



## Key Contact

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*“firms must take all reasonable steps to identify conflicts of interest ... and to prevent conflicts of interest from adversely affecting the interests of their clients”*

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# CONFLICTS OF INTEREST UNDER MIFID

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## Overview

MiFID imposes detailed requirements about conflict of interest procedures on Common Platform firms. These requirements are set out in chapter 10 of SYSC and become mandatory on 1 November 2007. In addition to identifying and preventing conflicts firms must prepare, maintain and implement an effective conflicts policy, a description of which must be provided to retail clients.

Common Platform firms that have not identified the conflicts that might arise within their organisations and that do not have effective policies for dealing with these conflicts will have work to do between now and November in order to comply. Firms that have a clear understanding of relevant conflicts and effective procedures should nonetheless review their arrangements.

## The Obligations

The principal obligations (set out at SYSC 10.1.3 and 10.1.7) are that a Common Platform firm must take **all reasonable** steps to **identify** conflicts of interest between the firm and its clients and between one client and another and to **prevent** conflicts of interest from adversely affecting the interests of its clients.

These obligations apply in relation to conflicts that arise or may arise in the course of carrying out regulated activities or ancillary activities, where a service is being provided. The effect of a conflict of interest only needs to be considered in respect of clients to whom a service is being provided.

## Reasonableness

It is important to note that the obligations are not absolute; the requirement is only to take reasonable steps. This means that firms can take appropriate factors into account in determining what is reasonable. These factors might include the level of risk associated with a particular conflict, the nature, scale and complexity of the firm's business, the nature and range of products that it offers and the type of clients that it has.

## Identification of conflicts

In relation to conflict identification Common Platform firms must take into account whether the firm or a person linked to the firm:

- is likely to make a financial gain, or avoid a loss, at the expense of a client;
- has an interest in the outcome of a service provided to the client or of a transaction carried out on behalf of a client, which is distinct from the client's interest in that outcome;

*“The policy must specify procedures to be followed and measures to be adopted in order to manage conflicts.”*

*“firms must provide retail clients with a description of the conflicts of interest policy”*

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- has a financial or other incentive to favour the interest of one client or group of clients over another;
- carries on the same business as a client;
- receives from a person other than the client an inducement in relation to a service provided to the client, in the form of monies, goods or services, other than the standard commission or fee for that service.

### The Policy

The requirement here is to establish, implement and maintain an effective and appropriate conflicts of interest policy. The policy must identify the circumstances which constitute or may give rise to a conflict of interest and it must specify procedures to be followed and measures to be adopted in order to manage such conflicts. The policy must be designed to ensure that relevant persons carry on activities that might involve a conflict with an appropriate level of independence and should include the following to the extent appropriate:

- procedures to prevent or control the exchange of information;
- separate supervision of relevant persons (note: there is a separate requirement at SYSC 5.1.7 requiring firms to define arrangements relating to segregation of duties);
- removal of any direct link to remuneration in circumstances involving a conflict of interest;
- measures to prevent or limit the exercise of inappropriate influence over the way in which services are carried out;
- measures to prevent or control the simultaneous or sequential involvement of persons in separate services or activities where such involvement may impair conflicts management.

The policy will need to be tailored carefully to the activities and perceived conflicts of the firm concerned and be updated as new conflicts are identified.

If the procedures adopted are, in the firm's view, not sufficient to manage a particular conflict the firm must disclose the general nature and / or sources of conflicts of interest to the client before undertaking business, to allow the client to make an informed decision.

### Description of policy to be provided to retail clients

Under COBS 7.1.4 firms must provide retail clients with a description of the conflicts of interest policy and further details of the policy if requested. This requirement is likely to be satisfied by including generic conflicts wording in the firm's terms of business.

### Summary

Senior management need to be fully engaged in the development of the conflicts policy and its effective ongoing application. Key action points include:

- identify and record potential and actual conflicts;
- develop an appropriate policy and supporting procedures, in the light of the conflicts identified;
- use disclosure if the procedures are not sufficient in a particular case;
- provide retail clients with a description of the policy;
- maintain a record of actual conflicts that arise and the way in which they have been handled (in accordance with the policy).