# The Danish Financial Supervisory Authority's guidance on the interpretation of the ban on payments of commission

On 1 July 2017, a ban on payments of commission from investment funds in connection with discretionary portfolio management will enter into force. In this connection, the Danish Financial Supervisory Authority (FSA) has issued a long-awaited interpretation guidance.

When entering into force on 1 July 2017, the ban on receiving and keeping commission in certain cases from investment funds – and other collective investment institutes – will affect for example banks and investment service companies ('investment companies') that include the investment funds in question in their portfolios.

In this connection, the Danish FSA has issued a guidance on the interpretation of Section 46 (b) (1) of the Danish Financial Business Act, which implements the ban. This provision was introduced by Act no. 632 of 8 June 2016 implementing Article 24 (7) (b) and (8) in the Markets in Financial Instruments Directive 2014/65/EU of 15 May 2014 (MIFID II) issued by the EU Parliament and the EU Council.

The guidance is long awaited, and its purpose is to help the industry with ongoing adjustments of business models, etc., to the future rules and possible considerations concerning payment of capacity costs, etc.

## What are the contents of the ban – and to whom does it apply?

The provision reflects an implementation, resembling the MiFID II directive and implies a ban for investment companies to receive and keep fees, commission, or other monetary or non-monetary benefits from for example investment funds in connection with the provision of discretionary portfolio management to customers.

The ban does *not* apply to investment products sold by a regular order execution (execution only) or subsequent to preceding investment advice. Article 24 (9) of MiFID II requires that an investment company must only receive commission in case of provision of non-independent investment advice and other investment services. This provision will be introduced with the executive order on commission payments, which is expected to come into force together with the ban.

Nor does the ban apply to non-monetary benefits of *minor value*, which may increase the quality of the service provided to the customer and which cannot prevent the investment company in question from complying with its duty to act in the best interests of the customer.

The ban is aimed primarily at the distributor and is intended to remove the incentive of the investment company to act against the best interests of the customer by selectively choosing certain investment products rather than others.

## The FSA's interpretation of the ban

It appears from the Danish FSA's guidance that an investment company is not allowed to receive and keep payments that *actually depend on the investment company's distribution efforts*. This is emphasized by the fact that it is not sufficient that a payment does not formally constitute a payment in connection with the provision of portfolio management to the customer.

The ban also applies even if the payment only covers the expenses relating to the provision of portfolio management to customers. Whether an investment company may receive and keep a specific payment will always depend on a specific assessment, and it is up to the companies in question to make such an assessment.

Furthermore, the Danish FSA states when it is likely that a situation will be covered by the ban pursuant to Section 46 (b) (1) of the Danish Financial Business Act. In case of doubt, the investment companies should consider *whether* they will receive less money for a specific task if they distribute fewer investment products for the portfolio management customers. If this is the case, the ban on receiving and keeping the payment applies.

However, it appears from the guidance that there is no general ban against an investment company receiving a variable payment for the provision of services to the investment fund. This implies, however, that the service and the payment are not related to the provision of discretionary portfolio management to a customer.

## Investment funds – outsourcing of tasks

Investment funds are generally allowed to outsource various tasks – such as investment management, administration, or marketing. In that context, the FSA points out that such outsourcing will have consequences for the types of task, for which the investment companies may receive payment from the investment fund to solve if the outsourcing is made to an investment company comprised by the fund's line of distribution.

Basically, the FSA assesses that an investment company may still receive and keep payments for tasks related to administration and/or investment management. The guidance mentions a number of tasks for which an investment company generally may receive and keep payment.

For example, this applies to payments covering the operation and development of IT systems related to the fund's administration or investment management or execution of investment analyses. In addition, the investment companies may naturally receive and keep payments for investment counselling provided to funds with the view of optimising the funds' investment management, etc.

## Are you allowed to receive or keep payment for counselling/distribution, sale, or marketing?

According to the FSA, investment companies are not allowed to receive or keep payment for tasks *related to counselling/distribution, sale and marketing* if it must be expected that the payments are …" related to the provision of the service in question (discretionary portfolio management) … " to the customers, cf. FIL Section 46 b (1).

It concerns tasks relating to the discretionary portfolio management agreement entered into between the investment company and the customer – e.g. marketing material for the portfolio management arrangement – as well as tasks with tactical allocation and rebalancing of the investment certificates comprised by the customer's portfolio management arrangement.

The ban also applies to payments related to the investment companies' general compliance with the MiFID rules such as the development of the investment company's IT systems, which can support the implementation of applicability and suitability tests.

## Payments in kind of minor value: What is the minimum amount?

Finally, the FSA states in which cases an investment company may receive payment for the training of the investment company's advisors. The FSA stresses the importance of the distinction between training in relation to the fund's products, etc., and general training in relation to e.g. the competencies required for the investment company's advisors.

It appears from the guidance that courses regarding the products of an investment fund (departments) may be included in the exemption in FIL Section 42 b (2) concerning payments in kind of minor value.

However, the investment companies may not receive any payment for the training activities required in order for the company to meet the competency requirements applicable to investment companies' advisors.

## Would you like to know more?

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