Financial Services User Group's (FSUG)

response on

Review of the Markets in Financial Instruments Directive (MiFID)

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FSUG response on Review of the Markets in Financial Instruments Directive (MiFID)

INTRODUCTION AND SUMMARY

The FSUG is pleased to submit its views to such an important review. We support the overall aims of the MiFID review which if implemented successfully should bring significant benefits the millions of ordinary investors in the EU. This submission should be read in conjunction with our submissions on PRIPS, UCITS, IMD, and Sanctions. The recommendations set out in our responses constitute A New Investor Protection Framework develop (see below).

- investors have justified confidence in;
- are secure and stable;
- operate fairly, transparently, and with integrity;
- are competitive and efficient, and provide access to value-for-money, socially useful products and services.

To meet these objectives, FSUG considers that all investment-based products and services (regardless of legal or corporate structure) should be covered by a coherent, consistent regulatory regime for investment services. This regime should apply to all parts of the investment 'supply chain', not just those parts who deal directly with investors.

We support the Commission's objective of improving competition, efficiency, and behaviours at all parts of the investment 'supply chain'. Market activities upstream may not always be apparent to end-investors. However, these can have a significant impact on the value, quality, and suitability of the investment products and services received by the retail investor. We also support the Commission's intention to create a more consistent, coherent regulatory regime for investment services.

We have provided a response to most of the questions in the consultation including those on market issues. However, our main focus is on investor protection issues.

The key investor protection issues we would highlight are:

- MiFiD scope – i.e. which products should be covered by MiFiD;
- execution-only;
- management of conflicts of interest;
- provision of ongoing information.

MiFiD SCOPE

All types of structured products should be covered by MiFID. Simple, pure deposit accounts should not be covered by the full set of regulatory requirements contained in MiFiD (such as conduct of business rules). However, it is important that even simple, pure deposit accounts are covered by regulation covering disclosure of information, marketing and promotions[1]. Moreover, if firms use the marketing of deposit accounts to cross-sell investment products, then these sales should be covered by full conduct of business regulation.

Furthermore, we are concerned that the previous approach to regulation has been too reactive and not responsive to 'innovation' in the market. Therefore, MiFID should be an 'enabling' directive allowing regulators to bring new products and services within the scope of regulation without requiring new legislation.

[1] This would not be covered by MiFiD of course.

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EXECUTION-ONLY

We have tried to produce a common position on all the questions we have responded to. However, we have not achieved complete unanimity on the question of whether 'execution-only' services should be banned outright.

There is some support amongst FSUG members for Option B set out in the consultation paper – i.e. prohibiting execution-only. However, the majority of FSUG members are of the view that execution-only should not be banned outright but a limited range of simple products should be allowed to be sold on execution-only basis under very tightly regulated conditions.

A risk based approach is needed to determine the limited range of products which could be safely sold on this basis and robustly monitored and enforced by European and national regulators.

In practice, this means:

- Regulators should assess and 'rate' complex products/instruments to decide if they are appropriate for distribution via execution-only. One practical way of implementing this would be for the new European Supervisory Authorities (ESAs) to have the authority to maintain and update an approved list of products and services. Clearly, this assessment and rating system has to be flexible enough to cope with market 'innovation'. As outlined above, this means that MiFiD and other directives should be 'enabling' regulation allowing EU and national regulators the scope and power to proactively define products as complex/non-complex without requiring new, long drawn out legislation.
- The question of suitability should not be based on legal or corporate structure per se. This means for example that UCITS as a class of investment would not be excluded simply because of the legal structure. The key criteria for suitability should be based on potential risk to investor and complexity. Risk in this case could mean risk to capital preservation, potential volatility, the use of complex financial instruments, complex charging structures, exposure to counterparties, regulatory jurisdiction and so on. At this stage, given time constraints, we are unable to provide the Commission with detailed criteria for assessing whether certain products should be included/excluded. However, we would welcome the opportunity to develop this risk based model.
- Investors should be warned in clear terms about the risks associated with execution-only such as the potential loss of consumer protection regulation and rights to redress. It is important that these warnings are clearly and prominently displayed, not hidden in small print.
- Specifically, we support the removal of services that would allow leveraging.
- UCITS should not continue to be treated automatically as non-complex instruments.

MANAGEMENT OF CONFLICTS OF INTEREST

We strongly support the objective of improving the level of disclosure and accountability to clients. Disclosure should cover:

- the basis of the advice (independent whole of market, restricted, single firm etc);
- the status of the intermediary (whether independent, sales agent etc);
- basis of remuneration and other potential conflicts of interest (including relationships with product providers and others in the financial supply chain);

- the level of professionalism, training and competence of the intermediary;
- reasons and justification for advice and recommendations made by intermediary.

The enforcement of the inducements provisions of MiFID has unfortunately been rather poor. CESR – to start with – has not disclosed these critical consumer protection rules in its 'Consumer guide to MiFID'.

However, it is important to note that, to address conflicts of interest in the financial supply chain, disclosure is necessary but not sufficient. We are of the view that the main cause of conflicts of interest in the financial supply chain are the inducements and remuneration policies that encourage intermediaries to recommend products that meet their own economic or commercial needs, rather than the needs of the consumer (indeed this applies not just to intermediaries at the point of sale but financial distribution generally – for example, the commercial relationships between investment companies who manufacture products and banks who distribute them).

Disclosure of status and inducements of course can be helpful in alerting consumers to the potential for conflicts of interest. However, the evidence from member states such as the UK suggests that information solutions per se have had a very limited success in actually constraining the behaviour of intermediaries, distributors or product manufacturers.

So, if conflicts of interest are to be addressed, other interventions are needed. For example, this could include:

- Requiring product providers to introduce more robust risk management procedures during the product development stage if they continue to distribute products through intermediaries who are rewarded by variable commission payments or other such inducements.
- Introducing a much clearer definition of intermediary status. There should be only two status definitions – independent and sales agents. Only intermediaries who i) do not accept any payments, inducements or benefits from product providers and ii) assess the full range of products on the market should be allowed to refer to themselves as independent advisers. All other intermediaries should be referred to sales agents or sales representatives regardless of whether they sell the products of one provider or a limited panel of providers. It is important that an independent adviser has a clear duty of care to the client and avoids conflicts of interest. An intermediary who accepts remuneration of any kind from a product provider is an agent of that provider, not the client.
- Requiring sales agents to justify orally and in writing why they have chosen to recommend a product (within the range of products they cover) that pays higher commission/rewards even though a similar product within the range would perform the same role.
- A major problem for the investor is how s/he can prove whether wrong advice has been provided by an intermediary or adviser. Indeed, this is a problem for the industry as well when it relates to disputes referred to Ombudsmen, or mediation and arbitration schemes. Our preferred option is taping of the sales 'interview', followed by placing the burden of proof on the provider, and then advice documentation with clear rules. The need to tape conversations between institutional market operators (such as equity salesmen/women) and their institutional clients is now accepted. This principle should be extended to advisers/intermediaries and retail investors.

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PROVISION OF ONGOING INFORMATION

We support the view that disclosure should be on an ongoing basis not just at the point of sale. Investment products and services are not one-off disposable purchases. The real value or benefit of an investment decision/purchase only becomes apparent over time so it is clearly appropriate that intermediaries who claim to be offering a professional service continue to monitor the appropriateness of the original recommendation. Moreover, investors' attitudes to risk may change over time as their financial circumstances change. A recommendation made at a given point time in an investor's life cycle may not hold true later on in the investor's life cycle.

However, we are concerned that less scrupulous financial providers and intermediaries will use the opportunity provided by ongoing contact to aggressively sell unnecessary or inappropriate products and services.

