



The Investor Compensation Company DAC

Risk Equalisation Rule

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Contents

1	Introduction	3
2	Responses to the questions posed on each proposal.....	4
	(i) Proposal (1) – Amendment to the threshold at which the RER becomes applicable	4
	(ii) Proposal (2) Amendment to the timeline for payment of the RER and the lookback timeframe	5
	(iii) Proposal (3) Amendment to address the interaction between the RER and the annual levy payment.....	6
	(iv) Proposal (4) Amendment to adjust the level of the Reserves Percentage applied in the RER formula	9
3	Transitional arrangements and related matters	10
4	Next steps	12
5	Revised Formula for the RER (<i>incorporates proposals 1, 2 & 4 from the consultation paper unamended</i>)	13
6	Addendum to the 2022 – 2025 Funding Arrangements to give effect to proposal 3.....	14
7	Glossary	15

1 Introduction

The Investor Compensation Company DAC ('ICCL') introduced the Risk Equalisation Rule ('RER') on 1 March 2020 to compliment the operation of the ICCL cascade model in scenarios where the transfer of significant amounts of covered assets into the Irish Investor Compensation Scheme ('the ICS') from other jurisdictions, either through newly authorised entities, or, to existing authorised entities (through an acquisition, restructuring, or other such arrangement) without an equivalent transfer of matching ICS funding arose.

The first review of the RER, which included a consultation, was published in November 2023 with the consultation phase closing in January 2024. Based on the ICCL's experience of operating the RER since 1 March 2020, the ICCL set out three proposed amendments to the RER and one proposed amendment to the Fund A basis of assessment contained in the Annual Funding arrangements¹. The ICCL has consulted with the Central Bank of Ireland ('the Bank') on the revisions to the Risk Equalisation Rule put forward, as required by the Investor Compensation Act, 1998.

While the ICCL received some engagement from participant firms and representative bodies during the consultation phase, we received only one substantive response to the consultation on the RER which is published separately to this document on the ICCL's website.

The RER is of relevance to current and prospective member firms of Fund A of the ICS. Such firms include licenced credit institutions, authorised MiFID investment firms, some UCITS and AIFM firms²:

- that cause the aggregate level of assets covered by the ICS to increase by €250 million or more upon authorisation by the Central Bank of Ireland ('the Bank') or at any point in the three-year period following authorisation by the Bank; and/or
- that acquire a book of business or enter into any transaction, restructuring, or other arrangement that causes the aggregate level of assets covered by the ICS to increase by €250 million or more upon the completion of a transfer, restructuring, transaction or other arrangement or at any point in the three-year period following the completion of the transfer, restructuring, transaction or other arrangement.

¹ [220518 - ICCL Funding Arrangements - Published.pdf \(investorcompensation.ie\)](#)

² UCITS and AIFMs authorised to provide individual portfolio management (IPM)

2 Responses to the questions posed on each proposal

(1) PROPOSAL (1) – AMENDMENT TO THE THRESHOLD AT WHICH THE RER BECOMES APPLICABLE

The ICCL proposed to amend the operation of the threshold at which the RER becomes applicable. The €250m level of the threshold would remain unchanged, however, for any RER transaction(s) that exceed the €250m threshold, the first €250m of client assets would not count towards the calculation of the RER levy itself. In effect, this would create a one-time, or for the avoidance of doubt, a life-time credit, for firms subject to the RER to ensure an even application of the RER to all firms.

Views were sought in respect of the proposal:

- to retain the threshold at €250 million, and,
- to provide a one-off credit against the first €250 million that is subject to an RER transaction.

Feedback received:

The response received indicated support for the proposed amendment while also indicating it was unaware of the rationale underlying the threshold, suggesting it appears to be arbitrary.

ICCL Response

The ICCL welcomes the feedback received and intends to proceed with the proposal as set out under proposal (1) of the consultation paper. The ICCL intends to incorporate any residual observations into a wider review of funding arrangements of the Investor Compensation Scheme that it intends to commence during 2024 and which is intended to conclude in 2025.

