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17th September 2004

By email to CESR at www.cesr-eu.org

Dear Sirs

Final Response to CESR on Advice on Possible Implementing Measures of the Directive on Markets in Financial Instruments (MiFID) – Section II Intermediaries

The Association of Private Client Investment Managers and Stockbrokers (APCIMS) is the organisation that represents those firms who act for the private investor and who offer them services that range from no advice or 'execution only' trading through to portfolio management for the high net worth individual. Our 217 member firms operate on more than 500 sites in the UK, Ireland, Isle of Man and Channel Islands and following the merger of EASD into APCIMS, increasingly in other European countries as well. APCIMS members have under management Euros 450billion for the private investor and undertake some 13 million trades for them annually.

This final response is in addition to our first stage response submitted to CESR on 10 September and covers the following sections:

13(3), 18 Conflicts of interest
13(5) Avoidance of undue operational risk in cases of outsourcing
19(2) Fair, clear and not misleading information
19(3) Information to clients
19(7) Client agreements
22(1) Client order handling

In preparing this response we have extensively consulted with our member firms both in the UK and other European countries. We have been keen to ensure that the issues that we raise and the answers to the questions posed by CESR are representative of as broad a range of intermediary firms as possible. We have concentrated on those proposed rule changes that our firms tell us may be workable, but which would result in increased costs for consumers and few, if any, regulatory or consumer protection benefits.

We wish to raise again the general observation made in the first stage of our response in respect to the agreement of grandfathering arrangements. It will be particularly important that CESR agrees to such arrangements in respect of situations where additional costs of implementation

will have to be borne by clients, but for no discernable benefit or additional protection for clients above those afforded under the existing regime. An example of this was given in our previous response of 10 September in respect to changes to the content of client agreements, where we gave an estimated cost to our membership of more than Euro 35million.

One final observation is that we note that CESR has taken as its own point of reference the CESR Standards on Investor Protection, which were drawn up in 2001 and 2002. We provided comments at that time on these Standards, and many of our comments remain valid. We were disappointed then at the lack of feedback to trade associations and industry from CESR and it is clear that much of industry's contribution was not incorporated for reasons that have not been explained to us. We hope, therefore, that CESR is undertaking a genuine consultation on this important subject and will be open to changing any Standards where industry evidence indicates that the proposed Standards are unworkable or too detailed or would not achieve the harmonisation that is the goal.

We hope these comments are helpful in the development of CESR's advice and should you have any further questions in this regard please do not hesitate to contact me at helenb@apcims.co.uk.

Yours faithfully

Helen Banks
Head of UK Regulation

CONFLICTS OF INTEREST

APCIMS General Response to the Proposals

We would like to highlight the importance of the general principle that the policies put in place by firms to manage potential conflicts of interest must be relevant to the nature, scale and complexity of the business. It is often not possible to "ring-fence" particular functions. For example, APCIMS has a large number of members who carry out both investment and portfolio management, where an individual will act as both investment manager and analyst.

In addition, we consider that it will be important for CESR to agree grandfathering arrangements where certain disclosures are to be made and consents obtained at the start of a relationship, in relation to potential conflicts. It would be a very costly exercise for firms to comply with any such requirements in respect of their existing customer base and is unlikely to bring them any benefits.

A further important issue is the need for clarification of the scope of application of the requirements in respect to counterparties. Recital 31 to the MiFID states that measures to protect investors should be adapted to the particularities of each category of investors (retail, professional and counterparties). However, in the absence of any specific exclusion in the CESR guidance on managing conflicts in relation to counterparties, who would fall within the definition of "client" given within Article 4, it would appear that the requirements of Article 18 would apply to counterparties. We suggest that the conflicts policy and disclosure requirements set out in the draft implementing measures are not applied to arms-length own-account trading between counterparties. In relation to the UK regime it should be noted that Principle 8 of the FSA Handbook text requires firms to manage conflicts of interest fairly between itself and its customers, the definition of which specifically excludes market counterparties.

Further points in relation to the detailed text are that:

- We consider that point 5 of the guidance should also contain reference to the classification of the firm's clients and to their experience and expertise. Note our general point above in terms of application of the regime to counterparties.

