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Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street NW.,
Washington, D.C. 20549-0609
USA

Our Ref: MS/jul25/COM3

18 July 2004

Dear Mr Katz,

**Complex Structured Finance Activities: Proposed Interagency
Statement on Sound Practices**

LIBA is the principal trade association in the United Kingdom for firms active in the investment banking and securities industry and, for convenience, a list of our Members is attached*.

We welcome the opportunity to comment on the proposed Interagency Statement, and our Members have asked us to do so given that – as currently drafted – all the proposals would appear to apply to the non-US activities of firms regulated by the Agencies (although it is noted that, in the case of US branches and agencies of foreign banks, the Agencies recognise that the policies “should be co-ordinated with the group-wide policies developed in accordance with the rules of the foreign bank’s home supervisor”).

We have seen some of the representations that have been drafted by other bodies and we agree that the issues that have been drawn to the Agencies’ attention are likely to be important for LIBA Members too. Our Members have asked us to stress the following four issues at this stage.

1. Extraterritorial application

At the most, the requirements in the proposed Statement should only apply to the *non-US activities* of a firm regulated by the Agencies where responsibility for the supervision of the conduct of that firm’s business outside the US falls to one of the Agencies. In addition, it will be essential that the Agencies have an understanding with the relevant regulators in jurisdictions outside the US on the application and implications of the proposed requirements.

2. Financial services firms as “gatekeepers”/responsibility for clients

We are concerned that at times the proposals conflate two separate issues, namely the policing of clients’ and counterparties’ business on the one hand and, on the other, the need for financial services firms to manage their business so as not to participate in illegal transactions and to address reputational and legal risk adequately. On the former, we believe that in many instances a financial institution will not be in the position to determine whether a client or counterparty is undertaking a transaction in order to circumvent regulatory or financial reporting requirements, evade tax liabilities, or is engaged in other improper or illegal behaviour. It is important, therefore, that the Statement be revised to make this clear: it is only when a structured finance transaction/product has been tailor-made for a customer by a financial services firm – and the firm will be acting as an adviser as regards the design of the transaction in such a case – that the kinds of measures envisaged in the Statement on assessing the customer’s motives may be applicable. Even then, it should be acknowledged that the firm may not hold sufficient information to understand the complete picture.

In addition, parts of the proposals deal with a customer’s understanding of the risks and return profile of a transaction: again it must be appreciated that there are many occasions where an assessment of a customer’s understanding is simply not possible on the basis of the information available to the financial services firm and, indeed, where the customer would regard enquiries by the firm as unnecessary and intrusive.

In particular, in the case where a client purchases on an execution only basis a product that has been structured and designed by a financial services firm – for example, an investment bank – the various procedural steps that are envisaged in the proposed Statement would be inappropriate.

It is important to get these aspects of the proposals right because otherwise – paradoxically – the proposed Statement could *increase* financial services firms’ legal risk. It should be made clear that the proposals do not introduce new legal duties for financial services firms and that the need to consider whether special provisions might apply is only necessary in the case where a firm has a substantial and active role – see above – in a transaction/group of transactions and where the customer is not assisted by his own professional advisers. It should be for the firm to judge whether these conditions have been met.

3. Scope of the proposed Statement and prescriptive requirements

It is important that the proposed Statement should focus on the kind of financial transaction *most likely* to give rise to difficulties – if it does not do so, it will lead to expensive and unhelpful over-reporting and will divert senior management attention from the significant issues that they should be addressing. With this in mind, we would suggest that the Agencies should review the description of Complex Structured Finance Activities in the proposed Statement because, as drafted, it would seem to apply to a very wide range of standard/“commoditised” products. A particular issue is the case where a client asks a firm to change a term in a standard contract: clearly, a definition of Complex Structured Finance Activity should not apply in such a case.

For similar reasons, we think that the Statement should focus on the *kinds of issue* that firms’ systems and controls should be designed to address rather than specifying in detail the *kinds of procedures* that firms should introduce (although we recognise that there are

parts of the proposals which make clear that a given procedure has been referred to as an *example* of what could be done). It will be particularly important to avoid over-prescriptive guidance if the provisions of the Statement are to be applied extraterritorially.

4. Implementation

The draft makes no reference to an implementation period for the proposed new framework. It would seem, however, that the Agencies consider that some of the firms that they supervise may not have procedures in place that satisfy the proposals: accordingly, it will be necessary to provide financial services firms with sufficient time to modify their systems and controls once the proposed Statement has been finalised before any new requirements come into force. This would also enable the Agencies to hold the discussions about the issues with their opposite numbers in other jurisdictions that are necessary (see point 1 above).

5. Conclusion

We would be pleased, of course, to discuss the issues covered in this submission, or to provide further information about any of the matters which our Members have raised, if that would be helpful.

Yours sincerely,

Peter Beales
Director and Secretary

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LIBA

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