TISA Response to CP16/29
MiFID II Implementation
Consultation Paper III

January 2017

About TISA

TISA is a not-for-profit membership association operating within the financial services industry. The focus of our recommendations and actions is improved outcomes for consumers and UK plc with this approach leading to a stronger UK financial services industry.

TISA's growing membership comprises over 150 firms involved in the supply and distribution of savings and investment products and services. These members represent many different sectors of the financial services industry, including asset managers, insurance companies, fund managers, distributors, building societies, investment managers, third party administrators, consultants and advisers, software providers, financial advisers, pension providers, banks and stockbrokers.

TISA has a successful track record in working cooperatively with government, regulators, HMT, DWP and HMRC to improve the performance of the industry and the outcomes for the public. Effective policy and regulation and the creation of efficient industry infrastructure continues to be the major focus for our members. TISA is unique in that it represents the entire financial services industry, incorporating cross-sector policy, industry and technical expertise. Whilst we maintain a solid partnership with government, the regulators and wider industry, we remain independent and develop neutral views and opinions. This impartiality is reflected in our ability to drive development projects which improve industry performance and consumer outcomes, putting us in the unique position of being able to constantly challenge the status quo to bring about material improvement.

Q1: Do you have comments on the general issues raised in this overview, such as: the application of MiFID conduct rules to non-MiFID business; our approach to applying COBS rules to firms selling and advising on structured deposits; and our approach to the structure of COBS?

We agree with the proposal to defer consideration of applying MiFID II Conduct rules to insurance-based investment business and pensions. We agree that it is sensible in principle to have similar rules for products and services that are economically similar, but that it is better to wait to see how the IDD implementing measures are finalised, before making rules in this area. We are glad that the concerns we raised in our response to DP13/3 about appropriateness tests in this area have been taken into account.

We think the proposed approach to applying COBS rules to firms selling and advising on structured deposits is sensible, and reflects our comments on DP15/3.

The approach to the structure of COBS seems acceptable.

In general terms, we would prefer that key articles in the Directive are spelt out or explained in the text of the CP, and later in the rules, as this makes commenting easier and simplifies reading of the rules. An example is the frequent reference to Article 3 firms. It would have been very helpful to have a read out of the text (once) and an explanation of what it means early on in the CP, or put it in the glossary, rather than requiring respondents to refer to the text of the Directive, and then puzzle out what, precisely, is the Directive means.

Conduct of Business, including adviser charging

The relevant sections of the CP to the following questions are 2.16, which summarises the proposals, and 2.44 to 2.46 inclusive, which discuss the implications for firms. For ease of reading these are set out below

***2.16** In broad terms, the proposals we are making in this paper involve:*

- *separating our core inducement rules for MiFID, equivalent third country and Article 3 firm (optional exemption) business (into a new COBS 2.3A) from other non-MiFID designated investment business (in COBS 2.3) in light of our current position on the IDD implementing measures discussed in Chapter 1*
- *retaining our existing domestic adviser charging rules in COBS 6.1A and 6.1B, and transposing MiFID II's new inducement bans into the new COBS 2.3A*
- *for firms providing independent investment advice and portfolio management services to professional clients, transposing (but not extending) MiFID II's inducements ban*
- *for firms providing investment advice and portfolio management services to retail clients, extending MiFID II's inducement ban in three ways:*
  - *firstly, so that it extends to restricted advice as well as independent advice*
  - *secondly, to prohibit the acceptance of commission and benefits rather than their acceptance and retention (ie to ban rebating of inducements to retail clients), and*
  - *thirdly, to amend the adviser charging rules by applying the ban to the business of providing advice rather than only to inducements provided in relation to the provision of a particular personal recommendation to a client13*
- *subjecting Article 3 firms to the same requirements in relation to inducements as MiFID firms*

Implications for firms
Independent investment advice
***2.44** Under our proposals, we will apply the MiFID II rules (extended to ban rebating) to firms offering either independent or restricted advice to retail clients. We propose amending the adviser charging rules to apply the MiFID II provisions relating to minor non-monetary benefits to business within the scope of these rules. We also plan to clarify that the commission ban in COBS 6.1A/6.1B should be understood as applying to the firm's wider business of providing advice, so that an activity does not need to relate directly to the provision of a personal recommendation for these provisions to apply. We do not expect there to be significant impact on firms that comply with our current rules and guidance on this.*
***2.45** The MiFID II rules apply equally to retail and to professional clients. For professional clients, we propose transposing MiFID II into our Handbook. This is likely to have some impact on firms that currently provide independent advice to professional clients, thereby restricting the types of payments they are able to accept from third parties in relation to independent advice.*
Portfolio management
***2.46** We propose that firms that manage portfolios can still accept fees, commissions or monetary benefits in relation to services provided to professional clients, provided they are rebated to the client; but that they should not be able to accept and rebate benefits in relation to retail clients. Non-monetary benefits may not be accepted, unless they are minor or constitute research that is received in line with Article 13 of MiFID II delegated directive.*

