



Rome, 4th April 2005

Mr. Fabrice
Demarigny Secretary general
CESR – The Committee of
European Securities
Regulators

Re. N. 277/05

Dear Mr. Demarigny,

Re: CESR's Draft Technical Advice on Possible Implementing Measures of the Directive 2004/39/EC on Markets in Financial Instruments:

- **Aspects of the definition of Investment Advice and of the General Obligation to Act Fairly, Honestly and Professionally in the Best Interests of Clients;**
- **Best execution;**
- **Market Transparency.**

In response to your invitation to produce observations and comments, contained in the consultancy document, this Association wishes first of all to thank you for the opportunity offered us.

Assogestioni is the Italian Association of the Investment Management Industry and its members, who manage asset portfolios and funds to a countervalue of over 900 billion euro, are directly affected by the regulations subject of the consultancy.

The following comments refer to the topics dealt with in the consultancy document in question, with the exception of those reported in the *Market Transparency* section. Our comments, therefore, focus on general and specific questions pertaining to the:

- general obligation to act fairly, honestly and professionally and in accordance with the best interest of the client [Article 19(1)] – lending to retail clients;
- the definition of investment advice [Article 4(1)(4)] – generic and specific advice;
- best execution [Article 19(1) and 21].



GENERAL OBLIGATION TO ACT FAIRLY, HONESTLY AND PROFESSIONALLY AND IN ACCORDANCE WITH THE BEST INTERESTS OF THE CLIENT (ARTICLE 19(1)) - LENDING TO RETAIL CLIENTS

The CESR proposes introducing the obligation to carry out an assessment of the suitability of the loan or credit granted to the client using one of the following three regulatory approaches:

- 1) in the case of granting loan or credit, suitability is to be assessed by referring to the credit/loan granted, both in relation to the underlying transaction and leaving aside what sort of suitability the transaction is normally subject to under art. 19, para. 4, 5 or 6;
- 2) a second approach is to let operate only those levels of protection at art. 19(4) and 19(6) as well as art. 19(1), without further specific provisions concerning the granting of loan or credit;
- 3) a third approach, preferred by the CESR and on the basis of which the draft technical advice has been prepared, is that whereby suitability must be assessed with reference only to the credit or loan granted and not to the underlying transaction.

Question 1: Do you agree with the proposed advice in this area, including the proposed limitations on the scope of the obligation?

Question 2: Do market participants consider that investment firms have to obtain the necessary information about the retail client's investment objectives in addition to his financial situation?

Although appreciating the end of completing the means of client protection to which this proposal is aimed, we consider that introducing an obligation to carry out a suitability test for the granting of financing is incompatible with the general approach resulting from the directive, as such approach is based on the macro-distinction between services for which prior advice is compulsory and those which can be provided leaving aside any assessment of the characteristics of the client or the order given.

In this sense article 19 to the directive thoroughly governs the procedures and timescale whereby companies must contact the client in relation to the various types of investment services provided. In particular, it is indicated in detail what services are compulsorily subject to prior advice and what, instead, under certain conditions, do not require the prior acquisition and consequent assessment of any information concerning the client.

We therefore consider that of the three approaches indicated as possible, the one which is absolutely preferable is the second whereby a simple referral to the



governing rules briefly described above and contained in art. 19 para. 4, 5 and 6, would operate.

Given this, in the event that this comment on our part should not be accepted and therefore in the event that the final advice should be confirmed as proposed today, we would like to indicate that the correspondence between the third regulatory approach proposed, indicated as that preferred by CESR and the hypothesis at b) to paragraph 1 to BOX1 is not clear to us.

The letter at b) seems in fact to indicate the need to assess the financing also in relation to the underlying transaction, in apparent contrast to the description of the third regulatory approach on which the advice should be based.

Therefore, alternatively and in sub-order to our main proposal to adopt the second of the three approaches, we propose removing paragraph 1 b) from BOX1:

Draft Level 2 advice

BOX 1

1. Before an investment firm, in the course of, or in connection with, the provision by it of an investment service, lends money or grants a monetary credit to a retail client for the purpose of allowing the retail client to carry out a transaction in a financial instrument, or arranges for a third party to do so, the investment firm must obtain from the retail client at least the necessary information about the retail client's financial situation so as to be able to determine that such loan or credit is suitable for the retail client.

