The Future of Regulatory Reform of Asset Management

A joint report
by ComRes and Cicero Consulting
on MEPs’ views towards asset management regulation
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CICERO | London - Brussels - Washington - Singapore
Financial Sector Communications

FOREWORD BY COMRES

In an age when uncertainty and a lack of political leadership blight the economies of all leading western economies, knowledge is at a premium.

The financial services sector in general, and asset management in particular, will need to balance the obvious hunger to regulate with the degree to which it wishes to, and can, influence the outcome of future negotiations over the design and implementation of that regulation.

We at ComRes cannot affect the propensity of the sector to shape its regulatory future, but we can help by revealing the thinking of some of the key audiences whose voices will carry weight over the coming months.

We hope very much that this report is useful both to those wishing to plan for regulatory change and to those seeking to influence it.

Researching the views of MEPs is a specialist, resource-intensive task so this project is our contribution to this important debate. We hope you find it useful.

Andrew Hawkins
Chairman, ComRes

FOREWORD BY CICERO CONSULTING

Since the financial crisis of 2008 and the G20 commitments that followed, the European financial services sector has been the target of a wave of reform. Efforts from Brussels to regulate a sector that is heavily driven from the UK have long been met by suspicion and antipathy - some warranted, some less so. While there are clear concerns about the motives of some regulations, much of the unease about EU regulation stems from a sense of helplessness in shaping policies that will have such a dramatic effect on industry. During negotiations on similar proposals in the UK, businesses will have a decent understanding of the main protagonists and their views. This level of understanding is often lacking in Brussels.

Our report on the views of MEPs towards the asset management industry seeks to address these concerns and illuminate the views of one of the key institutions in the legislative process. By doing so, the report will help the asset management industry prepare for 2012.

The asset management industry has been largely shielded from European regulations to date but this is set to change. The revised Markets in Financial Instruments Directive entered the Parliament in October and will bring in major changes to the way that products are described and sold to consumers. The interplay between MiFID and the UK's Retail Distribution Review will be an area to watch. In February, the Commission will publish its proposal for a new initiative on Packaged Retails Investment Products as well as an amended Insurance Mediation Directive. These two initiatives will also bring in strict new requirements for firms dealing with retail clients.

These initiatives will all be discussed by MEPs over the course of 2012 and the industry will need to engage closely to ensure that the final provisions reflect their concerns and do not place unnecessary burdens on business.

The busy regulatory agenda comes at a time when big questions are being asked about the UK's position in Europe. The details of the new inter-governmental treaty that was agreed by 26 leaders at the European Summit on 8 December are yet to be unravelled but David Cameron's use of a veto - when Europe was asking him for help - will not be forgotten soon.

FOREWORD BY CICERO CONSULTING

British officials are already facing difficult negotiations to retain concessions won in October on derivatives regulation and the use of a veto to protect the UK's financial services industry could have contributed to the prevailing view in Europe that the City of London is separate from the rest of the EU. An area to watch in 2012 is how widespread this sentiment is and whether it restricts the ability of UK businesses to articulate themselves in Europe.

Finally, the European Parliament itself is set for change with elections for a new President and Committee chairs scheduled for January. Sharon Bowles MEP, the influential Liberal Democrat, is fighting to retain her position as chair of the powerful Economic and Monetary Affairs Committee. French presidential elections in April 2012 may change the political dynamic further.

So 2012 will be a year of change - both political and regulatory - but we hope that by providing an insight into the MEPs' views of the asset management sector, we can provide some comfort to those of you who will be looking towards Brussels this year.

Helena Walsh

Regional Director, Brussels, Cicero Consulting

I. INTRODUCTION

The last three years have been turbulent times for the EU's financial services industry and have led the EU to rethink its role in regulating asset management, a vital part of Europe's financial infrastructure. At the end of 2010, assets under management by the European fund management industry reached over $19 trillion, a rise of 27% compared to the end of 2008, showing the industry to be a growing area of financial services despite the financial crisis and subsequent recession.

A multitude of legislative initiatives designed to govern various aspects of the financial services industry have been debated and passed over the last few years. Yet, there are still crucial policy areas awaiting the introduction of stricter and more harmonised rules to govern it, including many crucial aspects of asset management.

The financial services industry has never been enthusiastic about the efforts to regulate it at European level and asset management is no different in this respect.