Q2: Do you agree with our proposal to apply the MiFID II inducement rules for independent advice to all advice provided to retail clients? If not, please give reasons why, including evidence as to why, in your view, the costs of such an approach would outweigh benefits.

Yes

Q3: Do you agree with our proposal to ban firms providing advice or portfolio management services to retail clients from receiving and rebating monetary benefits to such clients? If not, please give reasons why, including evidence as to why, in your view, the costs of such an approach would outweigh benefits.

Yes

Q4: Do you consider that the ban on receiving and rebating monetary benefits to clients should also apply to professional clients? If so, please explain why and provide cost-benefit data. If not, please give reasons why.

We strongly support the concept that portfolio managers should be free to negotiate rebates etc. on behalf of professional clients as long as full rebates are made to those clients. The removal of that possibility would hamper significantly the ability of fund managers to negotiate reduced management charges in respect of funds of which they invest in on behalf of those clients as we believe that the appetite of funds group to issue a potentially significant number of new share classes would be very limited given the considerable administrative work involved. We believe this would be a particularly significant issue for managers who run authorised collective investment schemes and who negotiate rebates on behalf of those funds.

Managers of collective investment schemes reinvest rebate payments received directly into their collective investment schemes as an enhancement benefit for all end clients. As these rebates accrue on a daily basis, there is not an issue of one client being treated more favourably than another (i.e. a client exiting from the scheme) in between rebate payments being received. All clients receive full market entitlement for their holdings in the collective investment scheme.

Q5: Do you agree that we should apply MiFID II's requirements in relation to inducements to Article 3 firms? If not, please explain why, and also provide cost benefit data to support your explanation.

No. We do not consider that where the Directive does not impose an obligation that the FCA should then impose one anyway.

Q6: Do you agree with our proposal to extend the MiFID II limitation on non-monetary benefits to the wider business of providing advice in respect of RIPs? If not, please give reasons why.

Yes.

Q7: Do you think we should extend the MiFID limitation on non-monetary benefits to the wider business of providing advice for all MiFID products, and not just RIPs? If so, please explain why and provide cost benefit data.

Yes.

Q8: Do you agree with our proposal not to subject advice on structured deposits to our existing RDR adviser charging rules and, instead, to apply only the MiFID II inducement requirements to such business? If not, please give reasons why.

Yes.

Inducements and research

The relevant sections of the CP to the following questions are 3.16 to 3.19, which summarise the proposals, 3.20 to 3.29 inclusive (Application to MiFID investment firms and firms providing investment advice), 3.30 to 3.34 inclusive (Application to firms carrying out collective portfolio management (CPM)), and 3.35 and 3.36, which discuss the implications for firms. For ease of reading, sections 3.35 and 3.36 are set out below.

Implications for firms
3.35 *In considering MiFID II reforms and our implementation approach, it is important for firms to consider the key principles and outcomes these changes are designed to achieve, which are to ensure:*

- *investment firms account for third party research as a fixed, predictable cost, not linked to execution costs or charges or subsidised through other services*
- *research becomes a core management cost or is fully transparent to underlying investors, removing the inducement and conflict of interest risk for firms*
- *a transparent, priced research market emerges where recipients and providers establish upfront pricing based on agreements linked to the quality and quantity of goods and services to be supplied, and the expected benefit to investors*

3.36 *MiFID portfolio managers, independent advisors and collective portfolio managers will need to change their policies, systems and controls if they currently receive research from third parties relating to these services to clients, and they wish to continue to receive it. They will need to make a commercial decision about the approach they take to acquire third party research from 3 January 2018. If they choose to apply a research charge to their clients and use a research payment account (RPA), they will need to ensure their internal process and controls can meet the relevant requirements in Article 13 MIFID II delegated directive (and replicated in our COBS Handbook). If they choose to pay for research directly, they will need to be able to evidence this and show that it is not reflected in any execution costs and charges or other fees paid to brokers.*

Q9: Do you agree with our approach to transpose the MiFID II proposals for the receipt of research linked to the new MiFID II inducement rules as a new COBS 2.3B? If not, please state why and provide any suggestions for an alternative approach.

