

20 January 2005

By email to www.cesr-eu.org

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Dear Sirs

Response to CESR on Draft Technical Advice on Possible Implementing Measures of the Directive on Markets in Financial Instruments (MiFID) - 2nd set of mandates, covering Articles 22, 27 and 44

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 €400 billion for the private investor and undertake some 13 million trades for them annually.

We are grateful for the opportunity to comment on this important part of the implementing measures for the MiFID. These Articles are central to the entire Directive as they will affect market structures, and have an impact on how Stock Exchanges and Regulated Markets, and internalisers choose to provide trading facilities. Undoubtedly the Directive will shape and influence the services provided by investment firms to their clients both wholesale and retail. At one end of the retail spectrum are private clients buying or selling shares worth a comparatively small amount at several hundred euros per bargain, and at the other end are another set of private clients of a different complexion since they are charities, trusts and pension funds involved in transactions up to several million euros. All will be affected by the outcome of this work and we recognise the challenge of making the implementing measures effective for all users of financial markets.

We would like to preface our detailed comments in response to the questions posed by CESR with **three general recommendations** which are as follows:

1. CESR should concentrate on achieving an equivalent end result from the new rules;
2. CESR should seek the simplest approaches that are easiest to adopt and which will not have the effect of constraining markets or of decreasing choice to end investors
3. CESR should take serious note of any significant industry concerns about possible adverse effects on consumers and should restrict their advice to the minimum required in line with the level 1 text.

On the first of these recommendations, the differences that exist in market sizes and customer profiles is a significant consideration since CESR must take into account the variations in models across all member states, some with very small young financial industries, and others with larger established industries.

Our first recommendation is that CESR should concentrate on achieving an equivalent end result from the new rules. We believe that complete harmonisation is simply not possible, and different market cultures must be allowed to continue: harmonisation must mean standardisation and not equality. We are not starting from a single standpoint in terms of the industry since financial markets across the European Union have developed in terms of size and maturity and culture in very different ways.

It is a fundamental of markets that they will price around regulatory requirements and rules, and according to their competitors. We believe that what this means in relation to some of CESR's proposals is that if the requirements are too detailed and too onerous, then services will be curtailed or perhaps dropped completely. This could lead to less choice for consumers and customers and a shrinking of market capacity.

Our second recommendation is that wherever possible, CESR should seek the simplest approaches that are easiest to adopt and which will not have the effect of constraining markets or of decreasing choice to end investors. We ask that wherever possible, CESR's advice and new rules should be kept to a minimum so that member states can implement the major structural and detailed changes without hugely costly financial implications for their industries, many of whom are unlikely to see any early benefits from these changes.

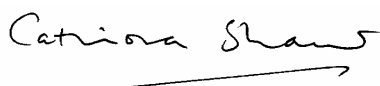
It is unfortunate that neither the European Commission nor CESR has completed any regulatory impact analysis on these proposals. While parts of industry have provided information on the likely costs of implementing the individual parts of this package, it is not easy in many instances to foresee what might be the overall result of many interlinking new requirements.

One particular example of this is the proposal and new rules on systematic internalisers (Articles 27 and 44), and the associated work to define 'average retail size' and 'standard market size'. We have found it difficult to envisage how the new rules in this area will work and indeed whether they will work. While the objective of achieving transparency in the markets is a worthy one, there is a real doubt to our members of the benefits of some of the 'pre-trade transparency' proposals and in particular the absence of ability to offer price improvement in certain circumstances. We remain unconvinced that the end clients will achieve a better overall outcome. It appears very possible that the flexibility in today's market structures could be damaged by some of the new proposals at no benefit to market participants or consumers.

Our third recommendation is that in considering industry comment on these implementing measures, that CESR should take serious note of any significant industry concerns about possible adverse effects on consumers and should restrict their advice to the minimum required in line with the level 1 text. If the pre-trade transparency proposals result in a curtailment or a change to the current market making activities of the specialist market makers in the UK (known as the RSPs), then there will be a resultant and substantial increase in costs to the end investor.

We would be happy to comment further on any of the points we have raised – please do not hesitate to contact us should you require any further information on our submission.

Yours sincerely

A handwritten signature in black ink, reading 'Catriona Shaw', with a horizontal line underneath.

Catriona Shaw
Head of European Affairs

Section III Markets

Display of Client Limit Orders (Article 22.2)

Box 13

Question 7.1 In your view, what types of arrangements other than RMs and MTFs could be considered as complying with article 22.2?

APCIMS Comment:

We believe that, currently, the only arrangements that would be complying with Article 22.2 are RMs and MTFs.

