# Review of the Markets in Financial Instruments Directive

# Questionnaire on MiFID/MiFIR 2 by Markus Ferber MEP

The questionnaire takes as its starting point the Commission's proposals for MiFID/MiFIR 2 of 20 October 2011 (COM(2011)0652 and COM(2011)0656).

All interested stakeholders are invited to complete the questionnaire. You are invited to answer the following questions and to provide any detailed comments on specific Articles in the table below. Responses which are not provided in this format may not be reviewed.

Respondents to this questionnaire should be aware that responses may be published.

Please send your answers to econ-secretariat@europarl.europa.eu **by 13 January 2012.**

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| Name of the person or organisation responding to the questionnaire | **The Association of Private Client Investment Managers and Stockbrokers (APCIMS**<br><br>The Association of Private Client Investment Managers and Stockbrokers (APCIMS) is a trade association representing 174 member firms. Of this number 116 members are private client investment managers and stockbrokers and 58 are associate members who provide related services to our firms. Member firms deal primarily in stocks and shares as well as other financial instruments for individuals, trusts and charities and offer a range of services from execution only trading (no advice) through to full portfolio management.<br><br>Our member firms operate on more than 500 sites in the UK, Ireland, Isle of Man and Channel Islands, employing c.30,000 employees. Over £475 billion of these countries' wealth is under the management of our members. Our aim is to ensure that regulatory, tax and other changes across Europe are appropriate and proportionate for the investment community. |

| Theme | Question | Answers |
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| **Scope** | 1) Are the exemptions proposed in Directive Articles 2 and 3 appropriate? Are there ways in which more could be done to exempt corporate end users? | In Article 2 the exemptions are, broadly speaking, appropriate. It will be particularly important for the market maker exemption to be retained in full. As regards corporate end users, much will depend on the definition of ancillary; this can be determined quite widely in relation to, for example, the activities of corporate treasurers and it is by careful use of definitional criteria in this area that the exempt status of corporate end users can be appropriately reinforced.<br><br>Article 3.1 in general refers to the Independent Financial Adviser, or IFA, sector. Article 3.1.new (ii) has inter alia the effect of making the definition of "independence" for an IFA the same as that given in Article 24.5 of the recast MiFID. Doing so will directly conflict with the new definition of "independence" created by the UK Financial Services Authority (FSA) in its Retail Distribution Review, which is targeted especially at IFAs. It will be important to ensure that the FSA aligns its definition with that in the recast MiFID. |
| | 2) Is it appropriate to include emission allowances and structured deposits and have they been included in an appropriate way? | No comment. |

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| | 3) Are any further adjustments needed to reflect the inclusion of custody and safekeeping as a core service? | The proposed rules governing 3rd country business could impact on the use of international custodians by APCIMS' firms. Although they are retail focused with an overwhelmingly retail client base, as investment firms they do not hold deposits and do not perform the lending, borrowing, or custodian functions of banks. The majority of them use companies like the Bank of New York (BONY) in London for the safekeeping of client assets. In the EU this is the London branch of the Luxembourg authorised firm. The question is whether under the new rules the BONY could, for example, hold in London 3rd country shares, such as Thai stock, invested in by our firms on behalf of retail clients, or whether this function would be forced to move to Thailand where the retail-owned assets might be less safe. If so then there should be some adjustment to allow holdings within the EU to continue, especially since there has been no reason to compel changes to the régime. |
| | 4) Is it appropriate to regulate third country access to EU markets and, if so, what principles should be followed and what precedents should inform the approach and why? | In APCIMS' view it is appropriate to regulate third country access but the approach proposed by the Commission is undifferentiated and too restrictive and risks damaging quite badly the EU's wholesale financial services markets in particular.<br><br>As an alternative we strongly support the exemptive third country régime approach proposed by the International Regulatory Strategy Group (IRSG) in answer to this question. We note in particular their comment on the importance of differentiating between third country access to retail investors, who need adequate and equivalent investor protection, and wholesale investors, many of whom routinely and easily need access to services provided from outside the EU.<br><br>There is no such differentiation in the Commission Proposal but, as a representative body of firms dealing almost uniquely with retail clients, we consider that on the issue of third country access, as on so many |

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| | | issues, the retail/wholesale distinction is vital to make for regulatory purposes. We consider that in amending the Commission text it will be very important for the European Parliament to take account of this point and to seek to implement the IRSG proposals as a better alternative to those in the Commission document.<br><br>In addition we think that care should be taken in dealing with the concept of 'equivalence'. This should not be addressed in a prescriptive or dogmatic manner but rather from the viewpoint of whether a third country régime shares comparable regulatory outcomes, standards and objectives to those of the EU. No two régimes are or can be identical in all respects and in the MiFID we should not be using language that suggests they might be. There has been international work on equivalence and the EU should use the guidelines adopted as a result of this rather than create new, overly-detailed definitions which may not work to the EU's advantage. |
| **Corporate governance** | 5) What changes, if any, are needed to the new requirements on corporate governance for investment firms and trading venues in Directive Articles 9 and 48 and for data service providers in Directive Article 65 to ensure that they are proportionate and effective, and why? | Clarification is required on whether the proposed limitations on Directorships in Paragraph 1(a) of Article 9 will also apply to those outside the financial services sector.<br><br>The restrictions on the number of non-executive directorships in Article 9.1(a)(i) and 9.1(a)(ii) - two when combined with an executive directorship and four when not - appears quite arbitrary. How was the figure of four arrived at for example? The Article does allow competent authorities to allow a higher combination of directorships. Given the diverse nature of businesses in different Member States, the relevant competent authority should also be permitted to set the minimum number of directorships allowed.<br><br>It is assumed that "geographical diversity" in Paragraph 3 of Article 9 refers to the desirability of having people from different parts of the world and of different national and ethnic backgrounds on the management body. |

