring point (i), the investment firm may exclude any double-counting that may arise in respect of gross revenues generated within the group.

[It is proportionate to ensure that any double-counting of gross revenues within a group may be eliminated, which could occur, where gross revenues are added on a combined basis.]

The conditions set out in points (c), (d), (e), (f) and (g) shall apply to each investment firm on an individual basis.

~~Where an investment firm no longer meets all the conditions set out in paragraph 1, it shall not be considered a small and non-interconnected investment firm with immediate effect.~~

[**This provision is better moved to paragraph 3.**]

3. Where an investment firm no longer meets all the conditions set out in paragraph 1, it shall not be considered a small and non-interconnected investment firm with immediate effect.

[**This existing proposed provision is relocated from above.** Note: “immediate” remains appropriate given that all zero thresholds relate to business decisions by the firm (and are predefined in the authorisation process).]

Where an investment firm no longer meets the conditions set out in points (a), ~~or (b)~~, (h) or (i) of paragraph 1 but continues to meet the conditions set out in points (c) to (g) of paragraph 1, it shall not be considered a small and non-interconnected investment firm after a period of 3 months, calculated from the date when the threshold has been exceeded.

[Given the possibility that an investment firm falling into class 2 could be exposed to additional binding capital requirements due to the application of the K-factors, it is recommended to introduce a deferral period also to a breach of thresholds in regard

to points (h) and (i), so as to allow some time for the firm to source additional capital should such a situation arise.]

The investment firm shall notify the competent authority without undue delay about any breach of a threshold.

[An ad-hoc reporting obligation is necessary to allow the competent authority to monitor where an investment firm prepares for the compliance with any additional requirements for a class 2 firm.]

4. Where an investment firm which has not met all of the conditions set out in paragraph 1 subsequently meets those conditions, it shall be considered, ~~subject to approval by the competent authority,~~ a small and non-interconnected investment firm after a period of 6 months from the date when those conditions are met. This is only deemed to be the case if within this period no breach of a threshold has occurred and the investment firm has notified the competent authority accordingly.

[This is to clarify that an investment firm would still be held in class 2 during a deferral period, in case there is any breach of a threshold during this time. The burden of approval by the competent authority seems dispensable and avoids the need for detailed criteria on which such considerations could be based, given that a holding period of 6 months can be considered neither too short nor too long.]

- ~~5. In order to take account of developments in financial markets, the Commission shall be empowered to adopt delegated acts in accordance with Article 54 in order to adjust the conditions for investment firms to qualify as small and non-interconnected firms in accordance with this Article.~~

[Classification is too important to be left to level 2 measures. Even as Art. 12 IFR delegation seems to be of smaller scope compared to the COM proposal of Art. 23 IFD, the “developments in financial markets” are not precise enough to indicate any need for a change of the rules precisely defined in the Level 1 text.]

Article 17 [IFR]

Measuring AUM for the purposes of calculating K-AUM

1. For the purposes of calculating K-AUM, AUM shall be the rolling average of the value of the total monthly assets under management, measured on the last business day of each of the previous 15 calendar months, excluding the 3 most recent calendar months ~~ly values~~.

AUM shall be the ~~average or simple~~ arithmetic mean of the remaining 12 monthly measurements.

K-AUM shall be calculated ~~within the~~ on the first ~~14~~ business days of each calendar month.

2. ...

Where another financial entity has formally delegated the assets under management to the investment firm, those delegated assets shall ~~not be included in~~ be excluded

from the total amount of assets under management measured in accordance with paragraph 1.