Yes.

Q10: Do you agree with our approach to extending the research and inducements requirements to firms carrying out collective portfolio management activity? If not, please give reasons why.

Yes.

Q11: Do you agree with proposals to retain some guidance provisions from the existing COBS 11.6 in the new COBS 2.3B section, where they continue to be relevant under the new proposals? If not, please give reasons why.

Yes.

Q12: Do you have any views on areas where we have proposed new guidance provisions to clarify our interpretation of steps firms could take to ensure compliance with the new inducements and research proposals and the detail of the proposals? If not, please give reasons why and any alternative suggestions.

No comment.

Q13: Do you have any views on whether further guidance provisions are needed to clarify other aspects of the new inducements and research proposals and how firms should interpret and implement changes to comply with these provisions? If so, please detail specific aspects on which you think FCA guidance is desirable.

No comment.

Q14: Should we consider any modifications to the requirements linked to the use of RPAs under the inducements and research provisions for full scope UK AIFMs of internally managed AIFs? If so, please provide details on what modifications we should consider and why.

No comment.

Q15: Should we apply the new MiFID II inducements standards to firms carrying out non-discretionary portfolio management activity (as defined in our Handbook glossary), including where they receive third party research, in the same way as for other types of portfolio management? Please provide evidence to support your views.

Could you clarify what you mean and the implications for customers and firms?

Client categorisation

TISA will not be commenting on these questions. The proposals do seem sensible, however.

Q16: Do you agree with our approach to revise the quantitative thresholds as part of the opt-up criteria for local authorities by introducing a mandatory portfolio size requirement of £15m? If not, what do you believe is the appropriate minimum portfolio size requirement, and why?

Q17: Do you agree with our approach to extend these proposals to non-MiFID scope business? If not, please give reasons why.

Disclosure requirements

A summary of the key paragraphs and proposals from the CP are reproduced below.

5.11 Unless the firm is an Article 3 firm carrying on MiFID-scope business, we do not propose to apply the effect of the new or revised MiFID II requirements to firms doing non-MiFID business. However, existing domestic requirements regarding treating customers fairly, post-sale reporting and record-keeping will continue to apply to firms doing non-MiFID business.

5.14 When considering the MiFID II disclosure provisions, following a cost benefit analysis, and pending finalisation of the IDD implementing measures, we sought to avoid applying these provisions in full to firms carrying on non-MiFID business. So, given our current proposals, firms carrying on non-MiFID business should not be subject to significantly different requirements to those that currently apply. However, where the MiFID II provisions are identical to, very similar to, or can be inferred from, existing requirements, we propose to amend rules relevant to non-MiFID business so they are consistent with the provisions that apply to firms carrying on MiFID business.

Article 24 of the MiFID II Directive is important and reproduced in bold below.

Article 24

Appropriate information shall be provided in good time to clients or potential clients with regard to the investment firm and its services, the financial instruments and proposed investment strategies, execution venues and all costs and related charges.

The information about all costs and charges, including costs and charges in connection with the investment service and the financial instrument, which are not caused by the occurrence of underlying market risk, shall be aggregated to allow the client to understand the overall cost as well as the cumulative effect on return of the investment, and where the client so requests, an itemised breakdown shall be provided. Where applicable, such information shall be provided to the client on a regular basis, at least annually, during the life of the investment.

Information on costs and associated charges (Article 50)

For firms doing MiFID business, we propose to implement MiFID II Article 24(4) (c) and second paragraph, to reflect the related detailed requirements in Article 50 of the MiFID II delegated regulation, by introducing new rules in COBS 2.2A, and COBS 6.1-A.2.8 EU. These provisions will apply in relation to all clients. In relation to firms providing investment services to professional clients and ECPs, the application of the rules on costs and associated charges disclosure is limited by Article 50(1) of the MiFID II delegated regulation. Article 50 will enable a firm doing MiFID business to agree with these clients to a limited application of the rules on costs and associated charges disclosure, subject to restrictions.

Costs and charges in relation to UCITS and PRIIPs (Article 51)

> *5.52 For firms doing MiFID business, we propose to give effect to MiFID II Article 24(4) and reflect the related detailed requirements of Article 51 of MiFID II delegated regulation by creating a new COBS 14.3A.8EU. This provision will be relevant to firms when distributing units in a UCITS scheme or PRIIPs. It refers to the interaction of the disclosure requirements in the UCITS Directive and the PRIIPs Regulation with those in MiFID II. Such firms will need to provide clients with additional information about other costs and charges related to the product purchase, which may not have been included in the UCITS KIID or PRIIPs KID, including the costs and charges relating to their provision of investment services in relation to that product.*

Q18: Do you agree with our approach to implementing the MiFID II requirements that relate to providing information to clients?

