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Our ref: N. 641/09

Reply to CESR's Consultation Paper "Inducements: good and poor practices"

Assogestioni welcomes the opportunity to comment on CESR's Consultation Paper "Inducements: good and poor practices"; we deem important that the industry position is taken into account with reference to a critical issue as inducements, in order to develop best practices across Europe in this respect.

Furthermore, we appreciate the practical approach adopted by CESR in such document, because it clearly indicates which practices are allowed and should be encouraged and which ones should be discouraged, giving to investment firms tools to correctly apply the relevant regulation.

Classifying payments and non-monetary benefits and setting-up an organisation to be compliant

Question I: Do you agree with CESR's views about the arrangements and procedures an investment firm should set up?

Question II: Do you have any comments on CESR's views that specific responsibilities and compliance controls should be set up by investment firms to ensure compliance with the inducements rules?

Question III: What are your comments about CESR's views that at least the general approach the investment firm is going to undertake regarding inducements (its 'inducements policy') should be approved by senior management?

From a general perspective, CESR has well focused on the main issues concerning the arrangements and the procedures that an investment firm should set up in order to comply with inducements rules. However, we underline that the proposed measures should, in any case, leave to firms the autonomy necessary to structure the above arrangements and procedures according to their specific activities and dimension; the definition – at level 3 – of each single step which the procedures

should respect should not undermine the flexibility granted by MiFID Implementing Directive.

With reference to good and poor practices list concerning recordkeeping, CESR should clarify that what should be recorded and tracked is not "every relevant action by the firm for the purposes of the MiFID inducements rules" but, instead, the procedures and arrangements adopted in this respect, considered as a whole. In other terms, firms should not register each action taken in accordance to the procedures and arrangements adopted, but should be able to demonstrate that such procedures and arrangements allow them to comply with inducements rules; to this end, recordkeeping of the procedures and arrangements should be considered sufficient.

As regards "good and poor practices" relating to the role of senior management and compliance function, we believe that the need to approve a specific "inducements policy" by the senior management should be considered only one of the possible options that firms can choose within their organisational autonomy, given that the definition of such policy is not required by the relevant MiFID Implementing Directive provisions on inducements nor by those on general organisational requirements. In fact, MiFID and MiFID Implementing Directive provide expressly the cases where a firm should adopt a particular policy (for example, execution policy, transmission policy and conflicts of interest policy).

Finally, in paragraph 35 of the Consultation Paper, CESR seems to admit the possibility that investment firms, receiving standardised recurring payments and non monetary benefits relating to the distribution of CIS, may classify such payments, not only under article 26, letter b), of MiFID Implementing Directive, but also under letter c) of the same article; given the relevance of such statement, we deem important a further clarification which includes also specific examples of good practices that investment firms could follow.

Proper fees

Question IV: Do you agree with CESR's view that all kinds of fees paid by an investment firm in order to access and operate on a given execution venue can be eligible for the proper fees regime (under the general category of settlement and exchange fees)?

Question V: Do you agree with CESR's view that specific types of custody-related fees in connection with certain corporate events can be eligible for the proper fees regime?

Question VI: Are there any specific examples you can provide of circumstances where a tax sales credit could be eligible for the proper fees regime?

With reference to question IV, we agree that the category of proper fees includes all kinds of fees paid by an investment firm in order to access and operate on a given

execution venue (under the general category of settlement and exchange fees) and specific types of custody-related fees in connection with certain corporate events.

Furthermore, we believe that also the fees paid by an investment firm to a service provider for the outsourcing of critical or important operational function or investment services or activities should be included in article 26, letter c). In fact, the right to outsource critical or important operational function or investment services or activities granted by MiFID Implementing Directive should be taken into account also with regard to the discipline concerning inducements. In this respect, the service carried out by the service provider is indispensable to the provision of the relevant investment service and, therefore, the fees paid by the investment firm to the service provider represent an example of proper fee under article 26, letter c), of MiFID Implementing Directive. It should also be considered that the outsourcing fees cannot, by their nature, conflict with the firm's duties to act honestly, fairly and professionally in accordance with the best interests of its clients.

As regards the so-called "Tax Sales Credits", it's not clear to what kind of credits the Consultation Paper refers to. Indeed, the "Tax Sales Credits", as described in the above mentioned paper, are unknown to Italian tax legislation and to our Associates' practice.