3. Where an investment firm has been in operation managing assets for less than 15 calendar months, or has done so for longer as a class 3 firm and now exceeds the threshold for AUM, ~~it may~~ shall use ~~business projections~~ historical data of AUM from the time period described under paragraph 1 as soon as it becomes available to calculate K-AUM. The competent authority may replace missing historical datapoints by regulatory determinations based on ~~subject to the following cumulative requirements:~~

- ~~(a) historical data is used as soon as it becomes available;~~
- ~~(b) the business projections of the investment firm submitted in accordance with Article 7 of Directive 2014/65/EU have been positively assessed by the competent authority.~~

[This provision needs to deal with the situation of “rapid growers” (breaking through the threshold of Art 12(1) IFR while only recently authorised or recently undertaking the relevant investment service). Such firms should be allowed to use the usual deferral period with a discretion of the NCA to set capital requirements on the basis of projections. After this period historical data is available and should be used.]

This provision should also address the first application of the K-factor to a firm which has been conducting the business for a longer time period, but as a class 3 firm (“steady growers”). Some may have stored all the data from previous periods to make full usage of averaging over time in the future, but others may have not (e.g. when reducing burdens of record-keeping). The group of steady growers will be significantly larger than the group of rapid growers.

Firms may not be eager to work with projected figures, because these often lead to higher capital requirement than relying on historic data. Under normal rules a firm uses historical data to determine its current requirements and even in the authorisation process the projected data will not have to be covered by current capital; rather, firms have to show that their capital will over time increase with any growing regulatory needs. As firms are unlikely to plan for a shrinking business their projected data will regularly be higher than historic data. Therefore firms should have a strong incentive to collect and use as much historical data as they have.]

Article 18 [IFR]

Measuring CMH for the purposes of calculating K-CMH

1. For the purposes of calculating K-CMH, CMH shall be the rolling average of the value of total daily client money held, measured at the end of each business day for the previous ~~36~~ calendar months, excluding the 3 most recent calendar months.

CMH shall be the ~~average or simple~~ arithmetic mean of the daily measurements ~~in from~~ the remaining 3 calendar months.

K-CMH shall be calculated by on the ~~end of first~~ business day ~~following the measurement referred to in the first subparagraph of each calendar month~~.

2. Where an investment firm has been in operation holding client money for less than 36 calendar months, it ~~may~~ shall use ~~business projections~~ historical data of CMH from the time period described under paragraph 1 as soon as it becomes available to calculate K-CMH. The competent authority may replace missing historical datapoints by regulatory determinations based on, ~~subject to the following cumulative requirements:~~
- ~~(a) historical data is used as soon as it becomes available;~~
 - ~~(b) the business projections of the investment firm submitted in accordance with Article 7 of Directive 2014/65/EU have been positively assessed by the competent authority.~~

[Justification same as for Article 17 and K-AUM above. (Except that there is no need to also provide for where a firm may hold client money as a class 3 firm given the zero threshold for CMH).]

Article 19 [IFR]

Measuring ASA for the purposes of calculating K-ASA

1. For the purposes of calculating K-ASA, ASA shall be the rolling average of the value of the total daily assets safeguarded and administered, measured at the end of each business day for the previous 6 calendar months, excluding the 3 most recent calendar months.

ASA shall be the average or simple arithmetic mean of the daily measurements from the remaining 3 calendar months.

K-ASA shall be calculated within on the the first 14 business days of each calendar month.

- 1a. Where the investment firm has formally delegated the assets safeguarded and administered to another financial entity, or where another financial entity has formally delegated the assets safeguarded and administered to the investment firm, these delegated assets shall be included in the total amount of ASA measured in accordance with paragraph 1.

2. Where an investment firm has been in operation safeguarding and administering assets for less than 36 calendar months, it ~~may~~ shall use ~~business projections~~ historical data of ASA from the time period described under paragraph 1 as soon as it becomes available to calculate K-ASA. The competent authority may replace missing historical datapoints by regulatory determinations based on, ~~subject to the following cumulative requirements:~~

- ~~(a) historical data is used as soon as it becomes available;~~
- ~~(b) the business projections of the investment firm submitted in accordance with Article 7 of Directive 2014/65/EU have been positively assessed by the competent authority.~~

[Justification same as for Article 17 and K-AUM above. (Except that there is no need to also provide for where a firm may safeguard and administer assets as a class 3 firm given the zero threshold for ASA).]