Product 'churning' is a major problem in many member states. Churning can occur in a number of ways:

- a rival provider/intermediary may target an investor to persuade him/her to switch from his/her existing provider to an investment fund distributed by the new intermediary or
- alternatively, an adviser/intermediary with an ongoing relationship with a client may try to persuade him/her to switch to a new provider/fund.

The development of an 'innovative' product often provides the marketing opportunity to persuade investors to switch funds. Of course, in many cases, 'innovative' financial products are simply variations on the same theme and add little value for consumers.

Indeed, the substitution of a replacement product results in consumer detriment as the investor can incur large switching costs. Incurring switching costs could be justified in certain cases if the investment performance of the new investment fund is superior to the old fund. However, as we know from experience, there is no evidence that past performance is an indication of future performance and intermediaries/fund providers who recommend switching to new funds may be guilty of providing poor advice.

Therefore, it is critical that MiFiD and other regulatory initiatives make it absolutely clear that intermediaries/advisers should not use the opportunities provided by ongoing communication to persuade investors to buy new products or switch products unless this is obviously justified by a change in financial circumstances or attitudes to risk.

Also, we have ample evidence that the MiFID provisions for a clear, fair and not misleading information have not been sufficiently enforced by national supervisors.

Therefore, it is important that regulators closely monitor ongoing relationships not just at the point of sale. This means that ESMA (and other ESAs) should pay as much attention to monitoring and enforcing regulation as developing policy. The use of 'mystery shopping' and sampling is a cost-effective way of monitoring market behaviour.

A NEW INVESTOR PROTECTION FRAMEWORK

The aftermath of the financial crisis presents the ideal opportunity to introduce a new robust and responsive regulatory system to ensure that all investment-based products and vehicles aimed at ordinary consumers (including pension scheme members) are covered by a coherent, consistent set of investor protection measures.

The principles underpinning our approach are:

- All agents in the investment supply chain, including those who do not deal directly with investors or undertake activities that are not visible to investors, operate to a high level duty of care to investors.
- Legal and corporate structures of investment products are secure and transparent, with assets valued and audited on a regular basis by independent third parties. Investors are informed clearly about the legal and regulatory jurisdiction of investment products being marketed to them.
- Corporate governance standards in the investment industry are improved to ensure all parts of the investment supply chain treat investors fairly. Senior directors (and shareholders) must take responsibility for corporate governance and be accountable for their actions.
- Conflicts of interest such as commission driven sales that are the root cause of most mis-selling scandals are addressed by a robust regulatory response (information disclosure is necessary but not sufficient to counter the aggressive selling practices driven by commission and other remuneration practices).
- Information provided to investors should be of a consistently high quality, and easy to understand. Investors should receive clear, relevant information post-sale, not just pre-sale and at the point of sale. Investors' financial circumstances and attitudes to risk change over time.
- Consumers receive advice on the most appropriate product/investment vehicle for their needs, not the product that suits the commercial needs of the firm or intermediary. Advisers/intermediaries should be required to operate to a general high level duty of care when assessing consumers' needs and level of financial sophistication (where possible). To ensure this happens, the Commission should review and produce clear guidelines about (i) needs assessment (for example, information gathering/'know your customer' requirements) to be followed in Member State regulations, and (ii) professional standards expected of intermediaries/advisers.
- Advisers, intermediaries, and sales staff should be appropriately and sufficiently trained and competent to provide the necessary advice and guidance to investors.
- There should be a level playing field between different types of provider to ensure fair and effective competition.
- Regulation should be risk based and proportionate – interventions should be proportionate to the potential for consumer detriment i.e. the duty of care, advice requirements, product standards and regulation should be matched to the complexity of the product, riskiness of the product, sales practices, distribution tactics, remuneration policies (for example, if firms are using aggressive remuneration policies linked to staff achieving sales targets).

Regulators have a problem more generally dealing with market 'innovation'. Too often, regulators are slow to respond to an emerging market innovation or practice which causes consumer detriment. By the time, the regulatory process has been completed, the practices that cause detriment may have stopped and a new form of detriment emerges. This is not helped by the 'silo' approach adopted by EU and national regulators – where regulatory policy is formulated and implemented according to legal and corporate structure of products and providers rather than according to consumer needs (a prime example is the way MiFID, IMD, and PRIPs have evolved over time).

To address this challenge we make two recommendations:

- An omnibus directive covering sales and distribution, conduct of business, conflicts of interest, product design, professional competence of intermediaries, of all products with an investment purpose regardless of legal or corporate structure would be the most effective way forward.
- Regulators should assess and 'rate' complex products/instruments to decide the appropriate method of distribution. One practical way of implementing this would be for the new European Supervisory Authorities (ESAs) to have the authority to maintain and update an approved list of products and services. Clearly, this assessment and rating system has to flexible enough to cope with market 'innovation'. 'Enabling' regulation should be developed allowing EU and national regulators the scope and power to proactively define products as complex/non-complex without requiring new, long drawn out legislation. A risk based approach should determine whether certain types of complex products (such as structured products) are suitable for sale to retail investors in any circumstances whether on an execution-only or advised basis.

RESPONSE TO SPECIFIC QUESTIONS

DEVELOPMENTS IN MARKET STRUCTURES

(1) What is your opinion on the suggested definition of admission to trading? Please explain the reasons for your views.

FSUG believes that admission to trading should remain a meaningful concept and is concerned that such a concept would be watered down by being applied to other organised trading facilities than Regulated Markets (RMs). It should neither apply to any new category of market venues to be invented by the European Authorities such as 'Organised trading facilities'.

(2) What is your opinion on the introduction of, and suggested requirements for, a broad category of organised trading facility to apply to all organised trading functionalities outside the current range of trading venues recognised by MiFID? Please explain the reasons for your views.

FSUG understands and supports the rationale behind the Commission's proposal for a broad category of organised trading facility (OTF), aiming at restricting the scope of unregulated OTC transactions and ensuring that trading systems with similar functionalities are subject to similar requirements. But FSUG is not in favour of creating another category of market venue to address problems coming from the first fragmentation of market venues by MiFID in 2007. Such a proposal would increase the complexity already created by MiFID. End investors would be even more confused than before. How they are supposed to understand the difference between:

- 'multiple trading facilities' (MTF) which already do not generally understand (for example there is not one word on MTFs in the CESR 'Consumer Guide to MiFID') and
- 'organised trading facilities'?

This would likely further increase the opacity of the equity markets for the end users: issuers and end investors.

FSUG believes the alternative solution to reduce the scope of OTC trading is to impose very low and carefully designed thresholds to OTC operators (crossing networks, etc.) above which they will be obliged to switch to a regulated market venue (RM, MTF or Systematic Internaliser). We even question the relevance of keeping this third regulated category of

'systematic internalisers' as only ten of these exist three years after the MiFID implementation.

(3) What is your opinion on the proposed definition of an organised trading facility? What should be included and excluded?

See our reply to Q2.

(4) What is your opinion about creating a separate investment service for operating an organised trading facility? Do you consider that such an operator could passport the facility?

See our reply to Q2.

(5) What is your opinion about converting all alternative organised trading facilities to MTFs after reaching a specific threshold? How should this threshold be calculated, e.g. assessing the volume of trading per facility/venue compared with the global volume of trading per asset class/financial instrument? Should the activity outside regulated markets and MTFs be capped globally? Please explain the reasons for your views.

See our reply to Q2. Yes, we believe OTC activity should be capped globally, in addition to the individual thresholds mentioned previously.

