

BVI¹ comments on the EBA data collection exercise on the revision of prudential framework for investment firms

BVI gladly takes the opportunity to present its views on the drafted data sheet and instructions for EBA's data collection exercise on the revision of prudential framework for investment firms.

I. General remarks

In general, we welcome EBA's initiative to collect data in order to review the prudential capital and remuneration requirements and to propose a new categorisation of investment firms based on their risk profile. We fully support EBA's view that one of the more specific challenges is related to the application of the proportionality principle because most investment firms commonly have different risk profiles, based on differing investor bases, risk appetites and risk horizons.

However, our members are mainly asset managers providing management services to collective investment undertakings such as UCITS or AIF. They also act as fund managers when they provide management services to UCITS or AIF by means of outsourcing agreements with regard to the full portfolio management of these investment funds or the management of certain segments (such as European corporate bonds, North American or South-East Asian equities) in which an investment fund is invested. While the business model of our members is different and the risks exposures of the investment funds are not shown in the manager's balance sheet, most of the data fields could not be completed or will always be left empty. We are therefore concerned that the exercise in our membership will lead to unsustainable outcomes.

In this context, we would like to draw EBA's attention to the fact that the ESMA is already collecting data about the risk exposures of investment funds and the management company itself in a very detailed way. In order to avoid conclusions based on an incomplete data collection exercise, we propose to contact ESMA to get an exacter overview of data. Moreover, we request to exclude investment management companies from the obligation to complete the drafted data sheet as a whole or parts of it.

II. Scope of the data sheet

From our view, the data sheet addresses the following issues:

- **Acting as an investment firm providing MiFID services**

As we understand the current instruction guidelines and the discussion at the EBA roundtable of 29 June 2016, the exercise addresses only MiFID investment firms and only UCITS/AIF management companies conducting MiFID activities or services.

¹ BVI represents the interests of the German investment fund and asset management industry. Its 95 members manage assets of some EUR 2.6 trillion in UCITS, AIFs and assets outside investment funds. As such, BVI is committed to promoting a level playing field for all investors. BVI members manage, directly or indirectly, the assets of 50 million private clients in over 21 million households. BVI's ID number in the EU Transparency Register is 96816064173-47. For more information, please visit www.bvi.de/en.



As described above, most of our members are management companies within the meaning of the UCITS Directive or the AIFMD which are offering services and products under the AIFMD and the UCITS Directive. Some of them are part of a banking group for which the CRD does not apply and the others are part of an insurance group or group-independent. Irrespective of the group context, about half of these members provide the MiFID service of portfolio management or non-core services such as investment advice (within the meaning of Article 6 paragraph 3a and b of the UCITS Directive and Article 6 paragraph 4a and b of the AIFMD).

If there is a need to include investment management companies into this data collection, the questions should be limited to MiFID services outside investment funds. Moreover, we propose to clarify that investment management companies providing only management services on behalf of UCITS or AIF and without original MiFID activities are not in scope of this exercise.

Unfortunately, a common understanding of the classification of delegated management services to UCITS or AIF is not existent in the EU. However, the German legislator qualified this kind of insourcing activities as a MiFID investment service of portfolio management as a result of a statement made by the European Commission in 2007 in its FAQ to the MiFID²:

“Question: When an investment manager is appointed as the manager of a UCITS fund/sub-fund, is it conducting the MiFID activity of portfolio management, and should the investment manager treat the UCITS fund/sub-fund as its client?”

Answer: The answer to this question depends on the nature of the service the ‘investment manager’ is providing. If the ‘investment manager’ is a management company within the meaning of Article 1a(2) of the UCITS directive or comparable national rules for non-coordinated collective investment funds, responsible for the activities mentioned in Annex II of the UCITS directive (investment management, administration and marketing), then the investment manager is not required to comply with MiFID, because it is exempted from MiFID by Article 2(1)(h).

However, if such management company does not perform all of these functions itself, but delegates the asset management functions to an ‘investment manager’, this delegated party will be providing the service of individual portfolio management to the management company.

In case of a UCITS management company, the delegation is subject to the conditions laid down in Article 5g of the UCITS Directive. A UCITS management company is notably only permitted to delegate all or parts of its investment management activities to an entity which is authorised or registered for the purposes of ‘asset management’.

(i) If the delegated party is an authorised management company pursuant to Article 5(3) of the UCITS directive, Articles 2, 12, 13 and 19 of MiFID will be applicable to its operation (see Article 5(4) of the UCITS Directive).

(ii) If the delegated party is a MiFID investment firm authorised for the purposes of individual portfolio management, the whole range of MiFID provisions applicable to portfolio managers is applicable.”