- We consider the guidance in relation to remuneration policies in point 8 (c) is inappropriate and goes far beyond the IOSCO recommendations to prohibit analyst compensation from being directly linked to specific investment banking transactions, which we would support. Implementing the CESR requirements could deter analysts from providing valuable support to a firm's activities.

- We consider that the requirements set out in point 11(b) in respect of annual notifications to clients of permitted inducements received by a firm are unnecessary and clients will not require such notifications. Clients will be able to view the firm's conflicts management policy, including how inducements are dealt with.

- We consider that the guidance in point 16(f)(iv) goes beyond what is reasonable and have highlighted above the difficulty within some firms of separating out functions. We consider the guidance provided by the FSA in COB 7.16.11 allows for a reasonable degree of flexibility in controlling the involvement of analysts in other activities within the UK. This states that "an investment analyst should not be involved in activities in a

way which suggests that he is representing the interests of the firm or a client if this is likely reasonably to appear to be inconsistent with providing an impartial assessment of the value or prospects of the relevant investments".

CESR Question 6.1

Should other examples of methods for managing conflicts of interest be referred to in the advice?

APCIMS Response

We consider that it is appropriate for a firm to have in place a policy for managing its conflicts, but that the specific details of what that policy covers should be determined by the firm, dependent on its nature, scale and complexity.

CESR Question 6.2

(a) Should paragraphs 8(a) to (f) (or the final list of measures for managing conflicts of interest adopted in response to question 1) be stated as examples of arrangements that may, depending on the circumstances referred to in paragraph 5, be effective methods of providing an appropriate degree of independence in respect of persons engaged in different business activities?

(b) Alternatively, should there be a requirement for an investment firm to include these measures in its conflicts policy to the fullest extent possible unless it is able to demonstrate that it has implemented alternative arrangements for effectively preventing conflicts of interest from adversely affecting the interests of clients?

(c) If the answer to question (b) is yes, which of these measures should be subject to the requirement referred to in that question?

APCIMS Response

We consider that the wording of alternative (a) will give the most flexibility to firms in arriving at a conflicts policy appropriate to their business model. The more rigorous the separation of functions, the weaker will be economies of scope and the important synergies in information collection which arise from combining corporate finance, research, market making and securities sales and distribution services. Option (b) is a more prescriptive approach, which would pose a significant threat to the benefits arising to the EU market place from these synergies.

Furthermore the wording of option (b) requires inclusion of the specific measures to "the fullest possible extent", which goes beyond the Article 13(3) requirement for firms to take "all reasonable steps".

CESR Question 6.3

(a) Is it appropriate for an investment firm that publishes or issues investment research to maintain information barriers between analysts and its other divisions?

(b) If so, which divisions should be separated by information barriers in order to prevent analysts' research from being prejudiced?

APCIMS Response

Whether or not it is appropriate to maintain information barriers depends on the nature of the barriers and it will not be effective to erect barriers to prevent all interaction and thus destroy information collection synergies. However, it is recognised that measures should be put in place to prevent, for example, corporate finance, proprietary traders, institutional salesmen and investment managers from attempting to influence the recommendations made in research.

This situation has been recognised by the FSA in regard to the UK regime through industry guidance issued in respect to COB 7.3, which states "the purpose… is not to limit the necessary interaction between research analysts and sales and trading personnel designed to assist research analysts in their work". (Point 8 of the Industry Guidance on COB 7.3 published 9th February 2004). Further examples of the use of the firm's conflicts policy are given in the guidance, such as "a firm's policy may allow it to use an analyst's knowledge and information to assist it to research corporate finance business opportunities and to provide ideas to sales and trading staff". (Points 5.2 and 5.3 of Industry Guidance on COB 7.3 published 19th May 2005).

CESR Question 6.4

Should the derogation from the requirements in paragraph 16(f)(i) to (v) be available if:

(a) the investment firm complies with the requirements in paragraphs 17, 18 and 19 of the first option set out below; or

(b) the investment firm complies with the requirements in paragraph 17 of the second option set out below?

