



Summary of Consultation Feedback

Working Group 1

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Requirements to the activities of investment intermediaries
Chapter 8 – Section II (Internal Control)

Section 1: What is the problem?

All stakeholders agree with problem identification. One of them expresses doubt whether the internal control provisions can address this.

1 Question: do you think consumers were adequately protected by the previous regulation on internal control? In what way the new regulation is better than the previous version

Section	Question					
1 - What is the problem		Bulgaria Association of Asset Management Companies	Central Depository	Investment intermediary "Beta corp"	Investment intermediary "STS Finance"	Investment intermediary "Elana trading"
	1			New regulation reiterates the internal control function		

2 Question: do you think the new regulation is clear about the duties of firms regarding internal control?

Section	Question					
1 - What is the problem		Bulgaria Association of Asset Management Companies	Central Depository	Investment intermediary "Beta corp"	Investment intermediary "STS Finance"	Investment intermediary "Elana trading"
	2	New regime is an upgrade of the previous one. Step forward. Better definition of duties of compliance officers.		The new one is not burdensome on a daily routine. Problem are compliance officers in each branch. Activities costs much more		

3 Question: to what extent did you have already in place an internal control mechanism similar to that set by the provisions (i.e. market-driven solutions)? Please give evidence.

Section	Question					
1 - What is the problem		Bulgaria Association of Asset Management Companies	Central Depository	Investment intermediary "Beta corp"	Investment intermediary "STS Finance"	Investment intermediary "Elana trading"
	3			Outsourced the legal transposition of the regulation. Apart the legal aspects, everything else was already in place		

Section 2: What are the possible policy solutions?

1.Question: how do you assess consumer protection is addressed with the new set of provisions?

		Bulgaria Association of Asset Management Companies	Central Depository	Investment intermediary "Beta corp"	Investment intermediary "STS Finance"	Investment intermediary "Elana trading"
1		The new regime can take benefit from international perspective (both for the investment firms both for consumers)	It is preferable that regulation (even though a flexible one) takes care of consumer protection			

The very critical point that arose from stakeholders feedback is the necessity of having internal control experts in each branch. It seems that this provision is really cumbersome.

2. Question In case the presence of internal control officers in each branch is eliminated, could you provide evidence of how the Ordinance objectives could be fulfilled? Which feasible alternative solutions do you propose? [art 76 – (4)]

There are not policy alternatives since it is a directive transposition but some issues could arise about alternative follow-up implementation steps that could be taken (e.g. self-regulation initiative).

		Bulgaria Association of Asset Management Companies	Central Depository	Investment intermediary "Beta corp"	Investment intermediary "STS Finance"	Investment intermediary "Elana trading"
2		Outsourcing this activity to external entities. The drawback is about the confidentiality of information		<p>Alternatives:</p> <ul style="list-style-type: none"> - a branch internal officer controlling the near-by branches or having a “mobile squad” responsible for several branches; - software platform sending scanned documents; - scanning documents in pdf file and send them to the hq; - division of labour between hq (periodical work) and the branch (day-to-day activity) (or having sb to co-authorize); 		

Section 3: Cost-Benefit Analysis?

I- Analysis of impacts (Users)

Costs

1.Question: what percentage(s) of the additional (incremental) cost of the new regulation can you pass on to the customers?

Section	Question			
		Bulgaria Association of Asset Management Companies	Central Depository	Investment intermediary "Beta corp"
	1			Difficult to say. Maybe in the long run, business model will change and intermediaries will charge for advisory services. However, it is not clear if this will be related to this new set of regulation.

Benefits

Unanimity about the relevant positive impact to consumers.

II - Analysis of impacts (Regulated firms)

Compliance costs:

Question: In many firms internal control departments were already established (due to previous regulation). Could you please define more precisely which additional costs (and their magnitude) are due to the **new** regulation on internal control (e.g. internal control officer per branch, hiring other staff, training costs, IT costs, etc.)?

Section	Question			
		Bulgaria Association of Asset Management Companies	Central Depository	Investment intermediary "Beta corp"
	1	Minor impact		Additional burden is not significant, apart from the provision on internal control officer per branch

Benefits:

1.Question: Could you be more specific on how this could be beneficial?

2.Question: Do the new internal control mechanisms protect investment intermediaries better from misconduct of its employees?

		Bulgaria Association of Asset Management Companies	Central Depository	Investment intermediary "Beta corp"
	2	Internal control mechanisms significantly reduce the risk for misconducts		In principle the internal control function should reduce the risk of misconduct. In practice there are some criticalities, mainly the internal control officer has not the knowledge that the (controlled) financial analyst/ salesperson has

3Question: Do the new internal control mechanisms help you to detect misconduct by clients?

4Question: Have you noticed the decrease in customer complaints since the regulation was enacted?

		Bulgaria Association of Asset Management Companies	Central Depository	Investment intermediary "Beta corp"
	4	FSC (as addressee of customer complaints): not possible yet, time since implementation is too short		

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Variety of products offered:

Question: For those that affirmed the positive impact, could you please explain more precisely why the variety of products will be higher? Through which mechanism does this occur? Which kind of products will be affected?

General comment on the questions relating to quantity, quality and variety of products:

There is a general sense that the regulations are beneficial (increased trust, confidence, possibly more demand for higher-risk investment products, etc.). However, it is difficult to assess which part of this is due to the regulations on internal control, internal audit and risk management or if this is due to the implementation of MiFID as a whole.

Comment from Beta Corp: In their opinion for investment intermediaries 95% of the change is market driven issue, only 5% are driven by MiFID/Ordinance 38.

Efficiency of competition:

Question: how many firms do you think will close down because of this regulation? How many firms will need to get restructured to face the cumbersome compliance rule requiring one internal control officer per branch?

		Bulgaria Association of Asset Management Companies	Central Depository	Investment intermediary "Beta corp"
	1		1-2%: out of the market; 20%-restructuring.	It depends on the enforcement of the regulation by FSC. It's difficult to say.

Question: Do you think that there will be large efficiency gains from restructuring?

Suggestions for policy recommendations

1. The FSC monitors the status of implementation of the rules (looking specifically at the potential identified problems: compliance officers for each branch). Dialogue with firms is necessary for that.
2. The FSC monitors the number of complaints which relate to this regulation.
3. The FSC monitors the market structure of the investment intermediaries market (i.e. how many firms go out of the market, how many firms enter the market)
4. If the FSC thinks after a certain (1 year?) that the implementation is not going smoothly, the FSC could suggest to:
 - Allow firms to use e.g. “mobile squads” of compliance officers or to have one compliance officer who is responsible for several branches;
 - This could be done either via FSC guidance or via revision of the Art. 76(4) of Ordinance 38;
 - It is important that the market participants should be consulted.