Article 20 [IFR]

Measuring COH for the purposes of calculating K-COH

1. For the purposes of calculating K-COH, COH shall be the rolling average of the value of the total daily client orders handled, measured ~~at the end of~~ throughout each business day over the previous 6 calendar months, excluding the 3 most recent calendar months.

COH shall be the average or simple arithmetic mean of the daily measurements for the remaining 3 calendar months.

K-COH shall be calculated ~~within~~ on the first ~~14~~ business days of each ~~quarter~~ month.

2. COH shall be measured as the sum of the absolute value of buys and the absolute value of sells for both cash trades and derivatives in accordance with the following:
 - (a) for cash trades, the value is the amount paid or received on each trade.
 - (b) for derivatives, the value of the trade is the notional amount of the contract.

COH shall include transactions executed by investment firms providing portfolio management services on behalf of investment funds.

COH shall exclude transactions handled by the investment firm that arise from the servicing of a client's investment portfolio where the firm already calculates K-AUM in respect of the client's investments, or where this activity relates to the delegation of assets under management to the investment firm not contributing to AUM of this investment firm by virtue of Article 17(2).

[Further clarification as to what is not COH and so relevant to determining whether the threshold is met.]

COH shall exclude transactions executed by the investment firm in its own name either for itself or on behalf of a client.

COH shall exclude orders, which have not been executed, neither by the firm itself, nor by a third party to which the order has been transmitted.

[As above, further clarification.]

3. Where an investment firm has been in operation handling client orders for less than ~~36~~ calendar months, ~~or has done so for longer as a class 3 firm and now exceeds the threshold for COH, it shall use business projections~~ historical data of COH from the time period described under paragraph 1 as soon as it becomes available to calculate K-COH. The competent authority may replace missing historical datapoints by regulatory determinations based on, subject to the following cumulative requirements:

- ~~(a) historical data is used as soon as it becomes available;~~
- ~~(b) the business projections of the investment firm submitted in accordance with Article 7 of Directive 2014/65/EU have been positively assessed by the competent authority.~~

[Justification same as for Article 17 and K-AUM above. Including the need to also provide for where a firm may previously have handled client orders as a class 3 firm below the threshold for COH.]

Article 32 [IFR]
Measuring DTF for the purposes of calculating K-DTF

1. For the purposes of calculating K-DTF, DTF shall be the rolling average of the value of the total daily trading flow, measured ~~at the end of~~ throughout each business day over the previous 6 calendar months, excluding the 3 most recent calendar months.
DTF shall be the ~~average or simple~~ arithmetic mean of the daily measurements for the remaining 3 calendar months
K-DTF shall be calculated ~~within~~ on the first ~~14~~ business days of each ~~quarter~~ month.
2. DTF shall be measured as the sum of the absolute value of buys and the absolute value of sells for both cash trades and derivatives in accordance with the following:
 - (a) for cash trades, the value is the amount paid or received on each trade.
 - (b) for derivatives, the value of the trade is the notional amount of the contract.
3. DTF shall exclude transactions executed by an investment firm providing portfolio management services on behalf of investment funds.
DTF shall include transactions executed by an investment firm in its own name either for itself or on behalf of a client.
4. Where an investment firm has been in operation and has a daily trading flow for less than 36 calendar months, it ~~may~~ shall use ~~business projections~~ historical data of DTF from the time period described under paragraph 1 as soon as it becomes available to calculate K-DTF. The competent authority may replace missing historical datapoints by regulatory determinations based on
 - ~~(a) historical data is used as soon as it becomes available;~~
 - ~~(b) the business projections of the investment firm submitted in accordance with Article 7 of Directive 2014/65/EU have been positively assessed by the competent authority.~~

[Justification same as for Article 17 and K-AUM above. (Except that there is no need to also provide for where a firm may have a daily trading flow as a class 3 firm given the zero threshold for DTF).]