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| | | It would be useful however if this could be made more explicit to help avoid the possibility of divergent policies between member states later.<br><br>Corporate Governance proposals in the MiFID must be aligned with those in the Capital Requirements Directive to avoid confusion and conflicting requirements being imposed on firms. Points which the MiFID should address in particular are:<br><br>• Small firms and proportionality: clear distinctions are needed between the governance requirements of larger institutions operating cross-border with wholesale market interests, especially where they carry systemic risks, and other non-systemic firms, especially with a retail focus, acting essentially within a national context and on the basis of local employment and operations. APCIMS' smallest firms are outside London and have 2 partners and 5 or 6 staff, yet they are required to be compliant with both MiFID and CRD. Corporate governance principles developed with larger firms in mind cannot apply in full to firms such as these. A proportionate approach is essential to accommodate the differences and the principle of proportionality explicitly with reference to corporate governance should be written into the Directive.<br><br>• Different types of firms: there is also an issue of firm structure. The Commission proposals appear directed towards the joint-stock kind of plc quoted firm that is organised as a company. In APCIMS we have also partnerships and LLP-type of businesses that are in the scope of the MiFID but for whom many of the standard corporate governance proposals are either difficult or impossible to implement. Needless to say, some of these are quite small so there is a double problem. The MiFID proposal should explicate more clearly to what kind of firm its governance proposals apply and if necessary what is expected of other types of firm. |

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| **Organisation of markets and trading** | 6) Is the Organised Trading Facility category appropriately defined and differentiated from other trading venues and from systematic internalisers in the proposal? If not, what changes are needed and why? | The limits to what organisations exactly the Commission is trying to capture with its OTF definition remain unclear as the drafting is very wide. Page 16 of the Regulation states that this new category is broadly defined so that now and in the future it should be able to capture all types of organised execution and arranging of trading which do not correspond to the functionalities or regulatory specifications of existing venues.<br><br>However there are certain exclusions that in the view of APCIMS are correct and which we believe should be maintained in the European Parliament's consideration and amendment of the Commission's draft Proposal. They are:<br><br>• UK Retail Service Providers (RSP) are excluded as the Regulation makes clear that an OTF should not be allowed to execute any transaction against his own proprietary capital, which an RSP does. RSPs are defined as "market makers" for the retail sector, which has a separate definition within MiFID. A short paper outlining the UK RSP model is annexed for information. Note that trades through an RSP are reported to a Regulated Market – usually the London Stock Exchange or Plus Markets – as 'on exchange' trades. Investors therefore receive the full protection of exchange rules to ensure, inter alia, prompt settlement and protection from counterparty default.<br><br>• Firms in the APCIMS' membership which are private client stockbrokers (PCS) are also excluded. Although they will occasionally conduct agency cross trades (where the same broker acts for both the buyer and seller) they will not be caught by the OTF definition as the clients, who are entirely retail, are not "able to interact in the system" as defined by the Commission.<br><br>We are content with the exclusion of the RSPs and PCSs from the OTF definition and would like to see these exclusions maintained in future texts |

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| | | of the Proposal. Our concern is that in drafting the definition so widely the Commission may inadvertently catch entities that are not engaging in relevant business, and it will be important for the EP to ensure that the drafting is precisely and appropriately targeted with the relevant exclusions retained. |
| | 7) How should OTC trading be defined? Will the proposals, including the new OTF category, lead to the channelling of trades which are currently OTC onto organised venues and, if so, which type of venue? | OTC trading should be defined as any trade that is not protected by the rules of a trading venue (RM, MTF or OTF). Bilateral trading that is concluded away from a venue's systems but that is brought under the rules of a venue should continue to be considered 'on exchange' as such trades are subject to specific market rules and regulations, thus offering superior protection to counterparties.<br><br>The proposed creation of the OTF venue type should capture Broker Crossing Networks which will therefore bring volume previously seen as being 'Off Exchange'/OTC into a venue, namely the Broker Crossing Network that has been reclassified as an OTF. |
| | 8) How appropriately do the specific requirements related to algorithmic trading, direct electronic access and co-location in Directive Articles 17, 19, 20 and 51 address the risks involved? | APCIMS' comments are confined to Article 17.<br><br>The APCIMS' membership comprises investment managers and stockbrokers whose clients are almost entirely retail investors. They are mainly based in the UK. This category of firm does not engage in algorithmic trading on behalf of their clients. APCIMS' firms therefore fall outside the scope of paragraphs 1-3 of Article 17.<br><br>There is however concern regarding paragraph 4 on the provision by an investment firm of direct electronic access to a trading venue. There are two points. First, the wording of this paragraph, which may catch APCIMS' firms in its scope, is ambiguous and misleading and needs to be amended. Second, retail agency brokers (ie the APCIMS membership) in the UK deal through Retail Service Providers or RSPs (see Question 6 above and Annex) and this system and its effects need to be taken into |

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| | | account. Attention is drawn below to the critical points.<br><br>On the drafting:<br><br>• "Direct Electronic Access" may need to be properly defined so it is clearly understood when the concept is being applied. Does it catch firms providing:<br>o direct access to the order book for clients?<br>o execution only services by telephone to clients?<br>o online trading facilities to clients?<br>Both firms and clients need to know which activities are covered by direct electronic access regulation. The Commission Proposal is opaque on this matter. The EP should clarify the situation.<br><br>• OTFs need to be clearly defined (see Qu. 6 above) so it is clear when access is to a trading venue and when it is not.<br><br>• For services that are caught the requirement is on the firm inter alia to ensure "a proper assessment and review of the suitability of persons using the service" before providing it. How does this requirement relate to the more normal regulatory approach in respect of retail investor access to markets, in which financial instruments and products are categorised as complex and non-complex, retail investors wishing to invest in the former are subject to an appropriateness test, and "suitability" is applied to the investment product or service, not to the client? In order to avoid confusion the Commission Proposal needs to be redrafted to determine clearly:<br>o what is meant by "suitability" in paragraph 4, and ideally to re-word the concept to avoid confusing it with the use of "suitability" in other contexts; |

