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SUMMARY OF SPOT INSPECTIONS ON PORTFOLIO MANAGEMENT

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INTRODUCTION

As part of its new Supervision#2022 strategy, the AMF announced at the beginning of 2018 its intention to conduct short, theme-based inspections known as "SPOT" (*Supervision des Pratiques Opérationnelle et Thématique* – operational and thematic supervision of practices) inspections, as well as its willingness to share the lessons learned from these exercises. Today, the AMF publishes the summary of these short inspections carried out in 2018 on ten investment services providers other than portfolio management companies (nine credit institutions and one investment firm authorised in particular to provide portfolio management services for third parties) on the themes of compliance of discretionary mandates and fees in portfolio management.

These inspections covered both the application of the rules imposed by European Directive 2004/39/EC of 21 April 2004 on Markets in Financial Instruments, which came into force on 1 November 2007 (hereinafter referred to as "MiFID 1") and certain changes resulting from European Directive 2014/65/EU of 15 May 2014 on Markets in Financial Instruments, which came into force on 3 January 2018, and Commission Regulation (EU) No 2017/565 of 25 April 2016 amending Directive 2014/65/EU (hereinafter referred to as "MiFID 2").

The purpose of this document is to provide a summary of all SPOT inspections on these themes relating to portfolio management and to shed light on the practices observed among the investment service providers inspected, the difficulties they encounter and the possible ways in which they can be supported. It is neither a position nor a recommendation. The AMF will review the positions-recommendations 2007-21 (on professional obligations towards individual clients in respect of portfolio management for third parties) and 2013-10 (on remuneration and benefits received in connection with the marketing and portfolio management of financial instruments).

1. SCOPE AND APPROACH OF THE INSPECTIONS CARRIED OUT IN 2018

Two SPOT inspection campaigns were carried out on the theme of portfolio management. These missions, which involved 10 institutions, focused on the "compliance of discretionary mandates" and "fees in portfolio management". Three other inspections, in a "traditional" format, were also carried out in 2018 on the theme of portfolio management. Information is provided in this summary for comparison purposes.

1.1. COMPLIANCE OF DISCRETIONARY MANDATES

These inspections on the compliance of the mandates were carried out jointly with four credit institutions and one investment firm, including two subsidiaries of French banking groups, two independent French institutions and one French subsidiary of a European banking group.

These inspections covered the following themes:

- ☐ Formalities and purpose of the mandate and nature of the service provided;
- ☐ Management objectives and authorised financial instruments;
- ☐ Periodic disclosures and information on management fees;
- ☐ Duration, modification and termination of the mandate;

- Withdrawals in cash or securities and liquidity risk;
- Other mentions: conflicts of interest, complaints/mediation and professional secrecy.

For each of the five institutions inspected, the inspection analysed a sample of 20 mandates selected from among the mandates of individuals directly managed by the institution, entered into or amended between 2016 and 2017 and representative of the institution's management profiles. The changes resulting from the entry into force of MiFID 2 (particularly in terms of information on fees) were also analysed with the new MiFID 2 discretionary mandate templates.

1.2. FEES IN PORTFOLIO MANAGEMENT

Five SPOT inspections were carried out on the theme of fees in portfolio management. The scope of these inspections covered the management activity outside life insurance. The objective of these controls was to analyse in particular the practices observed among these institutions in relation to the following points:

- The pricing policy applicable to portfolio management.
- The overall level of fees for the managed portfolios.
- The application of entry fees on subscription of units of collective investment undertakings (CIUs).
- Transaction fees and portfolio turnover ratios.
- The place of "in-house" funds within managed portfolios and the identification of potential conflicts of interest.
- The end of CIU management fee rebates (since 3 January 2018).
- Information provided to clients on costs and charges.

2. MAIN LESSONS LEARNED FROM INSPECTIONS

SUMMARY

Compliance of Discretionary Mandates

Among the good practices observed, one service provider adopted a new unique discretionary mandate template that brings together all the information relating to portfolio management that is relevant to the client.

The poor practices observed were:

- Splitting the information relating to portfolio management across several documents:
  - Not limiting the number of annexes to the discretionary mandate.
  - Separating the body of the discretionary mandate from its annexes, especially without listing or explicitly naming the annexes in the body of the discretionary mandate and without initialling or signing them.
- Not explicitly mentioning the investment universe and the allocations by asset class, including the limits (high or low) that may be reached in exceptional market conditions, which may justify the

agent temporarily deviating (in the interests of the client) from the predefined allocations in the discretionary mandate.

- Not informing the client about the consequences of frequent and/or significant withdrawals, including:

  - Not mentioning that they may deconstruct the managed account and thus make it necessary to profile the account again in accordance with the management profile defined in the discretionary mandate.