Yes. Clarity of explanation of costs and charges are critical to ensuring proper competition, quite apart from the fact that customers and potential customers should be able to clearly see what investment services are likely to cost in £s and, after investment have cost.

However, it makes little sense for there to be differences in cost and charge disclosure between LGPS, MiFID and PRIIPs. They should be on a common and consistent basis. Failure to address this issue will confuse customers as well as inflict unnecessary costs on firms trying to comply with conflicting disclosure requirements.
Particularly as the UK will be leaving the EU we believe the FCA should propose an overarching and consistent cost and disclosure regime that makes sense for the industry. This should be considered as part of the Asset Management Review.

Q19: Do you agree with the decision not to extend the 'fair clear and not misleading' information requirements to firms communicating with an eligible counterparty in relation to non-MiFID business? If not, and you think that we should extend the fair, clear and not misleading information requirements to non-MiFID eligible counterparty business, please provide evidence to support your view.

We agree that the FCA should not extend the 'fair clear and not misleading' information requirements to firms communicating with an eligible counterparty in relation to non-MiFID business.

Q20: Do you agree with our proposal not to extend the MiFID requirements in relation to costs and charges to non-MiFID business (that is not the business of an Article 3 firm)? Do you think there will be difficulties for firms if they need to comply with different disclosure requirements in relation to costs and charges for their MiFID and non-MiFID business?

We agree with the FCA proposal.

See our comments in response to Q18.

Q21: Do you agree with our proposal not to propose a standardised format to point-of-sale and post-sale disclosures? If not please give reasons why.

We believe that it will be helpful for firms and customers to be able to compare on a standardised basis. That is why TISA's members are developing a good practice guide for Costs & Charges, which will include a standardised format for disclosure. This will provide a starting point for many firms, but we also expect that firms will wish to tailor these to meet their own specific customer and distribution requirements.

Q22: Do you agree with our proposals to amend COBS 16.3 and 16.4 to allow firms doing non-MiFID business to avoid the need to provide their clients with periodic statements, so long as clients have accessed their statements via an on-line system which qualifies as a durable medium? If not please give reasons why.

Whilst we support the proposals in principle, we are concerned with the burden of having to evidence that direct investors have accessed their online statements. Firms have advised us that the functionality to support this is bespoke and expensive. Firms should like the facility to continue to offer periodic statements in hard copy, without charge to investors, but offer investors the opportunity to receive them online. This is consistent with retail practice in a number of other markets. Where investors have access to their statements via either media, why should firms police whether they are looking at them?

Independence

Chapter 6 of the CP discusses Independence. The proposals, which give a back drop to the questions, are paragraphs 6.5 to 6.7.

Proposals *We propose to implement the MiFID II independence standard for personal recommendations to retail clients in the UK for both MiFID financial instruments and structured deposits and for non-MiFID RIPs (such as insurance-based investments and personal pensions). For professional clients and, where relevant, retail clients outside the UK (who are currently not covered by the RDR independence standard), we propose to apply only what is required by MiFID II. This is the MiFID independence standard on financial instruments and structured deposits only.*

We are also proposing to include guidance to clarify our expectations of what the MiFID standard means to help firms demonstrate that they are meeting the standard and ensure firms interpret it consistently. For example, we propose guidance confirming that since the assessment conducted by an independent firm must ensure that the client's objectives can be suitably met, a firm providing independent advice should be in a position to advise on all product types within the scope of the market on which it provides advice. It will not, however, be necessary for firms to assess every single product available on the market. A firm not specialising in a particular market would generally be expected to be in a position to consider all financial instruments, structured deposits and other non-MiFID RIPs which would be capable of meeting the investment objectives of its retail clients.

Finally, for advice that falls outside the scope of MiFID II, with certain limited exceptions, we propose to apply as rules the provisions of the MiFID II delegated regulation. This will be relevant to, amongst others, non-MiFID (including Article 3) firms and MiFID firms providing advice to retail clients on RIPs which are not financial instruments. We propose to apply the provisions of the MiFID II delegated regulation in this way where:

- *we consider that they are needed to clarify or substantiate the requirements of the independence standard in MiFID II which we are adopting, or*

- *are otherwise consistent with our current rules and guidance.*

Q23: Do you agree with our analysis of the two (MiFID II and RDR) independence standards? If not, please give reasons why.