Question 7.2 Do you consider the proposal on publishing the client limit order in a quote driven system appropriate?

APCIMS Comment:

We are not clear how publishing a client limit order in a quote driven system would work in practice, nor what would be the benefits of such a system. Essentially, this would transform a quote driven system into a hybrid quote/order system, and would thus undermine the key features and benefits of a quote driven system.

Definition of systematic internaliser

Box 14

Our general comments are that it is difficult to see how CESR's proposals for systematic internalisers will work in practice, and we are doubtful whether the pre-trade publication of limit orders will in reality bring any benefits to market participants or consumers.

We note the previous work done by CESR on ATs, and believe it is still important to complete and publish a regulatory impact analysis on the effects of Articles 4 and 27 on those firms which CESR members believe fall within the scope of these Articles. We recommend this for several reasons.

First, it is clear within the industry that there is huge uncertainty over which firms will be regarded as systematic internalisers. We understand that individual CESR members are clear who they view as internalisers, but possibly for commercial reasons they are not making public this information. Secondly, it would be useful to complete an impact analysis both to gain knowledge of the possible impacts of these Articles, and perhaps more importantly to assess whether the proposed rules will properly manage the risks for which they have been designed. We have strongly supported CESR's endeavours to operate in an open and transparent manner, and we would hope that because of the depth of uncertainty and lack of clarity over these Articles, that CESR could take steps to provide some remedy. The course that we favour is for CESR to set out principles only on which types of firms should be regarded as internalisers, and for member states to make the final decisions. This should be reviewed as Level 3 develops its joint interpretation recommendations.

Question 8.1.: Do consultees agree with criteria for determining systematic internaliser? Should additional/other criteria be used and if so, what should these be?

APCIMS Comment:

We agree with the criteria for determining systematic internalisers, and are content that any additional or other criteria would add little of value.

Question 8.2.: Should the criteria be fulfilled collectively or used separately?

APCIMS Comment:

We believe that the criteria should be fulfilled collectively.

Question 8.3.: Should CESR set criteria for the term “frequent”? If so, do consultees support the setting of numeric criteria or do they believe that a more flexible approach would be useful? What should these criteria be?

APCIMS Comment:

We support maintaining a flexible approach, and believe that CESR should not set criteria for the term ‘frequent’ as this will differ in different countries depending on the size and liquidity of their markets.

Question 8.4.: Do you agree with the proposed obligation to disclose the intention to cease systematic internalisation? Should CESR propose more detailed proposals on this and if so, what should be the appropriate notice period?

APCIMS Comment:

We believe that the proposed obligation to disclose intention to cease internalisation is sensible, save that the firm should not be mandated to use the same channel if it cannot process such statements, and that more detailed proposals are not needed.

Scope Article 27.1

Question 8.5.: Should liquidity be measured on an EU-wide or national basis?

APCIMS Comment:

Our view is that the assessment of what is liquid is a perceptual view, determined not by pure size but on a comparable basis with such factors as overall market size and frequency of trading also being relevant. We therefore believe that liquidity should be measured on a national basis, using, for example, the top x% stocks in the UK, and the top x% stocks in Greece.

Question 8.6.: Do consultees have a preference in favour of setting pre-determined criteria or using a proxy approach?

APCIMS Comment

Whichever is easier and simplest to use should be chosen. On this basis, we favour the use of indices.

Question 8.7.: Regarding the different criteria described above, do consultees agree with the analysis of each of them, and are there other methods which should be evaluated?

APCIMS Comment

Yes, we agree with the analysis of the different criteria, although we are slightly surprised that CESR does not consider indices to be a relevant option for determining liquid shares.

Question 8.8.: Is it possible and/or appropriate to use for the purposes of article 27 a combination of absolute and relative criteria to define shares as liquid?

APCIMS Comment

As noted in our comments to 8.5, liquidity is often a perceptual view, and we believe whatever factors are chosen to define liquid, they should be as simple and easy to use as possible. As a general guide however we believe that trading activity in a particular stock can be an indication of liquidity.

Question 8.9.: Do consultees consider the proposed figures (i.e. 480 trades per day and 95% of total trading) as appropriate? If not, and where no figures are suggested what are the appropriate figures in your opinion?

APCIMS Comment

We believe that this is a somewhat arbitrary figure and it could be difficult and costly to incorporate in the relevant calculations. It would also have different consequences in various countries.

Question 8.10.: Do consultees agree with the analysis of the relative merits and drawbacks of using proxies such as indices?

APCIMS Comment

We understand that CESR is opposed to using proxies such as indices and is likely to choose another option. Our view however is that for the sake of ease and simplicity of calculation, indices such as the FTSE 100, CAC and DAX etc are the best method.

