Response to FSA Consultation Paper 12/22:
Client Asset Regime: EMIR, Multiple Pools and the Wider Review

1. The Wholesale Markets Brokers' Association & London Energy Brokers' Association

The Wholesale Markets Brokers' Association (WMBA) and the London Energy Brokers' Association (LEBA) (*referred to in this document as the WMBA*) are the European industry associations for the wholesale intermediation of Over-the-Counter (OTC) markets and trading venues in financial, energy, commodity and emissions markets and their traded derivatives. Our members are nearly entirely Limited Activity and Limited Licence firms and all act solely as intermediaries in the said wholesale financial markets. As Interdealer Brokers (IDBs), the WMBA members' principal client base is made up of global banks, primary dealers, large energy companies and other wholesale market participants. (Please see www.wmba.org.uk and www.leba.org.uk for information about the associations, its members and products.)

WMBA members operate three models to facilitate trades: ***Name Give Up***, ***Exchange Agency*** and ***Matched Principal***. These models are detailed on our website. Albeit that members use their own capital to facilitate the settlement of matched principal trades, this is purely facilitation in cash bond markets and should not be considered to confer the same as the risks and benefits associated with proprietary trading.

2. General comments

The WMBA welcomes the opportunity to comment on the second phase of the FSA Consultation on the Client Asset Regime: EMIR, Multiple Pools and the Wider Review (CP12/22). This submission is made on the basis of the business model described above and the WMBA comments are limited to areas that are directly relevant to their members.

All matched principal trades undertaken by our members are operated on a delivery verses payment basis and hence are not subject to the FSA client money or client asset regimes. However, these trades are subject to a 1-3 day settlement period during which time any dividends, coupons or corporate actions are directed initially to our member firms for onward transmission to their clients. As a result of the complexity of some trades, it is difficult to identify which clients are entitled to this money and hence cannot be repaid immediately. Thus as a result of this process, which is ancillary to our member firms investment business, they are subject to the FSA client money regime. WMBA is of the opinion that based on the limited risks inherent in the IDB business model (and hence the likelihood of an IDBs insolvency) it is difficult based on cost to justify the introduction of the new proposed Multiple Client Money Pools and would respectfully request that this type of ancillary service is taken outside the scope of the new requirements.

WMBA is of the opinion that the requirement to provide details of client money sub-pools to the FSA not less than three months prior to the setting up of such a pool is not practicable and should be subject to post event reporting. An example of the problem with the current proposal is provided in 3.11 where if the 3 months lead time is adopted for segregated pools at client level, it could seriously delay the client '*on-boarding process*' thus jeopardising a firm's ability to procure new business in the current competitive market place

Given that the definition of client assets in Part III: *Client Assets Regime: Achieving a better result (DP)* refers to both client money and custody asset, the WMBA feels that the FSA in their proposals for introducing Multiple Client Money Pools has pre-empted the outcome of this review in respect of the speed of return of client monies.

3. Response

Question 3: Do you agree that we should introduce Multiple Client Money Pools to facilitate porting of cleared positions?

WMBA welcomes the FSA's approach to introducing a voluntary system, based on bilateral agreements with a firms client, of operating Multiple Client Money Pools for a defined subset of beneficiaries.

However, the WMBA are concerned that the current wording of 3.11 is likely to result in pressure from clients to segregate client money at individual account level. It is arguable that this segregation will result in increased expenses and operational complexities for firms, which in turn will lead to increased costs for clients without the anticipated improvement in the recovery of client money in the case of any insolvency anticipated by the FSA. Hence, WMBA consider that the option for Multiple Client Money Pools should be limited to a subset of beneficiaries and not to individual clients.

Question 4: Do you agree that we should make the option of Multiple Client Money Pools available to other types of investment business?

As stated above, WMBA is of the opinion that the application of Multiple Client Money Pools **s**hould be restricted to investment business where, as a result of the business model of the firm, the costs of implementation is commensurate with the firms risk profile and client base.

Question 12: Do you agree these benefits would result from the segregation of retail and non retail client money?