However, establishing an appropriate regulatory framework is vital for restoring the confidence of investors in the industry and should therefore be in the interest of the sector.

In this respect, the European Parliament will play a vital part in negotiating and approving the final design of the upcoming regulations affecting asset management and understanding the MEPs' opinions is therefore instrumental in anticipating future of regulatory reform of the sector.

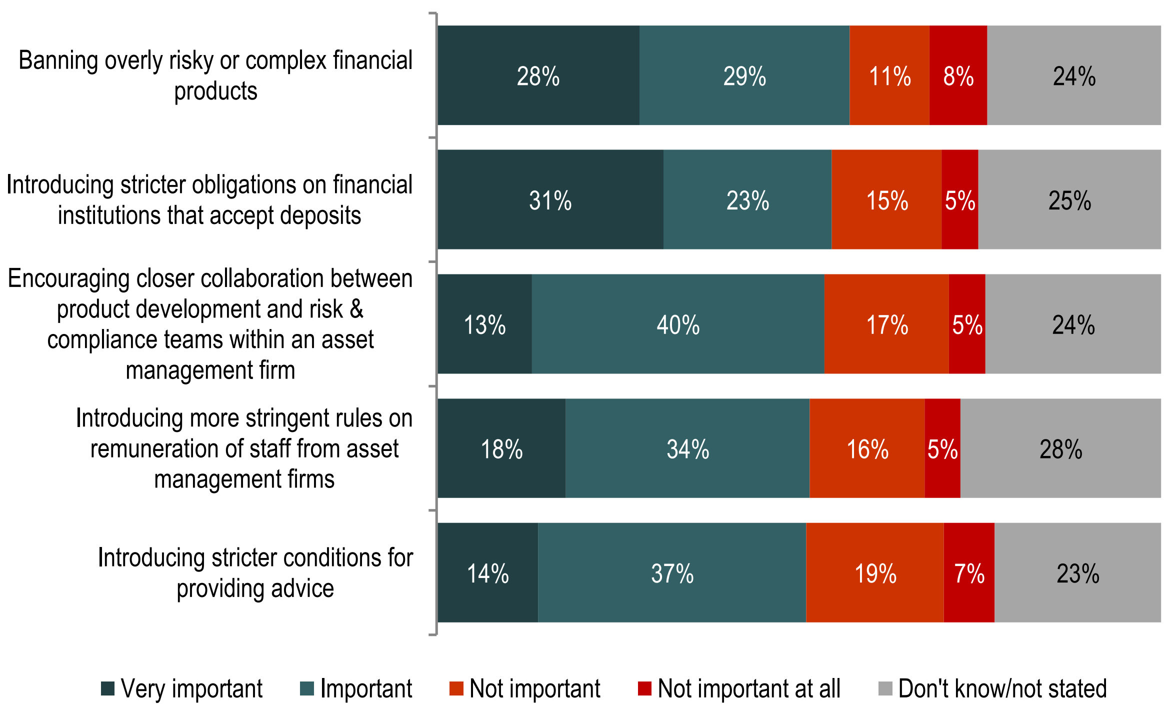
In this report we look at the views and perceptions of Members of the European Parliament with regards to the regulatory reform of asset management. The report summarises the results of a survey of 101 MEPs conducted by ComRes and Cicero Consulting between 25th May and 23rd July 2011. The results were weighted to be fully representative of the current Parliament, both politically and geographically.

II. IMPORTANT ASPECTS OF REGULATING ASSET MANAGEMENT

For a long time European policy-makers have been seeking to create new regulatory frameworks relating to asset management. However, the ongoing sovereign debt crisis and G20 commitments on safer banking regulation, banning short selling, and derivatives clearing over the past 12 months have taken priority.

The results of our survey suggests that MEPs consider banning of overly risky or complex financial products as the most important aspect of EU asset management regulation, though stricter obligations for deposit-taking institutions are also key.

Q: How important or unimportant do you consider each of the following aspects of EU asset management regulation to be?



Base: All 101 MEPs

57% of MEPs consider banning overly risky or complex financial products an important aspect of EU asset management regulation. This view is particularly strong among S&D Group where 75% of its members consider banning these products important compared to 40% of ALDE MEPs. Geographically, banning overly risky or complex financial products enjoys highest support among Eastern European MEPs (67% consider it an important aspect of EU asset management regulation) and, on the contrary, lowest support among Northern/Nordic MEPs (46%).