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| | | ○ whether the "assessment and review of the suitability of persons" is required when trading complex products or all products;<br>○ that, if the assessment applies in the case of all products, it is different from the appropriateness test (which applies only to dealing in complex products) and must therefore comprise different elements;<br>○ what those elements are in that case, and what is the justification for adding a new test of this kind where none exists at present.<br><br>• It should be noted that 60% of UK retail trades are now conducted online (around 12-13 million trades annually) and the percentage may be higher in other EU member states. This activity has taken place in the framework of existing regulation and almost no problems have been reported. If online trading is to be caught by the definition of "direct electronic access" then the reasons for additional regulation should be made explicit when it does not appear to be justified by the circumstances. This has not been done so far in this case.<br><br>• Finally, if online trading and execution only broking by telephone are covered by the scope of direct electronic access, there should be some explanation of how any additional regulations in this area relate to the framework for execution only broking set out in Directive Article 25 of the Commission Proposal.<br><br>On the RSP issue, the key point is that this is a quote driven system that facilitates an appropriate environment for 'retail' separately from the order driven 'wholesale' environment available in the UK. The effect of this structural separation is to isolate retail business from wholesale in the sense that, unlike in the bancassurance model, activities undertaken |

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| | | specifically in the order driven wholesale market, such as algorithmic or HF trading, do not directly impact on retail business.<br><br>Clarification is also required in respect of Paragraph 5 of Article 17 which refers to investment firms acting as general clearing members. A General Clearing Member (GCM) is not defined in either MiFID or MiFIR. In the UK a GCM has a specific role as a member of a Clearing House and is permitted to clear its own transactions as well as those of clients.<br><br>• It would be helpful if Article 17, paragraph 5, could be redrafted to clarify the definition of a GCM and to make clear who and what is intended to be covered by this paragraph. |
| | 9) How appropriately do the requirements on resilience, contingency arrangements and business continuity arrangements in Directive Articles 18, 19, 20 and 51 address the risks involved? | Please see the answer to Qu. 6 on the need to clarify the definition of an OTF so that the impact if these sections on investment firms can be better determined. |
| | 10) How appropriate are the requirements for investment firms to keep records of all trades on own account as well as for execution of client orders, and why? | Most APCIMS firms are solely agency brokers and do not trade on their own account. We nevertheless consider that it is appropriate for investment firms to keep records of all trades for their own account wherever and whenever these occur. |
| | 11) What is your view of the requirement in Title V of the Regulation for specified derivatives to be traded on organised venues and are there any adjustments needed to make the | No comment. |

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| | requirement practical to apply? | |
| | 12) Will SME gain a better access to capital market through the introduction of an MTF SME growth market as foreseen in Article 35 of the Directive? | APCIMS notes that SME growth markets already exist in the EU and that it is unclear how the new definitions will affect access to them. In the ideal it should be for the market rather than legislators or regulators to determine whether there should be new such markets or enhancements to existing markets and their public profiles.<br><br>The UK's AIM market has been established since 1995 as an International market for smaller companies. Since MiFID it has been categorised as an MTF. It would appear that AIM would likely qualify as an SME growth market. Plus Markets also operate an MTF for the listing smaller companies which would likewise be categorised as an SME Growth Market.<br><br>The provisions of Article 35 appear to be sensible requirements for anybody intending to admit securities for public trading and therefore the setting of a consistent minimum standard across such venues is unlikely to create negative effects.<br><br>In the current period there is an increased importance attached to securing a favourable climate for funding the growth and development of SMEs. In this context APCIMS welcomes encouraging moves such as the proposals for the creation within the MTF category of a new sub-category of SME Growth Market. This will help to raise the visibility of such markets and produce a better environment for raising capital for Europe's entrepreneurs and growth companies.<br><br>APCIMS also welcomes the Directive's proposal to reclassify ordinary shares on SME markets as "non-complex". This will facilitate retail and |

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| | | professional investor involvement in SMEs. |
| | 13) Are the provisions on non-discriminatory access to market infrastructure and to benchmarks in Title VI sufficient to provide for effective competition between providers? If not, what else is needed and why? Do the proposals fit appropriately with EMIR? | No comment. |
| | 14) What is your view of the powers to impose position limits, alternative arrangements with equivalent effect or manage positions in relation to commodity derivatives or the underlying commodity? Are there any changes which could make the requirements easier to apply or less onerous in practice? Are there alternative approaches to protecting producers and consumers which could be considered as well or instead? | No comment. |
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| **Investor protection** | 15) Are the new requirements in Directive Article 24 on independent advice and on portfolio management sufficient to protect investors from conflicts of interest in the provision of such services? | APCIMS strongly supports the need to protect investors, especially retail investors, from the possibly adverse consequences of conflicts of interest in the provision of financial services. In this context we support the aims of Article 24 of the Commission Proposal but have a number of general and specific concerns with its scope and drafting which should be put right if investors are to be appropriately protected all round.<br><br>At a general level the Proposal as drafted prohibits commission payments and inducements in relation to firms designated as "independent", but makes no mention of such prohibitions in relation to "restricted" firms. As a result, firms stating they are in the restricted category will continue to be able to charge commission to product providers. Not only will this perpetuate the very conflict of interest that the Commission is trying to prevent, but we foresee at least two damaging market consequences:<br><br>• Clients will have to pay for independent advice but will receive restricted advice without charge since the adviser will be paid by commission; this will occasion a drift towards restricted advice especially by those least able to pay, who are among those of concern in the financial inclusion context; if restricted advice offers less choice and potentially inferior results to independent advice, the situation will arise in which those with less money get worse outcomes, which presumably both the Commission and Parliament wish to avoid;<br><br>• Clearly a movement of the above kind will lead to market distortion in which there is a small category of independent advice for the wealthy and a large category of restricted advice for others. This will lead to changes in the market structure for advice including a reduction in the numbers of firms providing independent advice. The ensuing reduction in competition may not be healthy for the retail investor community as a whole. |

