



Summary of Consultation Feedback

Working Group 2

WG Coordinator: Ms. Valentina Stefanova (FSC)

Requirements to the activities of investment intermediaries
Chapter 8 – Section III (Risk Management), Section IV (Internal Audit)

Section 1: What is the problem?

1.Question: which risk management mechanism was already in place before the new regulation was introduced? Can you please specify?

Question	Bulgaria Association of Asset Management Companies	Central Depository	Investment intermediary "Beta corp"
1			Risk management is not only the compliance part but also the clients in the portfolio mgmnt in terms of risk. This rules address certain issues about large exposures, specific risk concentration. We had already in place a questionnaire to clients. Things brought by the new regulation: format of the contract, inclusion in the contract of the type of product

2.Question: which functions of internal control/internal audit overlap? How do you suggest to deal with that?

Question	Bulgaria Association of Asset Management Companies	Central Depository	Investment intermediary "Beta corp"
2		In general it is not necessary to have two different departments	Having two separate departments for internal control is a huge burden (also compared to banks which have both functions included in one division → suggestion of “2 in 1” solution, having one department responsible for internal control and internal audit

Section 2: What are the possible policy solutions?

Question: Do you think that consumer protection is adequately addressed with the new set of provisions?

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).

2.Question: Did you find the guidance prepared by the Bulgarian Association of Asset Management Companies helpful? Do you generally think guidance provided by the industry is good way to regulate a market?

→ see section on compliance costs

Section 3: Cost-Benefit Analysis?

I- Analysis of impacts (Users)

Costs

1Question: 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			Not too much at this stage

2Question: Does your firm plan to inform the customers of the **new** risk management mechanism?

3Question: Does your firm plan to inform the customers about the incremental benefits arising from complying with the regulation?

Section	Question			
		Bulgaria Association of Asset Management Companies	Central Depository	Investment intermediary "Beta corp"
	2			It is a difficult task. At this stage this kind of communication is difficult.
	3			It's hard to sell this at the moment

II - Analysis of impacts (Regulated firms)

Compliance cost:

1Question: Could you please define more precisely which additional costs (and their magnitude) are due to the **new** regulation on risk management and internal audit (e.g. hiring new staff, training costs, IT costs, etc.)?

		Bulgaria Association of Asset Management Companies	Central Depository	Investment intermediary "Beta corp"
	1			<p><u>Costs for legal advice:</u> 2500-5000 Euro are for Ordinance 38 as a whole.</p> <p><u>Training costs:</u> 7000 – 13000 Euros: Mainly for risk management; not that much for internal audit</p> <p><u>Software costs:</u> - 3.500 – 7.000 Euros - 4 people * 1 week each Approximately 90% of these costs were due to the new regulations.</p> <p><u>Implementation of new rules (Ordinance 38 / Mifid as whole:</u> - risk and compliance officer spends 6 months on new regulation - The regulations on internal control, internal audit and risk management possibly account for 15-20% of these costs.</p>

2Question (to firms): do you use the implementation guidance prepared by the Bulgarian Association of Asset Management Companies (BAAMC)?

3Question (to firms): Has the Guide helped to reduce implementation costs?

4Question (to BAAMC): have you a sense of savings the code has produced to the whole industry?

5Question (to BAAMC): How much did it cost to the association to produce the guide?

		Bulgaria Association of Asset Management Companies	Central Depository	Investment intermediary "Beta corp"
	2			No, Beta Corp. have not used it
	3			Not applicable here, as code was not used
	4	Most of the members have adopted the code. Savings in as "in house" legal assistance, Overall savings difficult to quantify		
	5	10 people*3meetings*1 Full-Time-Equivalent (FTE)+preparatory interim work		

Benefits:

General comment on the questions relating to benefits:

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.

Question could you please specify more in detail through which mechanism your firm will benefit from this regulation?

Question: Through which figure could you measure the benefit? (e.g. more product sales, higher profit margins, less complaints)

Question:

Do you think that complying with risk management provisions could bring a competitive advantage to the firm?

(please provide evidence on increase in clients, higher demand for asset management services..)

Which percentage of this advantage is due to higher trust/better reputation?

Quality of the products offered:

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

Efficiency of competition:

1.Question: how many (small) firms do you think will close down because of this regulation? How many other firms will need to get restructured to face the new regulation?

		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.

2. Question: How much do you think that international competition will increase because of MiFID overall?

		Bulgaria Association of Asset Management Companies	Central Depository	Investment intermediary "Beta corp"
	2	We expect an increase in competition. Foreign firms already have applied for membership in the BAAMC. BAAMC is considering this.		We expect foreign competition. It takes time to have large western competitors entering the market because it is still small to date. We think 2-3 foreign competitors will enter.

Suggestions for policy recommendations

1. The FSC monitors the status of implementation of the rules (looking specifically at the potential identified problems: overlap of internal audit and internal control). Dialogue with the 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 smoothly, the FSC could suggest to:
 - Allow firms to combine their independent internal audit and internal control departments into 1 independent department.
 - It is important that the market participants should be consulted