SECURITIES & INVESTMENT

REVIEW

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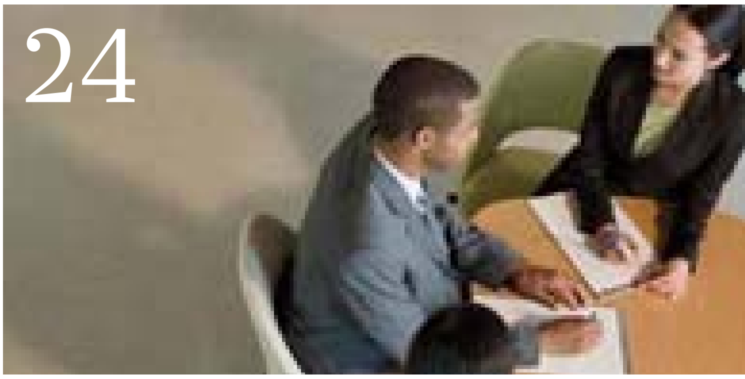


Contents

Information overload

CISI OPINION

The high volume and wide variety of written material emanating from the FSA is an impediment to good compliance

BETWEEN 1 JANUARY and 16 March 2011, the FSA issued 111 documents, comprising 1,929 pages. This output included 15 different types of document, ranging from formal discussion papers, consultation papers and policy statements to enforcement final notices and 'informal guidance', including newsletters and speeches. A CISI survey of members in the compliance sector highlights that this output is growing beyond the capacity of firms to absorb it. Of respondents, 88% agree with the statement that "the volume of FSA material with which I have to keep up to date is a serious drain on the compliance resource within my firm". Furthermore, eight out of ten say that a cut in FSA output would improve compliance at their firm. In the wake of this survey, the CISI is urging the FSA to reduce what has clearly become a counterproductive burden. This representation is being made by the CISI compliance professional interest forum, which carried out the survey, to the Financial Services Practitioner Panel, a body that provides industry input to the FSA.

Read it all

Part of the problem is that firms feel compelled to read almost everything produced by the FSA (69% of those surveyed said that they felt this). This is because the distinction in impact between different documents is blurred. While the FSA does use a 'star rating' system, indicating the relative importance of its material, this applies only to formal documents, such as consultation papers and policy statements. Although many documents may not be relevant to a given firm, such material cannot be set aside until it has been reviewed, for fear that there may be matters of importance that are not immediately obvious. A 'read it all' policy may be labour-intensive, but the wisdom of this approach has been often demonstrated. Specifically, documents stated as not being 'formal guidance' have appeared in disciplinary final notices, with the FSA criticising the firm in question for not taking account of the material's content. The situation is similar with speeches by senior FSA staff. The regulator points to these as indicative of the tenor of forthcoming regulation, and worthy of study. Such speeches can inform the priorities of supervision teams, which then measure firms' performance against such informal guidance as if it were rules. The amount of material issued by the FSA shows no sign of abating. Indeed, as we move closer to the institution of the Prudential Regulation Authority and Financial Conduct Authority, this volume will increase. Furthermore, the FSA is only one of several bodies whose material must be considered by firms. Others include the Panel on Takeovers & Mergers, the Financial Ombudsman Service and HM Treasury. This is without any consideration of output from non-UK bodies, in particular the European Commission. As indicated by our survey, reviewing the FSA's output can be a serious drain on the compliance resources within any firm, let alone smaller companies. This not only damages the compliance process but adds little benefit to consumers. Thus firms are forced to deploy resources to read the output, resources that could better be used in reviewing operational processes. To assist the FSA in getting its message across to firms, the CISI has suggested that:

- the star-rating system used for formal communications should be extended to all other FSA output (as supported by 91% of respondents to our survey)
- the FSA should consider the timetable of other institutions for issuing material, in particular the European Commission. It should avoid issuing its own documents when EU consultation is known to be in hand
- the regulator should reduce the amount of informal guidance issued. Speeches need not be accompanied by press releases; newsletters could be reduced in number
- the FSA should cease or limit its practice of issuing press releases. Regulated firms are well able to review material without the need for press releases.

While the CISI understands that the FSA needs to react publicly and swiftly to fast-moving events, we feel that the spread of issuance is out of proportion with any perceived problem. ■

A CISI survey of members in the compliance sector highlights that FSA output is growing faster than firms can absorb it

Got a story to tell or a view to share? Email Richard Mitchell at richard.mitchell@cisi.org

TECHNOLOGY

CISI smartphone app

Keep up with the *Securities & Investment Review* when you are on the move, thanks to the launch of the first CISI application for smartphones.

The CISI publications app allows members to download not only the *S&IR* but also the *Regulatory Update and Investment Management Review* (only available to Fellows and full members) directly to their smartphones. Members can then read articles from these publications on the go. The app automatically uploads the time spent reading to the member's CPD log.

The app will update when a new publication edition is released and archive the old version. It is free to members and can be downloaded from the CISI website on cisi.org/app, where it can be bookmarked to your smartphone.

CISI Chief Executive Simon Culhane, Chartered FCSI, said: "The changes to CPD are very significant for the retail financial services industry and, for the first time, the detail of CPD will be measured, monitored and audited to comply with the FSA requirements. This is particularly important in the light of the Retail Distribution Review (RDR) where there is a requirement for all retail advisers to complete annual CPD."

The CPD requirements for retail advisers, in the scope of the RDR, include 35 hours of retail-relevant CPD a year, 21 hours of which must be structured learning. The balance can be attributed to unstructured learning, which includes self-directed reading of publications, such as that provided by the CISI publications app.

The CISI publications app is available to members as a web app for the iPhone or iPad running IOS 4.2 and above and Android smartphones running Android OS 2.1 and above.

QUALIFICATIONS

Training first in Africa

KEDARI

Olusola Olowoyeye, Head of Risk Management & Consulting at Kedari

The CISI has accredited Kedari Consulting as its first training provider in sub-Saharan Africa.

Kedari, based in Nigeria's capital, Lagos, is tapping into growing demand for CISI qualifications in the region. It will initially offer training for the CISI's flagship Investment Operations Certificate (IOC) – also known as the Investment Administration Qualification – and the Advanced Certificate in Operational Risk (AOR). The IOC is designed to train staff working in the administration and operations areas of the business. AOR is aimed at staff regardless of their sector as it enables them to understand and limit the risks faced by firms.

Kedari Consulting, a subsidiary of Kedari Capital, runs a variety of training programmes on risk management, corporate governance and regulatory compliance for banks and other financial institutions, government bodies and investors.

Olusola Olowoyeye, Head of Risk Management & Consulting at Kedari, said: "Kedari Consulting is excited to be associated with a world-renowned professional body for the financial services industry.

"The recent global financial crisis has helped to highlight the urgent need for increased risk management knowledge and skills within Nigeria. Kedari Consulting aims to utilise its status as a CISI-accredited training provider to raise the risk management profile, not only within Nigeria but also across Africa. This will ensure that global best-practice permeates the industry on this side of the globe."

ETHICS

Left to right, CISI Chief Executive Simon Culhane, Chartered FCSI, with FinanceMalta's Head of Administration Dr Bernice Buttigieg and Head of Business Development Bruno L'ecuyer

Integrity at work in Malta

Members of the Maltese financial services community considered a series of ethical dilemmas at a CISI Integrity at Work session.

CISI Chief Executive Simon Culhane, Chartered FCSI, visited Malta to run the interactive workshop. The 20 delegates voted, via hand-held devices, on how they would respond to real-life business situations. The event was the first of a series of educational clinics being held by FinanceMalta, a public-private initiative set up to promote the island as an international financial centre. It was held at FinanceMalta's offices in Valletta.

The CISI is establishing a national advisory council (NAC) in Malta to support its development there. Alex Bustos, Chartered MCSI, has been appointed President of the NAC.

Some of the CISI's key qualifications have been approved by the Malta Qualifications Council as appropriate for those working in the Maltese investment industry. These include the Islamic Finance Qualification, Certificate suite and Investment Operations Certificate.

The CISI is working closely with the Institute of Financial Services Malta to promote its Certificate and operations exam suites to those sitting self-study qualifications.

Simon Culhane said: "We are very pleased to be invited by FinanceMalta to offer our insight into the ethics and integrity debate, which is integral to CISI's mission and to the continuing professional development of our global membership."

The CISI has delivered its Integrity at Work event in countries including India, Singapore, China, the USA, Sri Lanka and Poland.

40,954 *The number of entries to CISI exams in 2010/11. Of this figure, nearly 21% of exams – a total of 8,493 – were taken by candidates from outside the UK*

PROFESSIONALISM

CISI roadshows reveal gap in RDR awareness

The CISI has urged the FSA to take steps to raise awareness of the impact of the Retail Distribution Review (RDR) within the financial services sector. The call follows feedback from attendees at roadshows held around the UK by the CISI to help practitioners prepare for the RDR. More than 500 people attended the roadshows, with nearly 440 taking part in a survey.

A third of survey respondents – 35% – were still only a little familiar with the requirements of the RDR, with a further 6% not familiar at all. There was also a lack of awareness of how the RDR fits into the broader training and competence regime. CISI Managing Director Ruth Martin said: "It is crucial that the FSA proactively undertakes its own awareness-raising activities in this regard."

The roadshows were staged following the publication by the FSA of its policy statement and final rules about professionalism for the RDR (PS11/1). Retail investment advisers will need to obtain annually a Statement of Professional Standing (SPS). This will incorporate evidence of satisfactory qualifications at level 4 or above (including filling gaps via structured learning), completion of at least 35 hours of relevant CPD each year, and adherence to a professional body's code of conduct.

On a more positive note, the CISI survey showed that 81% believe that they will either definitely or probably satisfy the SPS requirements by the deadline of 1 January 2013, and more than 92% believe they will meet the CPD requirements.

Ruth Martin added that she was "particularly pleased" that so many CISI stakeholders are on course to satisfy these requirements. Of attendees, 85% believe that on balance, or definitely, the FSA's proposals will bring about higher standards of professionalism.

For further information about RDR requirements, visit cisi.org/rdr

Retail products ban

Seven out of ten financial services practitioners (72%) believe that the UK regulator should be given powers to ban retail products, according to the survey conducted at the RDR roadshows.

This question was asked within the framework of the announcement earlier this year that the new Financial Conduct Authority, one of the regulatory bodies replacing the FSA, will be entitled to ban retail products or limit their distribution for up to 12 months. Among those who favoured greater powers for the regulator, 27% were "strongly" in support and 45% agreed "on balance".

CHARITY

Cash for curry

The fourth annual Lord Mayor's Big Curry Lunch proved to be hot stuff, raising more than £214,000 for ABF, the Soldiers' Charity.

More than 800 tickets were sold for the buffet lunch at London's Guildhall. The proceeds will benefit former servicemen and women and their families affected by the conflicts in Afghanistan and Iraq.

Of the money raised, more than £60,000 was generated from a silent auction. Lots included dinner and an overnight stay at Mansion House, the Lord Mayor's residence.

EVENTS

Alan Yarrow, front, centre, with attendees at the lunch at Fishmongers' Hall. Hector Sants is pictured in the third row, left, and Angela Knight CBE is pictured in the second row, second from right

Honorary Fellows lunch

The CISI held an annual lunch for its Honorary Fellows at Fishmongers' Hall in the City of London.

Honorary Fellowship – which carries the designatory letters FCSI(Hon) – is awarded by the Institute Board to those who have contributed with distinction to financial services and the CISI. There are currently 45 Honorary Fellows.

The two latest Honorary Fellows – FSA CEO Hector Sants and Angela Knight CBE, Chief Executive of the British Bankers' Association – were presented with the distinction by CISI Chairman Alan Yarrow, Chartered FCSI(Hon).

To see a full list of Honorary Fellows, visit *cisi.org/mFCSIhon*

SURVEY

Are split bonuses the future?

More than three-quarters of financial services players believe that banks should follow John Lewis's lead and split their bonus pool among all staff as an equal proportion of salary, a CISI survey shows.

John Lewis employees – who are partners of the company – will each receive a bonus worth 18% of annual pay based on the store group's 2010 profits. Of respondents, 78% said that banks should use the John Lewis system of remuneration, while 22% opposed it.

"It's about everyone pulling together, not individuals," said one respondent in favour of a change. "Our industry needs to learn that it is about teamwork – front, middle, back and infrastructure working collectively." Another contributor said: "This sort of reward system is clear and transparent. Favouritism and inequality would become a thing of the past."

Opponents argued, however, that such a step would not be fair. "The hardest-working bankers should be rewarded more than those who just come to work to watch the clock and get paid," one said. "Anyone in a bank wanting similar treatment should consider applying to John Lewis instead!"

Echoing that view, another respondent argued: "Some employees will do the minimum and, by automatically receiving an 18% bonus, there would be no incentive to do anything extra."

To take part in the latest CISI survey, visit *cisi.org*

RECEPTION

Chartered members' celebration

The CISI has held an inaugural reception to congratulate members who have successfully qualified to become personally Chartered. More than 250 Chartered members and Fellows attended the event at Fishmongers' Hall in the City of London.

CISI Chairman Alan Yarrow, Chartered FCSI(Hon), addressed the reception. He said that Chartered membership signified reaching the pinnacle of professionalism and demonstrated commitment to the highest standards of integrity and excellence.

He said that members were rightly proud to achieve Chartered status and were "ambassadors for the Institute". The CISI also congratulated the latest 2,800 members to become individually Chartered via an advert in the *Financial Times*.

