

Annex to Working document ESC/17/2005

| <b>CESR's Advice</b>  | <b>Commission Position</b>                                   | <b>Comments</b>  |
|---|--|--|
| <b>Definitions</b>  |  |  |
|   | Personnel  | For reasons of drafting efficacy we also included a definition of personnel whose scope is smaller than that of 'relevant persons'.  |
|   | Person with whom a relevant person has a family relationship | We included this definition in order to clarify the scope of 'personal transactions' and to align it with the MAD.   |
| <b>BOX 2</b>  |  |  |
| <b>Supervisory function: general provision relevant to advice under Art. 13</b> | Partially retained in Article 7                              | Where appropriate, the supervisory function will receive the relevant reports.   |
| <b>Compliance function</b>  | Retained in articles 3 and 4.                                |  |
|   |  |  |
| <b>Compliance function: measures to foster independence</b>                     | Retained in article 4  | We have included as a principle that the compliance function has to be independent and that the formal measures for ensuring independence are to be the ones mentioned in CESR advice.   |
| <b>Compliance function: other measures to promote effectiveness</b>             | Retained in article 3 and 4                                  |  |
|   |  |  |
| <b>Role of the compliance function</b>  | Retained in article 4.                                       | We have pooled the reporting obligations in article 7  |
|   |  |  |
| <b>Compliance policies and procedures</b>                                       | Retained in Article 4  |  |
|   | .  |  |
| <b>Role of senior management in compliance</b>                                  | Retained in Article 7  |  |
|   |  |  |
| <b>Person responsible for compliance oversight</b>                              | Not retained.  | This is not considered necessary as we are already defining the compliance function, the responsibilities of the senior management and the means for making the function effective. We consider this as a burdensome obligation. |
|   |  |  |
| <b>Complaints handling</b>  | Retained in article 8.                                       | We have added an obligation for the investment firm to notify the complainant within 15 days of the name and contact details for the person responsible and the  |

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|   |                                 | timescale for the resolution of the complaint .   |
| <b>Code of conduct</b>  | Not retained.                   | Although we think that the code of conduct is a useful tool for spreading the values of the organisation we consider that, at this stage this is something that should not be regulated. This could be a point where CESR could issue very useful guidance.   |
| <b>Personal transactions: requirements</b>                                | Retained in article 9           | We specify what transactions the relevant persons are prohibited from entering into – these would be the transactions that would be prohibited under the MAD. We added the requirement for the investment firm to make relevant persons aware of any restrictions related to personal transactions.   |
| <b>Successive personal transactions</b>                                   | Not retained                    | We are not against this but think this would be more appropriate in a recital.  |
| <b>Personal transactions: exemptions</b>                                  | Partially retained in article 9 | We have struck out the exemptions on UCITS as we do not consider the diversification requirement as a sufficient reason to exclude all UCITS from rules on personal transactions. We consider that there is no reason for treating government bonds differently, especially when these transactions are not exempted by the market abuse directive. |
| <b>BOX 3 Organisation, Accounting, Risk Management, IA</b>                |                                 |   |
| <b>Factors to take into account for systems, resources and procedures</b> | Retained.                       | We have not included it as such but it is either explicit in particular provisions or implicit in that all the arrangements have to be adequate to the business that they are supposed to deal with.  |

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| <b>Organisational principles</b>                     | Retained in article 3                      |  |
| <b>Record keeping procedures</b>                     | Retained in article 3 and 14.              |  |
| <b>Accounting policies and procedures</b>            | Partially retained in article 3            | We retained the general obligation to submit financial reports that reflect a true and fair view of the firm's position. Other CESR requirements seem over-prescriptive and incomplete at the same time. This does not mean that they are not adequate or that they could constitute useful guidance but that Regulation should not enter into that level of micro-management. |
| <b>Risk management policy</b>                        | Retained in Article 5.                     |  |
| <b>Business continuity</b>                           | Partially retained in article 3            | Some of what was in CESR advice is already in level 1  |
| <b>Information processing systems and procedures</b> | Retained in article 3                      |  |
| <b>Internal control mechanisms</b>                   | Retained mostly in article 3               |  |
| <b>Additional requirements</b>                       | Partially retained in articles 3, 5 and 6. | In respect of external auditing we consider that it goes beyond the level 1.   |
| <b>Risk control function</b>                         | Partially retained in Article 5            | We do not require firms to have a risk control function as we believe regulation should be flexible enough to allow the investment firms to achieve the regulatory objectives through the means they consider more adequate. Most tasks related to the risk control function are retained in article 5.  |
| <b>Internal audit function</b>                       | Retained in articles 3, 6 and 7.           |  |