Another aspect of EU asset management reform very widely seen as important relates to introducing stricter obligations on financial institutions that accept deposits. More than half of all MEPs (54%) think that this is an important aspect. Eastern European MEPs are most likely to see this aspect as important (71%) as opposed to 35% of UK & Irish MEPs.

Banning products and stricter obligations are also the areas of reform most likely to encounter strong opinions in their favour, with over a quarter of MEPs (28%) seeing the former as 'very important' and nearly a third (31%) saying the same about the latter.

This suggests that whilst the majority of MEPs are broadly supportive of the full package of asset management regulation, it is perhaps these two issues that are most fuelling the drive for reform.

Another important EU asset management regulation concerns encouraging closer collaboration between product development and risk & compliance teams within an asset management firm. Overall, 53% of MEPs believe that it is an important aspect. This view is more widespread among S&D MEPs (69%) as opposed to ALDE members (33%).

Least important, out of those reforms tested with MEPs, is the introduction of stricter conditions for providing advice. 51% of MEPs say that it is important compared to 26% who consider it unimportant.

It does not come as a surprise that MEPs from the ECR Group are least in favour of regulatory intervention in asset management. More noticeable is the fact that, overall, ALDE MEPs attach less value to each of the aspects of EU asset management regulation tested than their EPP and S&D counterparts.

III. POTENTIAL CONSEQUENCES OF REGULATORY REFORM OF ASSET MANAGEMENT

As the most important aspects of regulatory reform become clearer and legislative proposals get under way, it is essential to understand the perceptions and expectations of MEPs on the effects of these initiatives.

The results of our survey show that MEPs are most likely to believe that regulatory reform of asset management at European level will provide a safer environment for investors, due to enhanced cross-border cooperation between supervisory bodies. More than a half of MEPs (54%) believe that this is a likely consequence. Interestingly, while this feeling is very strong among Eastern European MEPs (65%) it is less prominent among Northern/Nordic European MEPs (38%) and least among UK and Irish MEPs (22%).

One in two ECR MEPs do not believe that enhanced cross-border cooperation between supervisors is likely to result in a safer investment environment. In contrast 68% of EPP MEPs believe that this is the case.

The consequence of regulatory reform of asset management that is most likely to split opinion among MEPs is the potential capital migration to offshore financial centres. Overall, 36% of MEPs believe that capital migration to offshore financial centres is likely to be reduced as a result of the regulatory reform, and 37% hold the opposite view.

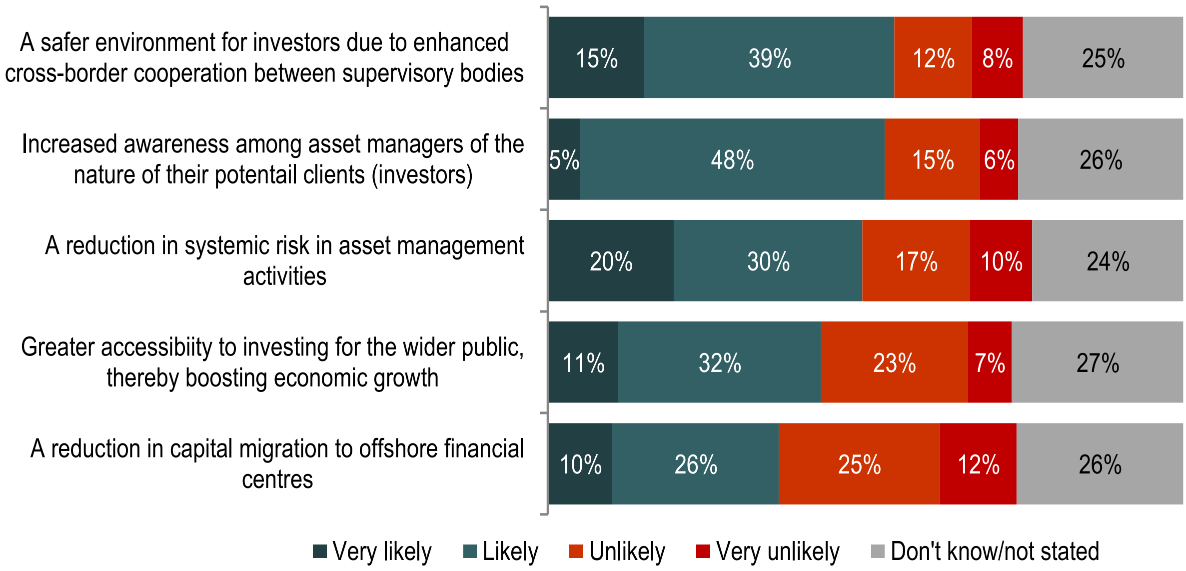
Looking at economic growth, MEPs are inclined to think that regulatory reform of asset management will have a positive impact. 43% of Members of the Parliament believe that it is likely that the reform will provide greater accessibility to investing for the wider public, thereby boosting economic growth.

