



Dr. Johannes Fiala

PhD, MBA, MM

Rechtsanwaltskanzlei

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Kick-backs and MiFID: Billions in liability for banks, intermediaries, asset managers

Veröffentlicht am 21.11.2006

“You only get rich by doing things you don’t desire.” (Mahatma Gandhi, Indian politician, 1869 – 1948)

Increasing dangers due to kick-backs

After Switzerland, the topic of kick-backs is now also increasingly leading to legal proceedings in Germany if a customer feels cheated by his financial service provider or financial services institution. The courts usually agree with the customers, so that they can sue for damages with relative certainty.

Of course, credit institutions are the most likely to be sued, because they usually have a better credit rating than a cooperating independent asset manager.

The accusation against the bank is then that illegal commissions’ have flowed to an asset manager or intermediary. These so-called kick-backs were then concealed from the client. The judges then often regard this as fraudulent and asset-damaging behaviour. Recently, this case law has also been applied to companies associated with intermediaries who are not themselves asset managers.

Occasionally, financial services institutions claim that there is no disclosure obligation towards the customer: The numerous judgments handed down over the years, especially those of the Federal Court of Justice (BGH) in civil, professional and criminal law, show that the legal situation in Germany is clear. The “surprise” of German market participants at current civil and criminal judgements from Switzerland can at best serve as an indication of not being well advised themselves.

Legal principles:

There is a duty of disclosure in the case of agreements on kick-backs.

Kick-backs Kick-backs are payments (e.g. as commissions or fee reimbursements) to the manager in addition to the fees paid directly to the manager by the client. Recently, it has also become clear that this obligation does not only affect asset managers in the narrow sense, but can also affect intermediaries. Mentally, it also helps to consider whether the client knows the total costs, including “overhead” and similar commissions: For in addition to the prohibition on concealed “kick-backs”, the transparency requirement vis-à-vis the client must be observed.

Obligation to deliver or agreement Kick-backs are to be delivered to the customer by the manager (or agent) in accordance with §§ 675, 667 of the German Civil Code (BGB), if there is no effective waiver of this by the customer. It follows from the transparency requirement that the customer must also know how much money is involved. A liability trap already results from the fact that information not understood by the customer due to inexperience can make a waiver ineffective or contestable.

This also means that some “portfolio commissions” and “service fees” (e.g. in the fund business or in the case of occupational pension brokerage or time account management) are at stake. Disclosure obligation for asset manager (or intermediary) and bank.

In the case of asset managers, the legal basis for the disclosure obligation is section 31 (2) sentence 1 no. 2 WpHG. The bank – especially if a securities account is maintained there and the fees are “deducted” from the client – is also obliged to disclose. This shows for years likewise countless judgements (e.g. BGH of 19.12.2000 – [XI ZR 349/99](#); OLG Cologne of 20.2.2002 – [13 U 140/00](#); OLG Stuttgart of 16.2.2005 – [9 U 171/03](#); LG Stuttgart of 12.9.2003 – [8 O 128/03](#)). This obligation to disclose exists legally independent of the obligation of the administrator (or agent). Always applies: A concealment can justify punishability because of fraud or breach of trust ([§§ 263, 266 StGB](#)).

And under the EC MiFiD Directive?

Every investment services company is required to inform the client about the repayment, even partial, of third-party costs charged to the client (“kick-back contracts”) and the obligation under commission law to repay these amounts. The institution shall also be obliged to disclose agreed cash payments or other benefits of monetary value (e.g. research results, service fees) which the investment services firm receives directly or indirectly and which are economically related to client transactions.

MiFiD provides in Article 18 that the investment services firm shall disclose to the client the general nature and/or sources of conflicts of interest before undertaking business on its behalf where organisational or administrative arrangements to manage such conflicts are not sufficient. This is intended to ensure that the risk of customer interests being adversely affected is actually prevented. Furthermore, in order to avoid conflicts of interest, organisational precautions must already be taken in accordance with Section 32 of the German Securities Trading Act (WpHG) in conjunction with Section E of the Code of Conduct in order to prevent the following sales or advisory methods:

Churning:

Recommendations induce a disproportionate number of transactions and the resulting costs are unreasonably high in relation to the capital invested and the profit that can be achieved.

Scalping:

Recommend transactions to the customer to influence the price with regard to own-account transactions. In particular, misleading influences on the formation of customers' opinions or deception of customers (e.g. through fictitious and arranged transactions) must be avoided. Front, parallel and

Crossrunning: The conclusion of proprietary transactions on the basis of the knowledge or expectation of a client order, which may result in disadvantages for the client.

Other conflicts of interest: For example, by combining different investment services under one roof. This may include kick-backs. If conflicts of interest cannot be avoided, the customer must be informed accordingly.

*by Johannes Fiala, Lawyer (Munich), Mediator (Univ.), MBA Financial Services (Univ.Wales), MM (Univ.), Certified Financial and Investment Advisor (A.F.A.), EC Expert (C.I.F.E.), Lecturer (Univ. of Cooperative Education), Banker (fiala4instalive.instawp.xyz)

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