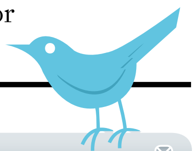
More than 3,750 members have secured a personal Charter since the CISI became a Chartered body in November 2009.

To find out more about the route to becoming personally Chartered, visit *cisi.org/individualcharter*

Personally Chartered members and Fellows gather at Fishmongers' Hall for their inaugural CISI reception

1,162

The number of student members in the United Arab Emirates taking CISI exams. It is the highest CISI student membership figure for any country outside the UK



ONLINE

BEST OF THE BLOGS

1 guardian.co.uk/commentisfree/2011
Spanish efforts to persuade investors that Spain should not be lumped with Portugal, Greece and Ireland appear to be paying off, says *The Guardian*. Deep spending cuts and efforts to clean up the troubled cajas – regional savings banks – have, the editorial observes, seen the interest rate on loans to Madrid drop to 5.2%, meaning that "the market judges its creditworthiness to be somewhere between that of Berlin and Lisbon".

2 nicksargen.com
Fort Washington Investment Advisors' Nick Sargen says that, so far, Spain has been successful in differentiating itself from Europe's problem countries. But it is "the pivotal country that could dictate whether the sovereign debt crisis is contained or morphs into a bigger issue". The Spanish Government has taken decisive action bolstering the country's financial system via increased capital requirements for cajas. Even though the Bank of Spain's €15bn capital deficit estimate falls short of the €50bn figure recommended by both Moody's and Fitch, it has "calmed concerns for the time being and Spanish banks have been able to reduce their borrowings from the European Central Bank significantly in recent months".

3 ftalphaville.ft.com/blog/2011
Joseph Cotterill for the *FT* suggests that the secret to dealing with Spain's cajas is: "Write down. Really write down. Then recapitalise. Then rebuild." Investors are "hugely wary" of how caja assets are being valued and many are not convinced they will find the private backing required to deliver the 8-10% core capital needed to avoid state help. Why might Spanish officials be concerned about signalling poor caja valuations to the market? Is it, asks Cotterill, because "they're worried about the real valuations of the 'better' banks and the loan loss assumptions that underpin them?"

See page 16 for a full discussion of Spain's cajas.

Do you have a blog recommendation?
Please send it to the Editor: ***hugo.cox@wardour.co.uk***

PROFESSIONAL STANDARDS

Disciplinary action

Member Graham Betton

As a result of action brought by the FSA, Mr Betton was deemed to be in breach of membership regulations 16.1(d) and 16.2(b) and was invited to appear before a CISI disciplinary panel.

The panel found him to be in breach of the aforementioned regulations and determined that he should be permanently expelled from the CISI.

Member Matthew Butterfield

As a result of action brought by the Guernsey Financial Services Commission, Mr Butterfield was deemed to be in breach of membership regulations 16.1(d) and 16.2(b) and was invited to appear before a CISI disciplinary panel.

The panel found him to be in breach of the aforementioned regulations and determined that he should be expelled from the Institute. He was advised that he could apply for re-admission after 1 August 2015 but that any application would be considered in the light of his situation at that time.

CLAY '*MUDLARK*' HARRIS

Back story on Graeme Parfitt of Williams de Broë

Inspiration can strike anywhere, even on crowded pavements. Graeme Parfitt probably wouldn't be where he is today – Operations Manager at Williams de Broë in Bournemouth – were it not for the hustle and bustle of the City of London. But fulfilment doesn't always run in a straight line.

Graeme's dream when he left school was to have a glamorous career as a criminal barrister. He went to City University to study law. The excitement he saw all around him, as City workers rushed past about their business, made him reconsider that focus.

It awakened an interest in company law. "By the end of my first year, I wanted to be a solicitor," he says. After getting his degree, he took the mandatory legal practice course, but the immediate prospect of working in a junior role for a large commercial law firm did not appeal. "I knew I couldn't bring myself to sit and draft financial contracts all day," he explains.

Graeme realised then that his original attraction to the law had been the right one and that becoming a barrister was still his dream. But two to three years of further training was not practical.

Illustration: Luke Wilson

So he went home to Bournemouth and took a job in credit control with an insurance company. "It was a practical decision as much as anything else," he says. Then a local recruitment agency suggested an administrative position with Williams de Broë.

Graeme joined the investment manager as an operations administrator at the end of 2005, a middle- and back-office role that involved stock transfers and setting up new accounts. Here his excitement for the City was re-kindled, he explains: "I fell in love with finance – the dynamism and rapid pace of things. Seeing the screens with prices going up and down is absorbing."

> "I fell in love with the dynamism and rapid pace"

He was asked to lead the account set-up team, much of whose activity involved bulk transfers of client business as Williams de Broë acquired teams of investment managers. And, in August 2009, Graeme became Operations Manager in Bournemouth, the hub of Williams de Broë's administration with 30 back-office staff. Functions such as settlements and corporate actions now became his responsibility.

"I find it very, very hard to stop doing day-to-day work," Graeme says of his move to a manager role, especially when it involves something like trusts.

The variety of work at Williams de Broë means that training plays an important role. Graeme didn't find the CISI's Investment Administration Qualification (IAQ) – now also known as the Investment Operations Certificate (IOC) – particularly difficult, in part because of his experience. "I had gathered the knowledge I had, colloquially, on the job." But it consolidated his knowledge overall.

For newer entrants, Graeme believes that the IOC/ IAQ is "genuinely useful", so he was encouraged when Williams de Broë substantially increased its training budget. "We're going for a higher level of formality in our qualifications."

Graeme Parfitt

Operations Manager, Williams de Broë

Do you have a back office story?

mudlarklives@hotmail.co.uk

OPERATIONS

Sri Lanka milestone

Minoli Bandara of Millennium Information Technologies

Three staff from a leading technology solutions provider are the first in Sri Lanka to attain the CISI Investment Operations Certificate (IOC). Mumtaz Rahim, Minoli Bandara and Nuvina Padukkavidana work in the software division of Millennium Information Technologies Pvt Ltd (MillenniumIT) in Malabe. The IOC (also known as the Investment Administration Qualification or IAQ) is a practitioner-led programme for administration and operations staff that comprises three units. Minoli said: "This exam has enhanced my knowledge about the financial services industry and helped me relate better to my day-to-day work." In 2010/11, 11,805 candidates sat the IOC/IAQ. Of those, 2,490 were outside the UK.

For further information about the IOC, visit *cisi.org/ioc*

60-second interview

with: **Karri Vuori ACSI,** the 5,000th candidate to complete IntegrityMatters, the CISI's online ethics workshop and test. He is Assistant Director in Corporate Finance at Charles Stanley Securities in the City of London

Q *In what way did you find the test useful?*

The test involves scenarios not dissimilar to those faced in everyday work situations. It is helpful to take a step back every now and again to think about the various ethical issues we face.

Q *How do you rate standards of ethical behaviour within financial services?*

I've always worked for firms that pride themselves on the independence and integrity of their advice, so I would rate the ethical standards of the people I have worked with extremely highly. That said, it takes only a few cases to undermine people's confidence in the industry.

Q *Are you surprised by a recent survey that shows that public trust in UK banks has slumped to 16%?*

Not in the slightest. The vast majority of workers in the sector have little or no ability to make the sort of decisions that led to the financial crisis. However, the culture at the top, and the nature of remuneration arrangements at many banks prior to the downturn, led to dangerous short-termism. The damage has been done and the public has every right to ask questions of the banking industry.

Q *How can the industry restore public confidence?*

Increased transparency, a focus on effective systems and controls, and – most importantly – a corporate culture, communicated from the top, that embraces ethical behaviour.

To find out more about IntegrityMatters, which the CISI launched in September 2008, visit *cisi.org/integritymatters*

Ask the experts...

Simon Willis FSCI

Daniel Stewart & Company Plc

EUROPEAN FINANCIAL STABILITY FACILITY (EFSF) BONDS

How the first bonds issued by the EFSF helped buoy confidence in the euro

The problem

During November 2010, confidence in the euro was evaporating fast as it became clear that Ireland would have to accept a bailout. In the spring of last year, Greece had been the first eurozone country to accept one following the financial crisis, with a three-year €110bn package.

Portugal was seen as the next domino likely to fall. More importantly, the market feared for Spain, a far larger economy than the others, raising fears about the stability of the single currency. Following the bailouts of Greece and Ireland, a Portuguese rescue would consume most of the €440bn remaining in the European Financial Stability Facility (EFSF), the fund created in 2010 to help maintain the stability of the euro when member states ran into difficulty. The EFSF is part of a larger safety net that includes the European Financial Stabilisation Mechanism (EFSM), an emergency funding programme guaranteed by the European Commission, and the International Monetary Fund.

Reflecting these worries, there was an increase in bond yields in these countries, and a widening of credit default swap spreads – an increase in the cost of insuring against the countries going bust.

The solution

One option was to increase the size of the EFSF. But by how much? When markets have a target in their sights, restoring confidence in it can become an impossible task. The alternative solution was the issuance of bonds, for the first time, by the EFSF. The key was that the EFSF enjoys a triple-A rating. While credit ratings have come in for their fair share of criticism post crisis, they are still the key to the pricing of many instruments.

For those investors around the world who are allowed to invest only in triple A-rated instruments, the EFSF bonds would offer higher yields than alternative equivalents.

The inaugural tranche of €5bn was placed on 25 January as part of both the EU/IMF bailout package for Ireland and the overall plan to issue up to €26.5bn of bonds during 2011 and 2012, together with €22.5bn in bonds from the EFSM.

The €5bn issue was priced attractively and, with demand for €44.5bn, the issue was nearly nine times over-subscribed. Notably, the Government of Japan took over 20% of the issue, providing an important vote of confidence in the euro from Japan.

Looking ahead, the issue of bonds by the EFSF and EFSM may prove to have stabilised the euro but also to have provided a significant step in creating a eurozone-wide bond market with significant liquidity.

Do you have a question on anything from tax to virtual trading?
richard.mitchell@cisi.org

SELECT BENEFITS

Year-round savings

The Thomas Cook Holiday Club is the passport to savings on thousands of breaks for CISI members.

A guaranteed discount of 8% is offered for online bookings on holidays from more than 100 tour operators. The choice of getaways includes cruises, ski holidays, tranquil spa breaks and relaxing weeks in the sun.

The deal is available through the Select Benefits package, which offers nearly 50 discounts.

A new benefit is supplied by TranslateMedia, a global, award-winning language-services agency with offices in the UK, Europe, Asia and the US.

The agency employs more than 5,000 specialist translators covering over 85 languages around the clock. Services include document translation, transcription and dictation, onsite and telephone interpreting, and typesetting.

CISI members get a 15% discount off standard translations and can save 20% on premium translations (this service includes an additional proof read by a second accredited translator).

For more information on how to obtain these deals and other savings, visit *cisi.org/memberlogin*

CISI Select Benefits is managed on behalf of the CISI by Parliament Hill Ltd of 127 Cheapside, London, EC2V 6BT.

QUICK QUIZ

Test your industry knowledge

Illustration: Cameron Law

The *S&IR's* Quick Quiz features questions from CISI elearning products, which are interactive revision aids to help candidates prepare for their exams.

The answers are on page 29.

To order CISI elearning products, please call Client Services on ***+44 (0)20 7645 0680*** or visit ***cisi.org***

Q1 Which ONE of the following types of institution would typically provide advice to, and arrange finance for, companies that want to float on the stock market?
A) Stockbrokers ***B)*** Retail banks ***C)*** Investment banks ***D)*** Custodians

Q2 Which ONE of the following statements relating to structured products is true?
A) They are primarily aimed at institutional investors ***B)*** They have a standardised, rigid product structure ***C)*** They are high-risk/high-reward investments ***D)*** They are packaged products based on derivatives

Q3 Which ONE of the following investments is outside the scope of insider dealing?
A) Commodity futures ***B)*** Gilts traded on the LSE ***C)*** Options on the FTSE 100 Index
D) Shares traded on AIM

Q4 Market abuse became a statutory offence under which ONE of the following Acts?
A) Banking Act 1987 ***B)*** Public Interest Disclosure Act 1998 ***C)*** Criminal Justice Act 1993
D) Financial Services and Markets Act 2000

Turning QE2

Investors should not worry over the imminent end to US quantitative easing: stimulus from the US Fed has not been the main force driving up risky assets over the past 18 months

"**THE ONLY THING** we have to fear is fear itself." Franklin D Roosevelt's words at his 1933 presidential inauguration – in the middle of a bank panic – are instructive now. The financial crisis has passed, but the global economy is still feeling its way to surer ground.

Given this lingering uncertainty about recovery, some investors worry that the Federal Reserve will pull the plug too soon on 'quantitative easing' (QE), a huge asset-buying programme designed to revive growth. If anything follows 'QE2', they say, it should be 'QE3': another round of bond buying to inject hundreds of billions more dollars into the financial system. One recent CNBC poll showed that a third of portfolio managers were positioned for an extension of QE beyond June.

These fund managers are kidding themselves. Judging by the comments of Fed officials, notably a hawkish James Bullard of the St Louis Fed, the US central bank is all but certain to end QE in the summer. There will be no gradual wind down into the autumn.

Nor should there be. Recent economic statistics have offered enough evidence of a turnaround in the US jobs market to suggest that America is firmly on the road towards a self-sustaining recovery. The spectre of deflation has been banished. Indeed, a rise in inflation seems more likely. Pumping up the monetary base further would only increase that risk.