  - Only mentioning the client's total liability in the event of frequent and/or significant withdrawals of securities and/or cash or, conversely, the agent's disclaimer of any liability in the event of frequent and/or significant withdrawals of securities and/or cash.

☐ **Fees in Portfolio management**

The good practices observed include:

- Implementing a pricing policy that allows the service provider to generate most of its income 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 client and his or her agent.
- Stating clearly and explicitly in contractual documents or fee schedules that the basis for calculating custody fees excludes cash from the portfolios entrusted to its management.
- Exempting investments in the group's investment funds from custody fees.
- Not charging entry fees on CIUs as part of portfolio management.
- Identifying any potential conflicts of interest associated with unjustified portfolio turnover (and consequently generate additional transaction fees for the client) and implement frequent first and second-level checks of portfolio turnover ratios accordingly.
- Among the potential conflicts of interest, clearly identifying those linked to the share of a group's own funds within clients' portfolios and managing this conflict of interest by implementing an appropriate fund selection policy for the management universe.
- Facilitating the client's access to and understanding of the information, in particular with regard to management fees, as soon as the discretionary mandate is signed and explicitly informing the client of any updates to this information.

The poor practices observed include:

- Including quarterly and pre-tax fee rates in the contract documents or fee schedule without indicating an equivalent annual rate and a rate inclusive of all taxes.
- When entry fees are charged by the manager on the CIUs selected in the mandate, not indicating in its fee schedule the rates actually applied on subscription of these CIUs.
- Splitting information on fees across several documents: the discretionary mandate, financial instrument account agreement, general and/or specific conditions, and fee schedule or brochure.
- Not explicitly informing the client of any updates to the information on management fees (for example, not informing the client that fees have been updated when the update is only available on the institution's website).

3. COMPLIANCE OF DISCRETIONARY MANDATES

Certain provisions of the former version of the AMF General Regulation (relating to retail clients), under which the AMF position-recommendation 2007-21 was adopted, no longer appear in versions after 3 January 2018. However, AMF Instruction 2018-11, applicable since 23 October 2018 and based on Article 314-11 of the AMF General Regulation in force since 3 January 2018, has incorporated most of these former provisions of the General Regulation to provide guidelines on the content of discretionary mandates for retail clients. This summary document identifies good and poor practices observed in terms of compliance of discretionary mandates, taking into account these regulatory changes.

3.1. FORMALITIES AND PURPOSE OF THE MANDATE AND NATURE OF THE SERVICE PROVIDED

Generally speaking, client record-keeping was insufficient in terms of the documents in the client files: discretionary mandate, general and specific conditions, financial instrument account agreement, and fee brochure or schedule.

Only one of the five institutions had complete, standardised documentation. In this case, all documents were included in the client files and were duly dated and signed by the client and, where applicable, by the agent too.

For the other four establishments, the following main anomalies were noted:

- mandates not signed by the client and/or the agent;
- mandates referring to information on the website that has not been archived, which prevents the institution from tracking the availability of this information to its clients;
- annexes to the mandate not mentioned in the body of the mandate, missing, not initialled or unsigned;
- general conditions of the mandate not signed by the client.

The inspection team noted that the shortcomings are particularly striking when the information relating to portfolio management is split across several documents and/or annexes. In this case, there are multiple operational risks: missing or unsigned annexes, references to unsigned documents or links to web pages that have been deleted or have not been updated, etc.
For one institution, the previous discretionary mandate templates (MiFID 1) include, as a preamble, the name and address of the client with whom the agreement is entered into as well as the identity of the agent. However, these templates do not include a reference to the client's resident status. In this respect, the institution has corrected its new discretionary mandate templates under MiFID 2.

For the other two institutions, the MiFID 1 and MiFID 2 mandates do not warrant any particular comments.

Good practice:

- Presenting complete, standardised contractual documentation.

Poor practices:

- Splitting the information relating to portfolio management across several documents.
- Not limiting the number of annexes to the mandate.
- Separating the body of the mandate from its annexes, especially without listing or explicitly naming the annexes in the body of the discretionary mandate and without initialling or signing them.

These practices did not comply with the provisions of former Article 314-59 of the AMF General Regulation applicable until 3 January 2018 and substantially incorporated by AMF Instruction 2018-11 published on 23 October 2018, which specifies Article 314-11 of the AMF General Regulation.

3.2. MANAGEMENT OBJECTIVES, AUTHORISED FINANCIAL INSTRUMENTS AND RISK INDICATOR

For one institution, an article of the mandate ("Management Objectives") refers to an annex entitled "Management Strategy" for the definition of the management objectives. The mandate states that: "To protect the Client's interests as far as possible and depending on market conditions, the Agent reserves the right to go below the minimum investment in shares stipulated by the chosen management strategy". However, these thresholds, which may, in exceptional market conditions, fall below the minimum levels set out in the discretionary mandate, are not specified. This may be similar to "discretionary" management, but without limiting the latitude accorded to the investment service provider (i.e. the agent). This applies to the MiFID 1 and MiFID 2 discretionary mandates.