Yes, we agree with the analysis. In our response to DP15/3 we welcomed the MiFID II independence standard. We do not believe there is any material difference to the RDR standard, so think FCA's adoption of the MiFID II standard is sensible, particularly as it more clearly reflects what firms actually do.

Q24: Do you agree with our proposal to apply the MiFID standard of independence to financial instruments, structured deposits and other non-MiFID RIPS for UK retail clients? If not, please give reasons why.

We agree.

Q25: Do you agree with our approach to implementing MiFID II's requirements around providing both independent and non –independent (restricted) advice? If not, please give reasons why.

We agree with the FCA approach.

Q26: Do you agree with our approach to reading across these further requirements from the MiFID II delegated regulation? If not, please give reasons why.

We agree with the FCA approach.

Suitability

Q27: Do you have any comments on our proposal to keep the current rules for non-MiFID products pending implementation of the IDD? If not, please give reasons why.

No. We agree with the FCA.

Q28: Do you have any comments on the new COBS 9A in Appendix 1?

No.

Q29: Do you agree that the new COBS 9A should apply in full to Article 3 firms? If not, please give reasons why.

No. We do not believe that Article 3 firms present a sufficient risk to justify the extension to them of obligations that MiFID II does not require.

Appropriateness

TISA have addressed these questions in the context of the work and output of the TISA MiFID II Appropriateness Executive Committee, which published its Guide to Implementation in September. A copy of this Guide is attached to this response.

Q30: Do you agree that, for non-MiFID firms, we should limit the current rules in COBS 10 to direct offer financial promotions relating to a non-readily realisable security, derivative or a warrant (and also, through COBS 22.2, to mutual society shares)? If not, please give reasons why.

Yes.

Q31: Do you agree with our proposal to limit the new COBS 10A to MiFID products? If not, please give reasons why.

Yes.

Q32: Do you have any comments on the new draft of COBS 10A?

TISA have, as noted above recently published an industry Guide to Implementation in relation to Appropriateness. We were pleased to note its consistency with the draft rules.

Dealing and managing

Q33: Do you agree with our proposed approach to implementing the MiFID II requirements on best execution? If not, how could we amend our proposed approach?

No comment.

Q34: Do you agree with our proposal to add new guidance to the Handbook chapter on best execution? If not, please explain why.

No comment.

Q35: Do you agree with our proposals for non-MiFID business? If not, what alternative approach could we consider?

No comment.

Q36: Do you agree with our proposed approach to COBS 11.3? If not, please give reasons why.

No comment.

Q37: Do you agree with our proposed approach to COBS 11.4? If not, please give reasons why.

No comment.

Q38: Do you agree with our proposed approach to retain the extension of MiFID requirements to

non-MiFID business and level-up the requirements to MiFID II standards? If not, please give reasons why.

No comment, though we do not see why the FCA should seek to go beyond the requirements of the Directive.

Q39: Do you agree with our proposed approach to implementing the MiFID II requirements on record keeping of client orders, decisions to deal, transactions and order processing to Article 3 firms? If not, please give reasons why.

No, we do not agree.

If the Directive does not impose these requirements on such firms then, at present, pending the review we call for in our response to Q42, we do not believe the FCA should go beyond the requirements of the Directive.

Q40: Do you agree with our proposal to apply the requirements to UK branches of third country firms? If not, please give reasons why.

No comment.

Q41: Please give us your views on whether we should apply the new MiFID II transaction record keeping standard to the following firms, for whom we currently propose to maintain the existing requirements in COBS 11.5 for

1. **Occupational pension schemes**
2. **Non-MiFID business related to commodity or exotic derivatives**
3. **Small authorised UK AIFMs and residual CIS operators**
4. **Authorised professional firms with respect to activities other than non-mainstream regulated activities**

No comment.

Q42: Please give us your views on whether or not we should consider applying new MIFID II standards on transaction record keeping to the following firms which are not currently subject to COBS 11.5, namely:

i. **Article 3 exempt corporate finance firms**
ii. **ii. UCITS Management companies**
iii. **iii. Full scope UK AIFMS and incoming branches of EE AIFMs**

There are two separate questions.

We do not agree with extending these new standards to Article 3 firms. MiFID II does not require this for Article 3 firms and we see no pressing case made in this CP to add to such firms' obligations.

In respect of UCITS management companies and full scope UK AIFMS and incoming branches of EE

AIFMS, we do not see merit in adding to firms' record keeping obligations without good cause, particularly in view of FCA's acknowledgement of a widespread cost increase.