Moreover, investors fretting about the implications for stock markets of an end to QE should relax. As Gerard Minack, a Morgan Stanley analyst, points out in a striking piece of research, the main thing to fear about QE ending is the fear itself.

The nervousness in the markets is based on a belief that the Fed's action has been the main driver of equities and other risky assets over the past 18 months. And, at one level, equities and QE do look correlated. The rally in the S&P 500, the benchmark US stock index, that began in March 2009 and the scale of the Fed's buying of Treasuries appear broadly synchronised.

But take a look at the relationship between the S&P and US initial jobless claims figures, a key measure of unemployment, over the same period. The correlation here is much more convincing. They track each other closely. As Minack says, the Fed's action has not been unimportant. The emergency monetary measures that followed the collapse of Lehman Brothers prevented a depression, sparking a powerful relief rally in equities. But, sentiment aside, nobody has adequately explained how QE should have a material effect on demand for risky assets.

The evidence of any impact on investor demand for Treasury bonds, the very assets that the Fed is buying, as well as activity in the wider debt markets, is mixed. For example, when the Fed sold Treasuries in late 2007, bond yields, which move inversely to prices, fell. They rose when the Fed bought in 2009 and fell when it stopped buying in 2010. When it started to buy late last year, yields fell.

Forecasting the bond market's direction based on what the Fed is doing does not look like a great idea. Similarly, betting on how stocks will behave when the Fed stops buying in June is a bold step, especially as swings in ten-year Treasury yields have tended to track surprises in economic data.

> *My best guess is that the bond market will take the end of QE2 in its stride*

My best guess is that the bond market will take the end of QE2 in its stride. The impact on equities is far trickier to predict. Currency markets are anticipating a rise in US interest rates by the end of this year – the dollar has started to rally. Premature monetary tightening would be cause for worry. Inflation is not yet a substantial enough force to raise rates and risk choking off the US recovery.

Reassuringly, those members of the Fed pushing for a rate rise are still in the minority. As long as payrolls impress, the bull run may last a while yet. ■

Christopher Adams *is the* Financial Times' *markets editor*

Photo: Johanna Ward

The lucrative business of exchange-traded derivatives has been instrumental in driving the latest super-merger of global exchange groups. **David Wigan** explains what is behind the merger and considers whether it means less competition in this sector

Merger *risks*

THE WORLD'S SECURITIES exchanges have been on a path of consolidation for many years. But the latest wave raises questions about whether the move to fewer providers will push up costs for exchange users. It entails the proposed $25bn merger of NYSE Euronext and Deutsche Börse, which looks increasingly likely after the NYSE board rejected a richer offer from Nasdaq OMX and the IntercontinentalExchange early in April. Users worry that the merger will lock out competition in the most heavily traded derivative contracts. The alliance will bring together Europe's two biggest derivatives exchanges: NYSE Liffe, owned by NYSE Euronext; and Eurex, majority-owned by Deutsche Börse. Between them, Liffe and Eurex control more than 90% of European equity derivatives business, a market dominated by options on the Euro Stoxx 50, the second most active index option in the world after Korea's Kospi 200 contract, according to the World Federation of Exchanges. NYSE Liffe, the consolidated derivatives business of the NYSE Euronext Group, operates futures and options markets beyond Liffe, in Amsterdam, Brussels, Lisbon and Paris. It accounts collectively for €2trn every day. Eurex, meanwhile, offers options on Dutch, Scandinavian, French, German, Italian, Russian, Spanish, Swiss and US equities, and an array of global indexes. Derivatives are an increasingly lucrative part of the business for global exchanges as volumes increase. The US-based Options Clearing Corporation said in January that total volumes rose by 8% in 2010, making last year the busiest in history and the eighth consecutive year of record options trading. NYSE Euronext's global derivatives business posted all-time-high volumes in 2010, with an average daily level of 8.43 million contracts, representing an increase of 24% on 2009. The deal is the latest in a line of tie-ups in the derivatives arena, which started in 2007 with the merger of Chicago Mercantile Exchange – the third of the 'big three' derivatives exchanges after NYSE Liffe and Eurex – and the Chicago Board of Trade, to form CME Group. From its art-deco Chicago headquarters, CME Group controls 98% of US futures trading. The growing appeal of derivatives to exchanges is matched by the waning appeal of traditional equity trading. European equities sector revenues have shrunk by 15% since 2008, according to a recent report by Morgan Stanley and Oliver

A history of consolidation

Key Deutsche Börse
NYSE Euronext
Others

1993
Deutsche Börse created as holding company for Frankfurt Stock Exchange

1998
Eurex formed by merger of German and Swiss derivatives exchanges, owned by Deutsche Börse and SWX Swiss Exchange respectively. By 2005, Deutsche Börse is receiving 85% of the joint venture proceeds

2000
Euronext formed by merger of Amsterdam Stock Exchange, Brussels Stock Exchange and Paris Bourse

2001
Euronext acquires London International Financial Futures and Options Exchange (LIFFE); becomes NYSE Liffe in 2007

Wyman. Driving the decline has been shrinking fee income in the cash equities market. Pan-European cash equity revenues were between €650m and €700m in 2010, against a total value traded of €9.1trn. That implies an average revenue per trade of 0.7 basis points – 0.007% – for the exchanges.

Revenues are now under pressure from multilateral trading facilities (MTFs), introduced in 2007 after the Markets in Financial Instruments Directive. MTFs brought fragmentation to the cash market, allowing equities to be traded across venues instead of concentrating liquidity on just one exchange. Average revenue per trade at MTFs is about 0.1 basis points, putting enormous downward pressure on exchange revenues and cutting exchange volume share from 70% in 2006 to 52% in 2010.

This has triggered consolidation in equities exchanges to keep down costs. The merger proposal of NYSE Euronext and Deutsche Börse came less than a week after London Stock Exchange (LSE) Group outlined plans to join with TMX Group of Canada in a $3.25bn deal. In February, BATS Global Markets, the fourth-largest operator of US equity markets, agreed to buy Chi-X Europe, the region's largest MTF.

Appeal of derivatives

In contrast with the pressure on equity trading, derivatives exchanges are showing an increase of between 3% and 5% in annual growth rates by number of traded contracts, Morgan Stanley and Oliver Wyman report. Traded volume in selected contracts has grown by 10% over the past five years. Operating margins for derivatives are estimated to be as high as 55%.

NYSE Euronext's cash equities business fell by 10% last year, and by 2012, the company may generate more than 50% of its revenues from options and futures, say analysts. "I've never thought that the future of exchanges was just about trading equities," said Duncan Niederauer, NYSE Euronext Chief Executive, in February (curiously, he chose to make his comment on the floor of the New York Stock Exchange, principally an equity-trading venue).

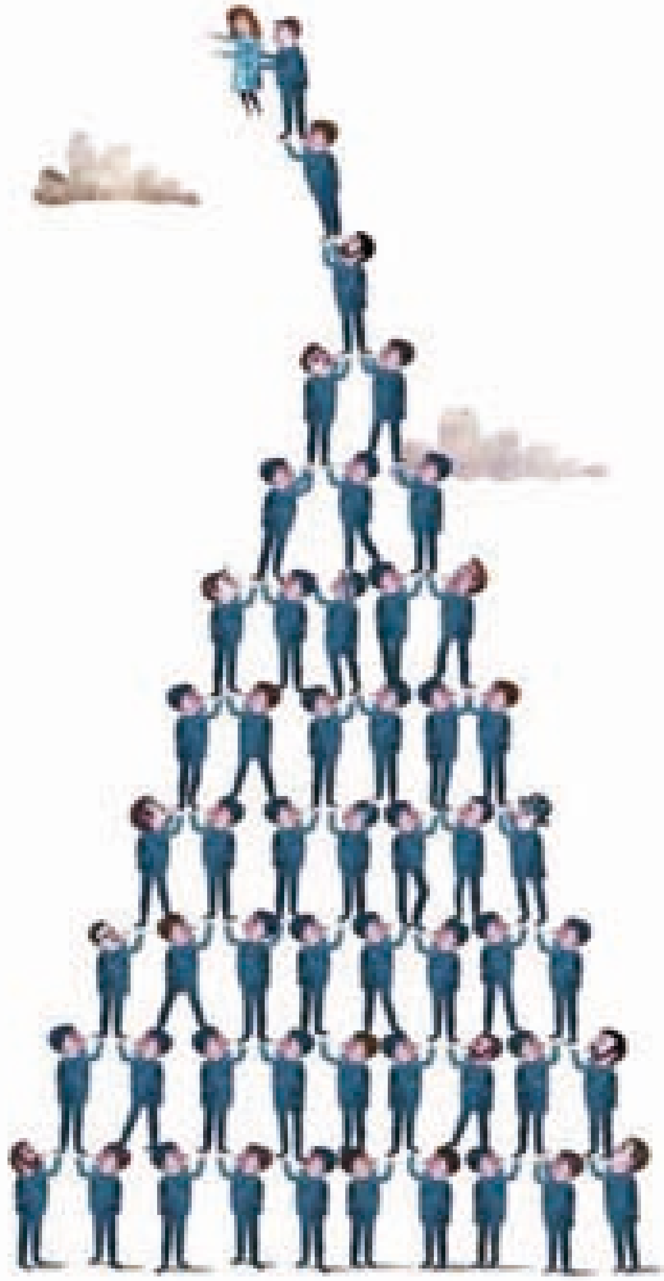
Combining NYSE Euronext's derivative operations with Deutsche Börse's Eurex will create a global behemoth worth $25bn. Analysts estimate that, within three years, this will earn some $1.18bn from derivatives in the US and Europe. There are concerns about the effect that this will have on competition and prices. "Now the two operators are merging, and naturally that is going to raise questions about the impact on competition," says Gerald Perez, Managing Director of Interactive Brokers in London. "We will need to wait and see whether exchange fees increase or decrease once the merger is approved."

But competition is already limited in this sector. "One thing we should be clear about is that consolidation will not lead to much less competition, since in most of these markets, there was very little competition already," says Ed Ditmire, an analyst at Macquarie Bank in New York. "Besides, we saw with the CME merger that consolidation did not lead to higher prices."

While the traditional exchanges have merged, the new breed of MTFs that have shaken up equity trading are now eyeing the derivatives space. BATS Chi-X has said that it expects to move into derivatives trading this year. "We are looking carefully at the derivatives business and there are certainly compelling reasons to get involved," says Mark Hemsley, Chief Executive of BATS Europe.

The LSE is in the process of migrating its EDX business on to its new Turquoise Derivatives platform, and The Order Machine, an alternative trading system based in Amsterdam, plans to move into single-stock options in the coming months. Turquoise Derivatives,

Investors fear that the merger will lock out competition in the most heavily traded derivative contracts by bringing together Europe's two biggest derivatives exchanges



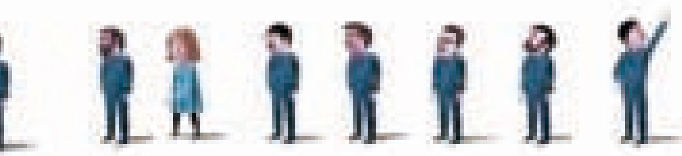


Illustration: Cameron Law

2003 Euronext shifts all derivatives products traded on its affiliated exchanges onto LIFFE's electronic trading platform

2004 Eurex US launched

2006 The New York Stock Exchange (NYSE) merges with Archipelago Holdings, the electronic communications group, to form NYSE Group

2006 Deutsche Börse launches a takeover bid for LSE and fails (following failed merger in 2001)

2006 NYSE and Euronext merge in a $14bn deal, creating a transatlantic stock exchange with a market capitalisation of $26bn

2007 Eurex acquires major US options exchange, International Securities Exchange (ISE), for $2.8bn

Clearing the key for NYSE Euronext

Central to the challenges faced by new exchange providers is ensuring that there is sufficient liquidity in the contracts that they make available. The must also provide access to clearing, the process by which credit exposure is managed in the period between the trade being made and completed, or settled. Derivatives traded through Eurex are cleared exclusively through Eurex Clearing, a 'vertical silo' arrangement that locks out competitive offerings. Similarly, in the US, CME clears its futures business through CME Clearing, owned by the CME Group.

The issue of this vertical clearing – where participants are limited to a single clearing provider that is affiliated to the exchange – has attracted the attention of the US authorities. In January 2008, the Department of Justice recommended "a thorough review of futures clearing and its alternatives", including the horizontal utility models employed in equities and options, where participants using an exchange may choose between various participants to clear their trades.

It is through the clearing route that NYSE Euronext wants to muscle in on CME's dominance of the futures markets in the US. In April, NYSE Liffe announced plans to launch a complete suite of interest-rate futures, from three-month Eurodollars to 30-year bonds.

The appeal of the new products is that users who trade other products on NYSE Liffe's other exchanges will end up with a small total bill for clearing. The key lies in a new company that will be responsible for clearing trades for the new initiative: the New York Portfolio Clearing (NYPC), a joint venture between NYSE Euronext and the Depository Trust & Clearing Corporation (DTCC), the leading provider of clearing and settlement in the US.