Regarding specifically authorised transactions, another article of the mandate invites the client to tick an "Express Agreement" box that appears at the end of the mandate. However, this is not particularly easy to understand because it only appears at the end of the mandate and not in the paragraph that mentions it. In addition, this box creates confusion between the client's overall agreement on the terms of the mandate and the client's express agreement to acquire a specific category of financial instruments. This applies to the MiFID 1 and MiFID 2 discretionary mandates.

For a second institution, in the former MiFID 1 discretionary mandate templates, the breakdown by asset class for the various management objectives is not defined by ranges expressed as percentages, for example. It is therefore impossible for the client to ensure that the management strategy for the "prudent" mandate specifies a maximum exposure to equities of 30%.

With regard to specifically authorised transactions, the three former MiFID 1 discretionary mandate templates do not mention the possibility for the agent to subscribe to or invest in collective investments managed by the portfolio management company or a related company or in financial securities issued by a group company. The institution has corrected its new MiFID 2 discretionary mandate templates.

With regard to the Synthetic Risk and Reward Indicator (SRRI) within the meaning of recommendation 2.2 of AMF Position-Recommendation 2007-21, only one institution does not mention it in its new MiFID 2 discretionary mandate template. According to this institution, "this indicator cannot be included in the discretionary mandates themselves because it changes over time". However, this risk/reward profile is included in its quarterly management reports so that, according to the institution, "clients are regularly informed in writing of changes in their risk profile".

Furthermore, during another "traditional" inspection, it was found that discretionary mandates did not include risk indicators for management profiles before January 2017 for natural persons and before June 2018 for legal entities.

For the other three institutions, the MiFID 1 and MiFID 2 discretionary mandates do not warrant any particular comments.

Poor practice:

- Failing to mention the investment universe and the allocations by asset class, including the limits (high or low) that may be reached in exceptional market conditions, which may justify the agent temporarily deviating (in the interests of the client) from the predefined allocations.

3.3. PERIODIC DISCLOSURES TO THE CLIENT

Regarding periodic disclosures sent to the client, the former MiFID 1 management templates of four institutions inspected comply with the regulations and provide for a periodic report (i.e. a management report) to be sent to the client every six months, or quarterly at the client's request, or annually if the client chooses to receive information on the transactions carried out under his/her mandate, transaction by transaction.

However, for one institution, 12 discretionary mandates (out of the 20 analysed) did not indicate that the periodic statement can be sent quarterly at the client's request. In addition, in two of the 20 discretionary mandates analysed authorising transactions with leverage, the mandate did not provide for a periodic statement to be sent to the client at least monthly because of the nature of the transactions. **These practices did not comply with the provisions of former Article 314-95 of the AMF General Regulation.**

Since the entry into force of the provisions resulting from MiFID 2, the regulations now provide for a periodic statement to be sent to the client on a quarterly basis, except in the cases specified in Article 60.3 of the Delegated Regulation (EU) 2017/565.

The new MiFID 2 management templates of three institutions inspected comply with the new regulations and therefore provide for a periodic report to be sent to the client on a quarterly basis going forward (in the absence of leverage products).

However, for one institution, one of the new MiFID 2 discretionary mandate templates still provides for a half-yearly, rather than a quarterly, periodic report to be sent to the client. For the last institution, the new MiFID 2 discretionary mandate template does not mention that the periodic statement is sent annually if the client chooses to receive information on the transactions carried out, transaction by transaction.

3.4. DURATION, MODIFICATION AND TERMINATION OF THE MANDATE

For the five institutions inspected, the former MiFID 1 discretionary mandate templates do not explicitly mention that the client will manage his/her own portfolio on the effective date of termination of the discretionary mandate, unless he/she appoints another agent.

The new MiFID 2 discretionary mandate templates for three institutions included this statement.

3.5. WITHDRAWALS IN CASH OR SECURITIES AND LIQUIDITY RISK

For the five institutions inspected, the former MiFID 1 mandate templates do not indicate the consequences that may result from withdrawals of financial instruments or cash, and in particular the possible tax consequences and difficulties that the client could experience in achieving the management objective defined in the mandate.