We think that a review of all of the current and proposed MiFID II obligations post Brexit should be undertaken as part of keeping the UK as Europe's centre of excellence. That might mean the extension of these obligations beyond MiFID's requirements, or improving them.

Q43: Do you agree with the approach to implementing the MiFID II requirements on personal transactions? If not, please give reasons why.

We have no objections.

Underwriting and placing

Q44: Do you agree with our proposed approach to implementing Articles 38 to 43 of the MiFID II delegated regulation on underwriting and placing? If not, please give reasons why?

No comment

Q45: Do you agree with our proposed approach to apply Articles 38 to 43 of the MiFID II delegated regulation on underwriting and placing to third country branches? If not, please give reasons why.

No comment.

Investment research

Q46: Do you agree with our proposed approach to implementing Articles 36 and 37 of the MiFID II delegated regulation on investment research? If not, please give reasons why.

No comment.

Q47: Do you agree with our proposed approach to apply Articles 36 and 37 of the MiFID II delegated regulation on investment research to third country firms, non- MiFID OMPs and EMPs, and Article 3 firms carrying out corporate finance business, in the same way as the current COBS 12 applies to them? If not, please give reasons why.

No comment.

Other conduct issues

Q48: Do you agree with our proposed approach for client agreements? If not explain why and provide cost- benefit data.

Yes. We do support the proposed approach.

Q49: Do you agree with our proposed approach to restructure and amend COBS 18.5 to make it clearer for firms carrying out CPM activity? If not, why not and what alternative approach you would

propose?

We think this approach is sensible but implementation should be subject to more detailed consultation with CPM firms.

Product Governance

Chapter 13 of the CP addresses Product Governance. Paragraphs 13.3 to 13.8 are set out below.

The new rules and guidance will replace broadly equivalent existing guidance in the RPPD. However, there are certain aspects of the MiFID II product governance provisions that go beyond the RPPD, as outlined below.

FCA consider the implications for firms in paragraphs 13.10-13.12

13.10 For firms involved in the manufacture of products:

- *product design, including product charges, should meet the needs of the target market and the firm should identify groups for whom the product is unlikely to be suitable*
- *firms should consider the impact of new products on the orderly functioning of the market*
- *the distribution strategy should meet the needs of the target market*
- *firms working together to develop a single product should have a written agreement setting out their share of these responsibilities*
- *the compliance function at the firm should monitor product governance and firm management Boards should have effective control and oversight over the process*

13.11 Firms working together to manufacture a single product should have an agreement setting out their share of these responsibilities.

13.12 For firms involved in the distribution of products:

- *before distributing a product, firms should consider for which target market it is likely to be suitable and any groups for whom it is unlikely to be suitable*
- *the distribution strategy should meet the needs of the target market*
- *products should be reviewed regularly to confirm they remain consistent with the target market's needs and make changes to the distribution strategy or other processes if they identify problems*
- *firms should provide product manufacturers with information on sales and, where appropriate, the regular reviews mentioned above*
- *the firm's compliance function should monitor product governance*
- *firms' management Boards should have effective control and oversight over the process*
- *firms working together to distribute a single product should share information with other firms in the chain*

> *MiFID II obliges us to introduce at least analogous standards for product governance for distribution firms that use the Article 3 exemption. We therefore also propose implementing the provisions as rules for these firms.*

Q50: Do you agree with our proposal to apply MiFID II product governance requirements as rules to UK branches of third country firms, on the basis that these requirements have a strong conduct-focus? If not, please give reasons why.

Yes.

Q51: Do you agree with our proposal to apply the MiFID II product governance provisions as rules for firms engaged in MiFID business? If not, please give reasons why.

Yes.

Q52: Do you agree with our proposal to apply the MiFID II product governance provisions as guidance for non- MiFID firms involved in the manufacture or distribution of MiFID products? If not, please give reasons why.

Yes.

We agree with the approach of applying the MiFID II product governance provisions as guidance for non MiFID firms involved in the manufacture or distribution of MiFID products.

We should note that, jointly with the Investment Association (IA), TISA intend to publish a Product Governance Good Practice Guide for Product Manufacturers. TISA will be building on this to cover responsibilities for Distributors. Copies of these are attached.

We have some more detailed points that we should like to raise, that we have discussed and agreed with the IA. These are as follows.

It would be helpful for firms to have all relevant guidance regarding product governance in one place and we welcome the generation of a specific sourcebook.