(7) What is your opinion on the suggested clarification that if a crossing system is executing its own proprietary share orders against client orders in the system then it would prima facie be treated as being a systematic internaliser and that if more than one firm is able to enter orders into a system it would be prima facie be treated as a MTF? Please explain the reasons for your views.

Yes, we agree.

(8) What is your opinion of the introduction of a requirement that all clearing eligible and sufficiently liquid derivatives should trade exclusively on regulated markets, MTFs, or organised trading facilities satisfying the conditions above? Please explain the reasons for your views.

Yes, we agree, except for 'organised trading facilities' (see Q2). This is the only way to ensure the protection of investors.

(9) Are the above conditions for an organised trading facility appropriate? Please explain the reasons for your views.

See Q2.

(10) Which criteria could determine whether a derivative is sufficiently liquid to be required to be traded on such systems? Please explain the reasons for your views.

This technical matter should be handed to ESMA.

(12) Are there existing OTC derivatives that could be required to be traded on regulated markets, MTFs or organised trading facilities? If yes, please justify. Are there some OTC derivatives for which mandatory trading on a regulated market, MTF, or organised trading facility would be seriously damaging to investors or market participants? Please explain the reasons for your views.

Yes: Forex products, CDS and interest rate swaps could be required to be traded on regulated markets or MTFs. Transparency does not hurt liquidity in contrary to what some financial industry people try to make European Authorities believe. One should remember that in 2008 the most illiquid markets were also the most opaque: fixed income and ABS in particular, whereas the main equity markets remained open and liquid at all time, even though they deal with the longest term and risky securities.

(13) Is the definition of automated and high frequency trading provided above appropriate?

Not applicable to retail investors.

(14) What is your opinion of the suggestion that all high frequency traders over a specified minimum quantitative threshold would be required to be authorised?

We agree (see Q2). FSUG believes these are often 'free riders' exploiting the data from 'real' end investors who do not benefit from their activities. Yes, it is necessary. Otherwise the asymmetry of information between these professional market participants and 'real' end investors will increase further, as the latter will never match the technology investments done by the former.

(15) What is your opinion of the suggestion that high frequency traders might be required to provide liquidity on an ongoing basis where they actively trade in a financial instrument under similar conditions as apply to market makers? Under what conditions should this be required?

We agree.

(20) What is your opinion about requiring orders to rest on the order book for a minimum period of time? How should the minimum period be prescribed? What is your opinion of the alternative, namely of introducing requirements to limit the ratio of orders to transactions executed by any given participant? What would be the impact on market efficiency of such a requirement?

Yes, a minimum period of time is a good requirement to avoid the multiplication of 'fake' orders by high frequency traders.

(21) What is your opinion about clarifying the criteria for determining when a firm is a SI? If you are in favour of quantitative thresholds, how could these be articulated? Please explain the reasons for your views.

See Q2

(23) What is your opinion of the suggestions to further align organisational requirements for regulated markets and MTFs? Please explain the reasons for your views.

Yes, we agree. We do not see the rationale for these to be unaligned in the first place. Regulatory arbitrage and uneven playing fields must be avoided.

(25) What is your opinion of the suggestion to introduce a new definition of SME market and a tailored regime for SME markets under the framework of regulated markets and MTFs? What would be the potential benefits of creating such a regime?

FSUG fully agrees with the essential economic and social need to promote SME markets. We believe a prerequisite step for the Commission is to research evidence on the impact of

MiFID on SME issuers. It would seem that the market venues competition generated by MiFID has mainly touched the most liquid issues, i.e. mostly the ones from large corporations. Therefore we are concerned that MiFID is having a negative impact on SMEs' access to capital.

PRE- AND POST-TRADE TRANSPARENCY

(27) What is your opinion of the suggested changes to the framework directive to ensure that waivers are applied more consistently?

The reference price waiver should be deleted.

(31) What is your opinion about keeping the large in scale waiver thresholds in their current format? Please explain the reasons for your views.

FSUG supports keeping the large in scale waiver thresholds in their current format. FSUG is indeed concerned that there is a widespread confusion when some industry participants mention a reduction in the size of orders and trades to justify a revision of the current format of large in scale waivers, i.e. to expand the scope of dark and OTC trades even further. There is absolutely no evidence (and we have not seen any research on this sensitive issue) that investors' orders size has decreased. Since MiFID implementation, it appears that the orders from investors are often sliced into pieces by market intermediaries, not by the end clients. Then, of course the sliced orders turn into sliced trades as well. The benefits of such practices for end investors – if any – should be investigated. At the very least, market information and statistics tools should distinguish 'real orders' coming from the end clients from the sliced orders engineered by market intermediaries.

(32) What is your opinion about the suggestions for reducing delays in the publication of trade data? Please explain the reasons for your views

FSUG supports suggestions for reducing delays in the publication of data. In addition, comprehensive trade data should be made available free of charge to all investors after five minutes.

(33) What is your opinion about extending transparency requirements to depositary receipts, exchange traded funds and certificates issued by companies? Are there any further products (e.g. UCITS) which could be considered? Please explain the reasons for your views.

Yes, FSUG supports such an extension to ADRs, ETFs and certificates. These transparency requirements should also apply to investment funds (UCITS or non UCITS) that are admitted for trading on regulated markets (RMs and MTFs).

(35) What is your opinion about reinforcing and harmonising the trade transparency requirements for shares traded only on MTFs or organised trading facilities? Please explain the reasons for your views.

We agree. We see no reason for lower transparency requirements to start with.

(36) What is your opinion about introducing a calibrated approach for SME markets? What should be the specific conditions attached to SME markets?

See reply to Q 25.

(37) What is your opinion on the suggested modification to the MiFID framework directive in terms of scope of instruments and content of overarching transparency requirements? Please explain the reasons for your views.

FSUG supports a modification of the MiFID framework directive to include a wider scope to include bonds, structured products and derivatives.

(38) What is your opinion about the precise pre-trade information that regulated markets, MTFs and organised trading facilities as per section 2.2.3 above would have to publish on non-equity instruments traded on their system? Please be specific in terms of asset-class and nature of the trading system (e.g. order or quote driven).

Same requirements as for equities. Plus availability free of charge to all investors after five minutes.

(40) In view of calibrating the exact post-trade transparency obligations for each asset class and type, what is your opinion of the suggested parameters, namely that the regime be transaction-based, and predicated on a set of thresholds by transaction size? Please explain the reasons for your views.

FSUG is not comfortable with transaction size being the only criterion. FSUG believes that, in particular, all large bond issues should be subject to the same transparency requirements as equities on the regulated markets. This implies that all these large issues have identified market makers with binding maximum spreads and minimum bids and offers within those spreads. This is working very well for ETFs, including bond ETFs.

(41) What is your opinion about factoring in another measure besides transaction size to account for liquidity? What is your opinion about whether a specific additional factor (e.g. issuance size, frequency of trading) could be considered for determining when the regime or a threshold applies? Please justify.

See reply to Q40 above.

(42) Could further identification and flagging of OTC trades be useful? Please explain the reasons.

Yes. As mentioned previously, the regulators themselves do not really know the size of the OTC market.

DATA CONSOLIDATION

(49) In your view, what would constitute a 'reasonable' cost for the selling or dissemination of data? Please provide the rationale/criteria for such a cost.

As far as small investors are concerned, this cost should by no means be superior to what was before MiFID, i.e. free of charge after some delay.

(50) What is your opinion about applying any of these suggestions to non-equity markets? Please explain the reasons for your views.

We agree with such an extension. We see no reason to have a lower quality of trade data for non-equity markets, especially for those most directly relevant to small investors (bonds).

(51) What is your opinion of the suggestion for the introduction of a European Consolidated Tape for post-trade transparency? Please explain the reasons for your views, including the advantages and disadvantages you see in introducing a consolidated tape.