For three of them, the new MiFID 2 discretionary mandate templates have not been corrected, or have been insufficiently corrected, in this respect. In addition, two of these institutions use wording such as "The Agent may not be held liable if the Client has made significant and/or frequent withdrawals that have not been taken into account in the management choices of this agreement". However, the client has the option of withdrawing financial instruments or cash, and the agent remains responsible, as part of its best endeavours obligation, for the management of the portfolio. The existence of such a clause without specifying the possible consequences of such withdrawals does not therefore appear to be sufficient.

Another institution correctly mentioned the consequences of withdrawals in its new MiFID 2 discretionary mandate templates, and one institution did not mention them at all.

Furthermore, the mandate does not draw the client's attention to the illiquid nature, where appropriate, of the financial instruments that his/her portfolio may be invested in.

Regulation reminder
AMF Instruction DOC-2018-11 on agreements entered into by investment services providers with retail clients for portfolio management for third parties specifies the provisions of the agreements "intended to inform retail clients precisely about the characteristics and terms of the investment service provided and the rights and obligations of the parties", in accordance with Article 314-11 of the AMF's General Regulation.

Poor practices:
- Not informing the client that frequent and/or significant withdrawals may disrupt the managed account and make it necessary to profile the account again in accordance with the management profile defined in the mandate.
- Mentioning the client's total liability in the event of frequent and/or significant withdrawals of securities and/or cash without informing the client of the possible consequences of such withdrawals.
- Mentioning the agent's disclaimer of any liability in the event of frequent and/or significant withdrawals of securities and/or cash without informing the client of the possible consequences of such withdrawals.

3.6. OTHER MENTIONS

3.6.1. Conflicts of interest

The terms and conditions relating to conflicts of interest in the MiFID 1 mandates analysed during the inspection were generally insufficient. For example, the following practices were observed among the five institutions:

- the mandates of one institution did not mention conflicts of interest at all;
- the mandates of three institutions mentioned the existence of a conflict of interest management policy but did not provide further details and did not specify how this policy would be communicated to their clients;
- the mandates of one institution mentioned the existence of a conflict of interest management policy and specified the procedures for communicating this policy ("on written request to the Agent").

In this regard, three out of five institutions inspected had improved their new MiFID 2 mandate templates. However, two others still had some deficiencies in the new MiFID 2 mandate templates:

- for one, "the conflict of interest management policy is available on request to the agent";
- for the other, "the client is invited to contact the agent for further information".

3.6.2. Complaints/Mediation

In terms of complaints and mediation, the former MiFID 1 mandate templates for the five institutions inspected appeared insufficient. These mandates were incomplete because they did not mention all of the following elements:

- contact details (name, telephone number, email address and postal address) of the person in charge of handling complaints;
- contact details of the appropriate Ombudsman, and in particular the AMF Ombudsman.

Of these five institutions, three had fully corrected these deficiencies in their new MiFID 2 templates. Another institution had partially corrected deficiencies in its new MiFID 2 template, but referred to Ombudsmen (ORIAS/ACPR) who were not appropriate for mandates. Finally, the last institution had not corrected these deficiencies in its new MiFID 2 templates.

By way of comparison, the same was true for two institutions reviewed during "traditional" inspections, for the former MiFID 1 discretionary mandates for one, and for the MiFID1 and MiFID 2 mandates for the other.

3.6.3. Professional secrecy

For two institutions, the confidentiality obligations relating to professional secrecy are not mentioned in the former MiFID 1 mandates. For one of these two institutions, the new MiFID 2 mandates do not include this information. Additionally, they also mention that the client is responsible for maintaining confidentiality.

These practices did not comply with the provisions of former Article 314-59 of the AMF General Regulation set out in AMF Instruction 2018-11.

4. MANAGEMENT COSTS AND CHARGES

The client of the portfolio management service pays several types of fees or costs as part of his/her relationship with his/her agent:

- **Management fees**: percentage taken from the assets under management;
- **Entry fees**: paid by the client when purchasing fund units and which increase the cost price of the units;
- **Transaction fees**: broken down into brokerage fees and turnover commissions;
- **Custody fees**: for the custody account-keeping of clients' securities.

Another source of income for discretionary managers must be included in the list of these fees, until their recent ban with the introduction of MiFID2: **rebates** on fund management fees. These rebates were paid to the portfolio manager by the investment fund management companies in which the clients' portfolios were invested. Before 2018, they accounted for a significant proportion[1] of income from portfolio management (see tables below).

4.1. INCOME BREAKDOWN

The investment services providers that were audited as part of the SPOT inspections[2] on fees are banks (private and retail banks) of very different profiles and sizes. The figures given in the tables below illustrate the proportion of income from portfolio management that each fee category accounts for, as well as the ratio of total income to assets managed at the end of 2017.