APCIMS Response

We consider that the option under (b) is to be preferred in that it relies on the distinction between objective and non-objective research and applies the requirements accordingly. Where firms clearly disclose that their research is not objective then it would seem reasonable to apply less onerous requirements to it. This is broadly in line with the requirements of the UK's conflicts regime, although the proposed disclosures are more extensive.

We consider that one impact of the first option could be to severely limit the production of research on SMEs, adversely affecting liquidity and the price-formation process. This is because option (a) would have the effect of limiting the information gathering synergies and thus make the provision of research on SMEs less economically viable. Draining liquidity from this marketplace will severely affect the ability of SMEs to raise capital to develop their businesses.

With respect to our preferred option, we do consider that section (b) of the requirements under point 17 to include "substantive descriptions" would lead to a disproportionate amount of material being included within the research. An alternative could be to allow the publication of such descriptions on the firm's website.

OPERATIONAL RISK IN CASES OF OUTSOURCING

APCIMS General Response to the Proposals

We are concerned that the scope of these requirements should not be all embracing and should not extend to entities such as software suppliers who are used to transmit orders. We are also concerned that there are a number of arrangements that have and continue to operate in the UK whereby business is "introduced" to firms. That is, an entity typically a legal firm, an accounting firm or a financial firm not regulated to undertake portfolio management would set up an arrangement whereby that portfolio management is undertaken by an APCIMS member firm. Although this typically happens within the UK, it can also be relevant in a wider context as our members play a strong part in international personal wealth management.

As stated in our previous response, we consider the key issue in respect to outsourcing is that firms bear the responsibility for the functions that they outsource and this is clearly set out within the guidance given under the subheading "Principles". However, we disagree with the statement in point 6 that "outsourcing cannot be undertaken in such a way as to render the investment firm a substantially empty box". Given that the outsourcing firm retains responsibility in respect of any outsourced activities, this should not be an issue.

Although we feel that the CESR guidance in respect of outsourcing arrangements may be unnecessarily prescriptive for Level 2 text, we do not perceive there will be any issues in implementing the detailed requirements. Of greater concern is whether the detailed advice is consistent with other developments currently taking place at the international level on the subject of outsourcing, for example the work being done by CEBS and recent papers from IOSCO and the Joint Forum. We suggest that prior to the adoption of detailed guidance; CESR first makes sure that there is a consistent approach in terms of high-level principles.

FAIR, CLEAR AND NOT MISLEADING INFORMATION

APCIMS General Response to the Proposals

In general we feel that the advice given by CESR on this issue is good and will assist firms in interpreting what is meant by fair, clear and not misleading information, particularly where this is a new concept in the local regime.

In regard to the detail of the text we do consider that there could be a difficulty in determining what is meant by the "average member" in the context of point 3 a), which states that investment firms must ensure that information and communications are likely to be understood by the average member of the group to whom the communication is directed and addressed.

INFORMATION TO CLIENTS

APCIMS General Response to the Proposals

Although the level of detail provided within the CESR advice is considered to be high, in general terms the information to be provided to clients appears relevant and reasonably in line with current UK requirements.

CLIENT AGREEMENT

APCIMS General Response to the Proposals

We are concerned that Article 19(7) extends the requirements to have a client agreement in place in respect of all services. Currently it is not a requirement within the UK to have an agreement for the provision of execution only services. We consider that it will be important for CESR to put in place grandfathering arrangements should these requirements result in the need for firms to update their existing customer agreements and particularly in respect of existing execution only customers.

We disagree with the wording of point 3 in that it states that the client agreement must be "easily understandable" by the client. It would be difficult for a firm to determine what any particular client could understand and we would prefer to see a link to the principle of being "fair, clear and not misleading". We do also support the principle of clearly disclosing to clients the types of service on offer.