FSUG asks for a publicly enforced and controlled 'consolidated tape' both for pre- and post-trade data. This 'tape' shall be easily and freely accessible by all investors in the equity market at least as before MiFID. This is a major failure of MiFID and of the fragmentation of equity markets it has generated. The very least the Regulator should do is fixing the fragmentation of market data, as this was done in the US. Currently, retail investors most often do not get any comprehensive trade data neither from their brokers nor intermediaries, and generally only get those of the 'home' market (the 'RM'). Also, we disagree with the proposed exclusion of pre-trade data from this market data consolidation proposal: this would increase the asymmetry of the market information between 'professional' and small end investors. For instance the US consolidated tape applies also to pre-trade data.

(52) If a post-trade consolidated tape was to be introduced which option (A, B or C) do you consider most appropriate regarding how a consolidated tape should be operated and who should operate it? Please explain the reasons for your view.

FSUG's first choice is Option A, i.e. a formal consolidated tape operated by a single, non-profit seeking entity, established and appointed by a legal act.

Indeed, three years after MiFID's implementation, the financial industry has not come up with anything close to a consolidated tape solution. It is not realistic to believe that the industry would come up any time soon with a consolidated tape as defined above. Such a solution is now very urgently needed.

Please note that this was the Option adopted for the US equity markets. If the European Authorities would still give in to some financial industry lobbies, option B would be a compromise/ESMA should manage the tender process. In any option, including option C, the European Authorities should set very tight and mandatory deadlines, as small investors have suffered long enough from the disappearance of the comprehensive equity market data in Europe.

(53) If you prefer option A please outline which entity you believe would be best placed to operate the consolidated tape (e.g. public authority, new entity or an industry body).

The new ESMA seems the obvious choice (or a new entity controlled by ESMA). In the US, the SEC tightly controls two not for profit associations dedicated to the consolidation of equity markets data.

(54) On Options A and B, what would be the conditions to make sure that such an entity would be commercially viable? In order to make operating a European consolidated tape commercially viable and thus attaining the regulatory goal of improving quality and supply of post-trade data, should market participants be obliged to acquire data from the European single entity as it is the case with the US regime?

Yes.

(55) On Option B, which of the two sub-options discussed for revenue distribution for the data appears more appropriate and would ensure that the single entity described would be commercially viable?

The first sub-option under which trading venues and APAs would make their data available to the single entity on a reasonable commercial basis is preferable as it mould more safely ensure timely and free of charge information to retail investors.

(56) Are there any additional factors that need to be taken into account in deciding who should operate the consolidated tape (e.g. latency, expertise, independence, experience, competition)?

The governance and independence factors are obviously key for such an essential economic and social service.

(57) Which timeframe do you envisage as appropriate for establishing a consolidated tape under each of the three options described?

The consolidated tape should be fully operational no later then 1 January 2012. That would be more than four years after the fragmentation of equity markets in Europe. Investors should not wait much longer.

(58) Do you have any views on a consolidated tape for pre-trade transparency data?

See reply to Q51. We do not see why – contrary to US investors – European investors should be deprived of comprehensive best offers and bids prices. This is generating a huge asymmetry and discrimination between professional and big investors on the one side (who can afford to pay for consolidated pre-trade data) and the small ones (who can't and who actually most often don't get it. We refer to the attached recent study published by FSUG: a consolidated tape for pre-trade data is necessary as well.

(59) What is your opinion about the introduction of a consolidated tape for non-equity trades? Please explain the reasons for your views.

FSUG strongly supports the introduction of a European consolidate tape for non-equity trades for the very same reasons as for equity ones.

MEASURES SPECIFIC TO COMMODITY DERIVATIVES MARKETS

(60) What is your opinion about requiring organised trading venues which admit commodity derivatives to trading to make available to regulators (in detail) and the public (in aggregate) harmonised position information by type of regulated entity? Please explain the reasons for your views.

Yes. Currently, these are very non transparent financial instruments.

(63) What is your opinion about requiring organised commodity derivative trading venues to design contracts in a way that ensures convergence between futures and spot prices? What is your opinion about other possible requirements for such venues, including introducing limits to how much prices can vary in a given timeframe? Please explain the reasons for your views.

FSUG agrees that commodity derivative contracts should be designed in a way that ensures convergence between futures and spot prices.

Also the information should be standardised to the maximum extent possible.

(66) What is your opinion on whether to classify emission allowances as financial instruments? Please explain the reasons for your views.

We agree with the Commission's proposal to consider this classification as an option in a forthcoming study.

TRANSACTION REPORTING

(67) What is your opinion on the extension of the transaction reporting regime to transactions in all financial instruments that are admitted to trading or traded on the above platforms and systems? Please explain the reasons for your views.

Yes, but on RMs and MTFs only (see reply to Q2).

(68) What is your opinion on the extension of the transaction reporting regime to transactions in all financial instruments the value of which correlates with the value of financial instruments that are admitted to trading or traded on the above platforms and systems? Please explain the reasons for your views.

Yes.

(69) What is your opinion on the extension of the transaction reporting regime to transactions in depositary receipts that are related to financial instruments that are admitted to trading or traded on the above platforms and systems? Please explain the reasons for your views.

Yes.

(70) What is your opinion on the extension of the transaction reporting regime to transactions in all commodity derivatives? Please explain the reasons for your views.

Yes.

(72) What is your opinion of an obligation for regulated markets, MTFs and other alternative trading venues to report the transactions of non authorised members or participants under MiFID? Please explain the reasons for your views.

Yes.

(73) What is your opinion on the introduction of an obligation to store order data? Please explain the reasons for your views.

Yes.

(74) What is your opinion on requiring greater harmonisation of the storage of order data? Please explain the reasons for your views.

Yes.

(79) What is your opinion on introducing implementing acts on a common European transaction reporting format and content? Please explain the reasons for your views?

Yes, standardisation is definitely the way to go.

(80) What is your opinion on the possibility of transaction reporting directly to a reporting mechanism at EU level? Please explain the reasons for your views.

FSUG agrees. This also implies rationalisation and streamlining of the securities clearing and settlement processes in Europe.

INVESTOR PROTECTION AND PROVISION OF INVESTMENT SERVICE

(84) What is your opinion about limiting the optional exemptions under Article 3 of MiFID? What is your opinion about obliging Member States to apply to the exempted entities requirements analogous to the MiFID conduct of business rules for the provision of investment advice and fit and proper criteria? Please explain the reasons for your views.

We support the intention to limit the optional exemptions under Article 3 of MiFID. To ensure a level playing field, consistent and coherent regulation, it is important that there is limited scope for regulatory arbitrage.

(85) What is your opinion on extending MiFID to cover the sale of structured deposits by credit institutions? Do you consider that other categories of products could be covered? Please explain the reasons for your views.

We agree that structured products should be covered by MiFID as these are often sold as substitutes for deposit accounts and can result in investors being misled. Indeed, it is important that MiFID should be an 'enabling' directive allowing new products to be brought within the scope of regulation without requiring new legislation.

This requires a broad, flexible definition of investment products.

Any product that is:

(i) not clearly and purely deposit based;
(ii) utilises financial instruments (including insurance based products)to generate the expected return;
(iii) puts investors capital at risk (i.e. there is the potential for underlying capital to fluctuate or vary as a result of market movements);

should be covered by the full set of regulatory requirements.

Simple, pure deposit accounts should not be covered by the full set of regulatory requirements contained in MiFiD (such as conduct of business rules). However, it is important that even simple, pure deposit accounts are covered by regulation covering disclosure of information, marketing and promotions[2].