2017	A	B	C	D	E	F
Management fees	29.0%	73.9%	18.7%	46.0%	45.4%	34.9%
Transaction fees	10.2%	2.8%	31.5%	7.6%	6.3%	6.1%
Entry fees (CIUs)	17.6%	0.0%	21.9%	1.3%	10.5%	29.8%
Custody fees	12.6%	9.4%	8.0%	25.6%	17.9%	0.7%
Rebates on management fees	29.6%	12.7%	20.0%	19.5%	20.0%	28.5%
Other income	1.0%	1.2%	0.0%	0.0%	0.0%	0.0%

2018 (H1)	A	B	C	D	E	F
Management fees	41.4%	89.1%	52.1%	53.8%	42.1%	n/a
Transaction fees	18.1%	2.0%	7.1%	16.6%	11.3%	n/a
Entry fees (CIUs)	22.4%	0.0%	18.8%	0.2%	28.6%	n/a
Custody fees	14.8%	8.0%	22.0%	22.3%	18.0%	n/a
Rebates on management fees[3]	0.0%	0.5%	0.0%	7.2%	0.0%	n/a
Other income	3.2%	0.4%	0.0%	0.0%	0.0%	n/a

1 The proportion of rebates as a source of the income for the six institutions averaged 21.7% (in 2017).

2 And a "traditional" inspection in 2018.

3 Rebates received in 2018 for 2017.

2017	A	B	C	D	E	F
Income/assets ratio[4]	1.54%	1.04%	0.66%	0.85%	1.11%	1.72%

4.2. PRICING POLICY

The practices identified in the portfolio management activity's pricing policy reflect the diversity of the players, their business models and, in some cases, the group's history (mergers and acquisitions).

4.2.1. Management fees

Two institutions offer a simple pricing model with a single annual management fee rate, with no minimum charge per portfolio. The other institutions apply a sliding scale of annual rates per tranche of assets under management. The rates are in principle stated inclusive of all taxes. However, for one of the five banks, before a change in pricing to a uniform rate for each client segment, the information was presented in the form of quarterly rates excluding tax, which allowed particularly low rates to be displayed with clients being responsible for assessing the overall impact over the year themselves. Since April 2018, the pricing model has been modified and the rates are presented as annual rates including all taxes.

One institution offers clients who so choose a pricing model with variable management fees. In this case, the fixed management fees (1% on the managed assets) are reduced by 40% and the bank receives additional fees equal to 5% of the annual performance of the portfolio being managed. Unlike other banks inspected, this institution excludes the funds of the group's investment management company and all money market funds from its management fees calculation.

The pricing model of one of the five institutions changed between 2016 and 2018 as a result of the merger of group entities. The fee schedule therefore overlays several different scales (with low management fee rates compared with other banks inspected), for which harmonisation was envisaged following the merger. However, this harmonisation must take into account the contractual commitments already made to clients.

Regulation reminder
Article 50(10) of Delegated Regulation 2017/565 (Information on costs and related charges) provides that *"investment firms shall provide their clients with an illustration showing the cumulative effect of costs on return (...) on an ex-ante and ex-post basis (...) [which] shows the effect of all costs and charges on the return of the investment."*

Good practice:

- Implementing a pricing policy that allows the service provider to generate most of its income from portfolio management fees without an incentive to increase portfolio turnover in order to charge transaction fees.

Poor practice:

[4] Income for 2017 and assets managed at 31/12/2017.

- Including quarterly and pre-tax fee rates in the contract documents or fee schedule without indicating an equivalent annual rate and a rate inclusive of all taxes.

4.2.2. Fee level and performance potential of mandates

With the exception of one institution, all service providers offer their client, at the time of entering into the mandate, a choice of management strategy (i.e. mandate profiles ranging from "Prudent" to "Aggressive"). However, none of them has a pricing policy that takes into account the performance potential of the management profile chosen by the client. The same institution, which provides only for a purely discretionary type of mandate, excludes the funds of the group's investment management company and all money market funds from its management fees calculation. The amount of management fees is therefore significantly reduced for portfolios invested mainly in CIUs.

4.2.3. Custody fees

Two of the five banks apply a simple pricing policy with a single rate for custody fees (0.15% excluding taxes for one institution, and 0.30% including taxes for the other), with no minimum charge per portfolio. For these two banks, the group's funds are also exempt from custody fees.

The other institutions offer a sliding scale using the same tranches as those used for management fees. However, for one of the five institutions, the pricing conditions do not explicitly exclude the portion of the portfolio remaining in cash from the custody fee base. The basis for calculating custody fees must of course exclude cash.

Good practices:

- Stating clearly and explicitly in contractual documents or fee schedules that the basis for calculating custody fees excludes liquidity from the portfolios entrusted to its management.
- Exempting investments in the group's investment funds from custody fees.

