

27 April 2007

The Committee of European Securities Regulators
11-13 Avenue de Friedland
75008 Paris
France

Dear Sirs

**Response to the second Consultation Paper on Inducements under MiFID
(CESR/07-228)**

The Investment Management Association (IMA) is the trade body representing the UK asset management industry¹.

We welcome this second consultation, and were pleased to participate in the Open Hearing in Paris earlier this week. In particular, we welcome the additional clarity and flexibility set out in the Recommendations and Illustrative Examples. We support the additional transparency that will result from such disclosure obligations.

We do have strong concerns that as these disclosure requirements apply only to MiFID investment firms undertaking MiFID investment services and activities and that, in many Member States, no equivalent requirements exist for other products and services or other firms, there will exist the potential for a misleading picture being provided to investors. We believe that there will be a strong incentive for firms to use other equivalent products which are not included in the MiFID regime, and could be used. In any case some intermediaries will be subject to these disclosures and not others. We therefore welcome the confirmation, on page 6, that CESR will be raising the issue with the European Commission. We believe, however, that a great deal can and should be done at national level without waiting for intervention at EU level. In many cases, the CESR members themselves are in a position to bring national practices in line for different products. We are pleased that a number have already stated that they will do this and would strongly urge more to do so. We

¹ IMA members include independent fund managers, together with the asset management arms of banks, life insurers and investment banks, and occupational pension scheme managers. They are responsible for the management of nearly £3 trillion of funds (based in the UK, Europe and elsewhere), including authorised investment funds, institutional funds (e.g. pension and life funds), private client accounts and a wide range of pooled investment vehicles. In particular our members manage 99% of UK-authorised investment funds (i.e. authorised unit trusts and open-ended investment companies).

also believe that it will be important for CESR to cooperate closely with CEBS and with CEIOPS.

At the Open Hearing, if I recall correctly, it was stated that CESR would look at whether more could be done about defining the term “inducement”. This would be a helpful move. In particular, there seems to be an interpretation that the definition would include payments made by fund managers to non-MiFID entities for normal business needs. For example, a fund manager needs to have a number of electronic systems for different aspects of its business, and will purchase those items from their normal suppliers. But, as these systems would then be used by the investment firm in relation to its investment services, it could be argued that some form of disclosure is required. We do not believe that this is the intended result (no-one is inducing anyone else, nor is there such a potential), and that a definition of ‘inducement’, or of ‘fee’ would provide the relevant clarity.

To respond to the questions posed:

Question 1: Do you have any comments on the content of the draft recommendations?

Recommendation 4:

We believe that the introduction of the factors is helpful, and would suggest that they could be further enhanced by taking into account the potential for conflicts of interest to be taken into account. We attach – Appendix 1 – some suggested text for your consideration.

Recommendation 5:

We welcome the additional comments and flexibility set out. It mirrors our understanding of the position, and so it is helpful to have it confirmed.

Recommendation 6:

1. We believe that it is very important for CESR to provide guidance to competent authorities on the make-up of intra-group monetary and, more particularly, non-monetary benefits, and to how this could be adequately incorporated into a summary disclosure of the “essential terms”. We believe that there is a danger that a lack of standardisation will lead to different disclosures being required, with the potential for investor confusion or misunderstanding. It is important that disclosures are based on a strong arms-length approach and that there is genuine comparability between disclosures of in-house payments and disclosures of payments to a third party.
2. Sub-paragraph (c) proposes that each MiFID investment firm should have to comply with the disclosure requirements, at least to the extent that that firm is providing a MiFID service or activity. We confirm our understanding is that this is the limit of these disclosure requirements, and that there would be no obligation created that a MiFID investment firms must make disclosures relating to any other firm.

Therefore, if an investor was to place an investment into a CIS (MiFID exempt) via a financial adviser (MiFID exempt under Article 3), and where a MiFID investment firm was involved in the chain by marketing the funds (not a MiFID investment service), then no disclosure, at least under MiFID, would be required by any of the entities.

Question 2: Will the examples prove helpful in determining how Article 26 applies in practice? What other examples should be covered or omitted?

Question 3: Do you have any comments on the analysis of the examples?

We welcome the illustrative examples; we believe that they will help investment firms to understand and interpret their obligations.

Example VIII tackles the problem of differential commission payments, and raises the conflict that might arise within an advisory firm. However, the existence of such payments may not necessarily create a problem. It would depend on other circumstances. For example, is the starting rate lower than that available from other product providers? Has this same arrangement been made with all product providers? It is certainly for the receiving firm to identify such conflicts of interest and act accordingly, but it should not definitively be seen as preventing a product provider from arranging such terms.

Should you wish to discuss any of the points we have raised in further detail please do not hesitate to contact me.

Yours faithfully

Angus Milne
Senior Adviser

Appendix 1

Recommendation 4: Factors relevant to arrangements within Article 26(b)

CESR considers that among the factors that an investment firm should consider in determining whether an arrangement may be deemed to be designed to enhance the quality of the service provided to the client and not impair the duty of the firm to act in the best interests of the client are the following:

(a) The type of the investment or ancillary service provided by the investment firm to the client, and any specific duties it owes to the client in addition to those under Article 26, including those under a client agreement, if any;

(b) The expected benefit to the client(s) including the nature and extent of that benefit, and any expected benefit to the investment firm; the analysis about the expected benefit, can be performed at the level of the service to the relevant client group;

(c) Whether there will be an incentive for the investment firm to act other than in the best interests of the client and, ***as a consequence,*** whether the incentive is likely to change the investment firm's behaviour ***(the mere existence of an incentive is not by itself a relevant consideration)***.

(d) The relationship between the investment firm and the entity which is receiving or providing the benefit (although the mere fact that a group relationship exists is not by itself a relevant consideration);

(e) The nature of the item, the circumstances in which it is paid or provided and whether any conditions attach to it.

The evaluation of factors (a) through (e) shall be carried out taking into consideration the steps taken by the investment firm to prevent and manage conflicts of interest.