2. The obligation in paragraph 1 does not apply when:

(a) an investment firm settles a transaction of the retail client (in transferable securities, money market instruments or units in collective investment undertakings) because he has failed to pay or has paid late; or

(b) an investment firm covers a margin call made on a retail client for a period of no longer than five business days.



THE DEFINITION OF INVESTMENT ADVICE [ARTICLE 4(1)(4)] – GENERIC AND SPECIFIC ADVICE

The consequences of providing generic advice if it is not investment advice

Question 1: Do you believe that investor protection considerations require the application of the above conduct of business requirements from the point at which generic advice is provided or do you believe that sufficient protection is provided in any event to allow the definition of investment advice to be limited to specific recommendations?

Confirming the comments sent on the occasion of the first consultancy promoted by the CESR, it is our opinion that the general recommendations should come under the definition of investment advice. We confirm, in fact, that the activities constituting a consultancy relationship are not only those activities which are resolved in the indication of specific investment choices, but also those activities which find expression in general, systematic planning of the client's financial portfolio when this planning is intended to the underwriting of a financial product or service.

We would also remind you that all the recommendations in question are, before being general or specific, in particular personalised in respect of the figure of the client or potential client. They therefore base their indications on the in-depth knowledge of the characteristics of the party to whom they are addressed and for this reason presuppose that the suitability test will be carried out in advance.

Given this, for the purposes of protecting the client it appears relevant to establish the moment in time when making general personalised recommendations entails a need to apply the other rules of behaviour at art. 19 and, in particular, it is a case of establishing the moment when the obligation concerning a written contract has to arise.

In this regard Assogestioni deems it reasonable, in relation to protecting the client and also in relation to the dynamics and requirements arising from operating practice, to impose contractualisation of the relationship only at the time when the general recommendations develop into specific recommendations.

The scope of the authorisation requirement and the passport

Question 2: Do you believe that considerations relating to the scope of the passport and the scope of the authorisation requirements point towards the inclusion or exclusion of generic advice from the definition of investment advice?



Considerations linked to the scope of the prior authorisation and the scope of the European passport certainly appear relevant in the assessment intended to establish whether the general recommendations should or should not be included in the investment advice definition.

These considerations, in our opinion, would suggest inclusion.

In some countries, such as Italy, the general recommendations (and specifically the asset allocation and financial planning activities) are already considered – and consequently legally qualify as – constituting factors of a financial consultancy. In the event that CESR's advice should exclude them, therefore, the European passport would have a reduced application in respect of what was hoped for: considering the difficulty of clearly identifying the boundaries between general and specific recommendations, in fact, there would be uncertainty concerning providing a consultancy service on the basis of the European passport.

BEST EXECUTION [ARTICLES 19(1) AND 21]

On a general level Assogestioni keenly appreciates the regulatory adjustment carried out in this new consultancy document between the best execution obligation and the operating peculiarities of those brokers who do not have direct access to the negotiation platforms for executing orders from clients.

In this sense it is considered that the objective declared in the consultancy document has been consistently pursued, i.e. that of drafting provisions to protect investors that would not impose excessive charges on those companies carrying out the orders from clients through other brokers. Most of the regulatory provisions proposed appear in fact suitable for the characteristics of the investment service provided by every type of broker.

Given this, we wish however to indicate two themes, included in the *draft technical advice*, which in our opinion make further specification necessary: the first concerns the scope of application subject to the regulations proposed; the second pertains instead to the information system governed in BOX 4.