4.2.4. Entry fees

In the field of asset management, entry fees[5] can be an important source of remuneration for fund distributors. The entry fees are charged directly by the distributing bank on subscription of units. The fund prospectuses simply indicate the maximum rate that may be charged on the subscription of units. The observations made at the five service providers inspected show a diversity of practices.

For two institutions, no entry fees are charged on subscription of fund units. No distinction is made between group or external funds, which are therefore all exempt from entry fees. This means that a client portfolio invested solely in CIUs does not incur any transaction fees.

[5] Excluding entry fees charged by the fund.

One of the five banks does not charge any entry fees on CIUs invested in “defensive” mandates with a share of high risk assets of less than 30%.

The three institutions that charge entry fees on equity and bond funds do so in a uniform manner, without making any distinction between internal and external funds.

One institution displays CIU subscription rates in its fee schedule that are not those actually charged. According to the institution, the rates indicated in the mandate’s pricing conditions should be considered as maximum rates. In practice, clients were able to negotiate discounts with their bank and the actual entry fees were on average lower than the figures displayed.

Finally, unlike the observation made at one of the service providers in relation to SPOT inspections on the compliance of mandates (see 3.3.2), no institution specifies in its pricing policy the possibility to cumulate entry fees and transaction fees on subscription of CIUs or on redemption.

The update of AMF Position-Recommendation 2013-10 on remuneration and benefits received in connection with the marketing and portfolio management of financial instruments will provide the necessary clarification for applying the regulatory provisions in force, in particular as regards entry fees for portfolio management.

Good practice:

- Not charging entry fees on CIUs as part of portfolio management.

Poor practice:

- When entry fees are charged, not indicating in its fee schedule the rates actually applied upon subscription.

4.2.5. Transaction fees

The obligation for a service provider to act in the client's best interests presupposes that the level of fees for mandates remains reasonable and does not hinder the profitability of the investments. The pricing policy on transaction fees may also create conflicts of interest.

All the service providers inspected display a scale applicable to stock market orders (equities and bonds) in their fee schedule. For example, the table below compares the brokerage fee rates applicable for equity orders:

2017	A	B	C	D	E
Euronext	1% (min. €25)	0.20% (no minimum)	1% (min. €7.50)	0.80% (€0-75K) 0.50% (>€75K) (min. €25)	1.166% (min. €25)
Other stock exchanges	1.20% (min. €75)	Actual brokerage fees	1% + broker place + €51	0.80% (€0-75K) 0.50% (>€75K) (min. €50)	Actual fees + intermediation commission

The overall amount of transaction fees depends on portfolio turnover, based on the manager's decisions, and the scale applicable to stock market orders. The inspections found that transaction fees could represent a significant proportion of income from portfolio management (see table under 4.1 above), which would not be a good practice given the conflicts of interest that this creates.

By way of example, for one of the five banks, in 2017, these fees represented 31% of income and 0.21% of assets under management. The bank justified the high level of transaction fees in 2017 with the decision by its management committee to align the management profiles of the other group entities. The pricing conditions in the mandates were applied, but no additional information related to this portfolio realignment was provided to clients. The level of transaction fees returned to a more reasonable rate in 2018. At the AMF's request, the institution concerned has undertaken to reimburse its clients for the transaction fees charged as a result of the realignment of its portfolios related to its internal reorganisation.

Reminder
Article L. 533-11 of the Monetary and Financial Code states that "when providing investment and related services to clients, investment services providers other than portfolio management companies shall act honestly, fairly and professionally, in the best interests of their clients".

Poor practice:

- Charging clients for fees resulting from decisions on the institution's internal organisation does not seem to be in their best interests. This is the case for fees related to the cost of realigning portfolios to management profiles whose composition is modified due to a rationalisation or merging of profiles within the bank.

4.2.6. Rebates

The retention of rebates paid by CIU management companies to portfolio managers has been banned since 3 January 2018. Article L.533-12-3 of the Monetary and Financial Code stipulates that *"investment services providers other than portfolio management companies that provide the investment service [of managing portfolios for third parties] shall not accept, unless they refund them in full to clients, any remuneration, commission or other monetary or non-monetary benefits in connection with the provision of the service to clients, paid or provided by a third party or by a person acting on behalf of a third party."*

Rebates on fund management fees accounted for a significant proportion of the income of the providers inspected: 21.7% on average and up to 30% for one of the institutions in 2017. The impact on income in 2018 as a result of the ban on rebates was lower for one of the service providers, for which management fees remained the main source of income for the activity (74% in 2017 and 58% in 2016).

For two institutions, information on the possibility of receiving rebates was (before 2018) provided in discretionary mandates without information on their amount. However, the rate ranges applied were available on each provider's website.

Finally, one institution reported that it had stopped receiving management fee rebates since 2018, including for the delegated management activity related to life insurance policies.