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| | | We believe that the European Parliament will wish to investigate this situation and ensure that there is a level playing field in the regulatory treatment of independent and restricted advice for conflicts of interest.<br><br>More specifically we have concerns with the drafting of Article 24 at particular points. We deal with these below.<br><br>• The wording in Article 24.3 states<br><br>*....when investment advice is provided, information shall specify whether the advice is provided on an independent basis and whether it is based on a broad or on a more restricted analysis of the market and shall indicate whether the investment firm will provide the client with the on-going assessment of the suitability of the financial instruments recommended to clients,*<br><br>The drafting appears wrong. Advice is either independent or restricted depending in part on the breadth of view of the market that is taken. So the phrase *"and whether it is based"* should be deleted and the section altered to read *whether the advice is provided on an independent basis from a broad analysis of the market or is more restricted.*<br><br>• We are supportive of<br>o clients being made aware as to whether or not they will receive an ongoing assessment of the suitability of the financial instruments;<br>o independence being judged by reference to a sufficiently large number of financial instruments.<br>This should be in the context of the service that the firm and client agree together should be provided, which should be reflected in the drafting.<br><br>• Article 24.5(ii) states:<br><br>*... shall not accept or receive fees, commissions or any monetary* |

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| | | *benefits paid or provided by any third party or a person acting on behalf of a third party in relation to the provision of the service to clients.*<br><br>As drafted this leaves us unclear in some areas. For example, what would the position be if a lawyer paid the investment management fees on behalf of a trust? This shows that the definition of third party needs to exclude inter alia legal persons making or receiving payments on behalf of a client, and that there may be other similar exclusions that should be made.<br><br>• Article 24.6 states:<br><br>*When providing portfolio management the investment firm shall not accept or receive fees, commissions or any monetary benefits paid or provided by any third party or a person acting on behalf of a third party in relation to the provision of the service to clients.*<br><br>We believe the existing MiFID rules on inducements, at least in the UK, adequately address this issue. We are unclear why in the Commission Proposal there are specific requirements for managing portfolios and different requirements for managing portfolios and providing investment advice.<br><br>• Article 24.7 states:<br><br>*... When an investment service is offered together with another service or product as part of a package or as a condition for the same agreement or package, the investment firm shall inform the client whether it is possible to buy the different components separately and shall provide for a separate evidence of the costs* |

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| | | *and charges of each component.*<br><br>This is not clear on the criteria firms should use to determine when an element in their service provision is a separate component. There will as a result be significant variation between firms as to how this will be implemented in practice. The ensuing lack of consistency may cause regulators to set out criteria, although this may well increase variations, especially between member states, and have the unintended consequence of trying to impose on firms requirements that they cannot meet because they cannot divide their service offering in the manner envisaged. However, we assume that if a service is not available as different components then no further analysis will be required. The European Parliament should in our view seek to add to the drafting some clarity about what is to done here, including potentially allocating to ESMA the responsibility for determining relevant criteria and situations.<br><br>Please also see the Comment section at the end on Article 24. |
| | 16) How appropriate is the proposal in Directive Article 25 on which products are complex and which are non-complex products, and why? | APCIMS has the following comments on this question, reflecting drafting ambiguities or gaps in the Commission Proposal rather than any difference in principle:<br><br>• The product provider should be responsible for determining whether or not an instrument is complex or non complex, not the intermediary except in very specific situations noted below. The assumption in Article 25 appears however to be that the responsibility should fall to the intermediary and we consider that the draft should be amended to change this. The outcome of the product provider's determination should be clearly displayed in the product description. For certain |

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| | | types of instruments, such as very infrequently traded shares, the responsibility would fall on the intermediary firm.<br>• Article 25.2 requires an investment firm to assess whether a service or product is appropriate for the client. It is important not to confuse concepts that have become established in earlier regulatory work within the EU and this reference might be better written "is suitable for the client". As drafted the article risks mixing suitability and the appropriateness test, which are distinct ideas with the latter applying to people not products.<br>• Articles 25.3.(ii) and (iii) refer to the effects of the incorporation of a structure in a financial instrument which makes it difficult for the client to understand the risk involved. The determination as to whether or not an instrument is complex or non complex by reference to whether or not it is difficult for the client to understand the risk involved means that an instrument may be complex or non complex depending on the knowledge and experience of the client. Such an approach will create variable results and be very costly to implement. A definition which determines complexity by instrument rather than by client could be more efficiently administered and would be consistent with the approach in the rest of Article 25.<br>• It is also important in determining complexity and risk not to confuse the two: it may sometimes be hard to understand how a complex product is put together and how it works in the market, but such products may be inherently less risky than a non-complex product that a client may be permitted to purchase without an appropriateness test. The language in the Directive should be such as to ensure a clear distinction between the concepts of complexity and risk. |