Moreover, if firms use the marketing of deposit accounts to cross-sell investment products, then these sales should be covered by full conduct of business regulation.

(86) What is your opinion about applying MiFID rules to credit institutions and investment firms when, in the issuance phase, they sell financial instruments they issue, even when advice is not provided? What is your opinion on whether, to this end, the definition of the service of execution of orders would include direct sales of financial instruments by banks and investment firms? Please explain the reasons for your views.

[2] This would not be covered by MiFiD of course.

We agree that MiFID rules should apply to credit institutions and investment firms when selling financial instruments irrespective of the circumstances in which the firm operates. Similarly, the service of execution of orders should include direct sales of financial instruments by banks and investment firms of any other financial provider. Also, this should apply when an investment firm does not sell its own securities but acts on behalf of an issuer.

The key reason for our view is consistency and coherence. Investor detriment can occur at all parts of the financial supply chain, not just at the point of sale/advice. The behaviour of market participants can impact on the quality, value for money and suitability of investment products/services received by investors even though explicit advice has not been received.

Another important issue to mention is that intermediaries of grey market products (such as closed funds) must not be out of the scope of MiFiD as is the case today.)

(87) What is your opinion of the suggested modifications of certain categories of instruments (notably shares, money market instruments, bonds and securitised debt), in the context of so-called 'execution only' services? Please explain the reasons for your views.

(88) What is your opinion about the exclusion of the provision of 'execution-only' services when the ancillary service of granting credits or loans to the client (Annex I, section B(2) of MiFID) is also provided? Please explain the reasons for your views.

(89) Do you consider that all or some UCITS could be excluded from the list of non-complex financial instruments? In the case of a partial exclusion of certain UCITS, what criteria could be adopted to identify more complex UCITS within the overall population of UCITS? Please explain the reasons for your views.

(90) Do you consider that, in the light of the intrinsic complexity of investment services, the 'execution-only' regime should be abolished? Please explain the reasons for your views.

'Execution-only' is a difficult issue for investor representatives. The essence of execution-only is that investment firms provide investors with a means to buy and sell certain financial instruments in the market without undergoing any assessment of the appropriateness of the given product - that is, the assessment against knowledge and experience of the investor.

FSUG members are very concerned about the risks involved with execution-only. For example, the existence of the execution-only option creates the risk that firms, intermediaries, and distributors (such as banks) can guide or 'steer' consumers away from regulated advice (with higher standards of consumer protection) towards execution-only services which can allow firms/intermediaries/distributors to transfer much of the risk of inappropriate or unsuitable sales of financial products to the consumer. This risk is likely to increase with the growth of 'platforms'[3].

The consultation paper sets out two options for dealing with risks such as this. Option A represents a risk based approach which seeks to control the financial instruments which could be sold on an execution-only basis. Option B implies the abolition of the execution-only regime.

There is some support amongst FSUG members for Option B – i.e. prohibiting execution-only.

However, a risk based approach outlined in Option A has greater support.

[3] Such as fund 'supermarkets' or 'wraps'.

Clearly, there is a risk involved in the selling and distribution of all financial instruments and assets (even those that are deceptively simple) and it is advisable for investors to obtain professional advice. However, this has to be balanced against the rights of more sophisticated investors who may have the confidence to buy products on an execution only basis and who want to have the choice to do so.

To balance the interests of different groups of investors a risk based approach should be more effective. This means that, while execution only would not be banned outright, the circumstances in which it is allowed should be narrowly, and clearly, defined and regulation enforced.

It must be stressed that this risk based approach would need to robustly monitored and enforced by European and national regulators.

In practice, this means:

- Regulators should assess and 'rate' complex products/instruments to decide if they are appropriate for distribution via execution-only. One practical way of implementing this would be for the new European Supervisory Authorities (ESAs) to have the authority to maintain and update an approved list of products and services. Clearly, this assessment and rating system has to flexible enough to cope with market 'innovation'. As outlined above, this means that MiFiD and other directives should be 'enabling' regulation allowing EU and national regulators the scope and power to proactively define products as complex/non-complex without requiring new, long drawn out legislation.
- The question of suitability should not be based on legal or corporate structure per se. This means for example that UCITS as a class of investment would not be excluded simply because of the legal structure. The key criteria for suitability should be based on potential risk to investor and complexity. Risk in this case could mean risk to capital preservation, potential volatility, exposure to counterparties, regulatory jurisdiction and so on. At this stage, given time constraints, we are unable to provide the Commission with detailed criteria for assessing whether certain products should be included/excluded. However, we would welcome the opportunity to develop this risk based model.
- A risk based approach should determine whether certain types of complex products (such as structured products) are suitable for sale in any circumstances to retail investors whether on an execution-only or advised basis.
- Investors should be warned in clear terms about the risks associated with execution-only such as the potential loss of consumer protection regulation and rights to redress.
- Specifically, we support the removal of services that would allow leveraging.

Specifically, UCITS should not continue to be treated automatically as non-complex instruments. For instance, some hedge funds recently obtained the UCITS label enabling them to distribute complex UCITS products in the EU. In addition, recent supervisory experience highlights that a number of UCITS are too sophisticated (complex formula funds) to be easily understood by retail clients. Clearly, such highly complex products should not be recommended to retail clients.

As a result, there is a case for treating structured UCITS and UCITS which employ complex portfolio management techniques as complex financial instruments for the purposes of the appropriateness test. ESMA could define criteria on this basis.

(91) What is your opinion of the suggestion that intermediaries providing investment advice should: 1) inform the client, prior to the provision of the service, about the basis on which advice is provided; 2) in the case of advice based on a fair analysis of the market, consider a sufficiently large number of financial instruments from different providers? Please explain the reasons for your views.

(92) What is your opinion about obliging intermediaries to provide advice to specify in writing to the client the underlying reasons for the advice provided, including the explanation on how the advice meets the client's profile? Please explain the reasons for your views.

(93) What is your opinion about obliging intermediaries to inform the clients about any relevant modifications in the situation of the financial instruments pertaining to them? Please explain the reasons for your views.

(94) What is your opinion about introducing an obligation for intermediaries providing advice to keep the situation of clients and financial instruments under review in order to confirm the continued suitability of the investments? Do you consider this obligation be limited to longer term investments? Do you consider this could be applied to all situations where advice has been provided or could the intermediary maintain the possibility not to offer this additional service? Please explain the reasons for your views.

We strongly support the objective of improving the level of disclosure and accountability to clients. Disclosure should cover:

- the basis of the advice (independent whole of market, restricted, single firm etc);
- the status of the intermediary (whether independent, sales agent etc);
- basis of remuneration and other potential conflicts of interest (including relationships with product providers and others in the financial supply chain);
- reasons and justification for advice and recommendations made by intermediary.

We support the view that disclosure should be on an ongoing basis not just at the point of sale. Investment products and services are not one-off disposable purchases. The real value or benefit of an investment decision/purchase only becomes apparent over time so it is clearly appropriate that intermediaries who claim to be offering a professional service continue to monitor the appropriateness of the original recommendation.

Disclosure should also cover advice documentation which should be standardised, monitored, and enforced robustly by regulators.

However, it is important to recognise the risk that less scrupulous financial providers and intermediaries will use the opportunity provided by ongoing contact to aggressively sell unnecessary or inappropriate products and services.

Also, we have ample evidence that the MiFID provisions for a clear, fair and not misleading information have not been sufficiently enforced by national supervisors.

Therefore, it is important that regulators closely monitor ongoing relationships not just at the point of sale. This means that ESMA (and other ESAs) should pay as much attention to monitoring and enforcing regulation as developing policy. The use of 'mystery shopping' and sampling is a cost-effective way of monitoring market behaviour.

