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By email to **CARconsultation@centralbank.ie**

31st October 2013

CAR Consultation
Securities and Markets Supervision Division
Central Bank of Ireland
Block D, Iveagh Court
Harcourt Road
Dublin 2

Re: Consultation Paper CP 71- Client Asset Regulation and Guidance

Dear Sir/Madam,

We welcome the opportunity to provide you with comments in respect of CP71.

Whilst we are fully supportive of the initiative to enhance the current Client Asset regime, we believe that there are a number of important areas that require clarification, many of which were referred to in the joint industry consultation workshops and are restated herein. It is our opinion that the proposals in their current form do not address all of the stated objectives of this process.
We have highlighted these points below in respect of J&E Davy. We have not provided comments for Fund Service Providers. For ease of reference, we have repeated the questions and noted any comments underneath.

We have also participated in a separate Group submission with other stockbroking firms, representing shared views and comments and this will be submitted under separate cover. We trust that this submission letter provides some valuable input to this consultative process. We intend to seek a meeting to discuss the content of this submission in more detail with you.

Yours sincerely

pp

Ger Knowles
Head of Regulation and Compliance
J&E Davy

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CAR Consultation Paper- Questions & Answers

Q1. Do you agree that the Client Asset Core Principles encompass the key fundamental principles in protecting and safeguarding client assets? If not, please explain why.

While at a high level we agree, we would like to express our concerns that the new Client Asset Requirements ('CAR') still do not fully address the problems uncovered by CHC, particularly in relation to unregulated products (e.g. property, etc.). We believe that the new rules do not create sufficient safeguards to help protect all categories of client assets, despite various external reviews and reports.

In terms of specific examples, Davy considers transactions in private equity, exempt unit trusts and some direct investments in property which are structured as shares or notes, to be in scope of MiFID and CAR, although many of our peers disagree.

We are of the opinion that the new proposals have not fully addressed the apparent gap within industry on how firms choose to treat transactions in "regulated" and "unregulated" products. Davy has a very comprehensive MiFID authorisation across investment and ancillary services, financial instruments and IIA investment instruments. Based on our business model, nearly all assets are clients assets and afforded such protections; (the exceptions would include a small number of clients that choose to hold assets in their own name or unregulated investments such as direct investments in property that don't meet the definition of a financial instrument in MiFID). Therefore, CAR impacts on our entire business.

However, different firms may have a different application of MiFID and CAR, excluding some financial instruments from scope of same. For example, some firms could interpret a transaction in a financial instrument to be "unregulated," since the asset itself operates in an unregulated environment.

Ultimately the Central Bank should provide clarity in this regard so that the assets within scope of CAR are not open to wide interpretation but instead are consistently applied across all firms authorised to hold client assets.

Q2. Do you agree with the proposed wider scope in respect of 'client funds'? If not, please explain why.

Yes, we do agree with the proposed wider scope in respect of 'client funds.' Our view is that all cash whether for regulated or unregulated investments, such as direct property investments, should be classified as client assets.

Davy already applies this principle to its business.

Q3. Do you agree with the approach proposed to deal with instances where client funds are received but the firm has not identified the client or the necessary client paperwork is not complete? If not, please explain why.

We believe that the rule should permit the firm to hold unresolved client funds longer than two business days. The current rule of five business days is generally sufficient to positively identify the source of funds paid directly into the bank account.

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Based on our experience of replies from credit institutions, we believe that the two business day rule would result in the return of a substantial number of bank receipts which is likely to result in considerable client inconvenience.

In relation to pension contributions and accounts, substantially more information is required to match client assets internally and externally with third parties including the nature of the contribution (i.e. whether it is an Employer or Employee contribution), if the contribution is within maximum contribution limits or confirming pension transfer details, etc. In particular, since pension contributions are often submitted close to the tax year-end, a shortening of this holding period would cause significant client dissatisfaction with any returned funds and would result in clients missing the tax filing deadline for contributing to their pensions.

Q4. Do you agree that the Regulations should apply to funds that have been lodged into a Collection Account? If not, please explain why.

Not Applicable.

Q5. Do you agree for the purpose of segregating client assets and determining which clients are impacted if a third party fails, a firm should be able to identify where each individual client's assets are held? If not please explain why.