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| | | • Article 25.5 states that:<br><br>*... The client must receive from the investment firm adequate reports on the service provided to its clients. These reports shall include periodic communications to clients, taking into* account *the type and the complexity of financial instruments involved and the nature of the service provided to the client and shall include, where applicable, the costs associated with the transactions and services undertaken on behalf of the client. When providing investment advice, the investment firm shall specify how the advice given meets the personal characteristics of the client.*<br><br>Our understanding is that firms must provide suitable advice but we are unclear what is meant by the phrase *personal characteristics of the client* and whether **t**his phrase is intend to convey a different obligation to that of suitability.<br><br>• In Article 6(b) we do not understand why *products* has replaced *financial instruments* in the drafting, nor the purpose of the amendment. We believe that the Parliament should change the draft or clarify the situation in its amendments.<br><br>• In general a key element in considerations of complex/non-complex instruments is the nature of the client in question. It is essential that the provisions from the existing MiFID implementing directive Article 36 remain to allow firms to assume that a professional client has the necessary experience and knowledge to understand relevant risks involved. |

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| | 17) What if any changes are needed to the scope of the best execution requirements in Directive Article 27 or to the supporting requirements on execution quality to ensure that best execution is achieved for clients without undue cost? | APCIMS has the following general and specific comments on this question:<br><br>General:<br><br>• The requirements around best execution need to incorporate an element of flexibility with regard to the description of how an order will be executed for the client.<br><br>• While order execution may be a simple and formulaic process in some cases, there are many examples where execution may be more complex and incorporate a number of execution styles and processes.<br><br>• It is therefore essential that the requirement to explicitly describe the way in which a clients order will be executed be amended to explain how a client order is *'likely'* to be executed. The overwhelming obligation to the client is to deal in their best interests. The requirement to follow a disclosed execution model should therefore be inferior to the responsibility owed to the client.<br><br>Specific:<br><br>• Article 27.4 states that:<br><br>*Member States shall require that investment firms provide appropriate information to their clients on their order execution policy. That information shall explain clearly, in sufficient detail and in a way that can be easily understood by clients, how orders will be executed by the firm for the client.*<br><br>This may lead to major expense for no benefit: an order execution policy can be complex and a detailed explanation is not necessarily able to be provided in a manner that can be easily understood by clients. |

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| | | Please see also the Comment section on Article 27.<br>• Article 27.5 states that:<br>*Member States shall require investment firms to summarize and make public on an annual basis, for each class of financial instruments, the top five execution venues where they executed client orders in the preceding year.*<br>It is unclear whether the top five execution venues should be determined by values of trades or numbers of trades. We would suggest that a minimum level for disclosure is set and the revised wording we would prefer is:<br>*...the top five execution venues where they executed client orders in the preceding year .<u>Where an execution venue within the top five represents less than 10% of total trades they need not be reported.</u>*<br>Many of our firms tend to deal in UK financial instruments using a limited number of venues. The costs of monitoring a large number of venues to determine which venue would fall in the fourth or fifth position outweighs any benefits from publishing this information. |
| | 18) Are the protections available to eligible counterparties, professional clients and retail clients appropriately differentiated? | APCIMS believes that the protections are appropriately differentiated. |
| | 19) Are any adjustments needed to the powers in the Regulation on product intervention to ensure appropriate protection of investors | In APCIMS' view, where possible prior to an intervention ESMA should be obliged to consult on that proposed intervention. If this is not possible there should be a consultation period during the first three month banning |

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| | and market integrity without unduly damaging financial markets? | period before it is renewed. Our main concern is that the scope of intervention may be to widely drawn. We are particularly concerned that products which are unsuitable for most clients, but suitable for high net worth clients with an appropriate risk appetite, may be unjustifiably banned for all clients.<br><br>It is essential that any powers conferred to a regulatory body have appropriate accountability and be subject to appropriate independent scrutiny. There should be some form of independent body empowered to oversee any appeal against a product intervention to ensure appropriate accountability and recourse for individuals and firms affected by an intervention.<br><br>Please see also the MiFIR Comment section under Product Intervention Powers |
| **Transparency** | 20) Are any adjustments needed to the pre-trade transparency requirements for shares, depositary receipts, ETFs, certificates and similar in Regulation Articles 3, 4 and 13 to make them workable in practice? If so what changes are needed and why? | No comment. |
| | 21) Are any changes needed to the pre-trade transparency requirements in Regulation Articles 7, 8, 17 for all organised trading venues for bonds, structured products, emission allowances and derivatives to ensure they are appropriate to the different instruments? Which instruments are the highest priority for the introduction of pre- | No comment. |

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| | trade transparency requirements and why? | |
| | 22) Are the pre-trade transparency requirements in Regulation Articles 7, 8 and 17 for trading venues for bonds, structured products, emission allowances and derivatives appropriate? How can there be appropriate calibration for each instrument? Will these proposals ensure the correct level of transparency? | No comment. |
| | 23) Are the envisaged waivers from pre-trade transparency requirements for trading venues appropriate and why? | The provisions of Articles 4 and 8 - 'Granting of waivers' - are important recognitions that a single model will not be appropriate for all trading venues and instruments. The recognition of the issues of market impact relating to large orders is very important for the maintenance of orderly markets and the protection of investors. |
| | 24) What is your view on the data service provider provisions (Articles 61 - 68 in MiFID), Consolidated Tape Provider (CTPs), Approved Reporting Mechanism (ARMs), Authorised Publication Authorities (APAs)? | APCIMS agrees that the provision of consolidated data of a high quality and at a reasonable cost is important for retail investors.<br><br>We believe that the organisational requirements for Consolidated Tape Providers, Approved Reporting Mechanisms and Authorised Publication Authorities need to be consistent across Member States to ensure that data provision does not migrate to those Member States with less onerous requirements.<br><br>We note that the Commission will be able to adopt delegated powers under Article 94 – Article 68 refers to Article 34 in error – concerning measures clarifying what constitutes "a reasonable commercial basis" to provide access to data and information. We welcome the Commission's interest in ensuing that such provision is done so on a cost-effective basis for both the |

