Towards true transparency in funds distribution

What will it take for efficiency and transparency to co-exist in the fund distribution chain?

Fund providers find themselves between a rock and a hard place. Under Europe's new regulatory regime, MiFID II, it is they, not their distributors, who have the responsibility to ensure their investment products are not being mis-sold.

That means screening the end-investors. But the shift among platforms and distributors to omnibus accounts that bundle up transactions makes it increasingly difficult to identify the initial introducer or buyer.

This is a real concern, says Stuart Jehan, Funds Strategic Development Manager at Robeco: "As a large fund provider, it is virtually impossible for us to get a complete picture of who the underlying investors are. Too often the financial advisers are not providing the information back up the chain," he says.

Sonya Slater, Head of Fund Operations at Investec Asset Management, agrees: "Omnibus accounts tick a box for efficiency, but in addition to the concerns detailed above by Stuart, the incomplete picture makes it difficult for the internal recognition of fund flows to the management company."

Ironically, by clamping down on trailer fees and commissions, MiFID II has reduced the incentive for distributors to provide more than bare-bones information.

"The regulatory focus is on providing transparency to the investor. But that is resulting in less transparency for the fund manager," she remarks.

Confronting the internal MI challenge

The challenge is not just a regulatory one. The lack of information coming back up the distribution chain complicates the process of allocating internal recognition to the correct sales teams.

"One large Swiss entity books with us on an omnibus basis," says Ms Slater: "We see their booking centre but there is not enough detail to identify the underlying introducer. If you are structured around regional sales teams but have information coming in via a global omnibus account you need to be able to break that down to see how much each team is responsible for."

To fill in the necessary detail, both for regulatory and internal purposes, is costly. "The first stage is ensuring we have all the data-sharing systems in place. We routinely have to approach our end-intermediaries." says Mr Jehan.

Manual intervention is inevitable. Along with other fund managers, Robeco has used third-party firms that offer outsourced reporting solutions. Their principal target is the many platforms that fail to generate sufficient data.

Alexandre De Schaetzen, Funds Product Management at Euroclear says: "We believe the efficiency of omnibus accounts can be combined with full transparency. It requires the right framework, the right tools and the right transparency model. You can get the best of both worlds."

Interestingly, around two thirds of those attending a recent ITAS conference bringing together transfer agents and distributors agreed.

So how can that be achieved?

Standardisation and enforceability

Standardisation is key. Ms Slater says: "The industry needs to come up with a standardised template that could be used at every level. We need quicker, standardised feeds that will channel everything into ultimately a centralised depository and so create effective management information. The Wolfsberg questionnaire agreed for anti-money laundering (AML) purposes shows it can be done."

According to De Schaetzen, there are two keys to making this work: enforceability and the right tools. On enforceability, he says: "Either the regulators must oblige intermediaries to pass the information through or issuers must make it mandatory in their prospectuses."

Harmonisation across Europe would greatly help in order to drive down costs.

And the Funds Product Manager continues "There must also be the right tools to ensure the information flows back quickly to the fund managers. There are tools to do this at present, but full real-time transparency is not there yet."

Role for a centralised infrastructure

There is also a role here, he suggests, for a centralised infrastructure. "Fund managers don't want 50 different reports from 50 different distributors," he points out. "No fund manager wants multiple solutions to aggregate. It would make sense to be able to leverage an infrastructure where the AML/KYC information can be linked to the processing – allowing AML or investor suitability issues to be flagged at the right time. That way, a fund manager can see which distributor is playing by the rules and which is not."

France may be the testing ground for this solution. It already operates a centralised model and Euroclear is in discussion with the market and all the relevant industry parties to come up with a cross-asset solution.

Says De Schaetzen: "There is a working group targeting transparency across all assets – equities, fixed income and funds – working on identifying the right transparency solutions. It is due to come out with concrete proposals in the second quarter of this year."

If that were to be adopted as a standardised solution at a European level, the funds industry could soon find the trade-off between efficiency and transparency becomes a thing of the past.

Euroclear's FundPlace addresses the different funds market needs with a highly efficient and transparent funds processing infrastructure (order routing, settlement, asset servicing) in the different markets we service (whether CSD or transfer agent market) that cuts cost and risk throughout the fund distribution chain.