We are very concerned that point 10 (c) of the advice requires the establishment of a benchmark, against which the performance of a client's portfolio should be measured. In our view, in order to provide a meaningful analysis of portfolio performance it would be necessary to carry out a complete attribution, or performance, analysis. The costs of doing this could not be justified. As an example, a member firm with assets under management of Euro 10million and 20 thousand clients estimates this would incur a one-off cost of around Euro 450thousand, including software and staff costs, and an ongoing annual cost of around Euro 180thousand. Furthermore, where the portfolio management service being provided is not a full discretionary service, i.e. some transactions may be undertaken on an advisory or execution-only basis, a performance comparison against a benchmark will not provide a fair comparison as the firm may not have been responsible for all the decisions made in relation to the portfolio.

We should also point out that in respect of the portfolio management services provided by our member firms there are two very distinct levels of service. The requirement to monitor against a benchmark would have a huge impact on both levels of service, in terms of the data requirements and associated costs, but in particular this would mean significant price rises in respect of the lower level service, which could not be justified to clients who will have specifically requested this level of service.

We also consider that point 13 of the guidance is unfair in respect of the requirement on firms to provide at least two weeks notice of an intention to terminate the agreement. We believe that firms should also have the right to cancel an agreement with immediate effect, provided that the agreement allows for this and states that the termination will not prejudice the completion of transactions already initiated.

CLIENT ORDER HANDLING

APCIMS General Response to the Proposals

We consider that the key to compliance with the requirements of Article 22(1) is the adherence to the principles of acting in the best interest of clients and treating them fairly. Systems and procedures for the handling of client orders form a key aspect of the business of an investment firm and the firm is best placed to ensure that those procedures have all the elements necessary to process orders efficiently and effectively, including the handling of any exceptions.

CESR Question 1

Do you agree with the definition of prompt, fair and expeditious execution of an order from a client? Do you think that it is exhaustive? If not, can you suggest any elements to complete this concept?

APCIMS Response

The requirement of the mandate from the Commission is not to provide a definition of "prompt, fair and expeditious execution", but to advise on the conditions necessary to achieve compliance with this principle. We consider that, in general terms, the advice achieves the requirements of the mandate, although it is overly prescriptive. However, we would refer to the specific comments made in response to the questions below.

CESR Question 2

Do you think that the details of the orders included under paragraph 2 of the draft technical advice should apply also to professional clients?

APCIMS Response

No comment

CESR Question 3

Which arrangements should be in place to ensure the sequential execution of clients' orders?

APCIMS Response

We do not think it is necessary to add further detail to the advice given in points 6 and 7.

CESR Question 4

Do you agree with the reference in paragraph 7 of the draft technical advice to prevailing market conditions that make it impossible to carry out orders promptly and sequentially?

APCIMS Response

Yes, we agree with the advice given in point 7 of the guidance.

CESR Question 5

Do you think that the possibility that the aggregation of client orders could work to the disadvantage of the client is in accordance with the obligation for the investment firm to act in the best interest of its clients?

APCIMS Response

In line with the principles of treating its customers fairly and acting in their best interests, a firm may have procedures in place for the aggregation of customer orders, which should generally act to the advantage of the customers whose orders are being aggregated. In any case it is sometimes necessary to aggregate orders, such as for discretionary clients. However, it is not possible to determine with certainty how orders will execute in the market and this may occasionally lead to clients being disadvantaged.

We consider that the key requirement here should be to disclose to the client that orders may be subject to aggregation and that on occasion this can disadvantage the client. These requirements are currently applied to UK investment firms through the FSA's conduct of business rules.

CESR Question 6

Do you think that the advice should include the conditions with which the intended basis of allocation of executed client orders in case of aggregation should comply or should this be left to the decision of each investment firms?

APCIMS Response

We do not think it is relevant to include further advice in respect of the intended basis of allocation of aggregated orders. This decision should be left to each investment firms to determine, based on the principles of acting in the best interest of customers and of treating them fairly.

CESR Question 7

Do you consider that CESR should allow the aggregation of client and own account orders? Do you think that other elements (i.e. in respect of the arrangements in order to avoid a detrimental allocation of trades to clients) should be included?

APCIMS Response

We consider it acceptable to allow the aggregation of client and own account orders, provided this is done in accordance with a firm's normal procedures for the aggregation and fair allocation of orders.

CESR Question 8

Do you think that paragraphs 15 and 16 of the draft technical advice should only apply to retail clients?

APCIMS Response

No comment.