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FCA commissions review tipped for global impact

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A review of the way fund managers pay for sellside research being conducted by the UK's financial services watchdog could have ripple effects for asset managers' global operations, consultants say.



A research paper, published this week by Edison Investment Research and Frost Consulting, predicts that any changes UK asset managers make in response to the Financial Conduct Authority's review of dealing commission rules will be rolled out across the regions in which they operate.

Frost is regarded by many in the industry as the authority on the issue of equity commissions.

Dealing commissions are what asset managers typically use to pay for services such as corporate access and investment research from banks. They are created when the buy-side trades with the sellside.

The report comes amid a sweeping review by the FCA of how investment research is paid for and how commission is spent. The regulator has been increasingly focused on conflicts of interest in the asset management industry and launched a consultation on commissions in November.

The FCA review in the UK – where asset managers manage about 12% of global AUM – is poised to have major implications for asset managers and the banks that produce investment research, the analysts say.

Neil Shah, director of research at Edison Investment Research, said: “Any asset manager who wants to be present in Europe – and Europe is a significant geography in terms of AUM - will have to look to adopt some of this regime and that is the reason it’s going to spread into other jurisdictions.”

The result of the review is expected to influence policies in US and Europe. In Europe, lawmakers are putting the finishing touches on Europe's new trading rulebook known as the Markets in Financial Instruments Directive II.

The Edison and Frost paper said ongoing global consolidation of the fund management industry was likely to result in firms adopting common systems across their international operations.

“What asset managers don’t want are multiple systems in terms of paying their brokers,” Shah said.

The paper predicts that UK fund managers will create budgets for each investment bank from which they buy research, be more selective in the services and products they purchase, and establish a more uniform way of determining what the cost of research should be.

The paper said: “Eventually we believe this is likely to evolve into a situation where each asset manager determines implicit prices they are willing to pay based on the perceived quality of the analysts/research and levels of service provided.”

Edison pointed to the rise of commission sharing agreements, or CSAs, as an example of how changes in the way that sellside research is paid for had previously spread from the UK to other markets such as the US. CSAs are accounts from which asset managers pay for research from a variety of sources beyond just investment banks.

The analysis also predicted a further reduction in research produced by the sellside and the growth of independent providers. Frost data suggest that investment banks spent \$4.6 billion on analyst costs last year, down from \$8.2 billion at the peak in 2008.

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