21 May 2019

The AMF publishes a summary of its thematic review of portfolio management practices

In 2018, the Autorité des Marchés Financiers (AMF) carried out two rounds of five thematic inspections of investment service providers, other than asset management firms (9 credit institutions and 1 investment firm authorised to manage portfolios on behalf of third parties). On the basis of its observations, it has prepared a list of good and poor practices and has issued reminders with respect to the rules applicable thereto.

Last year, as part of its #Supervision2022 strategy, the AMF carried out two rounds of "SPOT" (Supervision des Pratiques Opérationnelle et Thématique - operational and thematic supervision of practices) inspections of firms providing portfolio management services (discretionary mandates).

These inspections focused on:

- The compliance of such discretionary mandates regarding: the purpose of the mandate, management objectives, authorised financial instruments, transmission of regular information to clients, withdrawals and liquidity risk, duration, modification and cancellation of mandates, conflicts of interest, complaints, mediation and confidentiality.
- The fees charged for providing portfolio management services: pricing policy, overall costs, entry fees, transaction fees, portfolio turnover ratios, conflicts of interest and information given to clients on costs and fees.

In its summary, the AMF sets out the applicable rules, as well as the good and poor practices that were observed during the course of its inspections.

The AMF identified the following good practices:

- State clearly and explicitly in contractual documents or fee schedules that the cash reserve of the portfolios under management is excluded from the asset base for calculating custody fees.
- Make it easier for clients to access and understand information, particularly concerning management fees, from the moment the mandate is signed. The mandate should be set out in a single, comprehensive document and clients should be explicitly informed when information is updated.
- Implement a pricing policy that allows the firm to generate most of their revenues from portfolio management fees without an incentive to increase portfolio turnover in order to charge transaction fees. This aims at reducing the potential conflicts of interest between the firm and its clients.
- Identify any potential conflict of interest associated with unjustified portfolio turnover ratio (and consequently, generate additional transaction fees for clients) and implement frequent first and second-level checks of portfolio turnover ratios accordingly.
- Among the potential conflicts of interest, clearly identify those linked to the share of a group's own funds within clients' portfolios and manage such conflicts of interest by implementing an appropriate fund selection policy for the investment universe.
- Apply no entry fees for collective investment undertakings (CIUs) in which clients' portfolios investments are made.
- Exempt from custody fees investments made in a group's own investment funds.

However, poor practices were also noted, including the following examples:

- Disperse information relating to portfolio management services (particularly that relating to fees) in many separate documents.
- Fail to state explicitly the investment universe or allocations per asset class, including any thresholds that could be reached in exceptional market conditions.
- Fail to inform clients of the consequences of making frequent and/or large withdrawals from their portfolios.

- Within contractual documents or fee schedules, display quarterly rates for management fees exclusive of taxes, without providing information on the equivalent annual rates inclusive of taxes.

- When entry fees are charged by firms for investments in CIUs selected by the portfolio manager, fail to display in their fee schedule the rates of such fees applicable at the time investments in such CIUs are made.

- Fail to provide clients with explicit information regarding changes to the fees policy (for example, fail to informing clients that such fees have been changed and only making this information available on the firm's website).

Finally, the AMF reaffirms that the obligation to serve the clients' best interests entails not making them bear the cost of internal organisational decisions made by the service provider. This particularly applies to costs incurred as a result of bringing portfolios in line with management strategies that are being streamlined within a firm. It also states that investment firms must provide their clients with an illustration setting out the cumulative effect of costs on their returns on an ex-ante and ex-post basis.

The AMF reminds firms that when providing portfolio management services to clients, they must prepare a periodic statement which shall include information pertaining to the total amount of fees and charges paid over the reporting period, itemising at least total management fees and total costs associated with execution.

Upon completion of the SPOT inspections, the AMF has sent the inspected firms follow-up letters requesting that they rectify all observed instances of non-compliance with the rules applicable to portfolio management.

About the AMF
The AMF is an independent public authority responsible for ensuring that savings invested in financial products are protected, that investors are provided with adequate information and supervising the orderly operation of markets. Visit our website https://ww.amf-france.org

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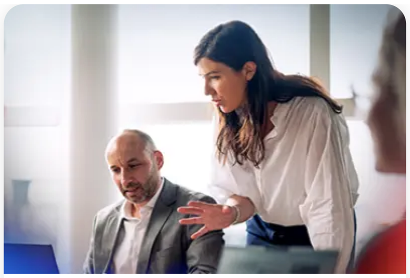

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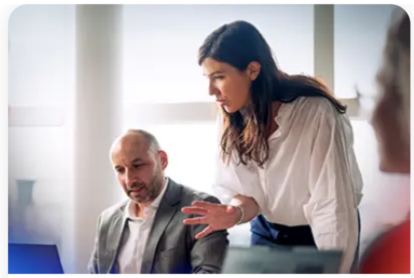

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