(II) PROPOSAL (2) AMENDMENT TO THE TIMELINE FOR PAYMENT OF THE RER AND THE LOOKBACK TIMEFRAME

The ICCL proposed an optional alternative payment mechanism whereby, at the request of the firm subject to the RER, a minimum initial RER payment of 25% of the estimated asset migration would be required within 30 days of the initial transfer (RER₀). Additional payments would arise at each 12-month lookback date. A firm subject to the RER, if it elected to stagger its payments, would therefore discharge its RER liability over up to four payment dates (broadly speaking, over a three-year period).

However, if a firm did not elect for the alternative payment mechanism, the firm would continue to make the full payment at RER₀ and continue to pay any additional lookback amounts arising at RER₁, RER₂ and RER₃.

It was also proposed to adjust the first lookback date (RER₁) (and subsequent lookbacks) from the date of the firm's financial year-end immediately after the first RER event (RER₀) to the initial date of migration plus 12 months (24 months and 36 months respectively) resulting in a full 3-year lookback period.

Views were sought in respect of the proposals to:

- provide an option to discharge the RER liability in four payments, and,
- align the lookback periods with the initial date of migration.

Feedback received:

The response received had no substantive comments on this proposal but did indicate it was generally in favour of providing firms with more options for payment of the REL in a way that more accurately reflects the timing of the transfers.

ICCL Response

The ICCL welcomes the feedback received and intends to proceed with the proposal as set out under proposal (2) of the consultation paper.

(III) PROPOSAL (3) AMENDMENT TO ADDRESS THE INTERACTION BETWEEN THE RER AND THE ANNUAL LEVY PAYMENT

The ICCL proposed to remove a one-off relief from the annual levy for firms that were both newly authorised and initiating an RER in-scope transfer within the same ICCL funding year within which they are authorised (e.g., between 1 August and 31 July) and to replace this relief with an enhanced relief that would also be available to existing firms that became subject to the RER.

The alternative relief proposed would be provided on an equal basis to newly established firms and existing firms that are subject to an RER levy and would apply to clients whose assets transferred as part of an in-scope RER transaction during the period between RER₀ and RER₃, and not solely in year one. The proposed relief provides a credit in respect of eligible client numbers that are included within the "CA" value migrated by the firm subject to the RER against the annual levy of the firm, for a maximum of three funding years during the application of the RER and related lookback period.

In calculating its annual levy, a firm's total number of eligible clients would be adjusted down as appropriate to exclude RER-related clients over the subsequent 3 years. This would be applied as follows:

- For each ICCL funding year during which a firm is subject to the RER, when submitting the value of "CA" to enable calculation of the Initial Risk Equalisation Levy (RER₀) (and/or) the Lookback Risk Equalisation Levy 1 (RER₁) and/or 2 (RER₂) and/or 3 (RER₃), the firm will advise the ICCL of the number of eligible clients to which the "CA" projected or known covered assets related to.
- When submitting the ICCL Return 1 (Self-assessment for annual levy) which currently requires a firm to identify the band within which its eligible client numbers arise, in order to avail of the RER annual levy relief, it would be necessary for the firm to undertake enhanced reporting to ICCL.
- Enhanced reporting would require the firm to report both its total eligible client number and the number of eligible clients that were in-scope for the RER during the firm's financial year which ended immediately prior to the commencement of the ICCL's funding year. This period will not

align with the RER periods (unless the RER initial transfer was on the first date of the firm's financial year) so it will create an additional reporting requirement for firms.

- This control is necessary to ensure, on completion of the RER lookback periods, that the number of excluded RER clients from the annual levy process aligns with the number of clients returned during the RER process.
- The proposed relief could only be claimed in three consecutive funding years during the application of the RER. This is to prevent a firm obtaining four years of relief which could otherwise occur due to the timing of an RER transaction whereby a firm's RER transaction could straddle four funding years. It is proposed that in such circumstances, a schedule of funding years to which the Annual Levy relief can be claimed will be considered and the firm will be notified by the ICCL which three years relief will be applied against.