We agree with the principle of accounting segregation for Client Asset Accounts and our policy is to operate individually designated call and fixed deposit accounts with credit institutions for clients. This ensures that there is complete transparency in respect of where client funds are deposited. For settlement monies we also operate pooled accounts with selected credit institutions which are subject to regular credit assessments in line with CAR and we believe that clients are adequately protected against the failure of third parties through this process.

Beyond this there are practical issues in identifying where each individual clients funds/assets are held in pooled Client Asset settlement accounts at a particular point in time in the settlement cycle.

Q6. Do you agree that a client's required margin should be better protected under the client asset regime? If not, please explain why. If you agree, please outline how this could be best achieved.

Yes we agree.

Q7. Do you agree that the records should be retained for six years? If not please explain why.

Yes we agree.

Q8. Do you agree with the new approach proposed in respect of Facilities Letters and Confirmations? If not please explain why.

We have some questions and comments on the Facilities Letters and Confirmations, as outlined below:

- Will the existing CAR letters with our counterparties be grandfathered into the new CAR regime? Will the Facilities Letters and Confirmations therefore be applicable only for new counterparties?
- We would like further clarification on the written Confirmations and what is envisaged by Regulation 3(9).

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- In cases where assets are held directly (e.g. directly held with a registrar or reflected on CREST), we assume the Facilities Letter will not be required in this circumstance. We believe the wording of requirement (g) is unclear as drafted so we suggest the wording is changed.
- Sometimes a custodian (e.g. Bank of New York Mellon / BNP) may unilaterally open a Client Asset Settlement Account to settle a particular trade. The firm only becomes aware of the existence of this new account when a statement is produced the following day. We would then follow-up immediately with a revised CAR letter which references the new account. This is an industry-wide issue.
- Foreign counterparties, in particular, may be reluctant to provide the firm with Facilities Letters and thus we will be forced to disadvantage clients by limiting their investment opportunities and/or the counterparties we can hold client assets with.

Some counterparties will not provide account numbers until such time as the account is actually opened. It may not always be possible to list account numbers prior to an investment on the Facilities Letter.

Q9. Do you agree that in the interest of protecting client assets, where a third party has not designated a client asset account/Collection Account as requested by the firm, these client assets should be withdrawn from the third party without delay? If not, please explain why.

While we agree conceptually, from a practical perspective we have some concerns.

In terms of the assurances from third parties, it is possible that a counterparty may incorrectly designate an account on its internal systems through clerical error despite having been in receipt of our Client Asset Letter and returning a signed copy of same. This would be through no fault of the investment firm and our clients should not be penalised as a result. In such cases, when the firm learns of the error, we must contact the counterparty and wait for it to amend the title on the account on its internal systems as soon as possible to comply with our requirements.

In terms of Davy's business model, there are different service level agreements (e.g. execution only, advisory and discretionary), allowing clients to trade in different manners with the firm. While Davy may make available a very large investment universe to our clients across the board, clients are also able to invest in bespoke investments on his or her own initiative. An execution only client can instruct Davy to trade in a specific financial instrument for his own trading account and he may be the only Davy client invested in this asset and bears the full investment risk. Where there is a problem dealing with the third party and receiving timely CAR assurances for a single transaction, investment firms may be forced to restrict clients' investment opportunities from the outset due to this requirement, which would be to clients' detriment. This scenario can be particularly problematic for certain transactions, such as private placements, where the window for investment is very short. It would not be best practice to contract with a firm during a private placement and then subsequently seek to unwind the investment.

Similarly, when Davy makes a particular product available to clients, after the necessary due diligence has been conducted, the firm will enter into a contractual agreement with the counterparty (i.e. fund house or private equity firm, etc.) on behalf of clients and usually the firm is committed to invest a certain level of capital for a specific length of time, known as the commitment period. During this period, the firm cannot exit the investment during the lifetime of the fund and any attempt to do so would be in breach of contract. Furthermore, for many of these investments, there is no "client asset account" or "account number" as such since these assets are held directly with registrars etc. and this matter often causes confusion with our counterparties prior to any

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investment. It is difficult to understand how this requirement would apply and we believe that it may therefore reduce investment opportunities in these asset classes for our clients.

Q10. Do you agree with the approach for reconciling client asset accounts that hold client funds? If not please explain why. If there are other types of accounts that do not readily conform to the frequency of reconciliations cited above, please provide details of same.

Currently investment firms are permitted 10 business days to reconcile non-call client deposit accounts i.e. term deposits with infrequent transactions. Rather than the proposal of 1 business day, we believe that 5 business days is a more realistic timeframe to ensure that the required reconciliation data is made available to complete the reconciliation.