Question 8.11.: Which criteria would best accommodate the needs of different markets within the EU?

APCIMS Comment

Given the widely different sizes and structures of markets across the EU, we would hope that the criteria to suit different needs would be very high level and general. If CESR is able to propose an alternative method or criteria that are easy to use, to understand and to operate, we would be pleased to offer further comment.

The determination of Standard Market Size (27.1 and 27.2)

Question 9.1: Do you agree with CESR's approach of proposing a unified block regime for the relevant provisions in the Directive or do you see reasons why a differentiation between Art.27 MiFID on the one hand and Art.29, 30, 44, 45 MiFID on the other hand would be advisable?

APCIMS Comment

We do not have a strong view since our members are very rarely indeed involved in block trading, but whatever regime is chosen, it should be consistent within the various MiFID Articles.

Question 9.2: Would you consider a large number of SMS classes, each comprising a relatively small bandwidth of arithmetic average value of orders executed, as problematic for systematic internalisers?

APCIMS Comment

We believe that a smaller number of SMS classes would be easier to operate, and our preference is therefore not for a large number of classes each comprising small bandwidths of orders executed.

Question 9.3.: In your opinion, would it be more appropriate to fix the SMS as monetary value or convert it into number of shares?

APCIMS Comment

We believe that volume ie number of shares can be used for deciding which stocks are caught, but value must be used for actual SMS.

Question 9.4.: Do you consider subsequent annual revisions of the grouping of shares as sufficient or would you prefer them to be more frequent? Should CESR make more concrete proposals on revision? In particular, should the time of revisions be fixed at level 2?

APCIMS Comment

Once the criteria have been set for groupings of shares, and hopefully the formulae for this will be simple, the exact time periods for revisions of these should not be contentious. A period of twelve months would be appropriate for revision and we would not favour revisions more quickly than six monthly.

Question 9.5.: Do you support the determination of an initial SMS by grouping the share into a class, once a newly issued share is traded for three months, or do you consider it reasonable to fix an initial SMS from the first day of trading of a share by using a proxy based on peer stocks?

APCIMS Comment

We understand that there is a view that this proposal would have the effect of forcing business onto an Exchange, and is at variance with the level 1 text. If this is the correct view, we would not support the proposal, and obviously there should be no additional restrictions on quoting off-market in the first 3 months of trading compared with after that period.

Question 9.6.: Do you consider a two week period from publication as sufficient for systematic internalisers to adapt to new SMSs?

APCIMS Comment: As above.

Question 9.7.: Do you agree on the proposal on publication of the classification of shares? Would you prefer the establishment of a single contact point (at level2)?

APCIMS Comment:

We agree with CESR's advice which is that each competent authority should make the information available "in an easily accessible manner, including at least on its website".

Article 27.3 Obligations of the Systematic Internaliser

Question 10.1. Do Consultees consider that there might be specific regulatory issues and specific provisions needed where a systematic internaliser is the trading venue with the largest turnover in a particular share falling within the scope of Article 27?

APCIMS Comment

We do not believe that there could be specific regulatory issues that need to be addressed at Level 2 where a systematic internaliser is the trading venue and has the largest turnover in a particular share.

Question 10.2: Do consultees agree that the availability of quotes during 100 % of normal trading hours of the firm is reasonable and workable requirement for “on a continuous basis”?

APCIMS Comment

Yes the availability of quotes during 100% of normal trading hours of the firm is reasonable and workable for “on a continuous basis”. But “on a continuous basis” needs to be expanded to exclude those periods where for reasons of systems difficulty or some other event outside the control of the firm, a quote cannot be maintained.

Question 10.3: Do consultees think that publication of quotes solely on the firm’s own website meets the “easily accessible”-test?

APCIMS Comment

It appears that CESR may have conflated 2 separate issues:

- Criteria for determining when a quote is easily accessible
- The means by which a firm may make its quotes public

Additionally CESR does not mention expressly that the ease of accessibility is to be as regards market participants on a commercial basis. The reference to investors in CESR’s comments is unhelpful and makes it appear that members of the public may be searching for information. The access to quotes by non-clients, will be on a commercial basis. Easy accessibility should at least include consideration of the data format, reliability of service and the method of accessing the information. To that end, websites or more widely communications based upon TCP/IP with a web interface are accessible at very low cost by anyone with access to the internet. As the quote information will undoubtedly be encrypted to prevent alteration and to prevent access by persons who do not pay, the real question we would suggest that CESR should consider is – will it cost market participants more or less to have web-based access available?

