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Consultation Paper CP 100 – Consultation on Risk Assessment and Capital Planning for Fund Administrators

Dear Sir/Madam,

Irish Funds welcomes the opportunity to comment on the proposed Central Bank Investment Firm Regulations relating to Own Funds Requirements and Capital Adequacy together with the Proposed Guidance which form part of the Consultation Paper (CP 100).

As noted in CP 97 (Consultation on Central Bank Investment Firm Regulations 2015) the Central Bank proposes publishing an Investment Firms rulebook which will consolidate into one document all of the conditions and requirements which the Central Bank imposes on investment firms. The Central Bank proposes to issue the rulebook in the form of Central Bank regulations under the 2013 Act. While we welcome the initiative to document and consolidate into one document all of the conditions and requirements which the Central Bank proposes to impose on investment firms, we would however question the intention to issue all such requirements in the form of Central Bank regulations. Some of the requirements contained in the proposed Central Bank Investment Firm Regulations are very detailed and process driven in their nature, such as those governing final NAV release, and we previously questioned their suitability for inclusion in regulation. We also previously

raised concerns regarding some of the proposed provisions and those concerns were articulated in our response to CP 97. We have similar concerns regarding the approach outlined in CP 100.

With regard to CP 100 we would question the appropriateness of mandating stringent requirements in relation to risk assessment and capital planning for Fund Administrators, particularly by way of a statutory instrument. We do not agree with the Central Bank's intention to impose bank like capital planning and risk assessment requirements on Fund Administrators. This approach is not commensurate with the business of a Fund Administrator which does not leverage its balance sheet, does not take deposits, does not have credit exposure due to lending, does not engage in proprietary trading and is already subject to the Central Banks PRISM regime. In addition, the balance sheet of a fund administrator is not as vulnerable to significant and relatively quick balance sheet movements such as those that banks would have arising from credit losses or mark to market valuations.

Furthermore, this approach is not consistent with the Central Bank's stated intention to focus more on supervisory work rather than rulemaking going forward.

While the stated intention is to formalise and bring into regulation what Fund Administrators have been doing as part of their capital planning exercise for the last number of years, moving such practice into legally binding requirements is a cause for significant concern for the industry. A regulatory approach which imposes bank like capital planning and risk assessment requirements on Fund Administrators is not in line with the approach of regulators in other jurisdictions and will make Ireland less competitive as a fund servicing centre by impacting on fees for fund administration services delivered, and ultimately be a cost to be borne by the investors in the Funds administered here.

In their Report on Investment Firms in response to the European Commission Call for Evidence in December 2014 the EBA recognises the need for a distinction to be made between "bank like" investment firms and other "non-systemic" investment firms. The following two recommendations are very relevant to the Central Bank current considerations on the matter:

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- **Recommendation for a new categorisation of investment firms distinguishing between systemic and 'bank-like' investment firms to which the full CRD/CRR requirements should be applied; other investment firms ('non-systemic') with a more limited set of prudential requirements; and very small firms with 'non-interconnected' services.**
- **Recommendation for the development of a prudential regime for 'non-systemic' investment firms.**

Regulation 98 - Risk Analysis and Capital Adequacy Assessment Process:

While it would be prudent for any business to have in place a risk management program however the proposed approach to align the requirements for Fund Administrators with MiFID firms does not reflect the different business activities of Fund Administrators and MiFID firms.

Regulation 101 – Sources of Risk:

We would question whether there should be references in the Statutory Instrument to sources of risk or whether it would be more appropriate to specify these risks in the Guidance Note. The intention should be to align the risks specified in the Regulation with those specified in the Central Bank's PRISM Guidelines. This would seem appropriate however we note Concentration Risk is not covered as a separate risk probability category under the PRISM Guidelines and Group Risk is specified in the Regulations but not in the PRISM Guidelines. Conversely, Conduct Risk is in the PRISM Guidelines but not in the Regulations. For liquidity risk, should the minimum time horizons be set out in the Statutory Instrument or should they be specified in the Guidance Note. In particular we would question the relevance of intra-day liquidity risk for an administration firm. This is more relevant to a bank where there is a need to maintain liquidity in order to cover deposits and demonstrates clearly, the inappropriateness of bank like capital requirements for Fund Administration firms. The minimum requirement for monitoring liquidity for a fund administration firm should be daily as opposed to intra-day. The intra-day requirement should only apply by exception. In the case of a Fund Administration firm liquidity needs are generally limited to payment of operating expenses and losses. In our view, there should be an element of materiality in terms of the risks. For example, liquidity and market risk would not necessarily be considered material risks for the Fund Administration business and would not require the same level of assessment as some of the other risks such as operational risk or

strategic risk. While Capital Plans may make reference to all the PRISM risks the focus should be on material risks in terms of further potential exposure.

While the Capital Planning process envisaged in the requirements is broadly in line with what may currently be in place on a bi-lateral basis with Fund Administrators, there is additional detail associated with some aspects of the process including those around testing and scenario analysis. In addition, statistical models and related back testing are more appropriate to banks than fund administration companies. We would consider the new requirement to have detailed wind down plans to be more appropriate to systemic institutions such as banks rather than pure fund administration companies. Fund Administrators are often subsidiaries of major global financial institutions and benefit from the infrastructure and support of such institutions. To impose local wind down requirements where such infrastructure and support is in place is not appropriate. If it was deemed necessary such organisations would need to ensure that the Irish requirements could be incorporated within the group's plans. This would take time and would benefit from further Central Bank guidance. In the last 25 years there has been no wind down of a Fund Administrator which would warrant such an onerous requirement.

The introduction to CP100 refers to a requirement to set aside capital to meet risks. We would like to understand what form it is proposed this additional capital should be in and whether this will be in regulation or guidance.

The consultation paper states that a fund administrator would need to ensure it has a linked risk and capital management system and should reconcile internal capital to own funds, however Regulation 4 defines internal capital as being equity that does not fall under the definition of own funds, we would appreciate clarification on this point. Furthermore, additional clarification is sought on the definition of both of these terms and on the purpose of the reconciliation in terms of what it aims to achieve.

Comments on Guidance

Para 5(d) - specifies the requirement to "estimate" the amount of residual risk and would seem to require that this is done in the case of all risks rather than risks that are material to a Fund

Administration business. In our view, it would be more appropriate to only include a requirement to quantify the residual risk types which are considered material to a Fund Administrator.

Para 15 - we would like to understand the purpose of this reconciliation in terms of what it aims to achieve.

We hope you find these comments helpful, and we remain at your disposal to discuss the issues raised in this response further.

Yours faithfully,

Patrick J Lardner

Chief Executive