Fidelity International Response to CESR Consultation 09-958
on Inducements: Good and poor practices – 22 December 2009

Section III: 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?

We agree with CESR's views.

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?

We agree with the CESR's view that firms should set up specific responsibilities and compliance controls to ensure compliance with the inducement rules.

We note that s34 states that "It is good practice that the compliance function is involved in these procedures". We believe that the compliance function's role should not extend to authorising a particular payment as compliant since this would require the compliance function's direct involvement in the process.

In accordance with CESRs own guidance on MiFID, the compliance function should be an independent function with its main duties being to monitor and assess the adequacy and effectiveness of the measures and procedures put in place to ensure compliance with regulations and to advise and assist the persons responsible for carrying out investment services to comply with the firm's obligations. Furthermore the relevant persons involved in the compliance function should not be involved in the performance of services they monitor. Involvement in a business procedure could impair the independence of the function.

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

We agree with the view of CESR that at least the inducements policy should be approved by senior management.

Section IV: Proper fees

We have no comments on this section of the paper.

Section V: 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 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 accept CESR's basic proposition but do not believe that all continuing payments relate only to a one-off event. We believe that ongoing payments can still be justified (assuming they meet the conditions in article 26(b)) in cases where the service to the client is of an ongoing nature, e.g. an advisory relationship, a banking relationship. We would appreciate confirmation that CESR agrees with that interpretation.

Where a one-off payment is made, we could still foresee a risk that firms may not act in the best interests of their clients since there would be a greater incentive to churn client assets in order to generate additional revenue. We believe it is important that ongoing payments should not be prohibited where the service provided is a one-off, so long as they are designed to

enhance the quality of the relevant service to the client and do not impair compliance with the firm's duty to act in the best interests of the client.

It is difficult to envisage what sort of additional 'particularly robust' controls might be expected of a product provider making such a payment.

.**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?**

We agree with CESR's view.

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

Clarity & transparency over the nature of the service
We agree that product distribution and order handling services are two instances where significant potential conflicts of interest can arise. We are keen to have greater clarity and transparency for the end investor when receiving investment advice as to the allegiance of the adviser and their remuneration. For example, is the adviser connected to and/or paid by the product provider with the inherent conflicts of interest this entails or is the adviser independent, receiving a fee from the consumer irrespective of the advice given? In both cases the nature of the service being provided to the end investor needs to be clearly disclosed and preferably at the outset of the discussion. We regret that in its advice to the Commission on the KID for UCITS IV CESR did not assist this process by separating the cost of advice from the cost of the product in the charges table.

A level playing field across competing retail investment products
The approach in Article 26 (b) of MiFID Implementing Directive should be common to all retail investment products –including mutual funds, index-linked insurance products and structured products. Thus regulation should focus on the economic substance of the product rather than its legal form. Only this unified approach will ensure that consumers are able to make informed choices and compare competing offerings.

Tiered Commissions
We would appreciate confirmation that CESR's view of "tiered commissions" has not changed from that expressed in the May 2007 document "Inducements under MiFID". We agree that any type of one off sales bonuses or brokerage fee/custody fee related rebates that are dependent on certain levels of assets under management could lead to conflicts of interests that would be difficult to mitigate. However, we still believe certain tiered arrangements can be justified, so long as the arrangement is not designed in such a way that it will impair the investment firm's duty to act in the best interest of the client. Our understanding is that some arrangements where payments from a product provider to a distributor vary depending on the level of assets under management can be justified, for example where there is a smooth progression in the tiered structure. These arrangements in relation to the distribution of CIS are market-wide practice in many European Union countries.

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?

Whilst we agree that where the payment covers costs that otherwise would be charged to the client this alone is not sufficient to fulfil the requirement of being designed to enhance the quality of service to the client, there are circumstances where it is appropriate for the product provider to remunerate a wholesale fund distributor for the retail services the distributor is doing on behalf of the product provider and hence this is enhancing the quality of service for

the end clients. These costs are paid in the form of the management fee of the product to the product provider and are reimbursed to the distributor for the service the distributor is undertaking for the underlying retail clients which the product provider would otherwise have to undertake should the retail client be dealing directly with the provider. We would like to clarify that ongoing payments in the above mentioned situation would still be allowed in light of the regulation.

Section VI: Payments and non-monetary benefits authorised subject to certain cumulative conditions: – Disclosure

Question XI: Do you have any comments on CESR's views about summary disclosures (including when they should be made)?

We are concerned by the implications of CESR's comments on the level of detail to be provided in summary disclosures where the level of rebate can vary. As a fund platform, Fidelity has negotiated rebates with the providers whose funds we distribute and that rebate does vary, depending on the charging structure of the individual fund. Our understanding of CESR's guidance is that we would be expected to provide a band of payments for each category of fund if there are material differences. We are concerned that this would require us to make commercially sensitive information available to the market as a whole.

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

We have no comments on this part of the paper.

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

We believe that the use of bands can be a valuable way to make clients aware that the level of payment received may vary by fund. However, for cases where the level of payment can vary but will be the same for the majority of funds on offer we currently disclose the typical level of payment received rather than a range. We believe that this is an equally valid way of providing a summary disclosure to clients.

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

We agree with CESR's view.

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

We agree with CESR's view that there are situations where information to professional clients can be provided in a different way than to retail clients due to the fact that the level of knowledge, experience and sophistication differs between retail and professional clients.

We would also like to take this opportunity to comment on our experience of cross-border implementation. Although the MiFID rules are fairly similar in most of the European Union countries there are still differences between implementation. There have been differences in the approach of regulators in the various Member States on inducements and this had led to some difficulties for a wide cross border product offering. One example is the different approach taken for override or tiered commissions mentioned above where a higher rate of trailer commission is paid by a provider to a mutual fund distributor the more assets the distributor places with the fund provider. Such commission structures are accepted in most of Europe and as intimated above rarely would cause a client conflict but such arrangements are expressly banned by regulation in certain territories e.g. the UK. This makes pan-European fund distribution agreements complex in design and costly to implement. Further clarity on this area would be greatly appreciated.