At paragraph 13.6, the FCA says *'where appropriate, we have copied existing relevant FCA guidance, such as from RPPD, into the rules to help explain certain concepts'.* At paragraph 13.9, the FCA says *'The new rules and guidance will replace broadly equivalent existing guidance in the RPPD.'* In paragraph 13.19, the FCA says *'In the future, we can consider whether to move or replace the RPPD with guidance and rules in PROD for other market sectors.'*

The first statement suggests selective copying from the existing RPPD. The second suggests a broad replacement of RPPD. The third implies that PROD replaces RPPD for the market sector under consideration but remains for other market sectors.

Is it the case that PROD will replace RPPD for MiFID firms and non –MiFID firms manufacturing or distributing MiFID products? If it does, a clear statement to that effect in the feedback statement would be helpful in providing clarity. If, on the other hand, there are any other aspects of RPPD which will remain as guidance for such firms, we suggest that these are included in the sourcebook as guidance. If this is not done, firms will need to have regard to two sources and it may also give rise to uncertainty.

The above queries regarding the FCA commentary flow through to the draft rules/guidance too.

PROD 1.3.15 does appear to suggest that there may be parts of RPPD that will continue to apply. If this is the case, it would be helpful if these additional parts of the RPPD are set out in PROD.

PROD 3.2.7 – This refers to 'third country investment firms' (which is a defined term in the FCA Glossary) whilst the Delegated Directive refers to 'third country firms'. As third country firms would capture a broader suite of firms, we wonder whether PROD should use the terminology used in the Delegated Directive.

PROD 3.2.12 – This guidance does not appear to come from MiFID II or RPPD. We believe that PROD should go no further than reflecting MiFID II and existing RPPD requirements. Accordingly, this draft guidance should not be taken forward. Instead, it should reflect RPPD 1.19 which requires that manufacturers should take account of what information the customer needs to understand the product or service, its purpose and the risks, and communicate information in a way that is clear fair and not misleading.

Certainly, in the case of both UCITS and AIFs, managers are already required to provide sufficient information so as to enable a prospective investor to understand the product. Other material is required to be fair clear and not misleading, and lastly, PROD 3.2.19 requires that a manufacturer must ensure that the information is of an adequate standard to enable distributors to understand the financial instrument.

PROD 3.2.15 – This guidance does not appear to come from MiFID II or RPPD. We believe that PROD should go no further than reflecting MiFID II and existing RPPD requirements. Accordingly, this draft guidance should not be taken forward.

PROD 3.2.18 - This appears in neither MiFID II or in RPPD and is already sufficiently covered by the requirements of PROD 3.2.4. Accordingly, this draft guidance should not be taken forward.

PROD 3.2.23 - We appreciate that this is a direct lift from RPPD but it is not clear what 'to detect patterns of distribution' actually means and we do not believe that this guidance is necessary as the Directive requirement as set out in PROD 3.2.22 is sufficiently clear. We recommend deletion of PROD 3.2.23.

PROD 3.2.27 – Should this include reference to SYSC 5.1.5ABG? The equivalent provision in the distributor section (PROD 3.3.22 includes such a reference).

PROD 3.2.35 - The Delegated Directive - Art 9.7- requires the compliance function to **monitor** the development and periodic review of product governance arrangements. The rule requires the compliance function to **oversee** the development and review of product governance arrangements.

It would be helpful, for the sake of clarity, to have confirmation in the feedback statement that it does not necessarily have to be the compliance function that designs the product governance arrangements and the review thereof but it does have responsibility for monitoring compliance with the PROD requirements. In many firms, it is common practice that the product development/management function designs the product governance arrangements.

We would welcome further ESMA guidelines on this part of the product governance process as many members distribute their products cross border (within and beyond the EEA). A clear set of standards and harmonised rules is key for effective product governance, better consumer outcomes and efficient communication between different stakeholders in the often highly intermediated distribution chain of funds and investment services. In their engagement with other NCAs with ESMA we urge the FCA to keep in mind that the funds industry in Europe is already highly regulated through the UCITS and AIFM directives and that the overwhelming majority of products are generally non-complex and specifically designed for the mass retail investor.

Therefore, beyond what is provided in the draft ESMA guidelines, a practical example on what the regulator would expect of firms defining a target market for a mass retail market product would be very helpful.

Furthermore, the distribution chain is heavily intermediated and that this presents a number of challenges to firms, including the nature of the definition of target market but also in relation to obtaining information from distributors for target market oversight purposes. As recognised in the ESMA CP and by the FCA in 3.2.9 G, asset managers in most cases do not have direct contact with end investors and usually very little information about them and their needs and objectives. Therefore, additional clarity on what the regulator expects from manufacturers in terms of receiving and processing sales information from distributors would be very welcome.