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| <b>BOX 4 Outsourcing</b>  |  |  |
| <b>Application to material outsourcing only</b>                     | Retained in article 10.<br>Paragraph 2 not retained. | Paragraph 2 not retained as we think that it is more important to signal out what we are not covering than what we are covering.   |
| <b>Application to intra-group outsourcing</b>                       | Not Retained   | We do not think that it is necessary to include this as it is evident that the conditions under article 13 already oblige the IF to take into account the characteristics of the person to which the service is outsourced.  |
| <b>Arrangements not included</b>                                    | Retained in part in article 10.                      | b) does not fall under the definition.<br>c) is not necessary for the purposes of this legal text.<br>e) depositories are dealt with elsewhere   |
| <b>Effect of outsourcing on the position of the investment firm</b> | Retained in article 11                               |  |
| <b>Notification of material outsourcing to competent authority</b>  | Retained in article 12                               |  |
| <b>General obligation of due skill, care and diligence</b>          | Retained in article 12                               |  |
| <b>Specific obligations</b>   | Retained (in a general manner) in article 12         |  |
| <b>BOX 5 Record Keeping</b>   |  |  |
| <b>Minimum requirements</b>   | Not retained   | We think that the only records that, in respect of matters falling under the scope of this Directive, we can ask the IF to have are those established in the Level 1 text or the implementing legislation.   |
| <b>Specific requirements</b>  | Not retained   | We will not use the Annex. Instead, we have included a requirement for each CA to provide a list of records investment firms have to maintain. The list shall be based on a harmonized list of records established by CESR and may include additional records to those |

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|   |                                       | necessary under the Directive or the L2 measures only under restrictive conditions. We consider this approach to be important from the industry's point of view as one of the most common complaints is that IF are never certain as to what records they should keep. |
| <b>General requirements</b>                           | Retained Article 14                   |  |
| <b>Telephone orders</b>                               | Retained Article 13 (in part)         | We do not allow for a waiver of the record keeping of telephone conversations as we do not think it is justifiable (e.g. cost does not seem to be an issue).   |
| <b>Termination of authorisation</b>                   | Retained article 14                   |  |
| <b>Records of identical documents</b>                 | Retained article 14                   |  |
| <b>Records of documents sharing a common format</b>   | Not retained                          | We agree with the advice but think that these specificities do not have their place at a level 2 text.   |
| <b>BOX 6 Safeguarding of Client Assets</b>            |                                       |  |
| <b>Interpretation and scope</b>                       | Not retained                          | We believe that most of the advice in this section is either contained in L1 or is inappropriate for the L2 text (could be included in recitals)   |
| <b>Arrangements designed to protect client assets</b> | Mostly retained in articles 15        | Taking a lawful security interest or lien by a depository, should not be prevented by the legislation. However we think this is more appropriate for a recital.  |
| <b>Use of client assets</b>                           | Retained in article 18                |  |
| <b>Deposit and sub-deposit of client assets</b>       | Mostly retained in articles 16 and 17 | In article 17 we added a provision encouraging IFs to favour jurisdiction that regulate depositories. This is a  |

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| <b>Appropriate record keeping/clarity of ownership identification</b> | Mostly retained in article 15        | logical extension of CESR advice.<br>12a) excluded as it seems to prescriptive and unnecessary in view of the more general requirements.   |
| <b>Agreement with the client</b>                                      | Not retained                         | This area of this advice will be dealt with in another draft document  |
| <b>Appropriate controls</b>   | Retained in articles 3 and 15        |  |
| <b>External review of records and procedures</b>                      | Retained in article 19               |  |
|   |                                      |  |
| <b>BOX 7 Conflict of interest</b>                                     |                                      |  |
| <b>Conflicts policy</b>   | Retained Article 21                  |  |
| <b>Identification of conflicts</b>                                    | Retained Article 20 (in part) and 22 | For us it is very important that legal certainty functions. We could not imagine which other situations would give rise to conflicts of interest (especially when we have dealt with this issue in such a general manner). That is why we leave out 'at least' in the chapeau. Para 3 not retained, it could be included as guidance at Level 3. |
| <b>Content of the conflicts policy</b>                                | Retained Articles 21 and 22          | The way we have dealt with flexibility is not: "to the fullest extent practicable". With a view of adding some legal certainty to the text, we have tried to keep a detail of the different methods proposed by CESR but in a manner that makes more legal sense.  |
| <b>Inducements</b>  | Not retained                         | We will deal with inducements in a different document  |
| <b>Disclosure</b>   | Mostly Retained in article 23        |  |
|   |                                      |  |