It is important to note that, if we want to address conflicts of interest in the financial supply chain, disclosure is necessary but not sufficient. We are of the view that the main cause of

conflicts of interest in the financial supply chain are the inducements and remuneration policies that encourage intermediaries to recommend products that meet their own commercial needs, rather than the needs of the consumer (indeed this applies not just to intermediaries at the point of sale but financial distribution generally – for example, the commercial relationships between investment companies who manufacture products and banks who distribute them).

Disclosure of status and inducements of course can be helpful in alerting consumers to the potential for conflicts of interest. However, the evidence from member states such as the UK suggests that information solutions per se have had a very limited success in actually constraining the behaviour of intermediaries.

So, if conflicts of interest are to be addressed, other interventions are needed. For example, this could include:

- Requiring product providers to introduce more robust risk management procedures during the product development stage if they continue to distribute products through intermediaries who are rewarded by variable commission payments or other such inducements.
- Introducing a much clearer definition of intermediary status. There should be only two status definitions – independent and sales agents. Only intermediaries who i) do not accept any payments, inducements or benefits from product providers and ii) assess the full range of products on the market should be allowed to refer to themselves as independent advisers. All other intermediaries should be referred to sales agents or sales representatives regardless of whether they sell the products of one provider or a limited panel of providers. It is important that an independent adviser has a clear duty of care to the client and avoids conflicts of interest. All intermediaries have a general duty of care to consumers but an intermediary who accepts remuneration of any kind from a product provider is an agent of that provider, not the client.
- Requiring sales agents to justify orally and in writing why they have chosen to recommend a product (within the range of products they cover) that pays higher commission/rewards even though a similar product within the range would perform the same role.
- A major problem for the investor is how s/he can prove whether wrong advice has been provided by an intermediary or adviser. Indeed, this is a problem for the industry as well when it relates to disputes referred to Ombudsmen, or mediation and arbitration schemes. Our preferred option is taping of the sales 'interview', followed by placing the burden of proof on the provider, and then advice documentation with clear rules.

(95) What is your opinion about obliging intermediaries to provide clients, prior to the transaction, with a risk/gain and valuation profile of the instrument in different market conditions? Please explain the reasons for your views.

(96) What is your opinion about obliging intermediaries also to provide clients with independent quarterly valuations of such complex products? In that case, what criteria should be adopted to ensure the independence and the integrity of the valuations?

(97) What is your opinion about obliging intermediaries also to provide clients with quarterly reporting on the evolution of the underlying assets of structured finance products? Please explain the reasons for your views.

(98) What is your opinion about introducing an obligation to inform clients about any material modification in the situation of the financial instruments held by firms on their behalf? Please explain the reasons for your views.

(99) What is your opinion about applying the information and reporting requirements concerning complex products and material modifications in the situation of financial instruments also to the relationship with eligible counterparties? Please explain the reasons for your views.

(100) What is your opinion of, in the case of products adopting ethical or socially oriented investment criteria, obliging investment firms to inform clients thereof?

We agree that intermediaries should be obliged to provide clients with the information outlined above prior to a transaction. Potential investors should be able to identify how investment products perform under different market conditions. The more complex or exposure to risk the product has, the greater the potential impact of adverse market conditions. It is not clear how clients could make a reasonable assessment of the suitability of a product without understanding how the financial instruments that comprise the product are expected to perform in different market conditions.

As above, we are of the view that reporting should be on an ongoing basis not a one-off basis.

We strongly agree with the proposal to oblige intermediaries to inform clients about any material changes to the position of the financial instruments. The essence of an investment product/service is the financial assets and instruments held within its structure. Any change to the financial assets and instruments clearly alters the essence and, therefore, the appropriateness of the product/service. The medium-long term nature of many investment products/services means that investors may not be aware of the consequences of the material change until it is too late and be unable to take remedial action.

We also agree that investors should be made aware of the involvement of counterparties. If investors are unaware that the involvement of counterparties can affect the delivery of a product/service, then this would be misleading. Investors need to be clear about who the relationship is really with.

With regards to products claiming to adopt ethical or socially oriented investment criteria, we think it is important that product providers and intermediaries should be explicitly required to disclose information.

As the research studies suggest (Martin, 2007)[4], investors with lower educational standards tend to behave 'socially and more altruistically', which can be in contradiction to their original aim (financial profit). 'Ethical' or 'social' investment products can be misused in this context[5].

(101) What is your opinion of the removal of the possibility to provide a summary disclosure concerning inducements? Please explain the reasons for your views.

[4] *A literature review on the effectiveness of financial education*, Martin, M., 2007, in Federal Reserve Bank of Richmond Working Paper 07-03, available at: http://www.richmondfed.org/publications/research/working_papers/2007/pdf/wp07-3.pdf.

[5] Let's not forget, that we are live in the era of 'social marketing' (financial services notwithstanding).

(102) Do you consider that additional ex-post disclosure of inducements could be required when ex-ante disclosure has been limited to information methods of calculating inducements? Please explain the reasons for your views.

(103) What is your opinion about banning inducements in the case of portfolio management and in the case of advice provided on an independent basis due to the specific nature of these services? Alternatively, what is your opinion about banning them in the case of all investment services? Please explain the reasons for your views.

The disclosure of inducements requirement of MiFID is not really enforced. To start with, CESR has entirely omitted this requirement in its 'Consumer guide to MiFID' despite the requests of investor and consumer advocates. Therefore, many national regulators have also omitted it.

It is critical that the amount of inducement an intermediary is expected to receive as a result of recommending a particular product should be disclosed clearly in monetary terms to the investor.

It is not appropriate to disclose ex-post relevant information relating to inducements an intermediary is likely to receive as a result of recommending a product. At this stage the investor is too far into the decision making process. Disclosure at that stage is unlikely to be effective at encouraging the investor to re-evaluate his/her decision.

Of course, as part of the regular ongoing reporting requirements outlined above, intermediaries should be obliged to report to clients the actual revenue received as a result of recommending a product.

Moreover, as mentioned above, disclosure per se appears to have limited impact in constraining aggressive sales practices. Intermediaries that act as sales agents should be required to justify orally and in writing why they have chosen to recommend a product (within the range of products they cover) that pays higher commission/rewards even though a similar product within the range would perform the same role.

As outlined above, we would support the proposal to ban intermediaries operating as independent advisers from accepting inducements/payments from product providers. It is important that an independent adviser has a clear duty of care to the client and avoids conflicts of interest. An intermediary who accepts remuneration of any kind from a product provider is an agent of that provider, not the client.

(104) What is your opinion about retaining the current client classification regime in its general approach involving three categories of clients (eligible counterparties, professional and retail clients)? Please explain the reasons for your views.

(105) What are your suggestions for modification in the following areas:

a) Introduce, for eligible counterparties, the high level principle to act honestly, fairly and professionally and the obligation to be fair, clear and not misleading when informing the client;
b) Introduce some limitations in the eligible counterparties regime. Limitations may refer to entities covered (such as non-financial undertakings and/or certain financial institutions) or financial instruments traded (such as asset backed securities and nonstandard OTC derivatives); and/or
c) Clarify the list of eligible counterparties and professional clients per se in order to exclude local public authorities/municipalities? Please explain the reasons for your views.

(106) Do you consider that the current presumption covering the professional clients' knowledge and experience, for the purpose of the appropriateness and suitability test, could be retained? Please explain the reasons for your views.

The high level principle to act honestly, fairly and professionally and the obligation to be fair, clear and not misleading when informing the client should apply to all market participants.

We support the current classification scheme – eligible counterparties, professional and retail clients.