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| | | providers and users. The Commission and Parliament will need to be careful however not to seek to set prices in what will be a commercial environment, particularly if the impact is to limit competition between providers. |
| | 25) What changes if any are needed to the post-trade transparency requirements by trading venues and investment firms to ensure that market participants can access timely, reliable information at reasonable cost, and that competent authorities receive the right data? | No comment |
| **Horizontal issues** | 26) How could better use be made of the European Supervisory Authorities, including the Joint Committee, in developing and implementing MiFID/MiFIR 2? | The ESAs and the Joint Committee must ensure that sufficient focus is given to developing and properly consulting on the technical standards for which they are responsible. These must be fit for purpose and consistent. Resources available to the ESAs must be appropriately aligned to their mandates; if this is not the case, and it is not at present clear that it is, there is the risk that technical standards will not be appropriate and that consultation periods will be inappropriately short. |
| | 27) Are any changes needed to the proposal to ensure that competent authorities can supervise the requirements effectively, efficiently and proportionately? | No changes are required. |
| | 28) What are the key interactions with other EU financial services legislation that need to be considered in developing MiFID/MiFIR 2? | There is significant overlap between MiFID/MiFIR and MAD/MAR, IMD, and parts of the UCITS Directives where client facing issues are concerned. There may well be overlaps beyond these of which APCIMS is not aware. |

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| | 29) Which, if any, interactions with similar requirements in major jurisdictions outside the EU need to be borne in mind and why? | All aspects of EU single market work, including on the MiFID, need to be considered in the context of the international marketplace of which Europe is a part. International political, economic, financial and market connections among others are all important to the EU and any potential isolation of the EU from these risks placing the European market at a comparative disadvantage. Policy makers should always have at the forefront of their minds the international standards of the G20, the Financial Stability Board, IOSCO, the BIS, the IAIS and other international bodies, while particular attention should as in the past continue to be given to US developments. |
| | 30) Is the sanctions regime foreseen in Articles 73-78 of the Directive effective, proportionate and dissuasive? | Yes. |
| | 31) Is there an appropriate balance between Level 1 and Level 2 measures within MIFID/MIFIR 2? | Broadly, yes, but much appears to have been left to Level 2 implementation. Consequently, firms face a long and uncertain lead time to the implementation of some technical standards. |
| **Detailed comments on specific articles of the draft Directive** | | |
| **Article number** | **Comments** | |
| Annex to Questionnaire response | Please see attached annex on the RSP model (see the answers to questions 6 and 8) | |

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| Article 4, old MiFID | In view of the proposed abolition of Article 4 of the former MiFID, the emphasis in the Explanatory Memorandum of the proposed new MiFID/MiFIR on the minimising of national discretions, and the advent of the single European rule book together with powers of the ESAs to enforce the consistent application of rules across the EU, will there be any ongoing possibility for national regulators to gold-plate the MiFID/MiFIR, even if they are minimum harmonisation directives? Will the European Parliament take steps to legislate against such gold-plating in the future? |
| Article 16 | In the UK the current rules governing the keeping of telephone recordings require this to be for a period of 6 months. Article 16 of the Directive Proposal increases the retention obligation to 3 years. The rationale for this is not given even though it is unclear from the UK experience that 6 months is inadequate. One consequence of the longer time period is that it will have an impact on storage capabilities and costs, even though in the retail sector covered by APCIMS there will almost certainly be no gain in terms of investor protection. So additional costs will be passed to the retail consumer for no clear reason.<br><br>In the light of this we recommend that the European Parliament in its assessment of the Proposal reconsiders the need for 3 years and redrafts the relevant part of Article 16 either:<br>• to shorten the time period, or<br>• to make the longer time period only applicable to the sections of the market operated by bigger firms more able to absorb longer retention periods, and in which the longer period will be beneficial in the pursuit of market abuse cases. |
| Article 17, paragraph 4 | On the issue of the Retail Service Provider (RSP) and Direct Electronic Access, it is important to recognise that the RSP model is a quote driven system that facilitates an appropriate environment for 'retail' trading separately from the order driven 'wholesale' trading environment available in the UK. The effect of this structural separation is to isolate retail business from wholesale in the sense that, unlike in the bancassurance model, activities undertaken specifically in the order driven wholesale market, such as algorithmic or HF trading, do not directly impact on retail business. |

