CONFLICT OF INTEREST IN PROVIDING INVESTMENT SERVICES

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Overview

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