



Plenary 3

The Regulation of Financial Analysts

Mr. J. B. Ram

Vice President of the Institute of Chartered Financial
Analysts of India

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Speech by Shri J.B. Ram in IOSCO at Sri Lanka dated April 7, 2005

“I wish to thank organisers of IOSCO and Sri Lanka for giving me and ICFAI an opportunity to express my views on the subject. ICFAI which is established in the year 1985 imparts training and conducts examination leading to CFA (India).

The Developments in India which may be seen as similar to Market Abuse directive of EU may be traced to Securities & Exchange Board of India (Prohibition of Fraudulent and unfair trade practices relating to securities market). Regulation was notified on June 24, 2003. The regulation defines acts of manipulative, fraudulent and unfair trade practices and stipulates penalties for the conduct. However, regulations similar to directive of fair presentation requiring disclosures from the producer of researcher are not yet been framed.

As regards the disclosure of conflict of interest of institution with respect to material investment banking services over the previous year, my observation is in India investment banking activities and broking activities are generally required to be segregated under rule 8 of securities contracts (Regulation Rules 1957). Hence, the conflict of interest as envisaged in implementation directive is eliminated. But in a few cases where both activities are permitted to be carried out under same corporate entities like commercial banks, such safeguards need to be built into.

No similar provision as that of framework Directive of April'04 exist in Indian Securities laws. One way of harmonizing could be to develop regulatory regime covering analysts, research reports and entities providing research reports. These directives are highly desirable.

2. Issues and question raised today:

How should one define investment research.

My view is that instead of trying to define research reports and providing an exception to reports in nature of marketing communications with suitable health warning, it may be preferable not to define. Alternatively, a report may be taken as research report if it is 'perceived' to be so.

As regards dissemination of reports, it may be worthwhile to consider QIBs out of scope as QIBs can and should take care of themselves. However, the responsibility of ensuring these reports meant to QIBs not landing in the hands of non QIB clients should be put upon investment firm/research firm.

Because of retail nature of equity, it is desirable to differentiate between equity analysis from credit and bond research.

4 b) How does the receipt of research affect assessment of best execution.

It is widely recognised that research on its own is not a viable business as yet. Broking firms by providing research report as 'free of charge' are able to maintain competitive coverages over large number of securities of the companies. Any over regulation in these areas may lead to shrinkage in coverage of research. Unbundling of research from execution may thus lead to ultimately increase in cost of execution.

c) Should minimum qualifications be required of analysts? While my answer to this question is affirmative, the type of examinations to be taken and follow up training programs should be worked out by regulator of specific jurisdiction. Any frame work in this regard should focus on analysts' technical and academic qualifications as well as on ethics and local market place practices, code of conduct etc.

5) How can an equal access to issuer information be ensured for analysts and how can undue issuer influence and retaliation against analysts for unfavorable coverage be prevented.

In India, the issue of providing equal access to issuer information has been addressed by making it a duty under model code of conduct for prevention of Insider trading for listed companies as well as for others the duty of employees/directors to maintain confidentiality of all price sensitive information. Providing selective access to such information to any person is discouraged. There are requirements for creating chinese walls over inside area and public area. In India, current guidelines require that any information provided in conference held with analysts by issuer be disclosed immediately at the website of the issuer.

d) Regulation of independent research

Approaches could vary from requiring independent research firm to registrar or be regulated or analysts could be regulated. My view is approach similar to proposed regulation of Analyst certification by US. Securities Exchange Commission addresses the issue of maintaining quality and independence.

e) Nature and size of a position held by financial institution or the individual analysts that should trigger a disclosure requirement.

The requirement in India is disclosure to companies of all holdings in securities of directors/designated employees at the time of joining, periodic statement in any transaction in securities and annual statement of all holdings. Take over regulations require disclosure to stock exchange and public when holding in securities crosses 5% and 10%.

f) Cross border situation

While I can offer no answer, possibly common approach to standards and jurisdiction may achieve the result.

i) Quiet periods around primary market transactions:

Requirement of quiet period vary over jurisdictions Practices vary. Common approach to the extent possible is desirable”.

Thank you,