

## Summary – August 2016

### Key Requirements – Page 2

- Setting and assessment of research budgets – *at strategy level at the very least.*
- Client agreement of research budgets
- Regular assessment of research quality and the ability to aid the investment process
- Enhanced disclosure of research costs to clients
- Written policy on research valuation and division of research costs between clients

### Brexit – Page 3

- Zero impact on MiFID II compliance for UK firms

### Payment Mechanisms – Page 3

- Own P&L/Swedish Model/CSA-RPA
- Options 2 and 3 above require research budgeting in the best interests of clients, acquisition of Fixed Income Research, need to pay US brokers providing research and potential application of VAT.

### Research Budget Considerations/Key Questions – Page 5

- Size of research budget?
- How is it allocated internally at the asset manager?
- Who controls the budget?
- At what level of granularity should the budget be?

### Fixed Income Research – Page 6

- IA takes the view that if some asset managers are paying for fixed income research via P&L then the investment bank cannot represent that the cost of the fixed income research is “in the spread” for a client that does not pay for FI research directly. (Frost Consulting does not share this view).

### US Brokers – Page 7

- Recognition that there needs to be a solution for US brokers to take cheques for research. Suggests a possible SEC ruling as a solution.

### Broker Research Pricing/Supply – Page 8

- Suggests that asset managers should not pay the full price for research while they are assessing its usefulness. Suggest a “trial period”.
- Firms must assess all pricing models (investment banks/independent research providers) and make a business decision on how best to meet their research requirements
- Once an asset manager has made an earnest effort to ask a research provider to stop sending unsolicited research, the IA believes that the burden should then be on the provider to make sure it is not providing inducements by continuing to send it.

### Equity Order Flow – Page 9

- Depending upon CSA/RPA arrangements, order flow from EU and non-EU clients might have to be separated

### Existing CSA Balances – Page 9

- Managers should consider how to run down existing CSA balances by Jan. 2018 by refunding money to clients or transferring balances to the RPA.

## Application of VAT – Page 10

- No clarity on VAT status in the UK. Three possible outcomes:
  - a) VAT exemption for research will continue
  - b) VAT will be applied to research
  - c) A partial continuation of the VAT exemption for firms operating the CSA/RPA model.
- If option C happens, there could be different VAT outcomes for different research purchase methods.

## Assessing Research Quality – Page 11

- The IA believes that if research meets the FCA COBS 11.6.3R definition of “substantive”, then it would meet the quality assessment standard.

## Disclosure of Research Costs to Clients – Page 11

- *Prior to onboarding new clients*, asset managers should give clients a basis point of AUM figure for the research charge for the fund.
- For managers operating RPAs *actual* per client total research costs must be communicated annually (at a minimum).

## Client Access to Research Spending Detail – Page 12

- Upon request clients have a right to a detailed breakdown of research spending.
- This can be satisfied by **a strategy level** summary of:
  - a) Amounts paid per provider
  - b) Benefits and services received by provider
  - c) How the total amount compares to the research budget

## Client Agreement of Research Budget – Page 12

- Clients must agree both the quantum of the research charge and the frequency with which it will be deducted. This is a one-off event, and can only be changed by notification.

## Legal Status of Monies in an RPA – Page 12

- MiFID II Delegated Acts do not define the status of monies held in RPAs.
- IA does not consider this “client money” under CASS.
- However, if the RPA is administered by a broker it should be the asset manager’s money. This will likely require a re-papering of current agreements.

## RPAs – Pages 12/13

- RPA must be controlled by the asset manager and is their responsibility.
- RPA may delegate administration of the RPA to a third party

## When Not All Clients Agree To Pay The Research Charge

- Options:
  - a) Top up the RPA from the firm’s P&L to cover those clients not paying for research
  - b) Decline business from clients unwilling to pay the research charge

## Research Charge Methodology – Page 14

- Charge is likely to be determined on a range of inputs including, but not limited to, AUM, strategy, fund type etc.

## Allocating Research Costs to Clients – Pages 14/15

- Should be part of terms of business. This should state that 3<sup>rd</sup> party research will be used in a given strategy, but that the research may be used in other strategies as well. (This results in economies of scale).

- The IA considers that it is more efficient to let investment teams share research and allocate costs accordingly.
- “A robust research budget, at a strategy level allocated to fund level via AUM would represent a baseline starting approach for research cost allocation mechanism.”

#### RPA Operation – Page 16

- If the RPA is a separate account, it will require re-papering with brokers and outsourced aggregators.
- RPAs can be funded by CSAs

#### Treatment of Aggregated Trades – Pages 16/17

- Trades done on behalf of multiple funds, some of which might have achieved their research budget and are therefore trading ex-only together with funds that have not reached the ex-only stage, will require an industry solution.

#### Conclusion – Page 17

- The IA calls upon the FCA and ESMA to develop a harmonized approach to research funding.

[www.frostconsulting.co.uk](http://www.frostconsulting.co.uk)

[www.frostrb.com](http://www.frostrb.com)

For more information please contact:

*Neil Scarth*

*UK cell +(44) 774 865 2356*

[neil.scarth@frostconsulting.co.uk](mailto:neil.scarth@frostconsulting.co.uk)

*Thomas Auschill*

*German Mobile +(49) 0170 936 3752*

[thomas.auschill@frostconsulting.co.uk](mailto:thomas.auschill@frostconsulting.co.uk)

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