

## Review of the Markets in Financial Instruments Directive

### Which? response to the 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](mailto:econ-secretariat@europarl.europa.eu) by **13 January 2012**.

**Which?** is an independent, not-for-profit consumer organisation with around 1 UK million members and is the largest consumer organisation in Europe. We have a long and successful track record of campaigning for improvements in financial consumer protection.

Theme	Question	Answers
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?	We have concerns about the exemption for the administration of employee participation schemes. Share offers to employees can prove a risky investment as the case of Enron has shown where employees were encouraged to buy Enron shares for their own pension plans, had a company pension plan with a significant exposure to Enron shares and obviously relied on Enron for their salary <sup>1</sup> . These staff members lost their whole livelihoods when Enron went into administration. Such a high exposure to just one company is something that should not be

<sup>1</sup> <http://fpc.state.gov/documents/organization/9102.pdf>

		<p>recommended to a retail investor. Companies with share-saving schemes can exercise significant pressure on staff to take up share-offers and refusal to do so could be seen as a lack of dedication to one's employer. However, more junior employees are very often inexperienced investors and would find it difficult to assess the suitability of the investment.</p> <p>We therefore support the removal of the exemption for in article 2, paragraph 1 e and the amendment of paragraph 1 f to reflect this position.</p>
	2) Is it appropriate to include emission allowances and structured deposits and have they been included in an appropriate way?	<p>In our view one of the key reforms to the Mifid regime that will benefit consumers is the proposed inclusion of structured deposits. Our research has found problems with structured deposits, which despite being relatively complex products are not subject to MIFID or the reforms currently being undertaken in the UK as part of the FSA's Retail Distribution Review. We see significant risk that if this is not amended then more firms in the UK will move towards selling structured deposits to evade the requirements. This research included a recent mystery shopping exercise<sup>2</sup>. Our research supports our views that the way structured deposits are being sold at the moment has the potential to cause significant consumer detriment. Many of these products present poor value<sup>3</sup> and we have seen several cases where the marketing material was misleading.</p> <p>We also attach a letter from Which? to Mr Martin Wheatley, Managing Director of the Conduct Business Unit at the FSA which sets out our concerns regarding sales of investment products, including structured products by high-street banks. This letter follows our mystery shopping investigation referenced in footnote 2.</p>
	3) Are any further adjustments needed to	No comment

<sup>2</sup> Which? magazine December 2011: Investment Advice on the high street.

<sup>3</sup> Which? Money magazine December 2010: Investments that don't fit the bill.

	reflect the inclusion of custody and safekeeping as a core service?	
	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?	No comment
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?	We are supportive of the changes proposed in articles 9 and 48. The UK regulator, the FSA has recently issued a number of fines to firms for failings in investment sales. The cases highlighted investment firms' shortcomings with regard to the procedures governing investment sales <sup>4</sup> .
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?	No comment
	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	No comment

<sup>4</sup> In January 2011 the FSA fined Barclays £7.7 million for investment advice failings. In October 2011, the FSA fined Credit Suisse £5.95 million for failings in relation to sales by its private bank of structured capital at risk products. In November 2011 the regulator fined Coutts & Company £6.3 million in connection with the sale of the AIG enhanced variable rate fund.

	of venue?	
	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?	No comment
	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?	No comment
	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?	The record keeping requirements in the Directive are not suited to investments with a long maturation periods where investors may only become aware of problems with the product many years after the advice and sale took place. This is evidenced by the problems with mortgage endowment products in the UK, where in some cases problems only became evident more than a decade after the sale took place. We therefore suggest that the record keeping period is extended to cover the investment period plus one additional year. We are also in favour of the harmonisation of telephone and electronic recording in cases where the contact with the consumer leads or could lead to giving personal recommendations (financial advice) or collecting orders.
	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 requirement practical to apply?	No comment
	12) Will SME gain a better access to capital market through the introduction of an	No comment

	MTF SME growth market as foreseen in Article 35 of the Directive?	
	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
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	In our view, the proposals do not go far enough. The definition of independence should follow the one which will be applied in the UK when the retail distribution review is implemented. The text should therefore be amended to read as follows:  Article 24, paragraph 5.5 "When the investment firm informs the client that

