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6 REGULATORY CAPITAL AND LIQUIDITY

6.1 Introduction

This section of the Manual sets out the Firm's arrangements to maintain adequate capital resources. This reflects the Firm's prudential supervision under the Investment Firms Prudential Regime (IFPR) from January 2022 as a small and non-interconnected (SNI) firm.

6.2 Overall Financial Adequacy Rule (OFAR)

The Firm has been categorised as an SNI firm. On that basis, the Firm comes under the rules in the MiFIDPRU Prudential Supervision sourcebook.

The Firm must at all times hold own funds and liquid assets which are adequate, both as to their amount and quality, to ensure that the Firm is able to remain financially viable throughout the economic cycle, with the ability to address any material potential harm that may arise from its ongoing activities, and that the Firm's business can be wound down in an orderly manner, minimising harm to consumers or to other market participants. This is known as the overall financial adequacy rule.

Essentially, the Firm must have capital resources to meet its liabilities as they fall due, and additionally have processes, strategies and systems to assess and maintain adequate (financial, capital, internal capital) resources to withstand the risks it is exposed to, and to meet all regulatory obligations.

6.3 Responsibility for Maintaining Adequate Capital Resources

The Compliance Officer in conjunction with any other partner(s) is responsible for monitoring capital resources and capital requirements and ensuring that there are sufficient capital resources.

6.4 Ongoing Capital Resources Requirement

As an SNI firm, the rules in MiFIDPRU state that ongoing capital must be comprised of an own funds requirement and a liquid assets requirement.

The own funds requirement is further comprised of a firm's permanent minimal capital requirement (PMR) under MiFIDPRU 4.4 and its fixed overheads requirement (FOR) under MiFIDPRU 4.5. The Firm's PMR is £75,000, subject to any transitional arrangements that apply on own funds as an existing firm prior to the implementation of IFPR.

A firm's FOR is an amount equal to one quarter of the firm's relevant expenditure during the preceding year. The accounting framework applied must accord with the criteria set out in MiFIDPRU 4.5.2R and set out at 6.10.1 below.

6.5 Annual Operating Expenditure

The Firm's relevant expenditure is defined as follows:

'The sum of the amounts described as total expenditure in the 4 quarterly financial returns up to (and including) that prepared at the firm's most recent accounting reference date, less the following items (if they are included within such expenditure)'.

- Staff bonuses, except to the extent that they are guaranteed, and other variable remuneration.
- Employees' and partners' shares in profits, except to the extent that they are guaranteed.
- Other appropriations of profits.
- Non-recurring expenses from non-ordinary activities.
- Shared commission and fees payable, which are directly related to commission, and fees receivable, which are included within total revenue.
- Interest charges in respect of borrowings made to finance the acquisition of the Firm's readily realisable investments.
- Interest paid to customers on client money (not applicable).
- Interest paid to counterparties.
- Fees, brokerage and other charges paid to clearing hours, exchanges and intermediate brokers for the purposes of executing, registering or clearing transactions.
- Taxes where they fall due in relation to the annual profits of the firm.
- Other expenses to the extent that their value has already been reflected in a deduction from own funds under MiFIDPRU 3.3.6R (Common equity tier (CET) 1 deductions).

FOR should be based on the last audited accounts. However, if the FOR increases by 30% or more during the year, this must become the new FOR requirements under the ICARA with immediate effect. If the FOR reduces by the same, FCA consent to reduced capital requirements must be obtained in advance.

A firm's financial resources requirement will be recalculated annually when its fourth financial return is prepared. The Firm must maintain financial resources sufficient to meet its new financial resources requirement from the date on which the fourth quarterly financial return is prepared and no later than 80 business days after the Firm's accounting reference date. The above FOR applicable at the accounting reference date will be based on the 4 quarterly financial returns prepared up to and on that date.

6.6 Liquid Assets Requirement

The basic liquid assets requirement for a firm equates to an amount of core liquid assets (defined in MiFIDPRU 6.3) which is equal to the sum of:

- One third of the amount of its FOR; and
- 1.6% of the total amount of any guarantees provided to clients.

The Firm normally holds its liquid funds requirement in cash.

6.7 ICARA

The Compliance Officer in conjunction with any other partner(s) is responsible for making sure that the OFAR is met. The Firm will utilise the internal capital adequacy and risk assessment (ICARA) process to identify whether it complies with the OFAR. This process is laid out in MiFIDPRU 7.

The ICARA is central to a firm's risk management process to identify and monitor the potential harms to consumers, to the market in which it operates and to the firm itself, and to reduce all potential material harms that may result from the ongoing operation of its business or from winding down.

Under FCA requirements, it covers:

- Identification, monitoring and mitigation of harms (in line with MiFIDPRU7 Annex 1).
- Business model planning and forecasting.
- Recovery and wind-down planning – assessing the adequacy of financial resources.

This will normally include a firm-wide Risk Register. The outcome may include holding additional own funds and liquid assets, where necessary.

The ICARA process should be reviewed at least once every 12 months but also to review this following any material change including an increase in costs. More complex firms might need to consider half yearly.

6.8 FCA Notification Requirements

Rules require that FCA investment firms must notify the FCA where their level of own funds and/or liquid assets fall below these intervention points.

The Firm needs to consider any notification impacts if own funds fall to within 110% of the requirement. Therefore, it is always recommended to hold more than 110% of the FOR and have additional surplus to avoid notification risk.

6.9 ARs and Capital Adequacy

ARs are not themselves subject to specific capital adequacy risks. However, the Firm as principal is required to ensure the financial soundness of its ARs in line with SUP 12 Annex 1. The Firm does this as part of onboarding a new AR but also on an ongoing basis through monthly reporting, receipt of at least quarterly management accounts from its ARs, and again as part of formal annual monitoring visits.

6.10 Financial Reporting

Principle 4 requires firms to maintain adequate financial resources. By submitting regular data, firms enable the FCA to monitor their compliance with Principle 4 and their prudential requirements in the FCA Handbook.

6.10.1 Electronic Reports

The Firm's required financial returns, as an IFPRI SNI, are showed at MiFIDPRU 9. The Firm's reporting schedule is listed on the FCA reporting system known as RegData. This normally requires the submission of quarterly financial statements based on the Firm's accounting reference date which is 31 March. In addition, annual audited financial statements must be sent to the FCA within 80 business days of its financial year end.

6.10.2 Submission of Data Items

When submitting the completed data item, except where there is no standard format, the Firm must use the format of the data item set out in MiFIDPRU9 Annex 1.
https://www.handbook.fca.org.uk/form/mifidpru/MIFIDPRU%209%20Annex%201R%20Data%20items%20for%20MIFIDPRU%209%20Annex%201R.pdf

Four guidance notes for completion of the data items are contained in MiFIDPRU9 Annex 2.
https://www.handbook.fca.org.uk/form/mifidpru/MIFIDPRU9_Annex2G_01012022.pdf

Sterling is the normal reporting currency; however, the systems permit reporting in the currency of the annual accounts.

Any non-standard format items must be sent to:

Central Reporting
The Financial Conduct Authority

12 Endeavour Square
London E20 1JN

Or via email to: Regulatory.reports@fca.org.uk

Copies of each submission should also be retained on the Firm's own records.