However, the views of UK and Irish MEPs specifically show a different direction. While 13% of them think greater accessibility to investing is going to be a likely consequence of regulatory reform of asset management, 54% think this is unlikely.

Furthermore, half of all MEPs believe that regulatory reform of asset management at European level is likely to lead to a reduction of systemic risk in asset management activities. This view is particularly strong among ALDE and S&D Groups where 65% and 60% of their MEPs respectively think a reduction in systemic risk is likely.

53% of MEPs also believe that increased awareness among asset managers of the nature of their potential clients (investors) is a likely consequence of the regulatory reform. This opinion is particularly evident among Eastern European MEPs (68%) compared to Northern/Nordic members of the Parliament (40%).

Q: How likely or unlikely do you believe each of the following consequences of regulatory reform of asset management at European level to be?



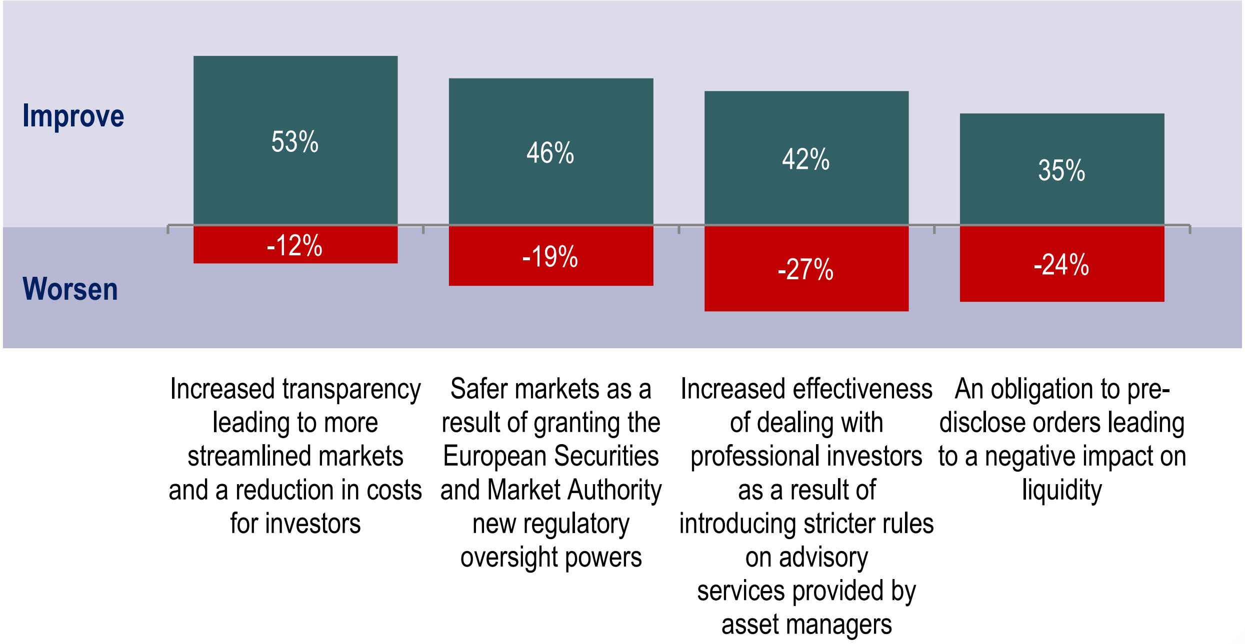
Base: All 101 MEPs

IV. INVESTMENT SERVICES – DIRECTIVE ON MARKETS IN FINANCIAL INSTRUMENTS

On 20 October the European Commission adopted its legislative proposals on the review of the Markets in Financial Instruments Directive and Regulation (MiFID 2 and MiFIR). These proposals include provisions on strengthening investor protection, including rules on the provision of advise and powers for regulators to intervene by temporarily banning products.