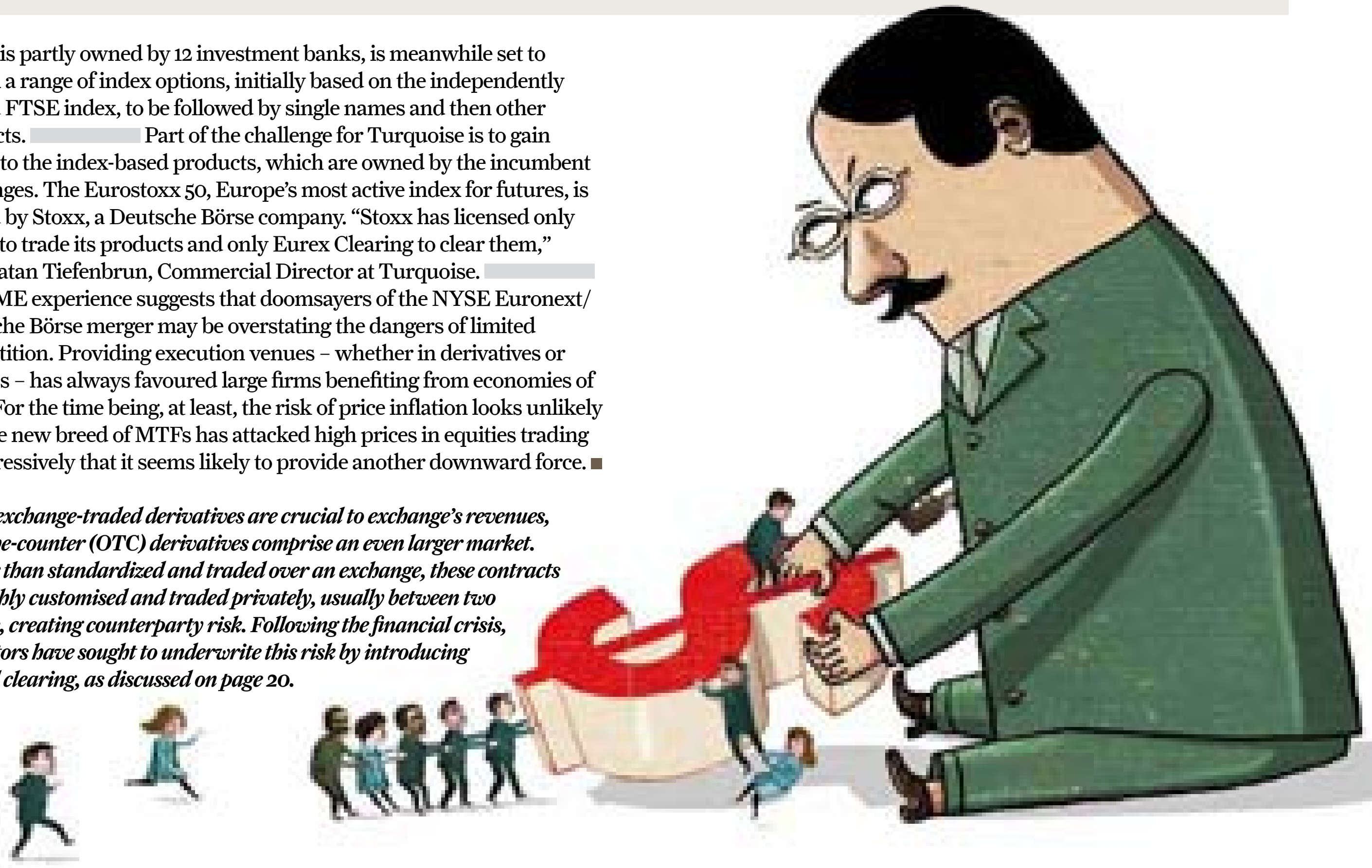
Uniquely, the NYPC will be a single clearing house for both cash instruments, such as equities, and futures. This will allow 'one-pot margining', enabling users to save on their clearing costs. A cross-margining agreement between DTCC and NYPC will mean that users who trade multiple positions in multiple instruments with NYSE Liffe will have their margin requirements netted into a single payment.

The horizontal clearing model – clearing trades from multiple exchanges – is already functioning efficiently in US options, where nine exchanges compete but where all trades are cleared by a single clearing provider, allowing cross-margining. Such has been the success of option competition in the US that the number of exchanges is set to increase, according to executives speaking at the recent US Futures Industry Association conference in Florida. *Bloomberg* reported Chicago Board Options Exchange Chairman and Chief Executive Officer William Brodsky as saying that up to five more options venues could be operational in the next three years, bringing the total to 14 from the current nine (compared with five in 2000).

"All of the options exchanges clear through the Options Clearing Corporation [the world's largest equity derivatives clearing organisation] and there is huge competition in that space," says Andy Nybo, Principal and Head of Derivatives at Tabb Group. "It's pretty easy to set up an exchange and provide execution competition, but the key to breaking into derivatives is to move away from vertical clearing."

which is partly owned by 12 investment banks, is meanwhile set to launch a range of index options, initially based on the independently owned FTSE index, to be followed by single names and then other products. Part of the challenge for Turquoise is to gain access to the index-based products, which are owned by the incumbent exchanges. The Eurostoxx 50, Europe's most active index for futures, is owned by Stoxx, a Deutsche Börse company. "Stoxx has licensed only Eurex to trade its products and only Eurex Clearing to clear them," says Natan Tiefenbrun, Commercial Director at Turquoise. The CME experience suggests that doomsayers of the NYSE Euronext/Deutsche Börse merger may be overstating the dangers of limited competition. Providing execution venues – whether in derivatives or equities – has always favoured large firms benefiting from economies of scale. For the time being, at least, the risk of price inflation looks unlikely and the new breed of MTFs has attacked high prices in equities trading so aggressively that it seems likely to provide another downward force. ■

While exchange-traded derivatives are crucial to exchange's revenues, over-the-counter (OTC) derivatives comprise an even larger market. Rather than standardized and traded over an exchange, these contracts are highly customised and traded privately, usually between two parties, creating counterparty risk. Following the financial crisis, regulators have sought to underwrite this risk by introducing central clearing, as discussed on page 20.



2007
NYSE beats off Deutsche Börse to acquire Euronext for $10.2bn, forming NYSE Euronext. Claims to be the "first global stock exchange"

2007
CME Group formed by merger of the Chicago Mercantile Exchange (CME) and the Chicago Board of Trade (CBOT)

2011
London Stock Exchange announces merger with TMX Group, operator of Toronto Stock Exchange. New group valued at $7.7bn

2011
NYSE Euronext announces merger with Deutsche Börse, rejecting susequent richer offer by Nasdaq OMX and the IntercontinentalExchange

2011
Australian Government blocks proposed $7.8bn merger of Singapore (SGX) and Australian (ASX) exchanges

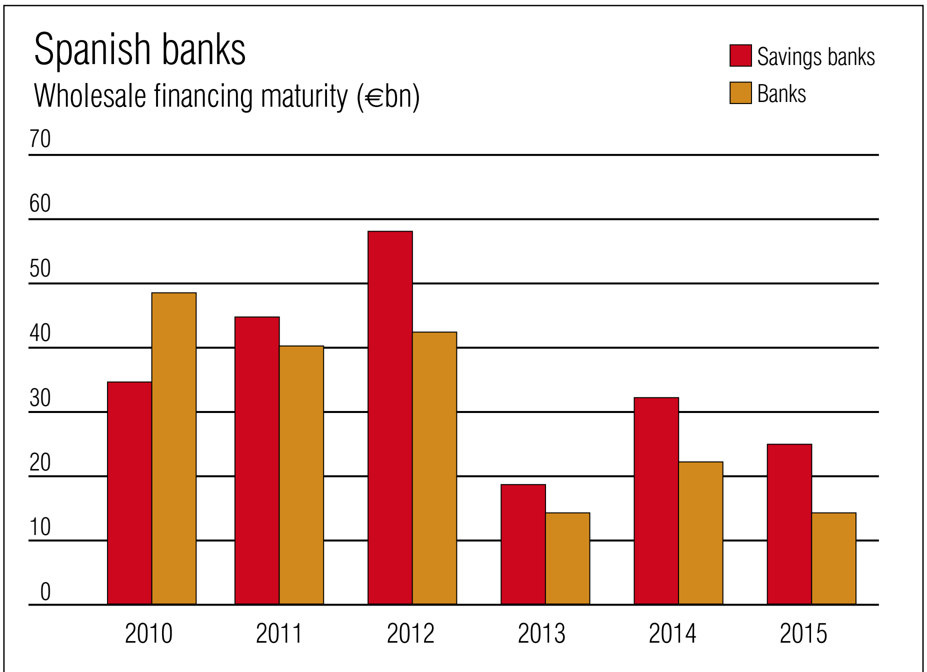
Saving the cajas

Spain's response to its troubled savings banks has been slow. **Andrew Maiden** wonders whether it is enough to avert another eurozone crisis

AFTER MONTHS OF debate and disagreement, the Spanish Government has finally acted to reform Spain's 'cajas', or savings banks. These largely unlisted financial organisations have become caught up in the ongoing European debate over sovereign debt risk. Although Madrid has been working hard to prevent Spain from following Greece, Ireland and Portugal in requiring an EU bailout, it has moved slowly to strengthen the cajas and it remains to be seen whether the newly adopted strategy will work in the long term. Spain experienced one of the world's biggest house price booms between 2000 and the global financial crisis, driven by both domestic demand and sales of second homes to northern Europeans. Commercial property prices followed a similar upward spiral. Like the blighted Irish banks, Spanish cajas – which comprise nearly half of the domestic lending market – lent heavily to developers and construction firms that were at the heart of the boom. When the market crashed, the cajas were left with a large portfolio of bad debt: some estimates put the number of homes that now lie empty waiting for a buyer at 1.5 million. The fear is that Spain's cajas will not be able to raise long-term money in the wholesale funding markets to keep them solvent. This is important if they are to maintain existing borrowing levels when current financing matures, much of which is due next year (see table, opposite). At the end of March, to meet a deadline set by Madrid, all of Spain's banks and cajas published plans to increase their capital ratios in order to avoid nationalisation. The key demand was that all listed lenders should increase their core capital ratios to 8% by September, with a 10% minimum for those with less than 20% of their capital listed, the group that includes most cajas. All of Spain's major banks have met the new requirements, with the exception of Bankinter, which will offer a bond to cover the shortfall. But only nine out of Spain's 17 cajas have done so, despite the fact that their average size is €7bn, two and a half times the average of just 12 months ago. The Spanish Government has already spent €15bn on recapitalising the cajas. In March, when the Bank of Spain published details of which cajas had already met the new requirements and how far others still had to go, it said that the sector as a whole needed no more than €15bn in capital to get there. But analysts disagree, with some suggesting that as much as €120bn may be needed to meet the final costs. Rating agency Moody's has put the required financing figure at €50bn.

Why cajas matter

Cajas keep 49% of Spanish deposits, more than the 45% held by Spain's banks. The importance of cajas to Spain's economic recovery can be seen in the impact of their woes on Spain's sovereign credit rating. In March, Moody's downgraded Spain's rating by one notch, to Aa2; one of the two reasons it gave was the parlous state of the country's banking system (the other was spendthrift regional government agencies). The €15bn of investment to date from the Spanish Government has come in the form of convertible preference shares from Spain's Deposit Guarantee Fund and the Fund for Orderly Bank Restructuring (FOBR), which is state-guaranteed and has the capacity to raise up to €99bn. Prime Minister José Luis Rodríguez Zapatero has forced mergers, which have reduced the number of cajas from 45 to 17. But further moves will meet with stiff opposition from some politicians: many cajas have strong



Source: AFI

regional roots that voters fear will become diluted by consolidation. In a refrain familiar to those who watched the Irish sovereign crisis unfold, many analysts complain that the Spanish Government's support has come too slowly and in too piecemeal a fashion: its staggered nature, they say, has merely prolonged the crisis. Despite the claim by the cajas that private-sector investors are falling over themselves to take out stakes in them, it looks likely that still more public money will have to be injected into the system. And it is not yet clear what rights private capital would have next to the public funding given by bodies such as the FOBR.

Ways forward

The eight cajas that have not yet achieved the capital requirements include most of the largest institutions. They face a range of options to avert nationalisation, including major asset sales, acquisition and applying for limited support from the Bank of Spain. Caja Madrid, Spain's oldest caja, which employs 15,000 people, has combined the asset sale route with a listing. It has ended its cross-shareholding agreement with insurance company Mapfre in return for a €188m payment. It has also sold its 20% stake in wind power company Generaciones Especiales to EDP Renewables of Portugal for €231m. It will then form a new savings bank with six other cajas, which will become the largest saving bank by assets, due to list later in the summer. Spain's second-largest caja, and its third-largest financial institution, La Caixa, is using a complex listing to hive off its more profitable division and reduce its capital requirements. The banking business will be moved into a listed holding company, Criteria, allowing it to reduce its capital ratio requirement from 10% to 8%. Its problematic real-estate assets remain outside, due to list in August. But if the market anticipates a slew of listings – either as a result of nationalisation or to avoid it – valuations will suffer. "When you warm up the markets and need to sell shares, everybody is waiting for you with a gun. Rushing in like this is not the best way," observes Fernando Bautista, a lawyer at Madrid-based Freshfields Bruckhaus Deringer. Other cajas have already asked for state support.