However, we take the view that local public authorities/municipalities, and pension fund schemes should be reclassified as retail/non-professional client with an opt-in for larger public authorities/municipalities/pension schemes.

The reason for this is that although public authorities/municipalities/pension schemes may have significant assets under their control, the individuals responsible for prudential oversight of these assets are not necessarily professional investors. For example, they may be local councillors or employee representatives and deserve the same degree of protection as retail investors.

Of course, it is important that the role of advisers in this market (such as pension fund actuaries and investment advisers) is addressed as well as retail intermediaries.

(107) What is your opinion on introducing a principle of civil liability applicable to investment firms? Please explain the reasons for your views.

(108) What is your opinion of the following list of areas to be covered: information and reporting to clients, suitability and appropriateness test, best execution, client order handling? Please explain the reasons for your views.

We support the introduction of a principle of civil liability under the principle of minimum harmonisation. A civil liability principle would be essential for ensuring a minimum level of investor protection in the EU.

Moreover, we are of the view that as part of a credible deterrence package, civil liability provisions as a sanction would be effective at deterring damaging behaviour on the part of market participants (see our response to the Sanctions Consultation).

We are not certain why the areas to be covered have to be prescriptively defined. We would argue that it should be more effective to apply the sanction to any behaviour that breaches MiFiD and results in losses for investors.

(109) What is your opinion about requesting execution venues to publish data on execution quality concerning financial instruments they trade? What kind of information would be useful for firms executing client orders in order to facilitate compliance with best execution obligations? Please explain the reasons for your views.

(110) What is your opinion of the requirements concerning the content of execution policies and usability of information given to clients should be strengthened? Please explain the reasons for your views.

This may be of limited use for retail investors. There is a much more pressing issue regarding 'best execution'. This was a major provision of the MiFID Directive. This consultation document does not address it, which is all the more surprising as 'best execution

is simply not happening for retail investors', and they have no means to ensure that their orders receive 'best execution'. What would be useful for retail investors to ensure they get the best execution of their orders is:

- going back to pre-MiFID levels of pre- and post-trade transparency;
- ensure the best price for their orders.

Currently, most retail brokers do not clearly explain to their retail customers that they channel their orders to only one venue (usually the RM), and that the pre- and post-trade data they provide are not consolidated but most often come from only one venue.

More importantly, research[6] shows that retail clients often do not get the best price because of the MiFID induced market fragmentation and because it is too complex and costly for retail brokers to find the best price among all the venues.

(111) What is your opinion on modifying the exemption regime in order to clarify that firms dealing on own account with clients are fully subject to MiFID requirements? Please explain the reasons for your views.

Firms dealing on their own account should be fully subject to MiFID requirements and alert their clients that they are acting as such. This is clearly one of the loopholes in the investor protection provisions that must be closed.

(112) What is your opinion on treating matched principal trades both as execution of client orders and as dealing on own account? Do you agree that this should not affect the treatment of such trading under the Capital Adequacy Directive? How should such trading be treated for the purposes of the systematic internaliser regime? Please explain the reasons for your views.

No comment.

(113) What is your opinion on possible MiFID modifications leading to the further strengthening of the fit and proper criteria, the role of directors and the role of supervisors? Please explain the reasons for your view.

We support the proposals on fit and proper criteria set out in 7.3.1, p66 of the consultation document. The main reason is to ensure that those people with responsibility for running the business and corporate governance exercise proper controls and due diligence.

It is also important that the Chair of the board should be a non-executive director.

(114) What is your opinion on possible MiFID modifications leading to the reinforcing of the requirements attached to the compliance, the risk management and the internal audit function? Please explain the reasons for your view.

We very much support the arguments and proposals set out in 7.3.2, p. 67. We especially support the emphasis on ensuring that compliance, risk management, and internal audit is a clear, accountable board level responsibility.

[6] See Annex 1: Reply from the European federation of Investors (EuroInvestors).

(115) Do you consider that organisational requirements in the implementing directive could be further detailed in order to specifically cover and address the launch of new products, operations and services? Please explain the reasons for your views.

(116) Do you consider that this would imply modifying the general organisational requirements, the duties of the compliance function, the management of risks, the role of governing body members, the reporting to senior management and possibly to supervisors?

We strongly support the modifications set out in 7.3.3, p68. We take the view that it is better to try to prevent detriment occurring in the first place rather than clear up the problem afterwards. This is more efficient for regulators, investors, and industry and of course would be more effective at maintaining investor confidence.

It is critical that the board and senior directors understand the risks involved in product development.

In particular, the requirements to stress test, risk assess, review products and services, and ensure staff understands products and services are critical. We would argue that this approach should be extended to apply to intermediaries. Product providers should be confident that the intermediaries selling their products understand the risks involved, and how the product actually works.

However, it is important to emphasise that enhanced governance arrangements will only be fully effective if the board takes ownership of governance and risk management. This means that regulators must make clear to board members the level of responsibility expected of them, and accountability mechanisms in the event of failure.

(117) Do you consider that specific organisational requirements could address the provision of the service of portfolio management? Please explain the reasons for your views.

No comment.

(118) Do you consider that implementing measures are required for a more uniform application of the principles on conflicts of interest?

Yes, we support the view that implementing measures are required to ensure consistency across the EU. We are particularly pleased that the Commission recognises that it is important to manage and avoid conflicts of interest – this goes beyond disclosure. We have set out a number of measures for the effective management of conflicts of interest, above.

In addition, any bonuses paid to senior management or directors should be linked to compliance with regulations. This would be an effective way of aligning the interests of the firm and customer, and managing conflicts of interest.

Implementing measures should be included the competencies of the ESAs.

(119) What is your opinion of the prohibition of title transfer collateral arrangements involving retail clients' assets? Please explain the reasons for your views.

Any title transfer should be formally approved by the client on the basis of clear information and fair remuneration, and the amount of transferred assets should not exceed the amount of the debt due by the client to the firm (increased by an appropriate 'haircut'.

(120) What is your opinion about Member States be granted the option to extend the prohibition above to the relationship between investment firms and their non retail clients? Please explain the reasons for your views.

(121) Do you consider that specific requirements could be introduced to protect retail clients in the case of securities financing transaction involving their financial instruments? Please explain the reasons for your views.

(122) Do you consider that information requirements concerning the use of client financial instruments could be extended to any category of clients?

(123) What is your opinion about the need to specify due diligence obligations in the choice of entities for the deposit of client funds?

We support the proposals 1-4 set out in 7.3.6, p. 70. The key reason, as we outline above, is that large investors such as pension funds, local authorities are often exposed to the same risks in the market as retail investors.

(124) Do you consider that some aspects of the provision of underwriting and placing could be specified in the implementing legislation? Do you consider that the areas mentioned above (conflicts of interest, general organisational requirements, requirements concerning the allotment process) are the appropriate ones? Please explain the reasons for your views.

No comment.

FURTHER CONVERGENCE OF THE REGULATORY FRAMEWORK AND OF SUPERVISORY PRACTICES

(125) What is your opinion of Member States retaining the option not to allow the use of tied agents?

(126) What is your opinion in relation to the prohibition for tied agents to handle clients' assets?

(127) What is your opinion of the suggested clarifications and improvements of the requirements concerning the provision of services in other Member States through tied agents?

(128) Do you consider that the tied agents regime require any major regulatory modifications? Please explain the reasons for your views.

We support the modifications set out in paras b)-e) of 8.1.1, p. 74. Member States should be allowed to retain the use of tied advisers.

However, additional measures are needed. We argue for introducing a much clearer definition of intermediary status. There should be only two status definitions – independent and sales agents.