4.3. CONFLICT OF INTEREST MANAGEMENT

The portfolio management activity can create conflicts of interest. Conflict between, on the one hand, the interest of the agent in generating income through excessive portfolio turnover likely to increase transaction fees or by investing primarily in group funds and, on the other hand, the interest of the client in minimising the impact of management fees. These aspects were analysed as part of the SPOT inspections.

4.3.1. Transaction fees and portfolio turnover

The conflict of interest mapping of two out of five institutions does not clearly identify the potential conflict related to unjustified asset turnover. For one of these institutions, turnover rates (many of which were above 100% in 2016 and 2017) and their suitability for the management profile were monitored by a half-yearly first-level control until the first half of 2017. The bank planned to reinstate this control as of December 2018. It had been suspended because of a merger of IT tools. The ratio of transaction fees to assets managed in 2017 (0.21%) was the highest of the five institutions inspected. The proportion of total transaction fees (transaction fees and entry fees) was particularly high in 2017, at 53%.

For one institution, the highest portfolio turnover rates related to "defensive" management strategies mainly invested in monetary assets (for which no entry fees are charged on CIUs), which reached 99% (in 2016) and 95% (in 2017). Transaction fees charged in 2017 represented 0.07% of assets under management, which is low compared to the other institutions.

The other institutions identified the potential conflict related to unjustified asset turnover and the generation of additional fees. For these banks, transaction fees charged in 2017 represented between 0.03% and 0.16% of assets under management.

Good practice:

- Identifying any potential conflicts of interest associated with unjustified portfolio turnover (and consequently generate additional transaction fees for the client) and implement frequent first and second-level checks of portfolio turnover ratios accordingly.

As a reminder, the AMF has incorporated into its new Position 2019-03, which came into force on 6 March, the guidance published by ESMA on "certain aspects relating to the suitability requirements of MiFID 2" (ESMA 35-43-1163), including the analysis of the costs and benefits of a change in investment provided for in Article 54.11 of the Delegated Regulation (EU) 2017/565.

4.3.2. Investments in "in-house" funds

For the five institutions inspected, there is no strong investment bias towards "in-house" CIUs. The proportion of a portfolio's assets invested in the CIUs of the group to which the agent belongs varies according to the management strategy. Therefore, the "prudent" or "defensive" profiles, whose assets are largely invested in money market or bond funds, are the ones most directed towards the group's funds. The table below shows an average for all the assets managed by each service provider. The last institution (F), which has the highest proportion of assets invested in its group's funds, was subject to a traditional inspection in 2018, and not a SPOT inspection.

2018 (H1)	A	B	C	D	E	F
Proportion of "in-house" funds in assets under management	47.7%	21%	44%	34.2%	20%	81%

In the mapping of conflicts of interest, two out of five institutions clearly refer to the potential conflict related to the proportion of the group's funds in client portfolios. One institution also refers to the potential conflict of interest related to the level of fee income and oversees it through its fund selection policy for the management universe and a pricing policy that does not apply entry fees to CIUs.

In the other institutions, the conflict of interest is not specifically identified. However, the portfolios are not primarily directed towards Group funds. No institution distinguishes between group funds and non-group funds when applying entry fees. One institution, which does not charge entry fees, also excludes investments in the funds of the group's investment management company from its management fees calculation.

Regulation reminder
Article L. 533-11 of the Monetary and Financial Code states that "when providing investment and related services to clients, investment services providers other than portfolio management companies shall act honestly, fairly and professionally, in the best interests of their clients".
Acting in the best interests of the client therefore requires that the group's funds are not given preference in the choice of investment vehicles when this would be to the detriment of the client's interests.

Good practice:

- Among the potential conflicts of interest, clearly identifying those linked to the share of a group's own funds within clients' portfolios and managing such conflicts of interest, in particular by implementing an appropriate CIU selection policy for the investment universe.
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4.4. INFORMATION PROVIDED TO CLIENTS

4.4.1. Regulatory background

Since January 2018, client reporting obligations are detailed in Article 50 of Regulation (EU) 2017/565 for the general reporting obligation and in Article 60 of Delegated Regulation (EU) 2017/565 for the *ex post* reporting obligation relating to portfolio management.

One of the agent's obligations is to send a "periodic statement" of portfolio management activities to the client. With regard to fees, Article 60.2(d) states that the periodic statement must include *"the total amount of fees and charges incurred during the reporting period, itemising at least total management fees and total costs associated with execution, and including, where relevant, a statement that a more detailed breakdown will be provided on request"*.

4.4.2. *Ex ante* information on fees

↗ **Access to information**

Based on the samples of MiFID 1 mandates analysed, it should be noted that, for the five institutions inspected, information on the fees related to portfolio management is not fully disclosed in the discretionary mandates.