WMBA do not believe that the segregation of retail and non-retail clients would result in any additional benefit accruing to retail clients. In respect of retail clients (eligible claimants), the FSCS covers losses of up to £50,000 and its rules state that it must pay the claim as soon as reasonably possible and at the latest within three months of the establishment of the claimant's eligibility. WMBA consider that the average retail client would be comfortable with the certainty of having all their assets back within this timescale given the costs of speedier payouts and the trade-off with accuracy. Hence, the segregation into multiple pools of this category of client's money is difficult to justify.

Question 13: Do you agree that these benefits would result from the segregation of business into margined and non-margined business?

WMBA agrees that to enable the "*porting*" element of EMIR and to enable the firm to be sold as a going concern prior to an impending insolvency, a firm should segregate client money between margined and non-margined business. However, to simplify the administration process, segregation should apply at activity level and not apply to client monies held in respect of other investment business.

Question 16: Do you think that any mandating of certain client money pools should be dependent on the complexity, size of client money holding and/or type of firm. (E.g. should we mandate segregation only for investment banks and large brokers?)

WMBA does not consider that Multiple Client Money Pools should be made mandatory by the FSA preferring the voluntary segregation approach proposed in Paragraph 3.7. The implementation of this bilateral approach by firms and clients would be subject to a cost/benefit criteria, would ensure that only firms with quantifiable risks would be targeted and that the complexity, size of the client money holding and/type of firm is taken into account.

Rather than mandating the use of Multiple Client Money Pools, WMBA would respectfully suggest that the FSA, or perhaps trade associations, provide guidelines that firms and clients can consider when agreeing to the voluntary segregation.

See the response to question 3 and 4 above.

Question 18: Should we incentivise the use of sub pools by requiring firms to notify their clients of the risks associated with general client money pools and the sub pools available?

As stated in our answer to question 16 above, WMBA would respectfully suggest that the FSA, or perhaps trade associations, provide guidelines that firms and clients can consider when agreeing to the voluntary segregation.

Question 20: Do you agree it is important to have a speedy return of Client Assets following a firm's insolvency? Please explain your answer?

WMBA agrees with the FSA that a speedy return of return of Client Assets would ensure the integrity of other firms and confidence in the market but considers that it cannot be viewed in isolation. WMBA considers that a balance needs to be struck between the firm's risk profile, the type of clients involved, potential loss of accuracy and cost of the segregation.

Any proposed amendment to the current client asset regime to ensure the speedy return of client assets needs to be put into context and consideration be given to the following:

- The SAR and recent developments in the client asset regime enabled IPs to identify issues very quickly in the aftermath of recent insolvencies. It highlighted the inadequacy of the firms'

record keeping and trust letters as major reasons for the IPs delay in returning assets. The imposition of additional segregation rules would not have alleviated these problems and it is the responsibility of the FSA via the "Auditors Client Monies and Safe Custody Report" to adequately supervise these areas. WMBA is pleased to note that staffing levels in the FSA Client Asset Unit have increased from 4 to 40 to facilitate closer supervision of this area.

- The "*porting*" requirements under EMIR and the proposed segregation of client monies in respect of margined transactions will significantly reduce the scale of client assets held by a large number of firms.

Question 22: Given the potential trade off between costs and speed how fast do you think client assets should be returned to retail clients following an insolvency and, as a %, what loss should a retail client be prepared to incur to have client assets back in that time period?

WMBA believes that the average retail client would not exceed the £50,000 limit set for the FSCS and hence, as stated in question 12 above, would be comfortable with the certainty of having all their assets back within the timescale set by the FSCS rules given the costs of speedier payouts and the trade-off with accuracy.

Question 24: Should retail / wholesale clients be treated differently in respect of client assets protection and distribution? Please explain your answer?

WMBA considers no client should receive preferential treatment in respect of the protection and distribution of client assets. It would also like to point out that should any difference in approach to the distribution of client assets be considered appropriate, the criteria would need to comply with the requirements of *Part VII of the Companies Act 1989* and the UK insolvency framework. It should also be consistent with the proposals in the recent HMT Treasury Consultation in respect of the UK insolvency framework.

Question 25: Are there any other impediments that impacts on the speed of return of client assets not identified above?

As a result of the duty of care to all creditors and the imposition of personal liability under the insolvency framework, IPs will be reluctant to return client assets except where "title is established to a high degree of certainty" and not within a specified timescale. Unless the rules governing an IPs liability is amended by HM Treasury during its implementation changes in respect of EMIR this will, of course, have an effect on the speed of return of client assets.

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