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#### COVER NOTE

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From:	Secretary-General of the European Commission, signed by Mr Jordi AYET PUIGARNAU, Director
date of receipt:	4 September 2014
To:	Mr Uwe CORSEPIUS, Secretary-General of the Council of the European Union
No. Cion doc.:	C(2014) 6200 final
Subject:	COMMISSION DELEGATED REGULATION (EU) No .../.. of 4.9.2014 amending Delegated Regulation (EU) No 241/2014 as regards own funds requirements for firms based on fixed overheads

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Delegations will find attached document C(2014) 6200 final.

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Encl.: C(2014) 6200 final



Brussels, 4.9.2014  
C(2014) 6200 final

**COMMISSION DELEGATED REGULATION (EU) No .../..**

**of 4.9.2014**

**amending Delegated Regulation (EU) No 241/2014 as regards own funds requirements  
for firms based on fixed overheads**

(Text with EEA relevance)

## EXPLANATORY MEMORANDUM

### **1. CONTEXT OF THE DELEGATED ACT**

Article 97(4) of Regulation (EU) No 575/2013 ('the Regulation') empowers the Commission to adopt, following submission of draft standards by the European Banking Authority (EBA), and in accordance with Articles 10 to 14 of Regulation No (EU) 1093/2010, delegated acts specifying the calculation of the own funds requirements for firms with limited authorisation based on the fixed overheads.

In accordance with Article 10(1) of Regulation No (EU) 1093/2010 establishing the EBA, the Commission shall decide within three months of receipt of the draft standards whether to endorse the drafts submitted. The Commission may also endorse the draft standards in part only, or with amendments, where the Union's interests so require, having regard to the specific procedure laid down in those Articles.

### **1. CONSULTATIONS PRIOR TO THE ADOPTION OF THE ACT**

In accordance with the third subparagraph of Article 10(1) of Regulation (EU) No 1093/2010, the EBA has carried out a public consultation on the draft technical standards submitted to the Commission in accordance with Article 97(4) of Regulation (EU) No 575/2013. A consultation paper was published on the EBA internet site on 17 July 2013, and the consultation closed on 30 September 2013. Moreover, the EBA invited the EBA's Banking Stakeholder Group set up in accordance with Article 37 of Regulation (EU) No 1093/2010 to provide advice on them.

Together with the draft technical standards, the EBA has submitted an explanation on how the outcome of these consultations has been taken into account in the development of the final draft technical standards submitted to the Commission.

Together with the draft technical standards, and in accordance with the third subparagraph of Article 10(1) of Regulation (EU) No 1093/2010, the EBA has submitted its Impact Assessment, including its analysis of the costs and benefits, related to the draft technical standards submitted to the Commission. This analysis is available at <http://www.eba.europa.eu/-/eba-consults-on-draft-technical-standards-on-own-funds-requirements-for-investment-firms>, pages 14-17 of the Final Draft Regulatory Technical Standards package.

### **2. LEGAL ELEMENTS OF THE DELEGATED ACT**

This delegated act covers the following areas:

First, the provisions in this delegated act relate to the calculation of the requirements of own funds based on fixed overheads, or projected fixed overheads in case a firm has not completed one year of business. The delegated act specifies what fixed overheads are in order to harmonise the methodology for the calculations and therefore to facilitate the application of the Regulation. The delegated act also elaborates on the calculation of projected fixed overheads; this projection shall be used in case a firm has not completed one year of business.

Secondly, the delegated act contains provisions regarding tied agents, because business carried out through a tied agent exposes a firm to risk in the same manner as business carried out by the firm itself. Besides, there should not be incentives for firms to reduce their capital requirements through the use of these agents. Therefore, a firm should maintain a capital component for tied agents. Given the practical problems with calculating fixed overheads for tied agents, the use of a fixed percentage of all costs related to a tied agent is introduced.

Thirdly, the delegated act provides criteria for determining when a change in the business activities of a firm is material, to the effect that competent authorities can make adjustments to the capital requirements of that firm.

Finally, it should be noted that this delegated act has been developed to complement the delegated act containing the draft regulatory standards on own funds, submitted by the EBA on 26 July 2013, which specify certain provisions relating to regulatory own funds.