Views were sought in respect of the proposal to alter the Fund A basis of assessment contained in the Annual Funding arrangements to exclude the number of eligible clients that are included in the RER calculation from the total number of eligible clients for annual levy purposes subject to the three-year limit as set out above.

Feedback received:

The response received is supportive of the proposed amendments but does not consider that the amendments go far enough. In summary, the respondent suggests that the entire ex-ante funding requirement is paid by way of REL and proposes that the relief period for those clients should go beyond the proposed three-year period.

The respondent also proposed that the Covered Asset (CA) value of the RER formula should be amended to only incorporate eligible investor assets as opposed to retail client assets.

The respondent further proposed that the exclusion of eligible clients within the scope of the RER levy, should be applied retroactively to firms that have already been required to contribute under the existing RER. The respondent is of the view that given the relatively short time-period that has elapsed since the introduction of the RER (1 March 2020), that such a retroactive amendment would not have a destabilising effect on the Fund, and, would help align the position for firms that were subject to the RER as introduced on 1 March 2020, and firms that may be subject to the RER post any finalised amendments.

ICCL Response

The ICCL welcomes the feedback received. The ICCL notes the opinion of the respondent that the entire ex-ante levy is paid by way of REL, however, this view does not recognise, as set-out in the consultation paper, that the annual levy addresses other costs besides the ex-ante fund requirement and includes operating costs, and/or, fund rebuilding costs linked to failure cases.

The ICCL notes the view of the respondent concerning the base assets used for calculating RER levy obligations. Any proposal to amend the base, given its direct link to the overall Cascade Funding model, would require a detailed review and assessment to ensure it would not have a destabilising, or other unintended or unforeseen effect on the fund(s) that might impact on the Scheme's capacity. It would therefore seem appropriate to consider any amendment to the base in the context of a wider review of funding arrangements of the Investor Compensation Scheme that ICCL intends to commence during 2024 and which is intended to conclude in 2025.

The ICCL intends to proceed with the proposal as set out under proposal (3) of the consultation paper.

In the context of the proposal from the respondent to retroactively apply the proposed amendment to firms that have been subject to the existing RER, this matter is addressed under section 3 of this document.

(IV) PROPOSAL (4) AMENDMENT TO ADJUST THE LEVEL OF THE RESERVES PERCENTAGE APPLIED IN THE RER FORMULA

The ICCL proposed aligning the RM factor for the RER with the relevant RM factor established in the triennial funding arrangements of the ICCL for the cascade model. The RM factor set out in the current funding arrangements document which is in operation from 1 August 2022 to 31 July 2025 is targeted at 28% (compared to the target of 33.3% as incorporated in the current RER).

It was also proposed that the RM factor for RER transactions that straddle two triennial funding cycles would also have the aligned RM factor applied to them. This would be the RM factor in operation for the triennial funding cycle at the lookback date Y₁, Y₂, or Y₃.

Views were sought in respect of the proposal to align the RM factor for RER transactions with the relevant target RM factor for the triennial funding arrangements period.

Feedback received:

The sole respondent is supportive of the proposed amendment.

ICCL Response

The ICCL welcomes the feedback received and intends to proceed with the proposal as set out under proposal (4) of the consultation paper.

3 Transitional arrangements and related matters

The ICCL is conscious that it was not possible to complete the review of the RER in line with the triennial funding review which concluded in May 2022, however, certain outputs from the triennial funding review have had a material bearing on the proposed amendments to the RER, such as the revised RM factor. In addition, the ICCL is aware that some RER transactions are “in-flight” at present while others have arisen since the revisions to the triennial funding arrangements took effect. It is therefore necessary and appropriate to clarify for those firms whether, and if so, how, the proposed amendments to the RER would impact on their transactions.

Accordingly, the ICCL has considered such circumstances, including in the context of the impact on the existing fund(s) and on the firms that were subject to the RER, and, from a cumulative levy liability perspective. The ICCL can provide the following clarifications to firms that have paid an RER levy between 1 March 2020 and the 31 March 2024 (the date when the RER was amended).