Payments and non-monetary benefits authorised subject to certain cumulative conditions – acting in the best interests of the client and designed to enhance the quality of the service provided to the client

Question VII: Do you agree with CESR's view that in the case of ongoing payments made or received over a period of time while the services are of a one-off nature, there is a greater risk of an investment firm not acting in the best interests of the client?

We believe that the approach described by CESR in paragraph 67 could be misleading because it could induce investment firms, on a prudential basis, not to adopt agreements according to which they receive ongoing payments for services of one-off nature, even when such solution is excessive. Therefore, it should be highlighted that the correct valuation of the cases illustrated always depends on the concrete circumstances of each situation taken into account; in this perspective, we disagree the way CESR has formulated its position, given that the main issue is not to establish if a specific situation gives rise to major or minor risks, but the concrete conducts that can be considered admitted or not.

Moreover, there are agreements which establish ongoing payments for activities that are not *per se* investment services but are provided, on an ongoing basis, in conjunction with investment services of one-off nature; such agreements do not increase the risk of an investment firm not to act in the best interests of the client. When an investment firm is providing a one-off nature investment service as placement of CIS, such investment firm can receive, for example, ongoing payments by product providers of CIS in relation to the placement and to another activity that

has an ongoing nature, such as post-sale assistance.

A further example that should be included in the good practices list occurs when CIS product providers stipulate an agreement with an investment firm that manages an electronic platform through which it distributes such products offering the relevant investment services to its clients; according to the agreement, the investment firm is remunerated by each product provider through ongoing payments (*i.e.* a percentage of the management fees of the CIS distributed). The described agreement is compliant with article 26, paragraph 1, letter b), of MiFID Implementing Directive because the perception of the inducement by the investment firm – which distributes the CIS included in the electronic platform through the relevant investment services – is designed to enhance the quality of such services; in fact, the use of an electronic platform in which several CIS of different product providers are available guarantees, through an open architecture structure, a wider offer to investors. At the same time, such structure does not impair compliance with the investment firm duty to act in the best interests of the clients, given that the nature of the inducement is not able to influence, in a negative manner, the conduct of such firm.

Question VIII: Do you have any comments regarding CESR's view that measures such as an effective compliance function should be backed up with appropriate monitoring and controls to deal with the specific conflicts that payments and non-monetary benefits provided or received by an investment firm can give rise to?

Question IX: What are your comments on CESR's view that product distribution and order handling services (mentioned in §74) are two highly important instances where payments and non-monetary benefits provided or received can give rise to very significant potential conflicts? Can you mention any other important instances where such potential conflicts also arise?

Question X: What are your comments on CESR's view that where a payment covers costs that would otherwise have to be charged to the client this is not sufficient for a payment to be judged to be designed to enhance the quality of the service?

As regards question VIII, we share CESR's position regarding the need that an effective compliance function shall be backed up with appropriate monitoring and controls to deal with the specific conflicts that payments and non-monetary benefits provided or received by an investment firm can give rise to.

With reference to question IX, we believe that, although inducements related to product distribution can give rise to very significant potential conflicts, the discipline provided by article 26 of MiFID Implementing Directive guarantees adequate measures to neutralise such conflicts. In this respect, however, CESR should not focus on the general issue of product distribution, which is not *per se* inconsistent with the relevant rules, but should take into account the specific cases

where the inducements received by the investment firm are legitimate or forbidden; therefore, what is relevant is not the fact that inducements related to distribution may potentially give rise to significant conflicts, but the concrete circumstances where such risk may arise.

Furthermore, level 3 measures should indicate with reference to the types of inducements related to all the relevant investment services the circumstances in which such inducements are legitimate or not, illustrating, with the same relevance, specific example of good and poor practices.

As regards example 1 of the good practices list, we appreciate that CESR considers legitimate the reception of soft commission including research, technical services and information technology from the firms which execute client orders; however, we deem important to specify that also goods or services related to the execution of orders are included in the soft commissions listed above. Furthermore, we deem useful to specify –for each type of "soft commissions" included in example 1, *i.e.* "research", "technical services" and "information technology" – a list of non-monetary benefits which could be considered included under the mentioned type of soft commissions together with a list of non-monetary benefits which could not be included under such soft commissions list. Moreover, given the non exhaustive nature of the two lists, it would be appropriate to indicate the relevant principles which a firm should take into account, in order to verify whether a specific non-monetary benefit can be remunerated through dealing commissions.