Only the new MiFID 2 mandate template of one institution presents the fees related to portfolio management in a unified manner. However, this mandate template also refers to the fee schedule in effect for all other fees, including transaction fees and bank charges.

For the other mandate templates, the information is split across several documents: an annex to the mandate or an ad hoc document such as a "guide to fees", "fee schedule", "pricing conditions" or in the "general and specific conditions". For one institution, the mandate refers to the information provided on the institution's website.

It is important that the discretionary mandates explicitly refer to the relevant documents and that the institution ensures traceability of the information provided to the client, as well as the date on which this information was provided. However, for several institutions, these ad hoc documents were missing or not signed by the clients.

For one institution, the basis and methods of calculating brokerage fees and custody fees, as well as their payment methods, are specified in the mandate. The discretionary mandate and the fee schedule present a breakdown of the fees, clearly distinguishing between the different types of fees.

↗ **"All In" or "All Inclusive" management fees**

For one institution, the new mandate template mentions the existence of an "all inclusive" flat-rate management fee,[6] based on a model portfolio, including in a single charge the management fees, custody fees, brokerage fees and subscription and redemption fees for in-house or external funds. The mandate refers to the fees annexe for the calculation of the flat-rate fee, which also specifies the arrangements for paying it. This presentation is unclear in that it provides a single calculation and a single charge that is supposed to include other fees that are calculated according to different arrangements and frequencies. This institution now routinely provides each client with an *ex ante* fee presentation when signing a contract, which provides a breakdown of portfolio management fees by category (recurring fees for providing the portfolio management service, costs relating to transactions carried out as part of providing the portfolio management service and fees collected by management companies). This document specifies that the estimated fees have been calculated based on model portfolios for a 12-month asset holding period.

By way of comparison, one institution (as identified in a "traditional" inspection in 2018) also offers, in its pricing policy applicable to its portfolio management service, an option called "all inclusive". Unlike the presentation mentioned above, the client is clearly informed of the fees that he/she does not incur by choosing this pricing option.

↗ **Transaction fees**

In its fee brochure, one institution specifies, concerning CIUs turnover commissions on subscription (1.5%) and on redemption (0.5%), but also entry/exit fees (in accordance with CIUs prospectuses), which could appear cumulative.

Poor practices:

- Splitting information on fees across several documents: the discretionary mandate, financial instrument account agreement, general and/or specific conditions, and fee schedule or brochure.
- Not explicitly informing the client of any updates to the information on management fees (for example, not informing the client that fees have been updated when the update is only available on the institution's website).

[6] The flat-rate fee rate and the applicable minimums are expressed in the fees annex by type of mandate, the most dynamic management profiles being more expensive.

4.4.3. *Ex-post* information on fees

Compliance with the provisions of Articles 50.9 (relating to annual *ex-post* information) and 62.1 (relating to alerting clients in the event of a decrease of more than 10%) of Delegated Regulation 2017/565 has not been audited as part of these SPOT inspections. Compliance with these articles and the other obligations brought by Delegated Regulation 2017/565 to the portfolio management service will be the subject of a SPOT inspection campaign on portfolio management in 2019.

Not all service providers inspected interpret in the same way what is meant by the notion of *"related costs and charges"* or *"the total amount of fees and charges incurred during the reporting period"*. One institution considers that custody fees are not related to management and therefore does not provide information in its periodic statements. To obtain an overall view of the fees relating to management, the client must examine the monthly account statements (including management fees and custody fees) on the one hand, and the management reports (including management fees and transaction fees) on the other. The bank plans to change the information on fees to include custody fees. By contrast, another institution details the management fees and custody fees in its management reports, but not the transaction fees.

With regard to transaction fees, all institutions provide information on fees related to management activities in transaction notices (brokerage fees, commissions and entry fees). One institution chose to include fee information in its portfolio statements (monthly) rather than in its management reports (quarterly). Another institution provides fee information in its monthly account statements (management fees and custody fees) and quarterly management reports (custody fees, management commissions and trading fees). Finally, one institution indicated that it makes use of Article 60.3(b) of the Delegated European Regulation 2017/565 by providing its clients with transaction notices (with details of brokerage fees) and is therefore required to provide them with a periodic statement at least annually. The information is presented in the portfolio statement sent at the end of the year, together with the annual statement of costs and charges including the execution fees charged over the year.

Regulation reminder
Article 60.2(d) of Delegated European Regulation 2017/565 (Reporting obligations in respect of portfolio management) states that the periodic statement shall include *"the total amount of fees and charges incurred during the reporting period, itemising at least total management fees and total costs associated with execution, and including, where relevant, a statement that a more detailed breakdown will be provided on request"*.