

New Fee Disclosure Requirements in European Offerings

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Summary

Readers will be accustomed to the typical level of disclosure given in offering documents on the various fees and commissions payable out of the transaction proceeds, particularly as regards amounts payable to arrangers, underwriters and, in the context of CDOs, asset managers. Historically this information has been fairly generic, even opaque; although investors in listed securities have generally benefited from listing rules that prescribe a minimum level of disclosure.

However, with the advent of The Directive on Markets in Financial Instruments (“**MiFID**”)¹, partial disclosure in an offering within the European Union is no longer sufficient as regards any fee, commission or non-monetary benefit in relation to financial instruments (including debt and equity securities) and firms that are within the scope of MiFID (generally, any firms selling or marketing investments within Europe). Specifically, with effect from November 1, 2007, the existence, nature and amount or method of calculating any indirect fees and commissions (i.e. those not paid by the ultimate investor) must be (i) fully disclosed, or (ii) summarised in disclosure with full details provided to investors on request.

Background

The European Union Financial Services Action Plan aims to create a single EU wholesale market for financial services and products. Directives that are part of the plan are being adopted on the basis of the “Lamfalussy approach” – a four level system, recommended in 2001 by the Committee of Wise Men², for EU institutions to prepare, adopt and implement new legislation. The approach involves “level 1 Directives”, which set out framework principles, and “level 2 Directives”, which set out the implementing

measures that allow these principles to be put into practice.

MiFID is one of four “level 1 Directives” enacted by the European Union’s legislators³ which, along with the Market Abuse Directive, the Prospectus Directive and the Transparency Directive, forms the framework for the EU Financial Services Action Plan. At level 2, MiFID is supplemented by the MiFID Level 2 Implementing Directive⁴ (the “**Level 2 Directive**”).

New Disclosure Law

The specific legislative provisions affecting disclosure of fees and commissions are:

- (a) Article 19 of MiFID, which requires an investment firm to act honestly, fairly and professionally in accordance with the best interests of its clients when providing investment services to clients; and
- (b) Article 26 of the Level 2 Directive which, in extract, provides that:

“Member States shall ensure that investment firms are not regarded as acting honestly, fairly and professionally in accordance with the best interests of a client if, in relation to the provision of an investment or ancillary service to the client, they pay or are paid any fee or commission, or provide or are provided with any non-monetary benefit, other than the following:

....

- (b) a fee, commission or non-monetary benefit paid or provided to or by a third party or a person acting on behalf of a third party, where the following conditions are satisfied:
 - (i) the existence, nature and amount of

the fee, commission or benefit, or, where the amount cannot be ascertained, the method of calculating that amount, must be clearly disclosed to the client, in a manner that is comprehensive, accurate and understandable, prior to the provision of the relevant investment or ancillary service;

....

Member States shall permit an investment firm, for the purposes of point (b)(i), to disclose the essential terms of the arrangements relating to the fee, commission or non-monetary benefit in summary form, provided that it undertakes to

disclose further details at the request of the client and provided that it honours that undertaking.”

For those wanting to know more, CESR⁵ has published detailed (but non-binding) guidance as to its recommended interpretation of these provisions, in its May 2007 Recommendations in relation to Inducements under MiFID⁶.

Alternatively please contact the author or your usual Milbank representative and we will be happy to discuss this further.

Notes:

1. Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EEC.
2. See the Final Report of The Committee of Wise Men on the Regulation of the European Securities Market, February 15, 2001.
3. MiFID came into effect on November 1, 2007, replacing the Investment Services Directive.
4. Commission Directive 2006/73/EC of 10 August 2006 implementing Directive 2004/39/EC of the European Parliament and of the Council as regards organizational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive.
5. The Committee of European Securities Regulators (“CESR”). Level 3 of the Lamfalussy approach mandates supervisory committees (e.g. CESR) to co-ordinate Member States implementation efforts and facilitate the convergence of regulatory practices. To date this coordination function has generally been implemented via consultations and recommendations, although there are a variety of other coordination measures such as league tables ranking Member States by their degree of compliance with the Financial Services Action Plan. Level 4 requires the Commission to ensure that Member States comply with the legislation and, where necessary, take enforcement action.
6. Ref: CESR/07-228b.