Typographical errors – PROD 3.**2**.30, 3.**2**.31 and 3.**2**.33 should be 3.**3**.30, 3.**3**.31 and 3.**3**.33 respectively.

PROD 3.3.30 - We think this rule should be extended to fully reflect Article 10(9) such that 3.3.30 (2) reads 'where appropriate, information on the reviews carried out under PROD 3.3.25R-3.3.27R to support product reviews carried out by manufacturers'

The purpose for providing the information is sufficiently important to merit being included in a rule rather than guidance only.

Knowledge & competence requirements

Q53: Do you agree with our approach to implementing the guidelines in TC and SYSC 5? If not, please give reasons why.

Yes

Recording of telephone conversations and electronic communications

Q54: Do you agree with our proposed unified approach to implementing the MiFID II requirements

on taping of telephone conversations and electronic communications? If not, please give reasons why.

We do not oppose taping.

Irrespective of any imposed taping requirements, firms would and probably should tape conversations with customers, in order to:

- improve customer experience,
- monitor customer interactions
- improve training, and
- enable disputes with customers to be resolved in an objective way.

Extension to Article 3 firms is, therefore, in principle, not objectionable.

Nevertheless, the extension of the MiFID II regime generally to Article 3 firms seems so significant for such firms when the Directive does not require this, that it would be better to defer such requirements until the FCA has carried out a review of all of the current and proposed MiFID II obligations post Brexit as part of the Government's and FCA's intention to keep the UK as Europe's centre of excellence. That might mean the extension of these obligations beyond MiFID's requirements, or improving them.

As the Directive requires only analogous requirements, does this extend to the length of retention.

In our experience, the kind of issues identified by FCA arise relatively shortly after transactions are incurred, so a shorter time frame might be more sensible.

Our concern is around the practicalities of retaining and accessing the records in a sensible way. Time adds to issues, as phone systems are changed, firms move offices, staff leave, thus making accessing the records over time more problematic. And, whereas the FCA is correct that storage costs have come down they are not free, and unnecessary extension of requirements will impact firms for little benefit to customers or enforcement.

Q55: Do you agree with our proposed approach for Article 3 firms including larger financial advisors? If not, please give reasons why. In your response, please identify the size of your firms eg provide details of the number of employees who will be subject to the new taping requirements.

See our answer to Q54.

Q56: Do you agree with our approach for Article 3 financial advisers? If not, what other alternatives do you suggest that may meet the analogous requirements of Article 3.2(c) of MiFID II for smaller financial advisers? Please also provide your views on what an appropriate threshold level to distinguish between larger and smaller financial advisers would be.

See our answer to Q54

Q57: Do you agree with our approach to extend the MiFID II requirements to corporate finance business and the service of portfolio management and to remove the exemption for discretionary

investment managers? If not, please give reasons why.

See our answer to Q54

Q58: Do you agree with our proposal to apply the MiFID II taping provisions to UK branches of third country firms?

See our answer to Q54

Q59: Some respondents to the CBA we undertook last year indicated that the costs for adhering to the new taping organisational requirements are likely to be minimal. Do you agree with this view? If not, please provide further empirical information as to why.

No. We disagree. See our response to Q54.

Supervision manual (SUP), authorisation and approved persons

Q60: Do you agree with our proposal to introduce specific Form As to for applications for the approval of individuals who will be members of the management body or who will effectively direct the business? If not, please give reasons why.

Yes.

Q61: Do you agree with our proposed approach? If not, please give reasons why.

Yes.

Q62: Do you see merit in allowing prospective MiFID firms to use the new Form As also for the appointment of persons who are not members of the management body or who do not direct the business? If not, please give reasons why.

Yes.

Perimeter guidance (PERG)

Q63: Do you agree with our proposed amendments to PERG 2 and 13? If not, please indicate where you disagree and why.

Yes.

Consequential changes to the Handbook

Q64: Do you agree with our proposed changes to these modules? If not, how could we amend them?

No comment.

Q65: Do you agree with our proposed consequential changes to IPRU(INV) 3? If not, how could we amend them?

Yes.

Q66: Do you agree with our proposed consequential changes to CASS? If not, how could we amend them?

Yes.

Jeffrey Mushens, Technical Policy Director, TISA

M: 079 3957 5093

E: jeffrey.mushens@tisa.uk.com