Our members often make use of the possibility to delegate the portfolio management of investment funds in particular in the area of alternative investment funds with institutional investors such as banks, insurance undertakings or pension funds. These investment funds are invested in financial instruments (securities-based investment funds) with equal investment strategies permitted by the UCITS Directive. In 2015 our members managed such securities-based investment funds with about 1.285 trillion Euro assets under management. About 60 percent of this portfolio (approximately 770 billion Euro assets under management) is delegated to external asset managers in Germany and abroad. The other 40 percent of these assets under management are managed by the management company itself.

Irrespective whether or not the management company makes use of the possibility to delegate the portfolio management, the manager is obliged in its fiduciary role to act in accordance with the investment objectives and guidelines set by their investors for a given risk/return level. In all cases, asset managers do not have custody over the assets, as these are held – or more precisely, “safe-kept” – by separate

² Cf. <http://ec.europa.eu/finance/koel/index.cfm?fuseaction=question.show&questionId=235>.



depository institutions (usually a credit institution, but with a specific licence). Therefore, they do not hold the client's money. The assets in the fund portfolio are kept segregated and are thus never part of the asset manager's own balance sheet. Importantly, the investment results – whether positive or negative – belong to the investor. Therefore, there is no direct link between the risk exposure of the managed assets and the solvency of the manager's balance sheet as they do not trade on the own books of the management company. Therefore, fundamental differences exist between the business models of asset managers and the banking sectors.

Moreover, rigorous capital requirements which reflect the risks of management of investment funds are already in place for the management companies under the UCITS Directive or the AIFMD. These capital requirements also encompass cases of delegation of portfolio management. Moreover, management companies are obliged to cover operational risks (such as professional liability risks) through additional own funds.³

While the current draft of the data sheet is focused on MiFID investment services as a whole, there is a need to distinguish the investment service of portfolio management in two parts to reflect the management of investment funds as a special business model in a more appropriate manner: the management of investment funds by means of an outsourcing agreement and the management of assets outside investment funds on an individual client basis.

To be distinguished from the services provided by a management company are the portfolio management services provided by investment firms which directly fall within the scope of the CRD because they only provide services regulated under MiFID such as portfolio management, investment advice or execution of orders on behalf of clients. They also act as fund managers when they provide management services to collective investment undertakings such as UCITS or AIF by means of outsourcing agreements as mentioned above. Therefore, questions addressed to these firms should also be limited to the MiFID services outside investment funds.

- **Liquidity requirements**

While management companies are already obliged to invest their own funds in liquid assets, the data of our members will not provide any added value, because their own funds' investments are liquid. In this context, we would like to draw EBA's attention to the FAQ published by BaFin last week in which BaFin states which kinds of assets should be considered liquid.⁴

- **Risk exposure and large exposure**

We don't see any added value in requiring management companies to complete the data sheet with regard to risk and large exposure. ESMA is already collecting data about the risk exposures of the investment funds and of the management company itself in a very detailed way. In particular, an AIFM shall regularly report to the competent authorities on the five most important markets and the five main instruments in which it is trading including the most important concentrations. Moreover, the values of assets under management for all AIFs managed should be reported to the competent authority and ESMA. An equal reporting applies for UCITS management companies under the Delegated Regulation under the UCITS Directive. In avoiding to draw conclusions based on a more incomplete EBA data collection exercise, we propose to contact ESMA to get an exacter overview of data.

³ Cf. Article 14 of the Delegated Regulation (EU) No 231/2013 of 19 December 2012, BaFin Circular 5/2010 on the minimum requirements of risk management for investment management companies.

⁴ http://www.bafin.de/SharedDocs/Veroeffentlichungen/DE/FAQ/faq_anlage_Eigenmittel_160628.html.



- **Remuneration**

Please be informed that management companies are obliged to prepare annual reports with, in particular, information relating to the number of staff whose actions have a material impact on the risk profile of the funds they manage and of the company (identified staff). Therefore, we refer to the published annual reports at www.bundesanzeiger.de. The published data would give a better overview than asking our members on a voluntary and best effort basis. Moreover, with regard to the scope of investment management companies providing MiFID services, the exercise would be limited to these kinds of companies.

However, the discussion with regard to remuneration should be strongly limited to MiFID firms for which the CRD apply. Management companies licenced as AIF or UCITS managers only fall under the remuneration requirements set out in the AIFMD and UCITS Directive. In this context, we refer to our reply to the European Commission on its public consultation on impacts of maximum remuneration ratio under CRD IV and overall efficiency of CRD IV remuneration rules.

- **Applying the capital requirements with regard to fixed overheads**

In our view, the data sheet does not recognise the relevant data with regard to fixed **and variable** overheads (for example as **variable costs such as** profit transfers which are based on contractual profit transfer agreements, taxes on income which depend on the yearly profitability, commissions which are paid out of a fund's management fee). While the fixed overheads requirements through references in the UCITS Directive and the AIFMD apply to all investment management companies, we would like expressly to request EBA to include ESMA in the debate.