The issue of finding the information raised by CESR is misplaced as the commercial arrangement will necessarily have been made beforehand by the market participant. If proprietary arrangements are to be limited to non-web-based solutions, then we can only expect that the costs of connection and interface will be higher. Obviously we support measures that prevent data fragmentation but in reality since that data is created in a fragmented manner – at different firms at different times, what matters is that market participants do not have to pay over the odds for it to be consolidated. Accordingly we had hoped CESR might have considered setting out criteria by which this might be assessed. We have in mind criteria such as:

- making data available to users, including potential resellers on an equal basis;
- identifying the costs of access openly;
- being prevented from entering into exclusive distribution agreements.

Question 10.4.: Do you agree with the proposed general criteria for determining when a price or prices reflect market conditions or do you think that more specific criteria should be added? In the latter case; which criteria do you think should be added?

APCIMS Comment

We agree with CESR’s proposed general criteria which are that competent authorities should evaluate internalisers’ prices and that published quotes should be close to prices on other relevant markets.

Question 10.5: Do you prefer either of the criteria defining exceptional market conditions, and should those criteria be supplemented by an open list of exceptional market conditions?

APCIMS Comment

The criteria defining exceptional market conditions ranges from ‘unusual’ to ‘extraordinary’, and CESR also suggests linking it to the decision made by RMs or competent authorities to suspend trading. We suggest the any criteria be kept to a minimum, and that an open list of exceptional market conditions would be difficult/too prescriptive.

Question 10.6.: Are there exceptional market circumstances where a systematic internaliser should be able to withdraw its quotes even though a trading suspension has not been called by the regulated market In the latter case, which market conditions should be added to an open list?

APCIMS Comment

We consider that in cases of fast markets or indicative markets, a systematic internaliser should be able to withdraw its quotes. Such circumstances should include systems difficulties where an internaliser is unable to display its quotes, or indeed where there are major difficulties on the main centre of liquidity.

It is also important that the clients of an internaliser should be aware of the events that may cause a firm to withdraw its quotes. Clients should know this in advance, and be subject to agreed terms and conditions.

Question 10.7.: Do you agree that the proposed approach to the updating of quotes is acceptable or would you prefer more specific criteria? In the latter case, which criteria could be added?

APCIMS Comment

We agree with the proposed approach to the updating of quotes, which is that they can reflect “prevailing market conditions”. We do not favour trying to establish more specific criteria, as again there are likely to be significant variations across the EU jurisdictions.

Handling of client orders

Question 11.1: Do consultees agree that it is unnecessary for CESR to provide additional advice in respect of the handling of client orders where a systematic internaliser publishes multiple quotes?

APCIMS Comment

Yes we agree it is unnecessary for CESR to provide additional advice.

Question 11.2.: Would there be any benefit to CESR making more detailed recommendations concerning how a firm should set the number and/or volume of orders that represents the norm? If so, what form should they take?

APCIMS Comment

We do not believe there would be benefit from more detailed recommendations.

Question 11.3: Do consultees agree with the definition of a transaction where execution in several securities is part of one transaction? In particular, is there a need to specify a minimum number of securities and if so, what should the number be?

APCIMS Comment (Box 20)

We agree with CESR’s advice that a basket transaction should normally involve 10 or more securities and we would recommend a minimum number to be set at 5 securities.

Question 11.4.: Do consultees agree with the approach to "orders subject to conditions other than current market price"?

APCIMS Comment

We have no strong views other than that the price should be fair.

Size of retail investor orders (27.3 (4))

Question 11.5: Should the size be based on an EU-wide criteria or would national approaches be preferred?

APCIMS Comment

There are several Directives which may offer a guideline, including Investors Compensation Schemes, Prospectus Directive, or Money Laundering. It would be simplest to have the size set in line with one of these.

Question 11.6: Do consultees prefer having a fixed threshold for all shares, or should the size be linked to the grouping of shares (and subsequently to the SMS of each class) or to some other factor? If so, which?

APCIMS Comment

Once again, it is simplest to have a fixed threshold for all shares.

Question 11.7: If a threshold is set, how should it reflect the different sizes around the EU, i.e. should it be the highest retail size, the lowest or something in between?

APCIMS Comment

We have data in relation to average sizes for retail investor orders in the UK. Our firms, which act for private clients, trusts, charities and pension funds, tell us that the range of order sizes and values can be very large, from a few thousand euro to several million euro. For private equity bargains for the individual customer, we can calculate an average of about €9,000. We would wish to see the threshold set at a sensible and low figure which would incorporate only the true bargains undertaken for private individual customer.