Q11. Do you agree that client financial instruments should be reconciled at least monthly or should the reconciliation be performed in a lesser time period? If so, please explain why.

Yes we do agree that client financial instruments should be reconciled at least monthly.

Q12. Do you agree with the time allocation of ten days to complete these reconciliations or should it be performed in a lesser time period? If so, please explain why.

Yes, we agree with the time allocation of ten business days to complete these reconciliations.

Q13 Do you agree that an investment firm should immediately make good or provide the equivalent of any shortfall in client financial instruments? If not, please explain why.

No, we do not agree that an investment firm should immediately make good or provide the equivalent of ***any shortfall*** in client financial instruments for the reasons outlined below.

First we are confused by this new guidance and its full implications for an investment firm. In the current documentation, there is no reference to this in the draft Statutory Instrument, but it is only mentioned briefly in the Guidance and Consultation Paper. How would an investment firm determine a shortfall in client financial instruments? How would the top-up happen? Would it become evident as part of the monthly reconciliations? Or instead would it be derived from a client financial instrument "calculation" similar to the daily calculation? All these questions would first need to be clarified.

If the guidance remains as currently drafted, the process of "topping up" client financial instruments by the firm would be a hugely onerous burden for any investment firm with little added benefit / protection to clients. If we were to estimate shortfalls in client financial instruments based on our current monthly reconciliation process, we note that the overwhelming majority of differences are due to timing where we are waiting on a third party to settle a trade or deliver stock. Delays can be caused by illiquidity in an electronic stock, counterparty not matching our trading or transfer instructions, trading in private placements off exchange, transferring certificated stocks etc., all of which take time to resolve. These delays are outside of our control and therefore so are the timeframes of the shortfall.

This guidance to make "good" clients investments could limit firms to trading only in highly liquid stocks and significantly disadvantage clients.

If it is intended to relate to a third party insolvency scenario, then the guidance wording is currently unclear and it must be re-drafted for this specific purpose.

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Q14. Do you agree that a Collection Account should be reconciled each time a transaction occurs on that account? If not, please explain why.

Not Applicable.

Q15. Do you agree that it is appropriate for a firm to report material reconciling items with the level of materiality determined by the firm? If not, please explain why.

Yes we agree, as the level of materiality may be different in each firm.

Q16. Do you agree with the components of an investment firm's Client Money Requirement and Client Money Resource? If not, please explain why.

We believe it should be optional for firms as to whether the cashbooks or counterparty statements are used as the source document (i.e. internal or external) as the appropriate adjustments will always be made to correctly reflect the status of reconciling items in the calculation of the Client Money Requirement.

Q17. Do you agree with the Central Bank's approach to the computation of the Client Money Requirement and Client Money Resource for FSPs? If not, please explain why.

Not Applicable.

Q18. Do you agree that a firm's Client Money Resource should only contain what it is required to hold for its clients on a given day? If not, please explain why.

No we disagree in relation to the maintenance of a buffer. As daily calculations are conducted on the following business day, to avoid shortfalls we believe that a firm should be permitted to operate a buffer if it deems it prudent to do so and the rationale and measurement criteria are recorded in the CAMP document.

Q19. Do you agree that the reporting of an investment firm's Client Money Resource shortfall should be investment firm specific based on its materiality appetite? If not please explain why.

Yes we agree, as the level of materiality will be different in each firm.

Q20. Do you agree that a statement should be provided on an annual basis or should it provided on a more regular basis?

An annual statement will be sufficient.

Q21. Do you agree that a) to g) above will provide clients with sufficient information regarding their holdings? If not please explain why, providing details of additional information which should be included.

In terms of the information listed, we have one concern as outlined below. Regulation 6(16)(a) requires the firm to provide clients with details of financial instruments and the jurisdiction where such assets are held. As discussed during the Joint Industry Working Groups last year, the jurisdiction where assets are "held" can be difficult to ascertain at a point in time due to standard industry

practices such as the use of sub-custodians. When an investment firm enters into a custody agreement with its global custodian, it is clearly outlined in the agreement that the custodian will rely on the services of sub-custodians to hold assets in other jurisdictions. While the custodian will conduct regular due diligence on its sub-custodians and provide assurances to investment firms in this regard, the custodian does not and is not obliged to provide real-time data on the exact location of all assets held in global custody. Therefore to comply with the letter of this Regulation (although not the spirit), investment firms will state the location of its custodian rather than "looking through" the global custody arrangement to the actual location of where assets may be held at that point in time. For example, if a financial instrument is held with our global custodian BNY Mellon in the UK, the firm would indicate "UK" for the jurisdiction on the annual statement, although the asset may actually be held in Japan with a sub-custodian. As such, we feel that the jurisdiction on the statement could be misleading and provide false assurances to clients in the case of a default of a custodian.