Spanish cajas – which comprise nearly half of the domestic lending market – lent heavily to developers and construction firms that were at the heart of the property crash

Novacaixagalicia, the country's fourth-largest caja, with assets of €78.1bn, moved first. CatalunyaCaixa, formed last summer by the merger of three cajas, announced subsequently that it would request €1.7 bn in state support. This was the sum needed to meet its capital requirements, according to the Bank of Spain; in return, the Spanish Government will become a shareholder. Both these cajas, as well as the Government, will be keen for the state to divest its interests in the sector, possibly through a private sale, bond issue or employee rights issue. Just as some of the Spanish cajas seemed to be getting their house in order, efforts received a major setback, as a key merger between four of the savings banks collapsed. Caja Mediterraneo (CAM), Cajastur, Caja Cantabria and Caja Extremadura were due together to form a new bank called Banco Base. But it became apparent that CAM, Spain's third-largest caja by market share, was in worse financial health than had been expected. On 29 March, it applied for state support to the tune of twice what the Bank of Spain had estimated it would require, apparently because of its exposure to bad property debts. All four cajas must now seek an alternative solution. The Government will probably be forced to intervene in the case of CAM, either by nationalising it or selling it on to an established bank, such as national giant Banco Santander or even a foreign player. The other three partners must identify a replacement partner if the merger is to go ahead.

Surviving, for now

It remains to be seen how much impact the failed merger will have on Spanish financial reforms and the wider creditworthiness of the Spanish Government. The listing of the new savings bank headed by Caja Madrid will be a crucial test of market confidence. David Gualtieri, Director of Equity Sales at broker Intermoney Valores SA, believes that the market is already aware of the risks in the sector and has priced these into valuations. "News about the reconstruction of the Spanish banking system has been going on for so long that people have discounted it massively," he says. "Obviously, there are going to be a few that fall off the bandwagon, but in general there's subdued optimism in Spain. We don't see the caja situation getting much worse for the time being." But the question of bad loans remains a problem and the Spanish Government must bear much of the blame. Zapatero insists that there is now sufficient disclosure on property assets at the cajas, but commentators disagree. *The Economist* reports that those savings banks involved in mergers have provided for 30% of real-estate assets going bad when the figure is actually between 40% and 50%. The market seems well disposed towards the move by La Caixa to hive off 'good bank' assets into the Criteria vehicle for listing. It looks likely that the Prime Minister's decision not to divide good debt from bad in Spain's banks was a mistake, especially in light of the success of the UK's model of creating 'bad banks' in cases such as Northern Rock and RBS. There may be hope for the Spanish cajas, but so far the efficacy of the reforms appears doubtful. ■

City beat

Sir Ian Andrews, Chairman of the Serious Organised Crime Agency, tells **Hugo Cox** how the organisation is dealing with the internationalisation of financial crime and the growing criminal opportunities that the internet offers

AS A SECTOR, financial services keeps Sir Ian Andrews' staff pretty busy. He is Chairman of the Serious Organised Crime Agency (SOCA), the national law enforcement agency that tackles serious organised crime affecting the UK, which has among its responsibilities gathering and acting on suspicious activity reports (SARs). SARs contain information, such as the cash purchase of a high-value asset or a series of large out-of-character deposits, that alerts SOCA to possible money laundering or terrorist activity. They are provided by individuals handling financial transactions, who face a statutory obligation to report concerns about suspicious practices and who may be liable, along with their employer, to civil and criminal penalties for failing to provide adequate reports. SARs are typically channelled through a money laundering reporting officer at a firm – the FSA requires that every regulated firm should have one – who decides whether the suspicion should be passed on to the UK Financial Intelligence Unit, which is hosted by SOCA. Last year's annual SARs publication, which covered the 12 months to September 2010, reported a total of just under 241,000 reports, from 5,100 organisations. Of the total, 78% came from those working in banking, a figure that was fractionally higher than that of the previous year. Of the ten largest reporting institutions, eight were banks, one was a money transmitter and one was a bookmaker.

SARs trends

"Clearly, we can't investigate every report but the data reveals significant patterns," explains Sir Ian. SARs provide valuable information that can be used by a wide variety of UK law enforcement bodies to help them investigate all levels and types of criminality, from benefit fraud and international drug smuggling to human trafficking and terrorist financing. They can also help establish a picture of the vulnerability of a particular sector or product. One of the striking recent trends, notes Sir Ian, is the growing internationalisation of financial crime following the breaking down of barriers between financial markets, especially in Europe, and the raft of opportunities revealed by the internet. A recent investigation by HM Revenue & Customs focused on both these developments concerned so-called 'carousel fraud' perpetrated in the European carbon emissions market. Seven Britons were charged in January with failing to pay VAT on €5bn worth of carbon credits. The suspects, arrested during 2009 and 2010, are accused of having bought the credits in the UK, where no VAT is charged, and selling them abroad in countries, including Belgium, where VAT is levied. The accused, it is alleged, then disappeared without paying the VAT back to the relevant governments. To prevent further frauds of this type, the majority of EU member states now require the customer, rather than the carbon trader, to pay VAT on carbon credits. But the market typifies the international and internet-enabled environment that is attracting the attention of today's sophisticated criminals. "SOCA therefore remains alert to the threat to the carbon emissions market and will continue to deploy its prevention and enforcement resources as necessary to thwart the organised criminals behind the frauds," says Sir Ian. The growth of the internet has seen cyber crime become a key concern of SOCA. Last year, the coalition Government's first national security strategy identified cyber attack, including large-scale cyber crime, as one of four principal security threats facing the UK. "Not only does the internet facilitate traditional crime, but it also introduces new types of crime," Sir Ian explains. Email scams and the like, targeting private individuals, cost the public about £3.5bn per year, according to the National Fraud Authority. Fraud costs the UK about £38bn in total, about half of which has an impact on the public purse, through crimes such as tax evasion and pension fraud. This is particularly significant, suggests Sir Ian, in the current economic climate.

Cross-border co-operation

The increasingly cross-border nature of crime, in part facilitated by the growth of the internet, has given rise to a greater co-operation between policing authorities in different jurisdictions. SOCA has 140 officers working abroad, out of a total staff of about 4,000, either embedded in local law enforcement agencies or influencing their work from a base in UK embassies and high commissions. SOCA works closely with the inter-governmental Financial Action Task Force and the EU, especially to achieve the restraint of foreign assets of criminals arrested in the UK. Sir Ian believes that there is a growing awareness at an international level, on the part of the law enforcement community and the judiciary, that a co-ordinated strategy towards preventing criminals from accessing their assets is "the best way of hitting them where it hurts". "Criminals regard the risk of being locked up as an occupational hazard," he explains, "but if you take away their fortune or otherwise disrupt them financially, this is more serious for them." Sir Ian argues that a focus on how much money is actually recovered does not always give an accurate picture of the damage law enforcement can do to criminal businesses by denying them access to the proceeds of their crime. The legion ways that SOCA can get in between criminals and their working capital, such as restraining orders or confiscation orders, are not all reflected in pure recovery figures (see table below for figures about the effectiveness of SARs in this area). The Assets Recovery Agency became part of SOCA in 2008 and Sir Ian concludes that the organisation's efforts here are having an effect that is visible in sometimes unexpected ways: "A good example is provided by the man who, when he was arrested, was found to have with him a well thumbed copy of the explanatory notes to the Proceeds of Crime Act!" ■

Hitting them where it hurts

Instances where SARs featured in a criminal investigation (over the 12 months to September 2010)

Means by which criminal separated from assets	Value of funds
Restraint order	£224.29m
Confiscation order	£41.95m
Cash seizure	£8.83m
Total	£275.07m

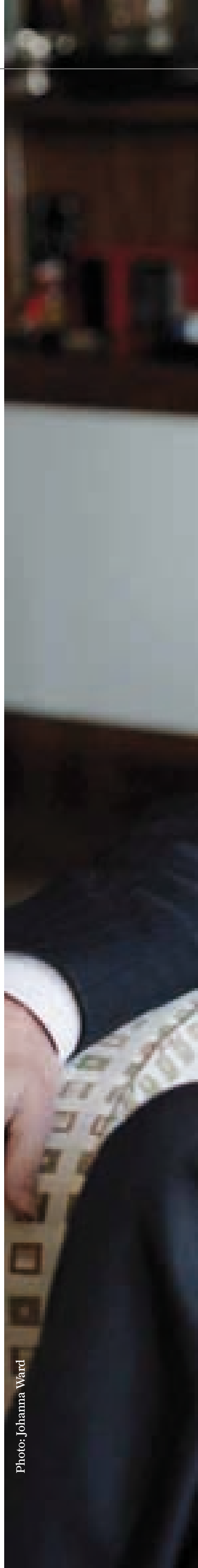


Photo: Johanna Ward

SOCA and its Chairman

The Serious Organised Crime Agency (SOCA) was created by the Serious Organised Crime and Police Act 2005. Labelled "the British FBI" by many in the press at the time, it has a range of responsibilities.

SOCA is a non-departmental public body, headed by its Director General Trevor Pearce and chaired by Sir Ian. It reports directly to current Home Secretary Theresa May and pursues her stated priorities to tackle Class A drugs, organised immigration crime, non-fiscal fraud and major gun crime. Parliamentary oversight is provided by the Home Affairs Select Committee.

The Government has announced that in 2013 it will establish a National Crime Agency (NCA) that will strengthen the operational response to serious and organised crime and incorporate the functions that SOCA currently performs. This will enable the NCA to build on the knowledge and expertise of SOCA and to exploit its intelligence, analytical and enforcement capabilities.

Graduating from Bristol University in 1975, Sir Ian went straight into the civil service. "My father was an inspector of taxes and spent my youth telling me not to become a civil servant," he relates, "but I always felt a strong public service ethos and the private sector didn't offer the same opportunity to make a difference." The benefits of co-operative effort provide much of his personal drive: "What really motivates me, I suppose, is inspiring people to achieve more collectively than they would do if they worked as individuals."

Sir Ian does not believe that his relative lack of law enforcement experience puts him at a disadvantage. "You ask the questions that people with prior knowledge of law enforcement don't think to ask," he explains. "It enables you to go in with a fresh view and consider more easily how effective the organisation is in pursuing its objectives."

Prior to SOCA, Sir Ian spent more than 34 years in defence. This included running the Defence Estates Agency and holding a senior post at the then Defence Evaluation and Research Agency, both highly technical departments in areas of which he had no prior specialist experience.

Sir Ian also points to the breadth of experience of other non-executives, who do not have a law enforcement background: Sue Garrard, was at the Department of Work and Pensions before departing to head the global communications team at Unilever, and Francis Plowden, who was previously a partner at PwC, chairs the SOCA Audit Committee and has extensive experience of non-executive roles in the public sector.

CV snapshot

2009 – Chairman, Serious Organised Crime Agency
2002 – Second Permanent Under Secretary, Ministry of Defence (MoD)
1998 – Chief Executive, Defence Estates Agency
1995 – Managing Director, Defence Evaluation and Research Agency
1995 – Civil Secretary, British forces in Germany
1986 – Assistant Private Secretary to the Secretary of State for Defence
1981 – Year-long army short service volunteer commission
1975 – Administrative trainee, MoD
1975 – BSc in Geography, Bristol University

Enforcing safety

Regulators believe that central clearing for over-the-counter derivatives is necessary to protect financial markets from future systemic collapse. **David Wigan** explains how it will work, whom it will affect and what it will cost

NOT SO LONG ago, the complex world of over-the-counter (OTC) derivatives was seen by many as the sector that would fuel a global economic revolution. Then, the 2007 collapse of the US housing market led to huge losses in derivatives underpinned by mortgages. The subsequent liquidity crisis left some of the world's biggest financial institutions teetering on the edge of extinction, only to be saved by more than a trillion dollars of handouts from the public purse.

Derivatives played a large part in the collapse. In the aftermath, regulators were charged with creating a new transparency framework for financial good behaviour, where elaborate derivative products would never again be allowed to pull the investment equivalent of a five-card trick.

In September 2009, the G20 group of countries called for "all standardised derivative contracts to be cleared through central counterparties by the end of 2012". This will provide a centralised underwriter of the counterparty risk created by a derivatives contract, protecting either party in the event of the default of the other side.

Risk control

It replaces the current bilateral system, where all the counterparty credit risk is borne by the two trading parties: should one collapse, as happened in the case of Lehman Brothers, the other is not protected. The Dodd-Frank Wall Street Reform and Consumer Protection Act enshrined central clearing when it was signed into US law last year. European Commission rules must come into force by the end of 2012.

The global dealer community committed to move some 70% of new interest rate derivatives and 80% of eligible credit default swaps from bilateral to central clearing by late 2009. In the event, it exceeded those expectations: last March, the Federal Reserve Bank of New York reported that 90% of eligible securities were being processed through clearers. “On the sell side, we are already clearing at or above targets,” says Andrew Ross, European Head of OTC Clearing at Morgan Stanley. “While there are issues in terms of cost and implementation, we are supporters of clearing because it will bring transparency, efficiency and huge reductions in counterparty risk.” The $700trn global OTC derivatives market has posted an average annual growth rate of nearly 19% over the past 12 years, according to research firm TABB Group, with turnover in 2010 reaching $1.7 quadrillion (a quadrillion is 1 followed by 24 zeros). With such huge sums at stake, the move to central clearing offers some obvious benefits. The most important is the transition from numerous bilateral counterparty relationships to a single multilateral relationship, reducing the counterparty risk that left so many clients of Lehman Brothers out of pocket. This so-called ‘loss mutualisation’ also brings capital advantages, cutting regulatory capital requirements for bilateral derivative positions and replacing them with a modest 2% requirement in respect of the clearing house, under current Basel III proposals. In order to be centrally cleared, products need to be consistent in terms of legal documentation and structure, or standardised. That is bad news for the sell side, which built huge profit silos pre-crisis out of manufacturing highly customised derivatives. But it is good news for investors, who will be able to compare prices across the market for precisely equivalent products, leading to tighter bid-offer spreads in products such as credit default and interest rate swaps. “If it’s done properly, central clearing will definitely lead to a decrease in systemic risk and have beneficial effects for market transparency,” says Stuart Anderson, Vice President in Multi-Asset Client Solutions at BlackRock. “On the other hand, there are a number of issues that need to be resolved over the coming period.” Regulators must now decide which products should be cleared and which can remain as they are. In Europe, the process will be managed by the newly formed European Securities Market Authority, which will decide which products should be subject to a mandatory clearing obligation. It will also consider issues such as the thresholds above which companies need to report and clear their derivatives contracts. Last September, end users of derivatives, such as corporates, were granted an exemption under European legislation as long as their derivatives contracts are “objectively measurable as directly linked to [their] commercial activity”. That brought Europe into line with the US, where the Dodd-Frank Act mandates clearing only for swap dealers (those who dominate the derivatives markets in the US) and major swap participants.

