Significantly higher initial capital requirement (ICR) may have an impact on matched principal dealers

- The regulators are effectively signalling an end to the 'matched principal' limitation currently awarded under CRDIV and matched principal dealing will be treated the same as 'principal dealing' for prudential purposes
- The new initial capital requirement (ICR) will be EUR750K for all firms dealing on own account (i.e. dealing in its own name) including matched principal dealers that were previously subject to a lower EUR125K ICR as 'limited license' firms
- Smaller dealers currently making use of the matched principal limitation will see a significant rise in ICR. This is of particular importance to matched principal dealers that currently don't possess total own funds (share capital, retained earnings/losses, etc) of EUR750K to meet the new ICR

Transitional provisions for matched principal dealers

- Transitional provisions to ICR: matched principal dealers are currently either BIPRU50K (not holding client money or assets) or IFPRU125K (holding client money or assets) and will be able to benefit from transitional provisions to build up the necessary own funds to meet the new ICR (EUR750K) with annual increments of at least EUR5K from current levels (EUR50K or EUR125K) leading up to meeting the full amount of EUR750K by 26th June 2026
- Variable capital requirements: matched principal dealers will be able to limit their own funds requirements derived from variable capital requirements, the fixed overhead requirement (FOR) and the K-factor requirements, to twice their relevant own funds requirement as calculated in line with the current provisions of the CRR

Liquidity requirement for matched principal dealers

- The mandatory liquidity requirement is to hold an amount of liquid assets (cash, etc) equivalent to at least one third of the fixed overhead requirement

Few salient points on K-factors requirements

- K-CMH (client money held): Eligibility for title transfer collateral arrangements (TTCA) under K-CMH will be assessed by the FCA on an individual firm basis
- K-CMH: Client money controlled under CASS 8 mandates do not have to be included in K-CMH
- K-DTF (daily trading flow): For both DTF what is included under a 'cash trade' is not defined within the IFR. The FCA believes it should include transactions where purchase and settlement of the instrument takes place on the same trading day, or in line with a market standard settlement or delivery date (or earlier)
- K-CMG (clearing members guarantee): Where applicable investment firms may only use K-CMG when the competent authority permits its use

From ICAAP to ICARA

- Investment firms have to documents an internal capital adequacy and risk assessment (ICARA) to capture capital adequacy, liquidity assessment, and stress testing requirements

The new Pillar 1 and Pillar 2 (P2R and P2G)

- The new pillar 1 consists of an initial capital requirement (ICR), fixed overhead requirement (FOR), K-factor requirements, and liquidity requirement
- Pillar 2 is here to stay and SREPs (Supervisory Review and Evaluation Process) will still take place albeit with a slightly different approach consisting of a legal minimum requirement under P2R replacing the current Individual Capital Guidance (ICG) and where appropriate also an additional buffer to sit on top of the minimum requirements under P2G

Matched principal dealers to be in scope of the recovery and resolution directive (RRD) under new EUR750K ICR category. Wind down to be linked to reverse stress testing and included as part of an ICARA

- BIPRU50K and IFPRU125K are not currently in scope of the recover and resolution directive (RRD). However, as EUR750K firms they will be in scope of the RRD under the new prudential regime
- Wind down will have to be considered as part of the ICARA process. Regulators are signalling the importance of quantification of wind down costs as part of an ICARA
- Wind-down plan should be linked to the outcomes of reverse stress testing. It also needs to consider both the qualitative and quantitative aspects and any applicable provisions of the recovery and resolution directive

Mandatory Risk Committee Requirement

- Matched principal dealers whose value of on-and off-balance sheet assets average is more than EUR100 million over the 4-year period immediately before the given financial year are required to establish a risk committee

Remuneration Code

- A new code is likely to replace existing BIPRU and IFPRU remuneration codes

Please note that this is not an exhaustive list of requirements applicable to matched principal dealers. Other requirements may apply depending on your business model. Please also read our full summary of the IFD/IFR under heading 'New prudential requirements for investment firms' on our website https://www.pillar4consultants.co.uk/insights. Speak to us for a free initial consultation.