## **COMMISSION DELEGATED REGULATION (EU) No .../..**

**of 4.9.2014**

### **amending Delegated Regulation (EU) No 241/2014 as regards own funds requirements for firms based on fixed overheads**

(Text with EEA relevance)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012<sup>1</sup>, and in particular the third subparagraph of Article 97(4) thereof,

Whereas:

- (1) Regulation (EU) No 575/2013 establishes, among other matters, prudential requirements for investment firms in order to ensure that investment firms are safe and sound and comply at all times with the own funds requirements. Own funds requirements established by that Regulation aim to ensure that risks stemming from business activities are covered by a sufficient amount of own funds. According to Article 97 of Regulation (EU) No 575/2013 firms (i.e. investment firms and entities referred to in point (2)(c) of Article 4(1)) can use an alternative method based on fixed costs to calculate the total risk exposure. It is therefore necessary to establish the

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<sup>1</sup> OJ L 176, 27.6.2013, p. 1.

methodology for calculating fixed overheads and the list of items that would be included in the calculations in order to have a common approach in all Member States.

- (2) In order to ensure that firms are able to organise an orderly winding down or restructuring of their activities, they should hold sufficient financial resources to withstand operational expenses over an appropriate period of time. During the winding down or restructuring, a firm still needs to continue its business and be able to absorb losses which are not matched by a sufficient volume of profits, to protect investors. While some costs (such as staff bonuses) may decrease other costs (such as legal expenses) may increase. Considering that not all firms use International Financial Reporting Standards (IFRS) and in order to avoid regulatory arbitrage, it is essential to follow a prudent approach for calculating own funds for firms, whereby changes to the accounting framework are automatically taken into account and cannot be arbitrated by changing the accounting categorisation. In order to more adequately reflect the effect of the variable expenses in the own funds, rules on the own funds of firms should be based on an approach whereby variable costs are deducted from total expenses.
- (3) Given that firms make use of tied agents and the business carried out through tied agents exposes those firms to risks in the same manner as the business carried out by the firms themselves, appropriate rules on the own funds requirements for firms based on fixed overheads should provide for the inclusion of costs relating to tied agents to reflect those risks. Nevertheless, given that costs related to tied agents have some element of variability but cannot be considered a fully variable cost item but it would be disproportionate to include the full amount of the costs related to tied agents to the own funds requirements, these rules should provide for the inclusion only of a percentage of these costs in the own funds requirements. Further, in order to avoid double-counting of amounts relating to tied agent fees, these rules should provide for the deduction of the fees related to tied agents before the addition of this percentage to the own funds requirements.
- (4) Regulation (EU) No 575/2013 provides that competent authorities can make adjustments in own funds requirements where there has been a material change in the business activities of the firm. In order to ensure that competent authorities apply the same conditions across the Union, it is necessary to establish criteria on what constitutes a material change. As firms vary in their size, there are some very small firms or firms in a start-up phase for whom it would be unnecessarily burdensome to impose adjustments in their own funds requirements, given that changes are bound to be frequent for them. Therefore minimum thresholds should be established so that those firms are exempted from the adjustments in own funds requirements if their own funds requirements fall below the threshold.
- (5) Commission Delegated Regulation (EU) No 241/2014<sup>2</sup> lays down regulatory technical standards for own funds requirements for institutions. This Regulation establishes the methodology for calculating fixed overheads for firms. To ensure coherence and to facilitate a comprehensive view and compact access to all the provisions regarding own funds by persons subject to those obligations, it is desirable to include all regulatory technical standards required by Regulation (EU) No 575/2013 on own

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<sup>2</sup> Commission Delegated Regulation (EU) No 241/2014 of 7 January 2014 supplementing Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to regulatory technical standards for Own Funds requirements for institutions (OJ L 74, 14.3.2014, p. 8).

funds in a single Regulation. Delegated Regulation (EU) No 241/2014 should therefore be amended accordingly.

- (6) This Regulation is based on the draft regulatory technical standards submitted by the European Banking Authority to the Commission.
- (7) The European Banking Authority has conducted open public consultations on the draft regulatory technical standards on which this Regulation is based, analysed the potential related costs and benefits and requested the opinion of the Banking Stakeholder Group established in accordance with Article 37 of Regulation (EU) No 1093/2010 of the European Parliament and of the Council<sup>3</sup>. The European Banking Authority has also consulted the European Securities Markets Authority (ESMA) before submitting the draft technical standards on which this Regulation is based.