The proposals aim to make financial markets more efficient and resilient and will have a profound effect on asset management. Entering the inter-institutional legislative debate, it is vital to understand MEPs' views on the perceived likely effects of the revision.

Q: How if at all will each of the following revisions of the Directive on Markets in Financial Instruments (known as MiFID) affect asset management?



Base: All 101 MEPs

MEPs from the EPP Group are strongest in their conviction that the increased transparency resulting from the MiFID review will lead to more streamlined markets and reduction in costs for investors, thus improving asset management. More than three-quarters of its members (76%) believe that it will improve the asset management practice in the EU. On the contrary, S&D members are the most undecided mainstream party group in the Parliament on this issue with 46% of its MEPs stating 'don't know' or not stating any answer at all.

The obligation to pre-disclose orders leading to a negative impact on liquidity has lowest levels of belief that it will improve asset management. Only 35% of MEPs think that it will improve asset management and this view is even less prevalent among ALDE members (25%) and MEPs from Mediterranean countries (30%). However, among EPP members this number is considerably higher; as more than half (54%) of EPP MEPs consider that greater pre-trade transparency – despite negative effects on liquidity – will improve the current regulatory framework and asset management industry in the EU.

This juxtaposes the EPP with the ECR Group of which almost one in two MEPs (49%) thinks that the negative impact on liquidity as a result of greater pre-trade transparency will worsen the regulatory environment for asset management.

Interesting too in this context is the fact that 35% MEPs do not know or did not state whether granting new regulatory oversight powers to the new European Securities and Markets Authority (ESMA) is a valuable addition to the regulatory framework. Of those who know, 46% agree in this view. ECR MEPs are least likely to agree with the positive effects of additional ESMA powers (24% this it will improve asset management); a sharp contrast to more than 60% of EPP MEPs

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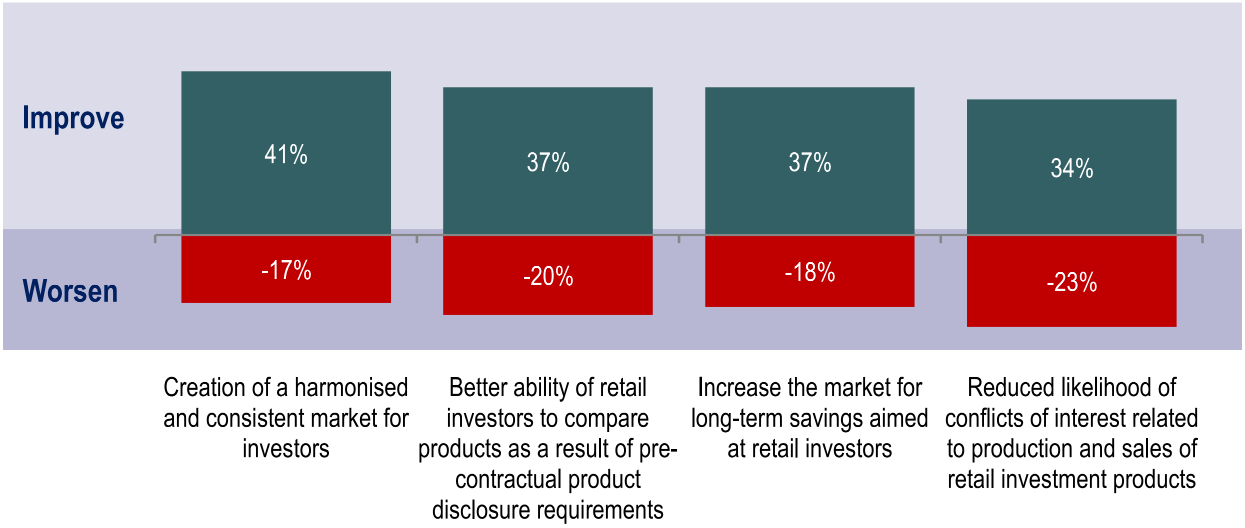
V. RETAIL INVESTMENT – FORTHCOMING LEGISLATIVE INITIATIVE ON PACKAGED RETAIL INVESTMENT PRODUCTS

The European Commission is currently preparing its legislative initiative on Packaged Retail Investment Products (PRIPs), expected to tackle the issues of product transparency through increased pre-contractual product disclosure, as well as harmonisation of sales rules for retail investment products.