Standardisation is bad news for the sell side, which built huge profit silos pre-crisis out of manufacturing highly customised derivatives, but good news for investors

Cost burden

But, by and large, the cost of clearing appears likely to fall primarily on the buy side: the asset managers and pension funds using derivatives in investment portfolios. This is a bone of contention for these participants, who argue that the burden is disproportionate, particularly given their relatively small role in the financial crisis. One of the biggest increases in cost will be on margins, the amount participants must pay as a guarantee to the clearing house. Under current OTC arrangements this payment, known as collateral, is made for 70% of OTC derivative trades by volume, according to TABB Group. But there is a significant degree of under-collateralisation by value as a result of competition among dealers for business, since dealers are prepared to take on more counterparty credit risk in order to win client business. Total liabilities to counterparties amounted to more than $3.5trn in 2009, TABB says. According to the International Swaps and Derivatives Association 2010 margin survey, some $1.6trn of collateral is committed in OTC markets. This leaves a shortfall of nearly $2trn, which can be seen as the nominal cost of switching from bilateral to central clearing. Another unresolved issue for investors is that of variation margining: the ‘top-up’ required when the price of a derivative moves after the agreement has been made. While initial margins can be paid in securities, variation margins payable to counterparties on movements in derivative values are traditionally payable in cash. For cash-rich dealers this is unlikely to be a problem, but fund managers often do not hold large amounts of liquidity in their funds. Higher margin requirements will sit alongside guarantee funds – financed by levies on all clearing members – as financial backstops in the case of the default of an individual clearing member.

Lines of defence

“Regulators need to monitor margins as they are the first line of protection,” says Hartmut Klein, Chartered FCSI, a consultant with Goodacre. “In the extreme situation where a clearing member defaults, there is a guarantee fund that, unless there has been a huge miscalculation, would cover the liabilities of that member.” Only if there were multiple member defaults would it be likely that the capitalisation of the clearing house itself would be called upon, Klein says. To strengthen clearing houses for this eventuality, the US is moving to ensure that clearing house ownership is not controlled by too small a group of dealers. Legislation proposed last October would prohibit swap dealers, such as Morgan Stanley or Goldman Sachs, from owning more than 20% of voting power in a clearing house, on aggregate, or 5% individually. It would also limit membership on boards of the clearing houses and establish rules aimed at limiting conflicts of interest. The proposals have sparked a furious debate, pitting those who favour the restrictions against those who argue that excluding the dealer community will increase risks and raise costs. “What we have seen in the past is that a group of banks working together can be extremely effective in creating efficiencies and driving down pricing,” says Morgan Stanley’s Ross. “But it’s a complex topic since you do not want too much risk consolidated in a few institutions, and in the end it’s a matter of getting the right balance.” With reform still at an early stage, it remains to be seen whether the transparency and security offered by central clearing will outweigh the additional costs to all participants. But with regulators in the US and Europe totally committed to reducing systemic risk created by the massive OTC global derivatives market, there is no turning back. ■

OTC v exchange-traded derivatives

There are two routes to trading derivatives: over-the-counter (OTC) or on an exchange. OTC derivatives are contracts that are made privately, usually between two parties. An example is the swap agreements that are popular in the US, where, for instance, one stream of cash flows is swapped for another, without exchanging the instruments generating those cash flows. Where OTC derivatives are tailor-made to the needs of the parties, derivatives traded over an exchange are standardised. The OTC market is the larger of the two markets and the contracts themselves are still not regulated. Apart from the level of standardisation, the main difference between the two markets is that OTC contracts entail counterparty risk, because the contracts are made privately and are unregulated. By introducing central clearing into OTC derivatives, regulators hope to remove this imbalance and reduce the counterparty risk posed by OTC derivative markets. Clearing in exchange-traded derivatives is also experiencing considerable change, as discussed in our cover feature on page 12.

In his award-winning essay, student **Nicolas Greilsamer** explains why banks must take a longer-term approach to regulatory reform if they are to tackle economic instability effectively

Response *mechanisms*

THE CHARTERED INSTITUTE for Securities & Investment's (CISI) annual Stephen Cooke Scholarship Premier Award is open to students of financial subjects at seven UK universities accredited by the CISI as Centres of Excellence. Last autumn, entrants were challenged to write an essay briefing the first meeting of the UK Banking Commission on the measures it should take to address the size and range of activities of the banking sector (the Commission published its interim report last month). The 2011 winner, Nicolas Greilsamer, is studying for an MSc in International Accounting and Finance at Cass Business School, London. Here is an abridged version of his winning essay:

Long-term measures

Through much of 2008 and 2009, governments, central banks and regulators globally intervened in a co-ordinated effort to fight the 'financial meltdown' and avoid a repeat of the great depression. Today, however, with the financial system stabilised and banks back to profitability, regulatory reform does not seem to have a globally synchronised direction. Even though the UK's Project Merlin and the US Dodd-Frank rules are steps towards avoiding bank risk mismanagement, the ultimate focus should be on avoiding extreme losses due to interconnectedness. We should establish long-term mediums to avoid the next systemic crisis, rather than focusing on short-term fixes. Historically, it has been proven that a sustainable banking system is essential for economic growth. In contrast, a stressed financial sector has repeatedly caused financial crises that affect other industries and the economy as a whole. The recent financial crisis has questioned the effectiveness of regulators' organised intervention. Quick and effective backing of financial markets is needed in order to halt the fire sales of assets and widespread financial contagion. This inevitably creates a 'too big to fail' moral hazard. Due to the difficulties in establishing an ex-ante rule that would outweigh these moral hazards, this report supports the idea that the traditional approach to assuring the soundness of individual banks needs to be supplemented by a system-wide macro-prudential approach.

Correlated risks

Systemic risk usually builds up as a consequence of banks taking correlated risks, often by preferring to lend to similar industries. This can then be intensified by complex patterns of inter-bank loans, derivatives and other transactions. Systemic risk was amplified and harder to measure in recent years due to unprecedented levels of financial innovation and the rising opacity of financial markets. Detecting systemic risk early on is of prime importance to regulators in order

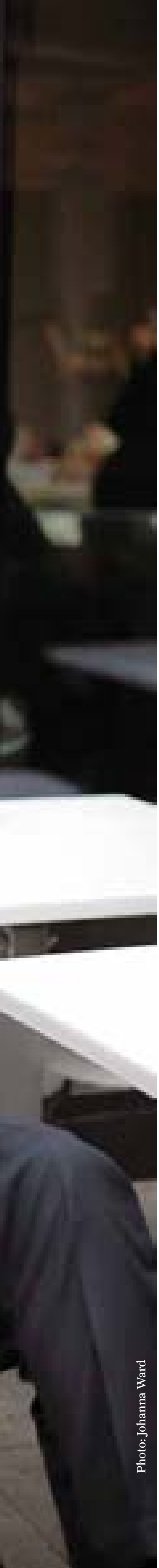


Photo: Johanna Ward

to mitigate the severity of a crisis and maintain liquidity. This was a key vulnerability during the financial crisis, as bank funding proved to evaporate extremely quickly due to the interconnectedness of banks and their over-reliance on short-term funding. One surprising element is that many institutions that subsequently failed still met minimum regulatory capital adequacy requirements in the early days of the financial crisis. While standard risk management indicators are still helpful in assessing individual vulnerabilities, the case for complementing these with other market measures linked to systemic stress testing is clear. Furthermore, standard tools could undoubtedly be broadened to better capture off-balance sheet exposures and liquidity mismatches. Capital adequacy requirements evaluate soundness of a financial institution by looking at directly observable accounting value. The rationale behind these capital adequacy ratios is that well-capitalised banks may withstand stronger shocks. Regulatory controls, in the form of capital adequacy ratio, consider only a bank's idiosyncratic risk and hence fail to prevent sector-wide risk taking. This may lead to accentuated systemic risk as firms act together in order to benefit from lower but more extreme probability of failure, with enhanced

A macro-prudential regulatory framework will help to avoid or mitigate widespread losses

guarantees from regulators and lenders of last resort. Macro-prudential regulation is shown to function collectively and can be foreseen with systemic risk models. These would regulate banks as a function of both their systemic risk with other banks and their idiosyncratic risk. In a downturn, a central bank acting as a lender of last resort will bail out institutions in order to cover the shortfall to the depositors and avoid ex-post costs (which include the what-if-it-failed implications). A central bank should step in only if the cost of the shortfall is below that implied by a bank's failure. Due to high levels of systemic risk resulting from greater interconnectedness of institutions and increased leverage, it is ex-post optimal (optimal in terms of predicting the costs in hindsight) to bail out the failed bank. With this in mind, the goal of central banks and bank regulators is to limit the ex-ante choice of risks taken on by banks. Efforts to limit this moral hazard, which leads to systemic risks, must be made in such a way that ex-ante measures outweigh ex-post costs of bailouts.

Too interconnected to fail

The return of the 'too big to fail' dilemma concerning bank rescues has serious consequences for longer-term stability. If the banking sector is to be sound and sustainable, individual banks must be given incentives to make themselves financially strong. Moral-hazard and joint-tail capital budgeting decisions may encourage excessive risk taking by financial system agents, which makes them weaker and financial markets more fragile in the long run. As shown during the recent crisis, 'too big to fail' is a valid concern, due to the system being 'too interconnected to fail'. According to this policy, central banks are unable to allow institutions to fail, out of fear for the consequence of linked failures within the financial system. This leads to banks becoming more complacent with their risk taking, even though, for a stable financial system, banks in fact need to attribute great importance to risk management. Although the Federal Reserve has clear incentives to rescue banks at risk, for the greater good of the financial system, they must then prevent these risks with ex-ante restrictions. One method could be the introduction of a systemic risk insurance fund. Banks would, hereby, purchase insurance against systemic crisis, with contributions going into a loss fund during the profitable years. Alternatively, but in the same spirit, it could be wise to tax each bank on its acceptance of state emergency capital and direct the money to a systemic loss fund, run by an independent regulator (preferably of global nature due to the worldwide repercussions of systemic risk). The capital for this fund would be sourced from banks, in the hope of avoiding using taxpayers' money in future crises and in order to be more prepared to intervene and liquidate large institutions. This, however, will continue to place a guarantee on banks, which would subsequently reduce their cost of capital, as investors view these institutions as 'too big to fail'. Moreover, the systemic risk fund means that retained earnings would be lost, lying dormant, as opposed to financing new projects or returning earnings to shareholders. The increased profitability would be foregone in a trade-off for enhanced sustainability of the system. An ex-post funded deposit insurance may be more realistic. This entails a bank, having survived a crisis, being taxed to repay the central bank that stepped in as a lender of last resort. This has indeed been seen in the past, notably during the Japanese 'lost decade'. Issues could arise, however, as such an ex-post crisis tax on bailouts still carries a moral hazard. Banks have fewer incentives to survive a crisis, knowing that they will have to repay losses at penalty rates. In order to combat a risky bank approach in the run-up to a crisis, the systemic insurance fund must be supplemented by capital ratios that adjust to any excesses in credit growth. This would allow minimum capital to withstand the risks of liquidity shocks and financial contagion, while limiting ex-ante the choices of correlated asset exposures.

New tools needed

To conclude, systemic risk is generally outside the control of each individual bank. Only if risk estimation techniques are effective can bank regulators tie standard risk measures to minimum capital requirements. As revealed during the crisis, standard measures did not capture the aggregate risks of the financial system. New tools should be implemented to predict system-wide and individual firm risk and these should be used for capital requirement decisions to avoid repetition of past mistakes and to prevent the next period of systemic risk. Predicting systemic risks early on is vital to mitigate risks of financial crises, which tend to affect the economy as a whole. A macro-prudential regulatory framework will help to avoid or mitigate widespread losses leading to financial and economic instability. As well as being implemented by the UK Banking Commission, this requires a co-ordinated approach from policy makers globally. ■

To read Nicolas's winning essay in full, visit cisi.org/cisiedtrust

Read a further CPD article about the UK's market abuse regime in the 'Online Only' section at *cisi.org/s&ir*

Here's the latest in our series of ethical case studies for you to consider and respond to

"Handle with the utmost discretion"

GRAHAM IS AN experienced discretionary fund manager with Icicle Wealth Managers, a firm with a reputation for the highest standards of integrity and a record of industry-leading performance. Graham has a high profile and regularly appears in media lists of top performers in his sector. At the weekly meeting of Icicle's Investment Committee, Graham discusses potential new investment in a number of established Far Eastern funds. He recommends, for its clients with an appropriate risk appetite, that Icicle should invest in Sampan Oriental Growth fund. Graham is confident that Sampan has an appropriate balance of risk to deliver a return of 7% for Icicle's clients. A number of people question whether this return can be delivered on a sustained basis, but after some discussion, the committee accepts Graham's recommendation.

