

The Committee of European Securities
Regulators
11-13 avenue de Friedland
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FRANCE

17 December 2004

**CESR's Draft Technical Advice on Possible Implementing Measures
of the Directive 2004/39/EC on Markets in Financial Instruments
1st Set of Mandates**

Second Consultation Paper (November 2004)

Comments of UBS Investment Bank

UBS Investment Bank (UBS-IB) is pleased to comment on CESR's second consultation paper (November 2004) addressing certain implementing measures under the first set of provisional mandates received by CESR from the European Commission on 20 January 2004. The second consultation paper seeks comments from all interested parties on specific questions arising from the initial consultation on the 1st set of mandates (June 2004). This draft technical advice will, in part, form the basis for the final advice CESR proposes to give to the European Commission in April 2005.

UBS-IB is the investment banking business group of UBS AG, employing 16,000 people in offices located throughout 30 countries. UBS AG is a global, integrated investment services firm and bank domiciled in Switzerland, with offices in over 50 countries worldwide. UBS AG's business is managed through four main business groups and its Corporate Centre.

Conflicts of Interest and segregation of areas of business

CESR previously consulted upon whether some areas of business should always be segregated to the full extent possible from other areas of business or whether CESR should simply recommend a list of examples of possible methods from which investment firms may choose the most appropriate methods given their own internal organisation. CESR acknowledges that with a few exceptions, the latter approach was favoured by respondents and indeed that is also UBS-IB's view as a general proposition.

In our earlier response, we noted that CESR defines an "information barrier" as:

"... effective procedures to control the flow of relevant information between persons principally engaged in the different activities that are to be separated by the barrier ..."

UBS-IB understood CESR to be proposing a *procedural* information barrier rather than a physical barrier, the former being considerably less stringent than the latter. We indicated that UBS-IB has in place various *procedural* barriers for the three business areas of concern to CESR, namely Proprietary Equity Trading, Asset Management and Investment Banking (Corporate Finance including Equity and Debt Capital Market business). UBS-IB believes that procedural information barriers between, respectively (i) Proprietary Equity Trading and Client Equity Sales and Sales Trading; (ii) Equity Investment Research and Equity and Sales Trading; and (iii) UBS-IB and UBS Global Asset Management, the asset management business are all appropriate and in line with best regulatory practice.

However, and whilst a physical information barrier is more intrusive, UBS-IB believes that a physical information barrier is both desirable and appropriate as between the Investment Research Department and the Investment Banking Department (including equity capital markets business and fixed income capital markets business). We also consider that physical separation should be mandated as between Investment Banking and Asset Management groups, as is the case as between UBS-IB and its sister business group, UBS Global Asset Management.

We have also indicated that we are exploring the relative value of establishing such a physical information barrier as between Investment Research and other business areas.

Investment Research

CESR has consulted upon whether it should differentiate between the treatment of research held out to be objective as distinct from other forms of research. It has concluded that there are different situations which deserve different treatment and that therefore it should admit the possibility for firms to produce "non-objective" research provided clear disclosure is given by firms where they are not fully complying with the requirements concerning objective research.

UBS-IB would advocate a rather different approach altogether, focusing not upon seeking to draw a distinction between objective and non-objective research, but in fact differentiating between, on the one hand, qualified analyst-produced research reports; that is research properly so called, and on the other hand material produced by other departments for distribution to clients which covers investment topics. We believe that any two-tier approach should distinguish between research reports produced by research departments comprising *qualified* and *registered* research analysts. We would favour mandatory qualifications for and registration of analysts as is currently required under NYSE and NASD regulations in the United States. Such a qualification forms part of an initiative under the auspices of the CFA Institute. This analyst research could therefore easily be distinguished from other analysis and recommendations emanating from non-research department sources within firms. We also think it appropriate to observe that from a conceptual perspective, research reports involve elements of subjectivity since the analyst who authors such reports necessarily gives views which are in essence his own opinions and as such are necessarily subjective.

We therefore strongly advocate an alternative approach of differentiating analyst research from other material in order that the former can be recognised as such and given the additional weight that we think such qualified analyst-produced research deserves. Establishing high standards of education and training, including training as to the ethical standards demanded of research analysts as part of the qualification and registration process is, we believe, likely to drive quality improvements in the area of investment research. At the same time, a lighter touch regime can perfectly well apply to non-analyst research materials.

We trust you find these comments helpful.

Yours faithfully,

UBS Investment Bank