We asked MEPs whether they felt various aspects of the PRIPs initiative would affect asset management positively or negatively

Q: How if at all will each of the following revisions of the Directive on Packaged Retail Investment Products (known as PRIPs) affect asset management?



Base: All 101 MEPs

Members of the Parliament are most likely to believe that the creation of a harmonised and consistent market for investors as part of the PRIP Directive will improve asset management in the EU. In line with previous findings, EPP Group is most likely to be positive towards the creation of harmonised market with 68% of its MEPs thinking that it will improve asset management as opposed to 36% of S&D and 26% of ALDE members.

Geographically, only 17% of UK and Irish MEPs believe this will be the case, suggesting that MEPs from the EU's most sophisticated asset management market are most cynical that new regulations affecting it can succeed.

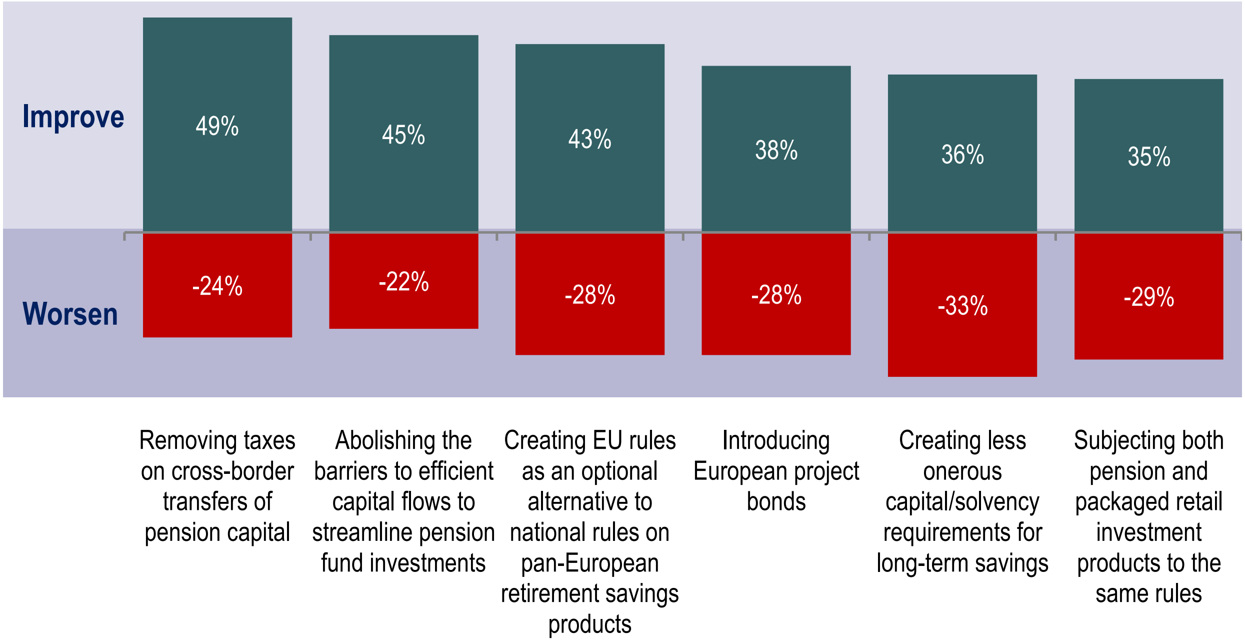
Overall, MEPs' opinions are more sceptical on reducing likelihood of conflicts of interest related to production and sales of retail investment products with 34% of MEPs feeling that this revision will improve asset management, and 23% believing it will worsen it. EPP MEPs are most likely to agree with this suggestion. 54% of its members believe that reducing likelihood of conflicts of interest will improve asset management.

It is concerning that 1 out of 4 MEPs do not know whether PRIPs will actually increase the market for long-term savings products aimed at retail investors. With a wave of people entering retirement in the coming years, retail investment solutions to supplement state-sponsored pensions will be required and it is important that MEPs recognise the value of these products.