Proposal 1:

This proposal amends the operation of the threshold at which the RER becomes applicable. The €250m level of the threshold remains unchanged, however, for any RER transaction(s) that exceeds the €250m threshold, the first €250m of client assets would not count towards the calculation of the RER levy itself. This proposal introduces a one-time credit to reduce the quantum of covered assets migrated by €250m.

The ICCL will apply this proposal to all RER transactions that were initiated between 1 March 2020 and 31 March 2024.

Proposal 2:

This first element of this proposal provides an optional alternative payment mechanism. A firm subject to the RER, if it elected to stagger its payments, could therefore discharge its RER liability over up to four payment dates (broadly speaking, over a three-year period).

However, if a firm did not elect for the alternative payment mechanism, the firm would continue to make the full payment at RER₀ and continue to pay any additional lookback amounts arising at RER₁, RER₂ and RER₃.

The second element of this proposal adjusts the first lookback date (RER₁) (and subsequent lookbacks) from the date of the firm's financial year-end immediately after the first RER event (RER₀) to the initial date of migration plus 12 months (24 months and 36 months respectively) resulting in a full 3-year lookback period.

The ICCL will apply the adjusted lookback dates to all RER transactions that were initiated between 1 March 2020 and 31 March 2024.

The ICCL does not intend to apply the optional alternative payment mechanism to any RER transactions that were initiated between 1 March 2020 and 31 March 2024 on the basis that those transactions are either completed or substantially completed at this time.

Proposal 3

This relief, which addresses the interaction between the RER and the Annual levy will be provided on an equal basis to newly established firms and existing firms that are subject to an RER levy and applies to clients whose assets transferred as part of an in-scope RER transaction during the period between RER₀ and RER₃, and not solely in year one. The proposed relief provides a credit in respect of eligible client numbers that are included within the "CA" value migrated by the firm subject to the RER against the annual levy of the firm, for a maximum of three funding years during the application of the RER and related lookback period. In calculating its annual levy, a firm's total number of eligible clients would be adjusted down as appropriate to exclude RER-related clients over the subsequent 3 years.

The ICCL will apply the relief which addresses the interaction between the annual levy and the RER to all RER transactions that were initiated between 1 March 2020 and 31 March 2024.

Proposal 4

This proposal will align the RM factor for the RER with the relevant RM factor established in the triennial funding arrangements of the ICCL for the cascade model. The RM factor set out in the current funding arrangements document which is in operation from 1 August 2022 to 31 July 2025 is targeted at 28% (compared to the target of 33.3% as incorporated in the RER which took effect on 1 March 2020 and operated until 31 March 2024).

The proposal also provides that the RM factor for RER transactions that straddle two triennial funding cycles would have the RM factor in operation for the triennial funding cycle at the lookback date Y₁, Y₂, or Y₃ applied to them.

The ICCL will apply the RM factor to all RER transactions that were initiated between 1 March 2020 and 31 March 2024 on the same basis as set out in the proposal.

4 Next steps

The ICCL will apply the revised RER as set out in section 5 to any in-scope transaction with effect from 1 April 2024.

In the context of firms that had initiated RER in-scope transactions between 1 March 2020 and 31 March 2024, the ICCL will engage with those firms directly to finalise the outcomes of the transitional and related matters set-out in section 3 of this document.

All firms in Fund A will be notified of the amended status of the RER, and the updated RER will be published on the ICCL's website for reference.

The ICCL will proceed to consider other matters raised in this consultation in the context of a wider review of funding arrangements of the Investor Compensation Scheme that is intended to commence during 2024 and which is intended to conclude in 2025, following a separate consultation process with the Bank and participant firms.

5 Revised Formula for the RER (incorporates proposals 1, 2 & 4 from the consultation paper unamended).

Participant firms should be aware that the formula below will take effect **from 1 April 2024**.