In order to assist investment firms towards a correct implementation of inducements rules, we deem also important that CESR adds to the good practices list the following example: an investment firm provides investment advice or general recommendations or placement and it does not charge a fee to its clients but receives a commission from the product providers when it arranges such sales. The distribution agreement establishes different amounts of such commission which increase each time several specific target levels are reached. This situation is consistent with the prohibition of payment of one-off bonus (or "override") provided by CESR in its 2007 Recommendations; in fact, while a bonus provided one-off can represent a very significant incentive to reach and override a certain target level, the provision of several specific target levels allows a gradual increase of the remuneration and, therefore, does not impair the compliance with the firm's duty to act in the best interest of the clients. In fact, the incentive of the investment firm to override several target levels is substantially equivalent to the legitimate interest of such firm to place financial instruments, within the limits and the duties provided by the relevant regulation.

We believe that example 1 included in the poor practices list, as defined by CESR, could be misleading because the ongoing payments from a third party, *i.e.* a product provider, in relation to distribution services for a range of financial instruments provided to clients on a one-off basis is not always forbidden, but may be consistent with the relevant MiFID Implementing Directive provisions. As said, the legitimacy of inducements should be valued on a case-by-case basis, given that there are distribution agreements which do not increase the risk of an investment firm not to act in the best interests of the clients (see our reply to question VII).

The abovementioned example 1 represents only a specific situation where the investment firm receives inducements which are – *per se* – legitimate, but become inconsistent with the relevant regulation because of the distribution policy internally adopted. In fact, there can be other situations where an investment firm receives inducements which are not only *per se* legitimate but also consistent with the relevant regulation; for example, when an investment firm receives rebates of entry and management fees from a product provider and such rebates remunerate, on the one hand, the distribution service provided by the investment firm and, on the other hand, the post-sale assistance, such rebates do not impair the investment firm's duty to act in the best interests of the client and are designed to enhance the quality of the relevant distribution service provided. In light of the above, we deem appropriate that CESR includes in the good practices list specific examples which represent cases of legitimate inducements related to placement.

As regards example 3 included in the poor practices list, CESR should specify in which circumstances rebates from product providers to investment firms distributing financial instruments and providing investment advice are legitimate. In fact, even if we agree that "strong suitability test" can not be considered as an appropriate measure to manage conflicts of interest that can arise in the described situation, we do not believe that the only recommendable solution is, as suggested by CESR, that "an investment firm could avoid this conflict by charging clients directly for investment advice". In fact, the suggestion of CESR is only one of the possible solutions and CESR, therefore, should take into account also circumstances where investment advice is remunerated by third-party payments, in accordance with Recital 39 of MiFID Implementing Directive. In this respect, we believe that examples of inducements "where the advice or recommendations are not biased as a result of the receipt of commission" should be included in the good practices list.

With reference to question X, we agree with CESR's view according to which where a payment covers costs that would otherwise have to be charged to the client this is not sufficient for a payment to be judged to be designed to enhance the quality of the service provided.

Payments and non-monetary benefits authorised subject to certain cumulative conditions - Disclosure

Summary disclosures

Question XI: Do you have any comments on CESR's view of the summary disclosure rule under Article 26(b)(i) of the Level 2 Directive (including when such a disclosure should be made)?

We deem reasonable that the summary disclosure on inducements should be provided to the client *ex ante*, in order allow him to understand readily how the firm is incentivised to act in a specific manner and that the *medium* chosen should be a durable *medium*.

As regards the content of the summary disclosure, we agree that it should cover all types of inducements received by or provided to investment firms and that it should include a reasonable band range of payments or, when the inducement consists in investment research, the fact that it is received from the broker to whom it transmits orders for execution. Furthermore, we agree that, when the exact amount of third-party payments made or received or the method of calculating that amount varies depending on the class of instrument (e.g. shares, bonds, UCITS), then the information should also be given per each class.