Article 45 [IFR – Disclosure by investment firms]
Scope

1. ...
2. ...
3. ~~Where a~~ An investment firm no longer meets all the conditions set out in Article 12(1) it shall publicly disclose the information set out in this Part ~~Articles 47 and 51 where it meets the requirements set out in Article 23 of Directive (EU) ... / [IFD].~~

~~The investment firm that meets the requirements set out in Art 23 of Directive (EU) / [IFD] shall disclose the information as of the financial year following the financial year in which it no longer met those conditions the assessment referred to in Article 23(1) of Directive (EU) / [IFD] took place.~~

[Consistent with alignment of Art. 23 IFD with Art 12 IFR as regards when a firm re-classifies. Also, it is more proportionate to provide adequate time for an investment firm to prepare to make all of the necessary disclosures set out in this Part when it moves from being in class 3 to class 2.]

4. ...

Article 4 [IFR] Definitions

1. For the purposes of this Regulation, the following definitions shall apply:

...

- (25) ~~‘K-AUM’ or ‘K factor in relation to assets under management (AUM)’ means the capital requirement relative to the value of assets that an investment firm manages for its clients under both discretionary portfolio management and non-discretionary arrangements constituting investment advice~~ of an on-going nature, including assets delegated to another undertaking and excluding assets that another undertaking has delegated to the investment firm;
- (26) ~~‘K-CMH’ or ‘K factor in relation to client money held (CMH)’ means the capital requirement relative to the amount of client money that an investment firm holds or controls, regardless of any legal arrangements in relation to asset segregation and irrespective of the national accounting regime applicable to client money held by the investment firm;~~
[See on ‘or controls’, the *Non-paper on client money held*.]
- (27) ~~‘K-ASA’ or ‘K factor in relation to assets safeguarded and administered (ASA)’ means the capital requirement relative to the value of assets that an investment firm safeguards and administers for clients,~~ including assets delegated to another undertaking and assets that another undertaking has delegated to the investment firm, irrespective of whether assets appear on the investment firm's own balance sheet or are segregated in other accounts;
- (28) ~~‘K-COH’ or ‘K factor in relation to client orders handled (COH)’ means the capital requirement relative to the value of orders that an investment firm handles for clients, through the reception and transmission of client orders and through the execution of orders on behalf of clients;~~
- (29) ~~‘K-CON’ or ‘K factor in relation to concentration risk (CON)’ means the capital requirement relative to the exposures in the trading book of an investment firm to a client or a group of connected clients the value of which exceeds the limits in Article 36(1);~~
- (30) ~~‘K-CMG’ or ‘K factor in relation to clearing margin given member guarantee (CMG)’ means the capital requirement equal to the amount of initial margins posted~~

~~with total margin required by~~ clearing member, where the execution and settlement of transactions of an investment firm dealing on own account take place under the responsibility of a general clearing member;

[See for these drafting proposals also the *Non-paper on the RtM K-factors*.]

- (31) '~~K-DTF~~' or '~~K-factor in relation to~~ daily trading flow ~~(DTF)~~' means the ~~capital requirement relative to the~~ daily value of transactions that an investment firm enters through dealing on own account or the execution of orders on behalf of clients in its own name;
- (32) '~~K-NPR~~' or '~~K-factor in relation to~~ net position risk ~~(NPR)~~' means the ~~capital requirement relative to the~~ value of transactions recorded in the trading book of an investment firm;
- (33) '~~K-TCD~~' or '~~K-factor in relation to~~ trading counterparty default ~~risk (TCD)~~' means ~~the capital requirement relative to~~ the exposures in the trading book of an investment firm in instruments and transactions referred to in Article 25 giving rise to the risk of trading counterparty default;

[It is unnecessary to define each K-factor, as these are defined in turn in Title II of Part Three of IFR. For example, K-AUM is defined in Art. 16(a) IFR, K-CMH in Art. 16(b), etc. Rather, for the purposes of Arts. 12 and 17 of IFR the terms AUM, ASA, etc., should be defined instead. This is easily achieved through the above amendments.]