1. With reference to the scope of application. Assogestioni hopes that an express specification will be entered in the final advice or in the explanatory text relating to it, concerning the non-applicability of the provisions of this advice to the activity of collective management of savings provided by management companies authorised on the basis of the UCITS directive, on the basis of the express, exclusive reference which art. 66 to the MifiD makes to paragraph 3 of art. 5 of the UCITS:



MIFID

Article 66

Amendment of Directive 85/611/EEC

In Article 5 of Directive 85/611/EEC, paragraph 4 shall be replaced by the following:

'4. Articles 2(2), 12, 13 and 19 of Directive 2004/EC⁽¹⁾ of the European Parliament and of the Council of..... on markets in financial instruments (*), shall apply to the provision of the services referred to in paragraph 3 of this Article by management companies

Paragraph 3 of art. 5 of the UCITS directive is in fact the one relating purely to individual management:

UCITS

Article 5

Conditions for taking up business

"3. By way of derogation from paragraph 2, Member States may authorise management companies to provide, in addition to the management of unit trusts/common funds and of investment companies, the following services:

(a) management of portfolios of investments, including those owned by pension funds, in accordance with mandates given by investors on a discretionary, client-by-client basis, where such portfolios include one or more of the instruments listed in Section B of the Annex to the ISD;

b)...(Omissis) "

2. With reference to the information system governed in BOX 4: although sharing the aims underlying the entire regulatory approach suggested concerning disclosure obligations, we are convinced that it would be preferable to make it incumbent upon companies to provide less, but better selected, information.

In fact, the number and type of information set down by the present proposal appears excessive and too detailed and, in some cases in particular, hardly responding to the practical interests nourished by most retail clients.

In this sense it is thought preferable to make it incumbent upon companies to provide, in clear and summary form, only that information relating to the key aspects of the investment service proposed and we do not agree with the tendency, which can be taken from the demands submitted in the consultancy document (cfr. *Questions* 110 and 115), to further increase the list of information to be provided to the client with information concerning percentage data on the number of orders carried out with that same executive broker or concerning the policies adopted by companies to correct errors noted in the execution policies.

Subordinate to this, should this degree of information detail be deemed essential, it is suggested that, where technically possible, the mechanism of "making" information "available" against a specific request from the client be adopted.

Given this, our comments regarding the specific demands related in the consultative document are given hereunder.



3.3.1. General obligation to act fairly, honestly and professionally and in accordance with the best interests of the client (article 19.1)

Questions for Comment:

a) How do firms compare venues (or intermediaries) that offer inducements with those that do not?

b) Where the fees and commissions that firms pay to execution venues or intermediaries include payment for goods or services other than execution, please indicate the circumstances in which firms might determine how much of these commissions represents payment for goods or services other than execution? Under what circumstances do firms consider the entire commission as payment for execution?

it is our opinion that the inducements do not represent the main selection criterion of the execution venue or intermediary. this is because it is not always easy to specifically determine which part of the execution commission paid by the company can be ascribed to the goods and services received from the execution venue or intermediary and which can only be ascribed to execution in the strict sense.

it is worth however stressing that there are utilities and services of extreme benefit to the investment service rendered to the client, which are not available on the market and which cannot be received except in the form of inducements.

Requirements for Selecting and Reviewing Execution Venues

Question for Comment: *Please suggest situations and circumstances in which a firm might satisfy the requirements of Article 21 while using only one execution venue.*

In relation to the execution of financial instruments characterised by economic or legal peculiarities, it is preferable to revert to particularly specialised intermediaries or execution venues. The case could therefore arise where only one intermediary or only one given execution venue is in fact able to carry out certain orders on the best possible conditions.

Equally the factor of the scale of the investment company charged with best execution can be of relevance: as established in other parts to the advice (cfr. compliance obligation) a specific derogation could be introduced for small companies in relation to the nature and complexity of the business.



Frequency of Venue Assessments

Question for Comment: *How do you assure that your execution arrangements reflect current market developments? For example, if you do not use a particular execution intermediary or venue, how would you know whether they have started to offer "better execution" than the venues and intermediaries that you do use?*

In the operating practice of our associates there are already standard procedures for selecting execution venues or intermediaries and for periodically updating them. Outside of those specific cases where the company receives specific notification of actual changes from those third parties it works with, the carrying out of a periodic assessment represents, in our opinion, the only effective instrument for ensuring that their choice of execution venue or intermediary reflects and is on a par with the current development of the markets.