Only intermediaries who i) do not accept any payments, inducements or benefits from product providers and ii) assess the full range of products on the market should be allowed to refer to themselves as independent advisers.

All other intermediaries should be referred to sales agents or sales representatives regardless of whether they sell the products of one provider or a limited panel of providers. It

is important that an independent adviser has a clear duty of care to the client and avoids conflicts of interest. An intermediary who accepts remuneration of any kind from a product provider is an agent of that provider, not the client.

(129) Do you consider that a common regulatory framework for telephone and electronic recording, which should comply with EU data protection legal provisions, could be introduced at EU level? Please explain the reasons for your views.

(130) If it is introduced do you consider that it could cover at least the services of reception and transmission of orders, execution of orders and dealing on own account? Please explain the reasons for your views.

(131) Do you consider that the obligation could apply to all forms of telephone conversation and electronic communications? Please explain the reasons for your views.

(132) Do you consider that the relevant records could be kept at least for 3 years? Please explain the reasons for your views.

Yes, we agree with the view that a common regulatory framework is needed. The main reason is to avoid regulatory arbitrage.

Indeed, there is a strong case for saying that this should apply to all transactions including those between intermediaries and retail investors. This would help avoid misunderstandings in the event of complaints and redress-able claims. It would also help regulators monitor whether sales staff are using aggressive verbal sales tactics to override written communication and disclosure.

(133) What is your opinion on the abolition of Article 4 of the MiFID implementing directive and the introduction of an on-going obligation for Member States to communicate to the Commission any addition or modification in national provisions in the field covered by MiFID? Please explain the reasons for your views.

No comment.

(134) Do you consider that appropriate administrative measures should have at least the effect of putting an end to a breach of the provisions of the national measures implementing MiFID and/or eliminating its effect? How the deterrent effect of administrative fines and periodic penalty payments can be enhanced? Please explain the reasons for your views.

Yes. The publicity of the sanction with naming the investment firm is effective. The amount of the administrative fines must also have a deterring effect and should be harmonised upwards at the EU level. Proceeds should be at least partly used to fund investor representatives as such a move has been a commitment of the Commission since early 2009, but not implemented as of today.

(135) What is your opinion on the deterrent effects of effective, proportionate and dissuasive criminal sanctions for the most serious infringements? Please explain the reasons for your views.

Criminal sanctions should be incorporated as part of a package of credible deterrence measures. For details of FSUG views on sanctions, please see our response on the Sanctions consultation.

(136) What are the benefits of the possible introduction of whistleblowing programs? Please explain the reasons for your views.

We support the establishment of a whistleblowing mechanism. The complexity, opaque and fast moving nature of financial markets means it can be difficult for regulators to respond quickly and effectively on every occasion. Enabling insiders to expose detrimental practices would be beneficial.

Moreover, as well as introducing a system for whistleblowing, it is important that regulators emphasise the 'duty' of senior management to inform regulators of any breaches of regulation. Reporting should not be an option.

(137) Do you think that the competent authorities should be obliged to disclose to the public every measure or sanction that would be imposed for infringement of the provisions adopted in the implementation of MiFID? Please explain the reasons for your views.

Yes. As we explain in our submission on Sanctions, these should be transparent and robust to promote good market behaviours.

(138) In your opinion, is it necessary to introduce a third country regime in MiFID based on the principle of exemptive relief for equivalent jurisdictions? What is your opinion on the suggested equivalence mechanism?

(139) In your opinion, which conditions and parameters in terms of applicable regulation and enforcement in a third country should inform the assessment of equivalence? Please be specific.

(140) What is your opinion concerning the access to investment firms and market operators only for non-retail business?

We are not against the idea of establishing an equivalence regime for third country firms. However, it is important that the Commission and ESAs transparently and robustly assess third country regimes for equivalence. This should apply to all aspects of the firm and products involved – including an assessment of the legal and prudential regulation of the third country.

REINFORCEMENT OF SUPERVISORY POWERS IN KEY AREAS

(142) What is your opinion on the possibility to ban products, practices or operations that raise significant investor protection concerns, generate market disorder or create serious systemic risk? Please explain the reasons for your views.

We strongly support this option. It is important that regulators have at their disposal all the necessary regulatory tools to protect consumers from unfair practices and products and make markets work in the interest of society. Product banning and product intervention generally can be a very effective way of driving out detrimental products. There is little evidence that 'natural' market forces such as competition are effective at doing so.

Moreover, there is little evidence that product intervention stifles innovation or competition. Indeed, the evidence from other sectors is that product intervention actually promotes consumer confidence and encourages consumer-focused innovation.

(143) For example, could trading in OTC derivatives which competent authorities determine should be cleared on systemic risk grounds, but which no CCP offers to clear, be banned

pending a CCP offering clearing in the instrument? Please explain the reasons for your views.

No comment.

(144) Are there other specific products which could face greater regulatory scrutiny? Please explain the reasons for your views.

Rather than focus on specific products, we are of the view that regulators should develop a risk based model for assessing and 'rating' financial products/instruments to determine which form of regulatory intervention is appropriate. In certain cases, the risks posed to consumers and the financial system would warrant an immediate ban or temporary suspension.

Products that are of specific concern include complex products offered through SIVs, uncovered short sells of CDS and derivatives, OTC derivatives not standardised sufficiently to be eligible for CCP clearing.

I wouldn't go so far with exemplification of products, especially with orientation on short sells on derivatives and CDS, which are registered on official regulated markets (or are covered by market makers). OTC derivatives and most of the OTC products possess far greater risks and require detailed scrutiny.

(145) If regulators are given harmonised and effective powers to intervene during the life of any derivative contract in the MiFID framework directive do you consider that they could be given the powers to adopt hard position limits for some or all types of derivative contracts whether they are traded on exchange or OTC? Please explain the reasons for your views.

(146) What is your opinion of using position limits as an efficient tool for some or all types of derivative contracts in view of any or all of the following objectives: (i) to combat market manipulation; (ii) to reduce systemic risk; (iii) to prevent disorderly markets and developments detrimental to investors; (iv) to safeguard the stability and delivery and settlement arrangements of physical commodity markets. Please explain the reasons for your views.

Regulators should be provided with the competence to adopt hard position limits and minimum margins amongst other regulator tools for all derivative contracts regardless of trading venue. This is most effective way of managing systemic risk and combating market manipulation.

In the case of products traded on regulated exchange, some corrective measures should be adopted first. Allowing immediate hard action from the regulators could even enlarge the systemic risk. For regulated derivative products, there should exist a methodology of hard position adoption with respect to the level of rules violation and potential damage. If the same regime is given to the exchange listed derivatives and OTC derivatives, we could face regulatory arbitrage.

(147) Are there some types of derivatives or market conditions which are more prone to market manipulation and/or disorderly markets? If yes, please justify and provide evidence to support your argument.

Based on the experience of the past two years, we think that short selling (but especially uncovered short selling) has been an important cause of unsound volume of derivatives

trades, and are a major contributor to volatility in the commodity markets. Indeed, these can threaten entire economies.

Short selling as a trading method should not be viewed as a cause of market behaviour. I would go with the combination of trading method and financial instrument with the respect to the overall volume on the market. Combining these three variables, some potentially disruptive behaviour can occur on the market.

(148) How could the above position limits be applied by regulators:

(a) To certain categories of market participants (e.g. some or all types of financial participants or investment vehicles)?
(b) To some types of activities (e.g. hedging versus non-hedging)?
(c) To the aggregate open interest/notional amount of a market?

These should apply to all market participants and financial instruments if they represent a systemic risk. A second threshold could be the aggregate open interest and size of the market.