HAS ADOPTED THIS REGULATION:

#### *Article 1*

In Regulation (EU) No 241/2014 the following Chapter Va is inserted:

#### *“CHAPTER Va*

#### *OWN FUNDS BASED ON FIXED OVERHEADS*

#### *Article 34b*

*Calculation of the eligible capital of at least one quarter of the fixed overheads of the preceding year for the purposes of Article 97(1) of Regulation (EU) No 575/2013*

1. For the purposes of this Chapter, “firm” means an entity referred to in point (2)(c) of Article 4(1) of Regulation (EU) No 575/2013 or an investment firm.
2. For the purposes of Article 97(1) of Regulation (EU) No 575/2013, firms shall calculate their fixed overheads of the preceding year, using figures resulting from the applicable accounting framework, by subtracting the following items from the total expenses after distribution of profits to shareholders in their most recent audited annual financial statements, or, where audited statements are not available, in annual financial statements validated by national supervisors:
  - (a) fully discretionary staff bonuses;

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<sup>3</sup> Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC (OJ L 331, 15.12.2010, p. 12).

- (b) employees', directors' and partners' shares in profits, to the extent that they are fully discretionary;
  - (c) other appropriations of profits and other variable remuneration, to the extent that they are fully discretionary;
  - (d) shared commission and fees payable which are directly related to commission and fees receivable, which are included within total revenue, and where the payment of the commission and fees payable is contingent upon the actual receipt of the commission and fees receivable;
  - (e) fees, brokerage and other charges paid to clearing houses, exchanges and intermediate brokers for the purposes of executing, registering or clearing transactions;
  - (f) fees to tied agents as defined by point 25 of Article 4 of Directive 2004/39/EC of the European Parliament and of the Council<sup>4</sup>, where applicable;
  - (g) interest paid to customers on client money;
  - (h) non-recurring expenses from non-ordinary activities.
3. Where fixed expenses have been incurred on behalf of the firms by third parties other than tied agents, and these fixed expenses are not already included within the total expenses referred to in paragraph 2, firms shall take either of the following actions:
- (a) where a break-down of the expenses of those third parties is available, firms shall determine the amount of fixed expenses that those third parties have incurred on their behalf and shall add that amount to the figure resulting from paragraph 2;
  - (b) where the break-down referred to in point (a) is not available, the firms shall determine the amount of expenses incurred on their behalf by those third parties according to the firms' business plans and shall add that amount to the figure resulting from paragraph 2.
4. Where the firm makes use of tied agents, it shall add an amount equal to 35% of all the fees related to the tied agents to the figure resulting from paragraph 2.
5. Where the firm's most recent audited financial statements do not reflect a twelve month period, the firm shall divide the result of the calculation of paragraphs 2 to 4 by the number of months that are reflected in those financial statements and shall subsequently multiply the result by twelve, so as to produce an equivalent annual amount.

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<sup>4</sup> Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EEC (OJ L 145, 30.4.2004, p. 1).

### Article 34c

*Conditions for the adjustment by the competent authority of the requirement to hold eligible capital of at least one quarter of the fixed overheads of the previous year according to Article 97(2) of Regulation (EU) No 575/2013*

1. For firms referred to in the second subparagraph, a change in the business of a firm shall be considered material where any of the following conditions is met:
  - (a) the change in the business of the firm results in a change of 20% or greater in the firm's projected fixed overheads;
  - (b) the change in the business of the firm results in changes in the firm's own funds requirements based on projected fixed overheads equal to or greater than EUR 2 million.

The firms referred to in the first subparagraph shall be those that meet either of the following conditions:

- (a) their current own funds requirements based on fixed overheads are equal to or more than EUR 125 000;
  - (b) their own funds requirements meet both of the following conditions:
    - (i) based on current fixed overheads, they are less than EUR 125 000;
    - (ii) based on projected fixed overheads, they are equal to or more than EUR 150 000.
2. For firms referred to in the second subparagraph, a change in the business of a firm shall be considered material where the change in the business of the firm results in a 100% or greater change in the firm's projected fixed overheads.

The firms referred to in the first subparagraph shall be those that meet both of the following conditions:

- (a) their own funds requirements based on current fixed overheads are less than EUR 125 000;
  - (b) their own funds requirements based on projected fixed overheads are less than EUR 150 000.

### Article 34d

*Calculation of projected fixed overheads in the case of a firm that has not completed business for one year according to Article 97(3) of Regulation (EU) No 575/2013*



Where a firm has not completed business for one year from the day it starts trading, it shall use, for the calculation of items in points (a) to (h) of Article 34b(2), the projected fixed overheads included in its budget for the first twelve months' trading, as submitted with its application for authorisation.”

## *Article 2*

This Regulation shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels, 4.9.2014

*For the Commission*  
*The President*  
*José Manuel BARROSO*