	services?	<p>investment advice is provided on an independent basis, the firm ÷</p> <p><b>(i) shall carry out a comprehensive and fair analysis of the relevant market and provide advice which is unbiased and unrestricted.<sup>5</sup></b></p> <p>In addition, we support a ban on inducements for all investment advice services, including those provided by all sorts of restricted advice (advice that is based on a less than independent analysis of the market for products and services), The key principle should be that product providers should play no role in determining the remuneration of the investment adviser and should be prohibited from paying commission or providing any other type of service which might influence the advice provided by the intermediary. We have strongly supported proposals by the FSA to introduce these requirements in the UK as part of the Retail Distribution Review.</p> <p>The evidence from the UK is that merely disclosing inducements (but allowing them to continue) does not lead to the appropriate degree of consumer protection.<sup>6</sup></p>
	16) How appropriate is the proposal in Directive Article 25 on which products are complex and which are non-complex products, and why?	We are supportive of the exclusion structured UCITS from the non-complex products category. However, the definition set out in the Directive is too restrictive as products like synthetic ETFs could fall outside the definition. We have carried out product analysis which underlines the complexity of synthetic ETFs <sup>7</sup>
	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	No comment

<sup>5</sup> See FSA publication PS 10/06 Distribution of Retail Investments: Delivering the Retail Distribution Review, March 2010

<sup>6</sup> [http://www.fsa.gov.uk/pubs/other/CRAreport\\_menu.pdf](http://www.fsa.gov.uk/pubs/other/CRAreport_menu.pdf)

<sup>7</sup> Which? Money magazine May 2011: Getting on the right track.

	execution quality to ensure that best execution is achieved for clients without undue cost?	
	18) Are the protections available to eligible counterparties, professional clients and retail clients appropriately differentiated?	No comment
	19) Are any adjustments needed to the powers in the Regulation on product intervention to ensure appropriate protection of investors and market integrity without unduly damaging financial markets?	<p>In many markets, competition provides an effective force in shaping the products on offer and ensuring they meet consumers' needs. However, effective competition relies on consumers being able to make informed choices, based on an ability to understand the characteristics and costs of products and to compare competing products. This should cause firms which offer poor value and poor quality products to lose business at the expense of their competitors. However, this is frequently not the case in the financial services sector, where consumers' ability to make informed choices are hindered by a combination of their lack of financial capability, product complexity, incomplete or unclear contracts, the length of time between the purchase of a product and discovering whether it has worked and a lack of transparency in the design and marketing of financial products.</p> <p>We believe that ESMA and national authorities need to be given the necessary powers to enable them to make use of the role that product intervention can play in addressing conflicts of interest, disciplining markets and aligning the interests of producers with consumers. In the UK, we have welcomed the intention for the new financial services regulator, the FCA, to be able to "make rules to place requirements on products or product features; mandate minimum product standards; or restrict the sale of a product to a certain class of consumers".</p> <p>Greater product intervention should have substantial benefits for firms as well as consumers. By tackling detriment at an earlier stage it will prevent firms incurring substantial redress costs and the associated administration expenses from redress</p>

		<p>and complaints processes.</p> <p>Wherever possible the regulator should exercise product intervention in a way which promotes effective competition. The regulator should explicitly state that it does not measure competition by counting the number of different products available, but by ensuring that consumers can compare and contrast products and providers and switch to ones which offer better value and quality.</p>
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-trade transparency requirements and why?	No comment
	22) Are the pre-trade transparency requirements in Regulation Articles 7, 8	No comment



	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?	
	23) Are the envisaged waivers from pre-trade transparency requirements for trading venues appropriate and why?	No comment
	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)?	No comment
	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?	No comment
	27) Are any changes needed to the proposal	No comment

	to ensure that competent authorities can supervise the requirements effectively, efficiently and proportionately?	
	28) What are the key interactions with other EU financial services legislation that need to be considered in developing MiFID/MiFIR 2?	No comment
	29) Which, if any, interactions with similar requirements in major jurisdictions outside the EU need to be borne in mind and why?	No comment
	30) Is the sanctions regime foreseen in Articles 73-78 of the Directive effective, proportionate and dissuasive?	<p>We are very supportive of the enhanced sanctioning regime proposed in the Directive. We believe that fines need to be of a significant magnitude to act as an effective deterrent. Fines need to be high enough to prevent rewards for errant behaviour. If a firm benefits significantly from misselling and the fine is insignificant in relationship to the revenue generated by the misselling then the fine will have no impact.</p> <p>Fines can also be used as an indicator of the failure to treat customers fairly and therefore could be used in assessing internal remuneration strategies or trigger more intrusive regulation.</p> <p>Damage to individual firms' reputation by publication of misselling practices is insufficient to discipline the market. Fines and sanctions are necessary to back up the regulatory regime.</p>
	31) Is there an appropriate balance between Level 1 and Level 2 measures within MIFID/MIFIR 2?	In our view there are several areas where too much is currently left to Level 2 measures within MiFID especially around the issue of avoidance of conflict of interest.

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