VI. PENSION FUNDS – DIRECTIVE FOR INSTITUTIONS FOR OCCUPATIONAL REVISION PROVISION

By establishing rigorous prudential standards to ensure that pension fund members and beneficiaries are properly protected, the Pension Fund Directive was a big leap forwards when adopted in 2003. A number of initiatives that are currently being discussed in the framework of financial services regulation will have a profound impact on the single European market for pension funds.

Q: How if at all will each of the following affect the single European market for pension funds (Directive for Institutions for Occupational Revision Provision)?



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Almost half of MEPs believe that removing taxes on cross-border transfer of pension capital will improve the single European market for pension funds as opposed to 24% who disagree. The removal of these taxes enjoys highest levels of support among EPP members of the Parliament where 72% of its MEPs believe that it will improve the pension funds' market in Europe. Likewise, Eastern European MEPs are most likely to believe that removing taxes on cross-border transfers of pension capital will improve the pension funds' market; 77% of these Parliamentarians think so.

MEPs are split on the issue of creating less onerous capital/solvency requirements for long-term savings through occupational pension funds. While 36% of MEPs believe that it will improve the single European market for pension funds, 33% think it will worsen it. Similarly, 35% of members of the Parliament think that subjecting both pension and packaged retail investment products to the same rules will improve the pension funds' market as opposed to 29% who think it will worsen the market.

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VII. CONCLUSION

The results of this survey of Members of the European Parliament shed light on important aspects of the upcoming financial services regulation. MEPs will play a critical role in shaping the regulatory approach to financial services, including asset management and understanding their views is therefore imperative to successfully comprehending the political opinion landscape and reacting to it effectively.

This research has shown that:

- ✓ While a majority of MEPs acknowledge the importance of various aspects of EU asset management regulation, they are less likely to be positive about the potential consequences of regulatory reform. MEPs are also less clear on whether the consequences of revisions of the individual Directives will improve asset management

- ✓ UK and Irish MEPs are generally more sceptical than their counterparts elsewhere in the EU on the necessity and efficacy of proposed regulations of asset management within the European Union. Given the concentration of asset management business within the UK, the lack of support from there is potentially troubling.

- ✓ One in two EPP MEPs thinks that the negative impact on liquidity as a result of greater pre-trade transparency will worsen the regulatory environment for asset management.

- ✓ More than two-thirds of EPP MEPs believe that PRIPs will create a harmonised and consistent retail investment market. This is considerably more than UK and Irish MEPs, of which only 17% believe that this will be the case.

- ✓ MEPs from the EPP Group are more likely to be positive about the likely effects of the various revisions of Directives affecting asset management than S&D and ALDE Groups and, overall, their members feel that these revisions will improve asset management across the EU.

- ✓ A significant minority of MEPs are undecided on the topic of asset management and refrain from disclosing their views and making any judgements. Given the importance of asset management to the European economy, both as an industry and in terms of encouraging investment, it is essential that Parliamentarians are informed of the potential consequences of new regulations in the sector.

VIII. ABOUT COMRES

A leading market and opinion research consultancy serving clients in Europe and Asia, ComRes conducts a full range of qualitative and quantitative research in Brussels. It offers both customised and syndicated research among stakeholders and consumers across all EU Member States, including the unique Europoll™ omnibus panel of MEPs and omnibus surveys of Brussels Influencers, legislators in France, UK and Germany, and European Parliament Staffers.

ComRes polls regularly for many blue chip companies, international development and other charities, trade associations, NGOs and national governments. Its media clients include CNN, BBC, ITV News and The Independent.

ComRes follows the ICC/ESOMAR Code on Market and Social Research.

ComRes won the Dods 2010 Public Affairs News Award for "Pollster of the Year" and has been a finalist in the prestigious Research Magazine Awards 'Best Agency' category for the past two years running.

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IX. ABOUT CICERO CONSULTING

Cicero is the leading provider of government relations, regulatory affairs and public policy information services to the financial sector, operating from offices in London, Brussels and Washington. Cicero's consulting practice provides counsel on lobbying, campaigning, crisis management and thought leadership generation. Other services offered by the Cicero group of companies include online policy and regulatory monitoring services, conferences, and the recently launched online news service and publication, Global Financial Strategy. Cicero are members of the Association of Professional Political Consultants.

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