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| Article 24 | An alternative solution to this article which the European Parliament might like to consider is that of forcing transparency on the commission/fee issue. In the retail sector the client does not at present in general know that the portfolio manager and independent financial adviser receive payments from each other in the form of, for example, trail or introducing commissions. The discrepancies between "independent" and "restricted" firms would be solved in this way as would the current differences between member states in their implementation of MiFID I. Retail clients are unlikely to be disturbed by the revelation of fee payments between firms provided they can be assured that their interests are being put first and their money is being invested as they wish. The terms of transparency set out and enforced by the regulator should ensure this. |
| Article 27 | The provision by firms of information to clients as part of helping them to understand the nature of choices being made, to make sure that firms are acting in their best interests, and to see that the processes for achieving best execution and other actions are also to the clients' advantage, is more difficult to implement effectively than it is to decide on in theory. There are, first, the well-known problems with clients. They frequently do not read the information or do not want it, in which case they may complain to the firm about receiving it. They may read and not understand the information, and spend lengthy periods asking the firm about it and why they have it, which can result in further confusion. Or they may become irritated that a firm cannot act immediately on a client's request because a piece if information must be sent to the client before an action can be taken, even though the client is not interested in it.<br><br>But there are, second, difficulties with the way business operates. In the UCITS IV case, for example, the requirement to provide the Key Investor Information Document, or KIID, to the client before undertaking an investment in an UCITS was made without regard to the business models of many firms and clients. A high proportion of UCITS are invested in as UCITS exchange traded funds, or ETFs, by clients requiring either execution only services (no advice) for on-exchange dealing on the spot via a telephone request, or by discretionary portfolio managers acting on behalf of clients, in which case they are entering the market regularly to get the client the best prices and outcomes.<br><br>In both these situations the requirement to provide the KIID prior to the deal has caused immense difficulties. In the first, execution only services have had to be held up while the KIID is provided. This has led to loss of immediacy in responding to client requirements and frequently to loss of best price for the client while the KIID provision takes place. In some cases potential deals have foundered altogether and the private investor has not made the investment. At present there is no solution to this problem and a well-functioning retail market with no evidence of difficulty has been abrogated and damaged to investor detriment by ill-thought through regulation. |

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| | In the second situation the UK regulator, the FSA, has had to seek a special dispensation from the European Commission to regard the discretionary manager as the investor. This has allowed the firm to receive the KIID from the UCITS ETF product provider and to undertake the trade on behalf of the retail client without providing him/her with the KIID. Without this dispensation the requirement for the discretionary manager to send a KIID to the end client each time a transaction was undertaken would have jammed the discretionary market altogether and probably brought it to a halt with catastrophic consequences for retail investors. But it is a hybrid solution only necessitated because the way the Directive is worded does not take account of market practice beneficial to the private investor.<br><br>It is clearly desirable not to repeat these kinds of errors in considering the information requirements in Article 27 – and indeed in the revised MiFID/MiFIR as a whole – and it is to be hoped that the European Parliament, when analysing the Commission Proposal, will be able to reflect in its redraft the need to accommodate existing business practices which work to the advantage of retail clients. |
| **Detailed comments on specific articles of the draft Regulation** | |
| **Article number** | **Comments** |
| Article 14 (2) | This section deals with 'Price improvement' and states that it will be permissible in 'Justified Cases'. This term requires definition as it is not in any way clear what would be interpreted as justification for dealing within the firm quote. |
| Article 15(b) | This cites the above mentioned Article and requires that investment firms comply with its conditions on price improvement. As stated above there are no conditions stated here so it is very unclear as to what the firm would have to comply with. |

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| Articles 21-23 MiFIR | Much of what is proposed in Title IV (Transaction Reporting) of the draft Regulation appears to be aimed at proprietary trading and algorithmic trading. The proposals will however also catch retail trades and involve significant costs for retail brokers and investment managers with very little evidence that it will benefit the relevant competent authorities. These costs will inevitably be borne by retail investors. The vast majority of retail trades are agency trades with a clear audit trail available to competent authorities where they need further information. For that reason if the specific requirements outlined in Articles 22 and 23 are to be introduced we believe that they should be aimed at those transactions that are undertaken by investment firms on their own account.<br><br>Article 22 (Obligation to maintain records) will require regulated markets, MTFs and OTFs to keep at the disposal of the competent authority for at least five years the relevant data relating to all orders (and not just executed trades). This will have a knock-on effect on those firms sending orders to those venues who may also need to maintain data about such unexecuted orders or send more details depending on the technical standards. Limit orders that fail to execute are one example. This is an additional requirement which we do not believe will provide the authorities with any meaningful additional information. There is also a data protection issue as to whether client information can be passed in respect of unexecuted orders.<br><br>Article 23 (Obligation to report transactions) will potentially allow ESMA to propose a unique client identifier across all firms rather than just within one firm. It is well known that there is no such unique code in the UK. We also understand that some Member States are already using a unique code (in most cases the Tax Identification Number) but are unable to pass any information to other Member States due to data protection constraints. There are also practical issues on how a charity or trust would be identified and whether individual trustees would need to have their own unique client identifier which would be consistent with an identifier if they had their own trading account.<br><br>Paragraph 3 of Article 23 would also require a transaction report to include a designation to identify the persons within the investment firm responsible for the investment decision and the execution of the transaction. Investment firms often have teams that identify investment opportunities whereas other individuals make the decision to invest for certain clients. It will not always be clear who therefore is ultimately responsible for taking the investment decision. We question what use this additional information will provide. For execution-only trades for retail clients, of which 80 per cent are now online in the UK, there is no individual in the investment firms responsible for the execution of that trade.<br><br>The drafting of Paragraph 4 is unclear. It appears to require investment firms that transmit orders (effectively portfolio |

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| | managers) to provide relevant information to the executing broker or to report that information direct to the relevant competent authority. The reference to "also" in the penultimate line appears to require both actions. This will lead to double-reporting which the Regulation clearly states should be avoided for the purposes of cost and efficiency. This may not have been the intention and merely be a result of unclear wording.<br><br>Paragraph 8(c) refers to ESMA developing draft regulatory standards which will include "the way in which the transaction was executed". It is unclear to what this refers although it may be a reference to the concept of "riskless principal" trade which was introduced in an earlier consultation on transaction reporting.<br><br>In conclusion we believe that the section on transaction reporting needs to be more clearly targeted at where the Commission and ESMA believe the risk of market abuse is most likely. We would argue that this is not by retail investors via retail investment firms. Where firms are required to have information we believe that it would be more cost-effective and efficient if it was held by the firm and made available to the competent authority on request. |
| Product Intervention Powers (Question 19) | The accountability and product availability points in our answer to Question 19 are important and should be taken into account in further work on the Commission Proposal. There is however another issue to consider in relation to intervention by regulators in the retail financial services market. In the recent Keydata case in the UK the Financial Services Authority (FSA) was aware of concerns in relation to Keydata at a relatively early stage but placed the firm into administration some years later.<br><br>The details of this case can be found at:<br>http://www.google.com/url?q=http://www.fsa.gov.uk/pages/consumerinformation/firmnews/2010/keydata_faq.shtml&sa=U&ei=YfwWT7KyBMaesAb55fVI&ved=0CAQQFjAA&client=internal-uds-cse&usg=AFQjCNEX0W9G4ogxMI3fzC4PvK2yPbqKaQ<br><br>The result of the intervention timing was that considerable additional costs were incurred by the industry to compensate |

