

FCA identifies IFPR failings

AT A GLANCE

February 2023

Contacts

David Croker
Partner

T: +44 (0) 7718 097331
E: david.w.croker@pwc.com

Andrew Strange
Director, FSRI

T: +44 (0) 7730 146626
E: andrew.p.strange@pwc.com

James Hawkins
Director

T: +44 (0) 7920 253161
E: james.m.hawkins@pwc.com

What's new?

- The FCA published initial [observations](#) from its thematic review into investment firms' implementation of the Investment Firm Prudential Regime (IFPR) rules on 27 February 2023.
- It focused on capital adequacy, liquidity adequacy and wind-down planning under the ICARA process, and wider regulatory reporting, finding several areas where firms are falling short of its expectations.
- Firms involved in the thematic review will have received individual feedback, but all investment firms must urgently consider the key findings and proactively address them. The FCA's thematic review is continuing.

What were the FCA's main findings?

- The FCA identified four areas where firms need to improve:
- **Investment firm groups:** many investment firm groups chose to complete a 'group ICARA process'. But when considering the thresholds of individual firms, the assessment didn't always comprehensively consider the risk and harms at each firm, and group level consolidated numbers were not adjusted for the effect of intragroup offsets.
- The FCA found that group-level financial resource requirements were allocated to individual firms without clear rationale.
- Groups undertaking a 'consolidated ICARA' must either have been invited to do so by the FCA or apply for a voluntary requirement (VREQ). Not all firms did this. Regardless, all individual firms must still complete a solo ICARA process, which again the FCA found was not always the case.
- **ICARA assessments:** the FCA found an absence of unified and integrated assessments, with a mismatch between risks assessed and associated risk management processes. Firms didn't use the risks they face when assessing risk appetite, warning indicators, early-warning triggers or stress testing scenarios. Firms also didn't consistently use reverse stress testing to quantify the cost of wind-down plans.
- Some firms significantly reduced their capital requirements for operational, credit and market risks under the IFPR, including ignoring risks not explicitly included in a K-Factor calculation despite acknowledging their presence, and often did not provide an explanation for these changes.
- Firms did not define own funds and liquidity triggers by reference to their own businesses, and failed to include orderly wind-down resources in calculations. There was also insufficient use of reverse stress scenarios to test credibility of intervention points.
- Where firm's OFTR/LATR were driven by wind-down resources, the FCA found firms often did not have adequate resources to minimise harm in failure.

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- If a firm's threshold requirement only equals its wind-down resource, its proposed actions would need to reflect its inability to absorb any further stress, and any breach of the threshold must be reported to FCA under Principle 11.
- FCA found some firms had failed to act on previous feedback. Board engagement was varied, with the best firms providing in-depth training to senior staff.
- **Wind-down plans:** Overall, wind-down own funds and liquid asset assessments were less robust, with unrealistic assumptions and poor modelling.
- Firms should have started wind-down planning estimates with a stress scenario or trigger event, rather than in a benign environment.
- Investment firm groups didn't consider critical wind-down dependencies over other group entities, such as the financial resilience of group service companies.
- Overall the FCA found wind-down planning was not often comprehensive, with elements (often bespoke processes or products) not assessed.
- **Data quality:** Some firms provided inaccurate or incomplete data, which the FCA specifically references back to SYSC and SM&CR responsibilities. The FCA cites a number of previous publications to underline the importance it places on regulatory reporting.
- It is clear that there are many areas where firms need to review and revisit their IFPR implementation and ICARA reporting to ensure alignment of risk processes and the ICARA.
- Firstly, all firms should review their existing ICARAs against the FCA's observations, and put plans in place to address any gaps through their 2023 processes and documents.
- Given the strength of the findings related to wind down planning, firms should revisit their approaches, taking into account the FCA's [wind down planning guidance](#) and the findings of this review
- All firms should review the governance over their regulatory reporting processes and should take steps to validate (and correct where necessary) the accuracy and quality of previous regulatory submissions.
- Investment firm groups must immediately reconsider their ICARA process, at both firm and group levels. This should include reviewing risks and harms, mitigants and thresholds.
- All firms should review the alignment of their risk management processes with their ICARAs, with a particular focus on the specific risks of harm being considered, the setting and use of risk appetites and own funds and liquid asset triggers and limits
- Boards, and SMF holders, will want to be sure they are comfortable with their firm's approach, and to revisit and challenge existing activities.

What do firms need to do?

- The FCA has published these initial observations but is continuing its review; this underlines the urgency and breadth of the issues they have identified at this stage.

Next steps

The FCA's initial observations allow firms to react swiftly to the regulator's concerns as part of their 2023 ICARA processes and prior to the conclusion of the thematic review. Firms should perform a gap assessment of their IFPR implementation against these preliminary findings.