Data Availability for Venue Assessment

Question for Comment: *Are intermediaries likely to inform investment firms that manage portfolios or receive and transmit orders about material changes to their business?*

Generally negotiating intermediaries chosen by those investment companies which do not directly access execution venues take care to notify their clients of the main actual changes occurred in the context of their business. We would point out, however, that paying a high level of attention to these matters is, for the execution venues or intermediaries, the means of not running into a reputational risk which would be potentially damaging to their commercial dealings with the management companies on behalf of whom they are operating.

Mandate 3.4.3 Information to the clients on the execution policy of the firm (21.3)

Proposal 1 in the Concept Paper: Information on Execution Venues

Questions for Comment:

- a) Please identify and estimate the specific costs that investment firms will incur to identify the execution venues and intermediaries that have executed or received and transmitted their client orders and to collect historical information about what portion of their client orders they directed to each such venue or intermediary. For example, what costs would be associated with determining what percentage of client orders an investment firm directed to each venue or intermediary it used in the last 12 months, based on both the number of trades and the value of trades?*
- b) Please explain what competitive disadvantage or other damage to their commercial interests firms would experience if they were to publish the percentage of their business that they direct to different execution venues and intermediaries.*



As already emphasised, we do not agree that it is advisable to increase the number and type of information to be provided to the client with this sort of data.

Questions for Comment

c) If firms are required only to make this information available upon request, would that address respondents' concerns about overwhelming clients with too much information?

In our opinion, the technique of making information available upon the client's specific request represents absolutely the best compromise between:

- on one hand the interest that the client be made fully aware of the characteristics of the investment service offered;
- on the other the interest of the company in being subject to appropriate, non-excessive charges such as would arise from the approach of making an excessive quantity of data available to the mass of clients.

e) Should there be information for execution venues that investment firms access indirectly?

And, if so, should it be on the main intermediaries to whom the firms usually entrust the execution of their orders?

Generally it is not thought that providing information on the intermediary is as useful as the information on the execution venues that the company can access directly. Should, however, such a provision be inserted, possibly through the technique of making the information available at the specific request of the client, it would be preferable to restrict the obligation to indicate only the most frequently used intermediaries (in some management companies, they can in fact exceed one hundred in number).

Proposal 2 in the Concept Paper: Information on Procedures for the Selection of Trading Venues and their Periodic Review.

Question for Comment: *With respect to the fourth disclosure suggested by respondents, CESR requests further comment on whether investment firms that execute client orders directly or indirectly should be required to disclose information about their error correction and order handling policies.*



As already emphasised, we do not agree that it is advisable to increase the number and type of information to be provided to the client with this sort of data.

Proposal 5 in the Concept Paper: Timing

Questions for Comment:

- a) How might an investment firm gain the necessary consents required under Article 21(3) of the Directive as part of a voice telephone communication?*
- b) What impact would there be on cross-border business and distance marketing if investment firms are not permitted to obtain the client consents required by Article 21 using voice telephone?*
- c) Can respondents suggest a different approach than the one used in paragraph 5 of the advice under Article 19(3) that would permit investment firms operating via voice telephone to satisfy the objectives of Article 21's consent requirements?*
- d) How might firms evidence that they had obtained client consent if they obtained that consent via voice telephone?*

In our opinion information on the execution strategy cannot fall under the category of the characteristics of the investment service, but rather comes under that different category of procedures for executing that same service.

This clarification is particularly relevant in relation to whether or not this information is to be included amongst that information which must be provided in telephone conversations. Also in relation to the difficulty of providing exhaustive, comprehensible information by telephone concerning the executive techniques used, it is thought preferable that it only be provided “*immediately after starting to provide the service to the retail client*”.

New Proposal: Information about the Relative Importance of the Factors for Retail Clients

Question for Comment: *Should investment firms that do not consider speed to be an important factor in the execution of retail orders be required to highlight this judgement?*

No. We think it preferable to keep only factors relating to price and costs as an indicator for assessing the execution of orders on behalf of retail clients.



We are at your disposal for any further clarification, and remain, with our best wishes,

Yours sincerely

The Director General

A handwritten signature in black ink, reading "Fabio Galli". The signature is written in a cursive style with a small dot at the end.