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| | investors over and above what would have been the case had the regulatory intervention occurred earlier. The question arises as to whether the proposed MiFIR product intervention powers would allow ESMA to intervene in relevant cases in a manner and at a time that would limit the compensation costs in any one instance to manageable proportions. APCIMS would support a suitably drafted text with appropriate caveats and limitations that would permit this in particular circumstances. In our view the European Parliament should carefully examine this issue in its consideration of the Commission Proposal. |

**APCIMS**
**13 January 2012**

**ANNEX**

**THE RETAIL SERVICE PROVIDER (RSP) MODEL**

**Description of the RSP model**

The RSP forms the backbone of the UK retail stock broking market, its primary role being to provide electronic quotation and dealing facilities to retail stockbrokers and other investment firms.

In practice a stockbroker will electronically connect to a number of competing RSP firms, requesting the RSPs' most competitive quote for their client's order. The brokers will select the most competitive price offered allowing their clients to benefit from price competition between RSPs and to deliver best execution to their clients.

One key element of the model is the price calculation mechanism employed by the RSP systems. Market Makers invest significant capital in the development of technology to allow the most competitive prices to be formulated and hence the most order flows to be won. RSP systems consolidate price data from the market data feeds of the regulated markets and MTFs (the "Exchanges") in order to build a consolidated best

bid/offer across those venues. The RSPs' investment in consolidation therefore provides significant benefits for the retail investor while reducing the risks associated and successfully delivering best execution.

Some key benefits of the RSP model are detailed below:

- Self Determination
    - The RSP model allows retail clients to access and interact with markets at their own discretion. The UK retail client has benefitted from the development of the RSP system which has significantly reduced the cost of trading and opened up equity trading to a wider audience.
    - This deeper pool of capital has assisted listed companies, particularly those admitted to small cap markets such as Aim and Plus Markets, to weather the financial crisis. These markets have provided access to much needed funding to create economic growth and jobs while offering returns to investors. This has been of critical importance given the widespread contraction in bank lending since the economic crisis and the smaller returns available to savers.
- Reduction in the cost of trading
    - Single execution means no clearing fees and a single settlement[1].
- Protects the investor
    - While executed away from the exchange systems, trades are reported to an Exchange as 'on exchange' trades. Investors therefore receive the full protection of exchange rules to ensure, inter alia, prompt settlement and protection from counterparty default.
- Pre-trade transparency
    - Registered market makers are required to make firm quotes in minimum sizes determined by an Exchange throughout the trading day. The RSP references these prices and hence cannot be considered a 'Dark Pool'.

[1] Cost is a key factor in obtaining best execution of a Retail Client order.

- Investors are shown the full terms of trade (price, quantity, settlement date) prior to committing to the trade. This allows client certainty that their trade has executed at a known price. This is not possible through other execution methods and offers the best element of a limit order (price certainty) and an 'At Best' order (immediacy).

- Prices provided by RSPs represent the tightest spreads available in a security by referencing multiple order books/market maker quotes in order to match the markets' best price.[2]

- Highly competitive

  - Up to 30 market makers may be competing for each order. In order to win the client's order the market maker will apply 'price improvement' to enhance further the price offered to the client.

  - Under the RSP model the market maker does not charge for access to RSP prices and no commissions are paid to RSPs for execution.

- Highly efficient

  - RSPs run highly automated systems: a very high percentage of all executions are processed and settled on a straight through processing (STP) basis which significantly improves the likelihood of settlement.[3]

  - STP also significantly reduces the operational costs of the RSP and broker, thus allowing low dealing costs and a very competitive broker market; best execution for retail clients should be considered against the full cost of a trade rather than just its price and the RSP model significantly improves this area to the benefit of the retail client.

  - The RSPs' price consolidation allows a single point for clients to access the prices available across numerous venues.

[2] Price is a key factor in obtaining best execution of a Retail Client order.
[3] Likelihood of settlement is a key factor for the best execution of a Retail Client order.

- Electronic trading via the internet allows investors instant access to the market; thus investors can easily take advantage of the market situation or dispose of existing positions.[4]

- Guaranteed execution: once a quote is received by the client, the price is held firm to allow the client to decide.[5]

- Highly Liquid

  - In addition to price improvement, market makers will offer liquidity improvement, providing more liquidity at current market prices than are available on the regulated market and MTF order books.[6]

As the above description makes clear, the UK's retail execution model for equity business is a well developed, competitive system that is highly efficient and delivers significant benefits to its end client, the retail investor. The service delivers against all of the execution factors determined by the Markets in Financial Instruments Directive ("MiFID") as the footnote references demonstrate. The model is highly effective and offers many advantages over the retail execution models prevalent in other markets, including those found elsewhere in the EU.

**APCIMS**
October 2011

[4] Speed is a key factor in obtaining best execution of a Retail Client order.
[5] Likelihood of execution is a key factor for the best execution of a Retail Client order.
[6] Likelihood of execution is a key factor for the best execution of a Retail Client order.