

INVESTOR COMPENSATION SCHEMES

Proposal for a Directive (amending Directive 97/9/EC)

BEUC position paper

Contact: Financial Services Team – financialservices@beuc.eu

Ref.: X/084/2010 - 08/12/10

BEUC, the European Consumers' Organisation

80 rue d'Arlon, 1040 Bruxelles - +32 2 743 15 90 - www.beuc.eu

 EC register for interest representatives: identification number 9505781573-45 

Summary

BEUC welcomes the changes to existing European rules aimed at improving protection for investors proposed by the European Commission on 12 July.

The Commission proposal contains many advances compared to the current legislation on Investor Compensation Schemes but there is room for some improvements.

BEUC welcomes the main modifications to the ICS Directive which are:

- the extension of protection to some cases that were not covered (failure of a depositary or a custodian chosen by the investment firm);
- protection for the unit holder in case of failure of the depositary of the UCITS assets;
- a higher protection level: €50,000 instead of €20,000;
- the exclusion of the co-insurance principle;
- the coverage of funds in currencies other than Member State currencies.

The main demands from BEUC are:

- all gaps in the protection of liquidities should be eliminated. Consumer protection should not be weaker for clients who enter the market via an Investment Firm than via Banks;
- the €50,000 protection level should be a minimum harmonisation level.

BEUC Requests

Services covered, alignment with MiFID

Art. 1(2) amending art. 2 and inserting art. 2a in Directive 97/9/EC (ICSD)

BEUC welcomes the broadening of the scope of ICS by covering all investments and activities covered under MiFID, in particular where the firm is acting in contradiction to his authorisation (i.e. the firm holds its clients' assets while it is not authorised to do so). The consumer is not able to check the exact authorisation of each investment firm and shouldn't be the one who bears the risk due to the breach committed by an investment firm.

Depository failure covered

Art. 1(2) inserting art. 2a in ICSD

BEUC welcomes and fully supports the proposition to explicitly cover the failure of the depository or custodian chosen by the investment firm who is unable to return the *financial instruments*. Actually, the client cannot be responsible for the choice made by the firm, even if this choice has been made without any fault or negligence. And there cannot be confidence if such a gap remains in the protection schemes.

However, this provision does not cover the failure of the depository or third party custodian who cannot return the *liquidities* deposited by the investment firm. In some cases, those liquidities can be protected by the deposit guarantee scheme (DGS) guaranteeing the deposits entrusted to the failing credit institution, but this is not always the case. Where the retail investor is acting via a credit institution, his liquidities are always protected by the DGS the credit institution is participating in.

BEUC contends that investor protection should not be weaker for clients who enter the market via an investment firm than via a credit institution. The entire portfolio of an investor (*financial instruments and liquidities*) should benefit from the same protection, whether the investors enter the market via an investment firm or a credit institution offering investment services.

Protection of the UCITS unit holder

Art. 1(2) inserting art. 2b in ICSD

BEUC welcomes and fully supports the protection of the UCITS unit holder when the depository or third party custodian to whom the assets of the UCITS are entrusted is unable to meet their obligations to the UCITS. UCITS are widespread investment products for retail investors who cannot – due to a modest portfolio or a lack of know-how in financial matters – diversify their own portfolio with direct investments in shares or bonds. The consumer who invests indirectly (via UCITS) in a financial instrument must benefit from the same protection level against depository default than the investor who invests directly in the financial instrument.

Level of compensation

Art. 1 (4) replacing art. 4 in ICSD

BEUC welcomes the increase of the protection level from minimum €20,000 to €50,000.

BEUC welcomes and fully supports

- the elimination of the co-insurance principle that was unjustified in the view of BEUC;
- the elimination of the ability to exclude non Member States' currencies.

However, BEUC considers that the €50,000 level should be a minimum harmonised protection level instead of a fully harmonised level as proposed by the Commission.

As long as wealth is unequally distributed within the EU region and the average investment portfolio differs according to national financial habits, the need for protection will differ also. Protection is currently higher in the UK and it would be unacceptable for UK consumers to see their level of protection reduced.

The eventual difference in protection level between firms depending on different ICS would have less impact on the choice of the consumer than the difference in liquidities protection between a bank and an investment firm.

Funding

Art. 1 (5) introducing new articles 4a & 4b in ICSD

BEUC¹ supports the *ex-ante* funding of the ICS. It achieves a level playing field between firms from different Member States; it makes the repayment within a short delay more feasible and does not work cyclically like heavy contributions in times of crisis.

END

¹ WHICH?, BEUC UK member, considers that it should be left to individual member states to decide whether they want to introduce ex-ante funding or not.