Additionally, it can be very difficult to classify certain financial instruments that trade in multiple jurisdictions. For example:

- Arytza is a Swiss stock traded in Crest and Crest stocks can be held in Irish, UK and other registrars. Davy may choose one jurisdiction for this stock while another investment firm may choose an alternative location. If this requirement remains, we ask that the Central Bank provides clarity as to what criteria should be used to determine jurisdiction.

If this Regulation is implemented in full, we would require a longer lead-in time to:

(i) Negotiate and amend our existing custody agreements with our custodians;
(ii) Identify the jurisdiction of all our stocks in-line with industry guidance from the Central Bank; and
(iii) Enhance our systems to record and report this information in a timely manner.

Q22. Do you agree that a Fund Service Provider should issue a receipt to the client? If not, please explain why and put forward an alternative approach that will provide confirmation to a client that his/her money is deposited in a Collection Account.

Not Applicable.

Q23. Do you agree that an investment firm should seek prior written consent from its client in respect of the circumstances listed in a) to h) above? If not please explain why, providing details of additional circumstances which should be included.

Yes, we agree. In terms of existing clients, when the new Regulations are implemented will a retrospective consent be required for such clients?

Q24. Do you agree that a FSP should obtain prior written consent from a client in respect of the circumstances listed in a) to c) above and with the medium used to obtain this consent? If not please explain why, providing details of additional circumstances which should be included.

Not Applicable.

Q25. Do you agree that the CAKID will better inform the client with a greater understanding providing information in clear plain English that will equip the client to comprehend where and how his/her assets are held when deposited with a firm? If not please explain why.

Yes, we agree.

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Q26. Do you agree with the need to provide the CAKID to both existing and new clients distinguishing clients of an investment firm and a Fund Service Provider as outlined above? If not please explain why.

No we disagree. Firms should not be obliged to issue the CAKID to existing clients but only to new clients at account set-up. Each firm can disclose its CAKID on its website.

Q27. Do you agree with appointing a person to the role of CAOR which will be a pre-approved controlled function? If not, please explain why?

Yes, we agree.

Q28. Do you agree with the responsibilities of the Client Asset Oversight Officer as provided for in a) to g) above? If not, please explain why, providing details of additional responsibilities which should be included.

Yes, we agree.

Q29. Do you agree with the purpose of the CAMP and the minimum that should be included in this document? If not, please explain why, providing details of additional records which should be included.

Yes, we agree.

Q30. Do you agree that Regulation 8.(3) provides for what should be included in a CAE? If not please explain why.

We have reservations that the firm's auditors may have difficulties receiving external confirmations from counterparties and positive confirmations from clients in a timely manner, which are both outside our control. Will clients understand this process and will there be standardised communications across auditors? We would like to minimise client confusion as much as possible. Lastly, what consequence would arise for the firm from nil responses from counterparties and clients?

Q31. Should this review be carried out more frequent than annually? If so, please explain why.

We believe an annual review will be sufficient.

Q32. Do you agree with the type of assessment that should be carried out on the firm's initial CAMP by an independent external expert?

No, we believe that the firm's auditors are best placed to carry out the firm's initial CAMP assessment.

Q33. Do you agree that 3 months is sufficient time for a firm to obtain an assessment of the CAMP from an independent external expert? If not, please explain why.

No, we do not agree that three months is sufficient for the firm to obtain an assessment of the CAMP for an independent external party, in part because of the firm would be relying on a third party to meet this deadline. First the firm must find and engage the services of this expert, which may be difficult to do considering all that all firms that hold client assets will be required to partake in this once-off exercise simultaneously. The resources of the audit firms will be stretched thin to

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accommodate all firms. In addition, the first review of the new CAMP documents may require consultation between the expert and the firm and subsequent amendments which can lengthen the process further. In the interest of ensuring that the new CAMP process is robust and comprehensive, we ask for more time.