What's in a name?

Following the meeting, Graham gives instructions to his support team to sell the firm's holdings in the Richter Reward fund and to purchase Sampan Oriental in its place. As he tracks Sampan's progress over the following days, he is reassured that it seems to be performing well. At the next quarterly review, Graham reports that his recommendation to invest in the Sampan fund is paying off and its performance is ahead of expectations. This will benefit Icicle's customers, cement his reputation as a leading investment manager and should, if current performance is sustained, positively influence his bonus. The week after the quarterly committee meeting, Lindsay, Icicle's Head of Fund Accounting, contacts Graham. Lindsay is having trouble reconciling Icicle's investment in Simplon Investments – for which she can find no paperwork – and asks whether Graham can shed any light on this. Graham responds that he assumes that Lindsay is referring to Icicle's holding of Sampan. This comment is greeted with a few seconds' silence before Lindsay says: "Graham, I think we have a problem." In the discussion that follows, it becomes apparent that Graham's instruction to purchase Sampan Oriental had resulted in a purchase of units of the Simplon fund instead. Graham is concerned at the possible ramifications of this, from both a risk and performance perspective. However, he is relieved to learn that Simplon's performance – although not quite as strong as Sampan's – is positive, meaning that he will not have to report a loss to the committee.

The erroneous investment has still produced a positive result

Who needs to know?

Having been made aware of this problem, Graham wonders whether he actually needs to do anything, reasoning that these are discretionary funds and the erroneous investment has still produced a positive result. However, he decides that he should report it to the Investment Committee, and an interim meeting is convened for the next morning. The next day, Graham explains to his colleagues what has happened, but reassures them that Simplon generated a positive return, albeit weaker than Sampan over the same period. He adds that, since the investment was made on behalf of Icicle's 'discretionary' clients, there was no need for them to be informed. At that point, the committee Chairman says that he does not feel that the decision is quite as straightforward as Graham claims. Leaving aside the question about how the situation arose, the issue was whether the firm had an obligation to its customers to put them in the position in which they would have been had Icicle actually invested in Sampan. He says that this was not a transaction that had been undertaken at the direction of the customers,

who do not know of all the discussions that take place within the firm when deciding on investment strategies. The original intention, however, had been for Icicle to invest in Sampan with a view to generating a certain level of income. The fact that the erroneous investment had performed positively, while reassuring, was not the issue, and neither was the fact that customers would not be aware that the return of the discretionary fund was not as high as it would have been had the Sampan purchase been made. Graham is asked to quantify the cost to the firm of paying into the fund an amount equivalent to the difference between the income received from Simplon and what would have been received from Sampan, as well as any cost of buying Sampan now. When he says that it would cost Icicle £200,000, there is a sharp intake of breath around the room. At this point, the Chairman comments that all members of the committee should be given the chance to express their view.

The options

These views come down to a straightforward choice between:

- those who consider that this is an entirely discretionary fund and that Icicle has no responsibility to compensate the customers whose funds have been invested in Simplon
- committee members who accept this argument, except for the fact that a definite investment had been agreed, the aim of which was to generate a certain level of return.

This latter group argue that the committee had made a corporate decision to invest in Sampan and the expectation was that it would be carried out. A mistake had been made and, therefore, the right thing to do was to put the customer in the position in which they would have been had the correct investment been made, whether or not they were aware of the background. Another committee member supports Graham in his view that Icicle did not need to take any action. This leaves the Chairman with the casting vote, and he sets out what he feels are their four possible courses of action:

- to top up the customers' funds, without making them aware of what has happened
- to compensate customers, giving them a full explanation
- to do nothing, since the customers are unaware of what has happened and Simplon is an acceptable alternative
- carry out an audit of operational procedures – and report the position to the regulator – before coming to a decision. ■

Which option would you choose? Visit cisi.org and let us know

The results, together with the CISI's own opinion, will be published in the July/August edition of the *S&IR* and will also be posted on the CISI website.

Hand in the till?

THE VERDICT

A number of debits to a charity's bank account are received in respect of a debit card issued to the Chairman. The Chairman, however, claims no knowledge of them. As financial controller of the charity, what would you do? This was a dilemma posed in the March *S&IR*. Readers were invited to vote in a poll on the CISI website for the course of action they would take, choosing from four options. Voting was convincingly in favour of telling the Chairman that, since the transactions on his card were fraudulent, the charity would have to involve the police.

The results were:

- Ask the Chairman to pay, since that is company policy (32%)
- Write off the amount and say nothing to the Chairman (0%)
- Write off the amount, record it as fees and report the information to HM Revenue & Customs (3%)
- Tell the Chairman that you must involve the police (65%)

CISI response

Clearly, this is a situation that needs to be handled sensitively. Some of the respondents who were keen to involve the police appeared not to recognise this, assuming that this must be a case of fraud. As with most dilemmas, before leaping to conclusions, careful consideration of all the facts is required.

Comments on the options:

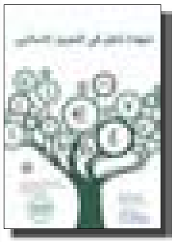
- Asking the Chairman to pay because it is company policy would be a reasonable response, except for the fact that he denies knowledge of the transactions. Would you be prepared to tell him that 'rules are rules'?
- Perhaps unsurprisingly, no one was prepared simply to write this off, since it leaves many unanswered questions – but so do the other responses.
- Option 3, as with the preceding option, deals only with the mechanics of the accounting and does nothing to resolve the more serious issue.
- While option 4 was the favoured course of action, would you really involve the police without further investigation?

Some readers have assumed, for example, that the Chairman keeps the card in his desk at the charity. Yet, as Chairman, he is unlikely to be a full-time employee and might easily have the card in a desk elsewhere, such as at home. This would put a different complexion on the matter. Equally, further enquiry should be made to ensure that the bank is certain of its facts. Mistakes are not that uncommon. It is almost inconceivable that the Chief Executive of a charity, or any type of corporate body, would involve the police before raising awareness of the issue among the trustees (directors), who might take a different view of how to handle it. Almost certainly, one or more of them would wish to raise the matter with the Chairman. The CISI's recommendation is that further investigation should be carried out, as speed is secondary in importance to getting the decision right. ■

Need to Read

The latest publications and study aids supporting CISI qualifications

NEW WORKBOOK



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- principles of exchange-traded futures and options
- principles of OTC derivatives
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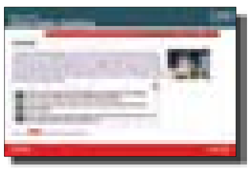

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Conferences

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Tuesday 14 June 2011 CISI Annual Conference 2011
Tomorrow's World: Risk, Regulation, Reputation & Revolution
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Financial Secretary to the Treasury

Kee-Meng Tan
Managing Director, Electronic Market Making, Knight Capital Europe

Sheila Nicoll
Director of Conduct Policy, FSA

- Ruth Lea, Economic Adviser, Arbuthnot Banking Group, former Economics Editor at ITN and Head of Policy at the Institute of Directors
- Robert Barnes, Chartered FCSI, Managing Director, UBS Investment Bank
- Remco Lenterman, Managing Director, IMC Financial Markets
- Khalid Rashid Al Zayani, Chairman, Al Baraka Islamic Bank
- Talal Al Zain, Chief Executive Officer, Mumtalakat and Chairman, Gulf Air
- Professor Michael Mainelli, Chartered FCSI, Chairman, Z/Yen Group
- Mark Cooke, Barclays Wealth Chief Risk Officer, Managing Director, Barclays Wealth
- Angela Knight CBE FCSI(Hon), Chief Executive Officer, British Bankers' Association

Tuesday 12 July 2011 Training & Competence 2011
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CISI, 8 Eastcheap, EC3

12 MAY Impact Investments: an Emerging Asset Class?
America Square Conference Centre, 1 America Square, 17 Crosswall, EC3

17 MAY State Benefits and Investment Planning
CISI, 8 Eastcheap, EC3

18 MAY An Outline of the Taxation of Financial Products – Tax Efficiencies and Tax Risks
Grant Thornton UK, 30 Finsbury Square, EC2

19 MAY Integrity at Work Workshop
CISI, 8 Eastcheap, EC3

23 MAY Founders' Series: Luke Johnson of Risk Capital Partners
Willis Ltd, 51 Lime Street, EC3

25 MAY Securities Lending in the Financial Marketplace – How Does It Benefit Clients?
BlackRock, Murray House, 1 Royal Mint Court, EC3

26 MAY Third Party Pensions Sponsorship – the Future of Pensions Provision?
CISI, 8 Eastcheap, EC3

6 JUNE The Middle Office: Impact of New Regulations and Infrastructures
CISI, 8 Eastcheap, EC3

8 JUNE An Introduction to SIPPs
Speechly Bircham, 6 New Street Square, EC4

9 JUNE Trends and Developments in the European Wheat Market
NYSE Liffe, Cannon Bridge House, 1 Cousin Lane, EC4

16 JUNE The New Face of Financial Services Regulation: What Will It Mean in Practice?
Olswang, 90 High Holborn, WC1

20 JUNE Clearing Services for Global Markets
SWIFT, The Corn Exchange, 55 Mark Lane, EC3

22 JUNE The Foreign Account Tax Compliance Act (FATCA) – Your Obligations Under the New US Tax Regime
Grant Thornton, 30 Finsbury Square, EC2

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Venue: London unless otherwise stated

10 MAY Pensions and Retirement Planning* £495.00

11/12 MAY Derivatives* (Manchester) £895.00

18 MAY Securities* £495.00

24 MAY Introduction to Financial Markets £495.00

7 JUNE Securities* (Glasgow) £495.00

16 JUNE Operational Risk: Taking it to the Next Level £495.00

22 JUNE Training Competence and Managing Expertise in a Regulated Environment £495.00

28/29 JUNE Understanding Regulation and Compliance £895.00

5 JULY Mastering Communication Skills in Financial Services £495.00

12 JULY Pensions & Retirement Planning* £495.00

13/14 JULY Derivatives* (Birmingham) £895.00

19 JULY Anti-Money Laundering and Terrorist Financing Introductory Workshop £495.00

21 JULY Pensions & Retirement Planning* (Manchester) £495.00

*This event fulfils the requirements for qualifications top-up to fill gaps between existing CISI exams and the new Retail Distribution Review exam standards

Regional Events

10 MAY AGM
West Country
Charles Stanley, Broadwalk House, Southerhay West, Exeter

11 MAY Political v Economic Drivers in Asset Management
Jersey
The Royal Yacht, Weighbridge, St Helier, Jersey

11 MAY AGM
Birmingham & West Midlands
Smith & Williamson, 9 Colmore Row, Birmingham

12 MAY Annual Dinner
Liverpool & North Wales
Crowne Plaza Liverpool Hotel, St Nicholas Place, Princes Dock, Pier Head, Liverpool
(Guest speaker: snooker player John Parrott)

12 MAY Golf Day
West Country
Exeter Golf & Country Club, Topsham Road, Exeter

17 MAY Personal Taxation
East Midlands & Lincoln
TBC

19 MAY The Investment Value Chain and Product Governance, Design and Oversight
Jersey
The Royal Yacht, Weighbridge, St Helier, Jersey

19 MAY AGM and Retail Distribution Review Seminar
Isle of Man
Palace Hotel and Casino, Central Promenade, Doulas, Isle of Man

25 MAY Golf Day
Guernsey
La Grande Mare, Vazon Bay, Guernsey

7 JUNE Golf Day
Manchester
Middleton Golf Club, Hopwood Cottage, Rochdale Road, Middleton

8 JUNE Using Appropriate Processes and Expertise to Manage the Impacts of Financial Disputes
Manchester & District
Manchester Conference Centre, Weston Building, Sackville Street, Manchester

9 JUNE Annual Dinner
Birmingham & West Midlands
Hyatt Regency, 2 Bridge Street, Birmingham (Guest speaker: golfer Peter McGovern)

23 JUNE AGM
Guernsey
Collins Stewart, Hirzel House, Smith Street, St Peter Port, Guernsey

7 JULY Annual Dinner
Yorkshire
Mint Hotel, Granary Wharf, 2 Wharf Approach, Leeds
(Guest speaker: former MP Lembit Opik)

28 JULY Annual Dinner
East Anglia
Norwich Cathedral Refectory, The Close, Norwich

To book:
cisi.org/onlinebooking *region@cisi.org* *+44 (0)20 7645 0652*

Professional interest forums

Spotlight on the compliance forum


Bobbie Melville ACSI

The CISI's compliance professional interest forum (PIF) meets six times a year in central London. It provides an opportunity for compliance officers to network over a light lunch and share experiences in a confidential setting, while earning CPD.

Forum member Bobbie Melville ACSI, who has attended events regularly over the past two years, finds the PIF an excellent "outlet where you can express your opinions, discuss issues, gain an insight into 'market practice' and learn from others under the Chatham House rule".

What's more, she finds that "the forum allows you to meet interesting people and have off-topic discussions prior to the main presentation… it provides a valuable sense of community and a trusted network of people."

Recent topics covered by the forum include financial crime and corporate governance. The forum also responds to FSA papers from time to time, such as the regulator's recent guidance consultation on assessing suitability. If you would like to view this response, as well as slides from past events, they are available to download from the PIF Archive, located in the members' area of the CISI website: cisi.org/membersarea

To join the 600 members already signed up to the mailing list of the compliance forum, please email *complianceforum@cisi.org*

The CISI's PIF programme is a free CPD benefit open to all Fellows, Members, Associates and Affiliate members of the CISI. There are currently seven PIFs – covering the areas of compliance, corporate finance, Islamic finance, IT, operations, risk and wealth management – that each meet at least quarterly.

