

# CONFLICT OF INTEREST IN PROVIDING INVESTMENT SERVICES

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# Overview

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- EU DIRECTIVE 93/22 ISD
- EU DIRECTIVE 2004/39 MIFID
- CESR GUIDELINES
- ESC WORKING DOCUMENT 17/2005
- INDUSTRY DEBATE

# EU Directive 93/22 - ISD

## (Articles 10 - 11)

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**Home Member State had to adopt**

- **ORGANISATIONAL REQUIREMENTS:**

**Banks and Investment firms are to be organized so as to minimize the risk of clients' interests being prejudiced by conflicts of interest**

**Host Member State had to supervise**

- **RULES OF CONDUCT:**

**Intermediaries shall try to avoid conflicts of interests otherwise ensure fair treatment**

# EU Directive 2004/39 - MIFID (Articles 13 and 18)

**Home Member State shall adopt (by April 2006)**

## ■ ORGANISATIONAL REQUIREMENTS:

- ✓ Banks and Investment firms shall maintain effective organisational and administrative arrangements to prevent conflicts of interest from adversely affecting client's interests

## ■ RULES OF CONDUCT

(Member States / UE Commission implementing measures):

- ✓ identification of conflicts of interest (including "linked persons") arising in *investment* or *ancillary* services
- ✓ clear disclosure to clients (if organisational arrangements cannot avoid, with reasonable confidence, risks of damage to client's interests)

# CESR Guidelines - January 2005

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## ■ CONFLICT POLICY

- ✓ includes at least certain conflicts of interest situations (generic examples)
- ✓ tailored organisational measures

## ■ CRUCIAL AREAS

- ✓ Proprietary trading
- ✓ Portfolio management
- ✓ Corporate finance, including underwriting and selling
- ✓ Inducements

## **ESC Working Document - September 2005** **(esc/17/2005 rev.3 - Article 21)**

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- **CONFLICT POLICY shall as a minimum:**
- ✓ Identify circumstances entailing a material risk of damage to the interests of a client
- ✓ Specify procedures and measures to manage situations that could cause damage to clients' interests
- ✓ Be set out in writing
- ✓ Be appropriate to the size, nature, complexity of the business
- ✓ Manage conflicts arising at a group level

# ESC Working Document - September 2005

## Art.21

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- Procedures and measures
  - ✓ adequate degree of independence for different business
  - ✓ to prevent or control the exchange of information
  - ✓ separate supervision
  - ✓ no direct linkages for remuneration
  - ✓ structures to prevent inappropriate influence
  - ✓ structures to prevent simultaneous or sequential involvement in different services
  - ✓ additional or alternative measures if the above ones do not ensure independence among business activities involving conflicts of interest.

# ESC Working Document - September 2005

## Art.20

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- **CRITERIA FOR DETERMINING CONFLICTS OF INTEREST WHOSE EXISTENCE MAY DAMAGE CLIENTS' INTERESTS**  
(only apply where an investment service is provided):
  - ✓ making a financial gain or avoiding a financial loss at the expense of the client [other than the commission or fee for the service]
  - ✓ having an interest in the outcome of a service which is distinct from the client's interest in that outcome
  - ✓ carrying on the same business as the client
  - ✓ having incentives to favour the interest of another client or receiving inducements in relation to services provided to the client (monies, goods or services)



# INDUSTRY DEBATE

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- In developing the process at European regulatory level could be appropriate:
  - ✓ A general preamble (“different interests” and “material risk of damaging client’s interest”) and
  - ✓ An effort in identifying more specific kinds of situations where presumptions may apply

- **Proposal:**

- ✓ to conduct a general check on relevant combinations of activities, such as different investment and ancillary services, issuing of financial instruments, credit exposure, shareholding ownership, insurance.
- ✓ to consider examples of measures appropriate to minimize the risk of conflict and to clear civil legal risk