However, a further differentiation of the information per family of instruments (e.g. UCITS investing in bonds, UCITS investing in shares, UCITS investing in money market instruments) or per provider of the financial instrument (third party products *vs.* in-house or in-group products, or products of one third-party *vs.* products of another third-party) can damage the correct development of the competitive market with reference to the relationship between product providers and investment firms that distribute financial instruments. In fact, CESR's approach would allow an investment firm to compare the remuneration that it receives from a specific product provider with the remuneration that the latter pays to another investment firm for the distribution of the same financial instrument. In this case, if the investment firm discovers that it is paid less than another one, then it would probably ask the product provider to align its remuneration with that paid to the other investment firm.

Detailed disclosures

Question XII: What are your comments on CESR's views about detailed disclosures?

Although we recognise the need to assure to the client an adequate disclosure on inducements to the maximum extent, investment firms should not be excessively burden beyond the requirement expressly provided by the relevant provisions of MiFID Implementing Directive. In this perspective, it should be considered that, independently from the modalities chosen by investment firms in order to provide to clients inducements disclosure – summary plus detailed disclosure on client's request *vs.* only detailed disclosure – such firms shall prepare the mentioned disclosure prior to the provision of the service. As a consequence, it is not relevant the moment in which the client, who has received a summary disclosure, asks for a detailed one (prior to or after the provision of the service), but the fact that, in any case, the investment firm is obliged to prepare the disclosure on inducements before the provision of the service, *i.e.* in a moment in which it may not know all detailed elements on inducements; a different approach would not be consistent with article 26, paragraph 2, of MiFID Implementing Directive and would oblige investment firms to prepare on an ongoing basis – after the provision of the service – several disclosures in order to give to clients further updated information, especially with reference to the exact amount of inducements.

In this respect, it should also be noticed that CESR's position will imply that clients, to whom is provided only the detailed disclosure or the summary disclosure plus the detailed disclosure which is asked prior to the provision of the service, will be treated differently from clients to whom is provided a summary disclosure plus a detailed disclosure which is asked after the provision of the service.

Therefore, we do not agree with CESR's statement, in paragraph 108 of the Consultation Paper, according to which "where the client request a detailed disclosure after the provision of the service, then the disclosure should provide the exact amount of the third-party payments and non-monetary benefits". In fact, as said, due to the circumstance that such disclosure has been prepared prior to the provision of the service, the investment firm may not know, in that moment, the exact amount of third-party payments or non-monetary benefits.

Use of bands

Question XIII: Do you have any comments on CESR's views on the use of bands?

In general terms, we agree with CESR's position according to which, when using bands, the range between the minimum and the maximum percentage of rebates should not be too large. However, given that, as said under our reply to question XI, we deem not appropriate a differentiation of the ranges of the rebates from a product provider to another, we believe that a distributor can disclose the band of rebates received from all product providers of a specific type of financial instrument, for example UCITS, provided that the percentages of rebates received by different product providers are very similar. For example, if a distributor receives rebates of 70% from a UCITS provider and 80% from another UCITS provider, then such distributor – given that the range is not excessively large – can inform its clients that it receives a band of rebates from all product providers of UCITS whose range is between 70% and 80%.

Documentation through which disclosures are made

Question XIV: Do you agree with CESR's views on the documentation through which disclosure are made?

In general terms, we agree with CESR that the firms are free to use different *media* for inducements disclosure as far as the latter is made in a manner that is comprehensive, accurate and understandable (as stated in article 26, paragraph 1, letter b).

With reference to example 1 of the good practices list, CESR should consider that the use of an "inducement calculator" should be only one of the possible *media* through which a correct disclosure of inducements can be provided, even when it is possible to know the exact amount of the inducement received. Furthermore, it

should be considered that there can be cases where the use of such a calculator is not possible. For example, when a CIS product provider rebates to a distributor a certain percentage of its management fee and the management fee is a percentage of the value of the fund, it is not possible to use an "inducement calculator" due to the fact that it is not known the exact amount of the management fee in relation to which the exact amount rebated to the distributor should be calculated.

Difference of treatment between retail and professional clients

Question XV: Do you agree with CESR's views on the difference of treatment between retail and professional clients?

We agree with CESR's position on the possibility to treat differently retail and professional clients with reference to the specific content that the disclosure concerning inducements can present. Such approach introduces an important element of flexibility which allows to take into account the different knowledge and experiences of clients.

We remain at your disposal for any request of clarification or further comments on the content of our reply.

The Director General