Definitions

- CA** Greater of the estimated covered assets migrated or actual covered assets migrated
- RM** is the reserves percentage of cascade model at the start of the current triennial funding cycle **(28% for the period 1 August 2022 to 31 July 2025)**
- RER₀** is the Initial Risk Equalisation Levy amount
- RER₁** is the 1st Risk Equalisation Levy lookback amount
- RER₂** is the 2nd Risk Equalisation Levy lookback amount
- RER₃** is the 3rd Risk Equalisation Levy lookback amount
- Y₀** Initial transfer date
- P₀** Initial payment (due 30 days from Y₀)
- Y₁** Initial transfer date + 12 months
- P₁** Look-back payment 1 (due 30 days from Y₁)
- Y₂** Initial transfer date + 24 months
- P₂** Look-back payment 2 (due 30 days from Y₂)
- Y₃** Initial transfer date + 36 months
- P₃** Look-back payment 3 (due 30 days from Y₃)

$$RER_0 = \{ \{ \{ CA^{Y_0} \text{ minus } \text{€}250\text{mn}^3 \} * 0.5\% \} * RM \} * 25\%$$

$$RER_1 = \{ \{ \{ \{ CA^{Y_1} \text{ minus } \text{€}250\text{mn} \} * 0.5\% \} * RM \} * 50\% \} \text{ minus } \sum RER_0$$

$$RER_2 = \{ \{ \{ \{ CA^{Y_2} \text{ minus } \text{€}250\text{mn} \} * 0.5\% \} * RM \} * 75\% \} \text{ minus } \sum \{ RER_0 + RER_1 \}$$

$$RER_3 = \{ \{ \{ \{ CA^{Y_3} \text{ minus } \text{€}250\text{mn} \} * 0.5\% \} * RM \} * 100\% \} \text{ minus } \sum \{ RER_0 + RER_1 + RER_2 \}$$

³ €250 million credit is a one-time credit and as such can only be claimed once by a member firm of Fund A

6 Addendum to the 2022 – 2025 Funding Arrangements to give effect to proposal 3

2.1.7 RER Eligible Client relief

Certain Fund A firms, that have undertaken a transaction that is in-scope for the Risk Equalisation Rule ('RER'), with effect from 1 April 2024, will be eligible to reduce their number of eligible clients, for the annual levy, by the number of eligible clients which were in-scope for the RER transaction.

For each ICCL funding year during which a firm is subject to the RER, when submitting the value of "CA" to enable calculation of the Initial Risk Equalisation Levy (RER₀) (and/or) the Lookback Risk Equalisation Levy 1 (RER₁) and/or 2 (RER₂) and/or 3 (RER₃), the firm will advise the ICCL of the number of eligible clients to which the "CA" projected or known covered assets related to.

To avail of the RER annual levy relief, the firm will need to undertake enhanced reporting which requires the firm to report both its total eligible client number and the number of eligible clients that were in-scope for the RER during the firm's financial year which ended immediately prior to the commencement of the ICCL's funding year. This period will not align with the RER periods (unless the RER initial transfer was on the first date of the firm's financial year) so it will create an additional reporting requirement for firms.

This control is necessary to ensure, on completion of the RER lookback periods, that the number of excluded RER clients from the annual levy process aligns with the number of clients returned during the RER process.

The relief can only be claimed in three consecutive funding years during the application of the RER and associated lookback period. This is to prevent a firm obtaining four years of relief which could otherwise occur due to the timing of an RER transaction whereby a firm's RER transaction could straddle four funding years. In such circumstances, a schedule of funding years to which the Annual Levy relief can be claimed will be considered by the ICCL and the firm will be notified by the ICCL which three years relief will be applied against.

7 Glossary

AIF	Alternative Investment Funds
ICCL	The Investor Compensation Company DAC
MiFID	Markets in Financial Instruments Directive
RER	Risk Equalisation Rule
The Bank	Central Bank of Ireland
The ICS	Investor Compensation Scheme
UCITS	Undertakings for Collective Investments in Transferable Securities

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