Forthcoming meetings include:

Operations Forum:
Recruiting, Training & Retaining Operations Staff
Date: 10 May
Time: 12.30pm to 2pm, including lunch from 1.30pm to 2pm
Venue: Standard & Poor's, 20 Canada Square, Canary Wharf, E14

Risk Forum: Basel III
Date: 12 May
Time: 12.30pm to 2pm, including lunch from 1.30pm to 2pm
Venue: AXA, 7 Newgate Street, EC1

Compliance Forum: Hot Topics
Date: 18 May
Time: 12.30pm to 2pm, including lunch from 12.30pm to 1pm
Venue: Travers Smith, 10 Snow Hill, EC1

Wealth Management Forum:
The Art of a Good Pitch
Date: 24 May
Time: 12.30pm to 2pm, including lunch from 1.30pm to 2pm

☛ *More information can be found at cisi.org/pif*

Membership admissions and upgrades

<u>**MCSI**</u>
ABN AMRO
Lai Tang
Barclays
Laura Murphy
Andrew Wimble
BlackRock
Claire Perryman
BRI
Oliver Mustin
Brown Shipley
Adam Horsley
Butterfield
Lynsey Carson
Capital Market Authority
Mohammed Almadhi
Charles Stanley
Darren Vickers
City
Alex Lander
Credit Suisse
Assad Malik
Duncan Lawrie
Paul Arnold
Alan Warner
First Bank of Nigeria
Semiu Lamidi
First Equity
Antony Laiker
Hargreave Hale
Andrew Baker
Adam Caplan
Mark Chadwick
Andrew Findlater
Giles Hargreave
Christopher Kennedy
Paul Mansfield
Leon Shuall
John Simon
Michael Stranks
Alexander Van Moppes
HSBC
Hugh Castle
IMS
Maria Douloubakas
Matthew Dyball
KPMG
Nicola Ball
Lloyds TSB Bank
Reza Nasehi
Macquarie
Wayne Leamon
Mirabaud
Christopher Wilson
Morgan Stanley
Jennifer Catlow
MPL
Simon Stodart
Nationwide
Richard Thompson
Oxford Capital
Andrew Sherlock
RBS Coutts
Peter Davies
Redmayne Bentley
Selina Hart
Rensburg Sheppards
Matthew Salmon
Scottish Power
Katherine O'Hagan
SG Hambros Bank
Stefano Del Federico
SG
Roderick Sallis
Sovereign Trust
Robert Shipman
Standard Life
Emer Murray
Thesis
Giles Hedley-Dent
UBS
Javid Canteenwala
Paul Raphael
Christos Spyridis
Vestra
Andrew Vacha
Walker Crips
Andrew Covell
Zurich
Gregorio Loayon
Others
Obinna Emelogu
Knut Fehling
Xinyao Huang
Jin Xin Lu
Mark Remington

<u>**ACSI**</u>
Abbey
Judith Philpotts
Aegon
James Quigley
AFEX
Martin Briggs
Nicholas Tubb
Ault
Jonathan Bradshaw
Bank Leumi
Thomas Hughes
Barclays
Andrew Wallwork
Zena Whiteley
BNP Paribas
John Barrowman
Edward Sanjuan
Border
Elizabeth Wild
Bravura
Benjamin Stanley
Brewin Dolphin
Daniel Evans
Susanne Evans
Carrie Keenan
Simon Moss
Beth Pearson
Arunkumar Subbiah
Katherine Tasker
British Arab Commercial Bank
Edward Freeman
Brown Shipley
Emma Moore
Business Link Northwest
Sarah Brennan
BWCI
Ashley Dye
Capita India
Marlin Blaise
Ronak Mehta
Capital International
Antony Kelsey
Stuart Smith
Cardale
Mark Puleikis
Cazenove
Marta Foster
Charles Stanley
Ross Brookes
Mark Craig
Jack Nichols
Combined Management Services
Jonathan Morris
Commerzbank
Adrian Byrne
deVere
Sajan Chugani
James Dodds
Jeremy Dodds
Stuart Holmes
Paul Howard
James Kennerdale
Alexandra Malkin
Noel O'Leary
Paul Rhodes
Brigitte Rupp
EFG Harris Allday
Naeila Kanwal
Evolution
Suzanne Wilkinson
Family Investments
Moesha Churchill
Carl Hayden
Financial Services Authority
Fiona King
Hargreave Hale
Jack Askew
Laura Eaves
Lee Finlayson
Mark Ingram
Nicholas Leigh
Marcos Mackie
Andrew McDowall
Adam Newman
Joshua Ross-Field
HBOS
Charlotte Pratt
Nicola Stainburn
HSBC
James Strange
Yuen Yeung
JM Finn
Iain Green
JP Morgan Chase
Daniel Schofield
Kleinwort Benson
Adrian Norman
Lloyds of London
Annette Stone
Lloyds Private Banking
Ross Henderson
Jiten Patel
Timothy Pethybridge
Abhishek Sachdev
Sathish Subbiah
Lloyds TSB
Henry Nicholls
Jake Van Beever
Louis Capital
Ryan Griggs
MPL
Aidan Vaughan
Northern Bank
Michael Hall
Andrew Lam
Emma Winter-McConnell
Pershing
John Billington
David Carter
Prime Fund Solutions
Maurice Murphy
Professional Portfolio
Gary Bradford
Protect and Invest
Michael Roberts
Rathbone
Tom Perks
Raymond James
Stuart Hutton
Redmayne Bentley
Sabine Le Brizoual
Rensburg Sheppards
Kenneth Clarke
Patrick Doig
Margarita Smith
Royal Bank of Scotland
James Burley
SDB
Stuart Bryant
Seeds
Jeffrey Lynn
Smith & Williamson
Edward Fox
Standard Bank
James Hibbs
Thomson Reuters
Jason Dias-Patel
UBS
Stephan Dorey
VTB
Andrew Kinsella
Others
Andrew Chamberlain
Richard Ian Cummine
Arnold Dublin-Green
James Faulkner
Angelina Foo
Nicola Oliver
Alan Penn
Abraham Rahman
Ramesh Rana
Wing Kan Tong
Simon Timothy Walton
Amiel Ziv

<u>**Chartered FCSI**</u>
ABN AMRO
Frank Moon
Bank of Ireland
Leona Nicholson
Barclays Wealth
Mike Kibble
Blankstone Sington
Joanna Jones
Brewin Dolphin
George Angus
Brian Boyd
Simon Inness
Mark McMullan
Buckland
Warren Cann
John Halley
Mark Sullivan
Mark Thistlethwayte
Capital International
Richard Wild
Cardale
Neil Brayshaw
Close
Eric Gabbitas
Collins Stewart
Glenn Coxon
Cornelian
Jamie Daniels
Coutts
Duncan MacIntyre
Deutsche Bank
Alison Leighton
Dulwich
Barry O'Connor
Equiduct
Peter Randall
Fieldings
Jonathan Adams
Fleming Family
Matthew Taylor
Generali
Tobias Hughes
GHC
Ian Nicol
Goldman Sachs
David Johnston
Hargreave Hale
Richard Collins
Hedley & Co
Timothy Scott
Hottinger & Co
William O'Leary
Invesco Perpetual
Philip Shearing
JM Finn
Gordon Adams
John Barstow
Charles Bathurst-Norman
Jonathan Goldring
John Bourbon Consulting
John Bourbon
Kingsworthy
Marcus Stanton
Kleinwort Benson
Damian Wiffin
Mason Philips
Edwin Braim
Mercater
David Oakes
Moore Stephens
Michael Norem
Morgan Stanley
Robert Tyley
National Australia Bank
Kevin Gaffney
Principal
Paul Surguy
Pritchard
David Gillespie
Quartet
Colin McInnes
Quilter
Michael Broadhurst
Rebecca Bryant
Stephen Clow
Duncan Taylor
Railpen
Paul Jeffries
Rensburg Sheppards
Rachel Kesby
Gregory Rowe
Charlotte Selby-Rickards
Rowan Dartington
Suzanne Evans
Smith & Williamson
Simon Witheridge
Standard Bank
Andrew Price
Thamesis
Paul Reynolds
Thomas Miller Investment
Susan Preskey
Volaw
Alan Edward Yates
VWM
David Thomson
WH Ireland
Leslie Ames
Williams de Broë
Winnie Perry
Williams
Valerie Wade
Others
Raymond Bugeja
Michael Collyer
Philip Dodd
Anne Ewing
Vanessa Jacka

<u>**Chartered MCSI**</u>
Aberforth
James Swaisland
Aegon
Neil Donaldson
AXA Rosenberg
Susannah Pitura
Brewin Dolphin
Matthew Brown
George Fortune
Richard Morley
Capita
Christopher Vaughan
Charles Stanley
Richard Sullivan
Collins Stewart
Chris Colclough
Elizabeth Dodd
Alison Schiffer
Commonwealth Bank of Australia
Alexandra Groben
CPP
Grant Hawthorne
Craigcrook
William Macdonald
Cratston
Vivien Crayston
Credit Suisse
Daniel Roberts
Cunningham Coates
Jamie Warnock
Fleming Family
Charles Ward
GAM
James MacEwen
HSBC
David Macfarlane
JM Finn
Stewart Harrison
JP Morgan Chase
Shireen Seakhoa-King
Morgan Stanley
Anirban Roy
Psigma
Timothy Gregory
QV Partners
David Noble
Rathbone
Andrew Lacey
Rensburg Sheppards
Andrew Grimes
Danielle Lloyd
Graham Reid
SG Hambros Bank
Christine Whitehorne
Wells Fargo Bank
Hiten Patel
Others
Paul Daly
Lisa Hemmings

This list includes membership admissions and upgrades from January 2011

Answers to the quiz from page 10. Question: 1:C, 2:D, 3:A, 4:D

Ebru Smith (front row, right) with Tonbridge Angels team mates

Ebru (second from left) in action on the volleyball court

Net gains

While most people applying for tickets to the 2012 Olympic Games will be vying for the opportunity to watch the athletics events, Ebru Smith ACSI has set her heart on attending a less acclaimed sport: volleyball. **Lora Benson** reports

EBRU SMITH HAS a lifelong passion for volleyball, which can be traced back to her Turkish roots. While volleyball may be a minority sport in the UK, it's a popular pastime in Turkey, where Ebru grew up. "I played volleyball at secondary school in Ankara, but my love for the game dates back to the long school summer holidays that I spent on Kargi beach in Bodrum," she explains. "In Turkey, volleyball is everywhere: courts can routinely be found in town centres and parks." Ebru's passion survived regular globetrotting – a result of her father's job as a diplomat – during her younger days. She has lived in Libya, Iran, Italy and what was then Yugoslavia, and moved to England in 1987 when her father was posted to the Turkish Embassy in London. Apart from a year spent working at the British Embassy in Ankara as an economic assistant in 1997-98, she has stayed in the country ever since. Nowadays, Ebru lives and works in Tunbridge Wells, Kent. She has 15 years' experience in financial services, which has included spells with Bloomberg and Schroders. For the past five years, she has been a fund manager, at Reliance Mutual Insurance Society, for a UK equity long-only authorised trust.

Part-time angel

In her spare time, Ebru plays volleyball for a local women's team, Tonbridge Angels. "I was looking for opportunities to play volleyball as a hobby and was delighted to find this team two years ago," she says. "We are in the third division of the National League, but we are working towards Division Two and are keen to attract new players." The Tonbridge Angels play matches throughout the South East and South West. As well as a two-hour weekly training session with the team, Ebru regularly takes part in an open practice for both female and male players of all abilities. She says: "I play right-back defence and outside hitter positions. I am also interested in the position of libero, which is a specialist defensive position that fosters more digs and rallies." Ebru feels that volleyball is an under-represented sport in the UK. "My ten-year-old son Ethan would like to take it up, but there are no real opportunities for him in Kent," she points out. "I hope that the 2012 Olympics in London will help to change that, by raising the profile of volleyball and encouraging more people to take up the sport. The game

> ***"The game is a great way to get fit, and it's exhilarating working as a team"***

is dynamic and a great way to get fit, and it's exhilarating working as a team. A good volleyball player needs to be agile, fast and have good reflexes." She adds: "I've applied for tickets to attend volleyball at the Olympics with my husband and son, as it will be a great occasion. "There will be two forms of the sport played: beach volleyball, which is two-a-side, and the traditional indoor version, with six players on each team." In addition to volleyball, Ebru loves watching movies and reading crime thriller novels. She says: "Once a year, I award myself 'me-time' and go back to Ankara alone to see my family and friends, do nothing and relax. This recharges my batteries better than anything else!" If you are interested in joining Ebru's volleyball team, you can find out more at ***tonbridgevc.co.uk***. For further information about volleyball, visit ***volleyballengland.org*** or ***fivb.ch*** ■

Your story here? »

Over the past four years, the *S&IR* has featured some amazing stories about Institute members who combine their day job with an interesting or unusual hobby or talent. People profiled have included professional sportsmen, published authors, a part-time DJ, a double bass player, an astronomer, a martial arts expert, a Royal Navy reserve, a Jersey state senator and a professional midwife.

Please contact Lora Benson at **lora.benson@cisi.org** with your story. If it is published, you will receive £25 of shopping vouchers.


Fast track
to RDR
compliancy
ATTENTION
December
2012 Deadline
Approaching