The Role and Employment of Corporate Brokers

A GUIDE FOR NON-EXECUTIVE DIRECTORS OF INVESTMENT TRUSTS

THE ASSOCIATION OF
INVESTMENT TRUST COMPANIES

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Foreword

Like almost every other aspect of the managed funds industry, the role of the corporate broker has evolved to match changing market conditions and the sector's legislative background.

The most obvious change is perhaps the move away from the gentlemanly, 'my word is my bond', City culture that tended to exist pre-Big Bang, towards the highly competitive, globalised, regulated and more formalised atmosphere of today. Thus at one time the appointment of a corporate broker – effectively as principal corporate adviser to an investment trust company – was politely and amicably agreed prior to the trust's launch and never altered or indeed challenged throughout the company's life. That cosy situation does not prevail today.

In this day and age of multiple regulation, complex taxation, institutionalised stock markets, volume trading, shareholder relations, share buybacks, formalised corporate governance, etc, most investment trust boards are likely to want advice on some or all of these areas.

A new more competitive environment has developed.
New brokerships are actively and constantly being sought by leading players in the corporate sector, armed with screen-based presentations describing "Why you should appoint us as your new corporate broker!".

Boards seeking advice and/or corporate support now have a greater range of options open to them, with varying levels of service and costing arrangements to consider, each offered by houses with sometimes widely differing corporate cultures of their own.

One side effect is that in this new, more demanding environment, the old way of doing things can only survive if it provides its own competitive advantage.

At the same time, it is important to recognise that corporate brokerage services have to be paid for if they are to survive.
At least four leading players – Credit Lyonnais Securities, Credit Suisse First Boston, Deutsche Bank and Merrill Lynch have, for various reasons, ceased providing corporate brokerage services to

the UK investment trust sector. Further consolidation is a real possibility and this would not necessarily be to the advantage of trust companies or their boards.

As one broker put it, somewhat directly, during research for this report: "it is essential that directors (and managers) grasp the economic facts of life before they wake up and find no-one making a market in their investment trust stock and their choice of broker being limited to a few, small boutique (part not full) service providers".

A methodology needs to be generated which provides the best possible level of advice to trust boards, while providing a reasonable way of attracting, retaining and remunerating brokers in such a way as to ensure their continuing presence in the investment trust sector.

In a people-oriented business such as the UK financial services industry, there is no standard solution and one size will never fit all. There will always be more than one way to achieve a given goal – in this case for the board of an investment trust company to employ and remunerate its corporate advisers, to the maximum benefit of the company's shareholders whom the board serves.

The purpose of this guidance document is to describe the options available so as to obtain 'best fit' corporate brokerage at the right price.

Executive summary

A range of alternatives is now available to the once accepted standard model for the services offered by a corporate broker.

Boards need to decide which is the best solution for their trust – and not simply accept the status quo based upon the principle: "that's the way it has always been done in the past".

The main services which brokers may provide include:

Acting as the 'eyes and ears of the board'; making a market in a trust's shares; monitoring the share register, including share buy-backs where appropriate; providing a sales function; providing research for publication on the trust in relation to performance, comparison with peer group funds, strategy and objectives; and providing corporate advice, including acting as a 'springboard' for new ideas.

Certain brokers are considered 'full service' while others are more specialist in nature.

Boards need to be aware that potential conflicts of interest can occur, particularly in the situation where brokers have an important client relationship with the manager. Boards should not be afraid to obtain independent advice from third parties.

Brokers can have very differing corporate cultures in which, for example, dialogue with arbitrageurs may be encouraged or, on the other hand, virtually forbidden. Similarly the global presence of a large multi-national house may be attractive to one type of investment trust but almost irrelevant to a small UK niche player. These factors make it even more important for boards to establish that they are getting the most appropriate brokerage services for their needs.

Paying for services puts an obligation on the provider in terms of quality and quantity. The widespread adoption of such retainers should help to ensure the continuing presence of a competitive and efficient corporate broking sector for investment trust companies.

There are four basic options available plus a number of variations on these primary themes.

They are:

a) **Nil retainer.** the traditional arrangement in which the broker sponsors a trust's launch and, without the payment of any annual retainer, remains available to advise it throughout the trust's life.

b) **Standard retainer.** A set menu of agreed tasks is provided in return for an annual retainer (typically of £20,000 to £30,000 pa at current levels).

c) **Bespoke retainer.** Negotiated on a one-to-one basis between a trust's board and the corporate broker; cost might vary from £15,000 to £125,000 or more per trust per annum.

d) **The DIY Option.** A sponsor is appointed for a trust's launch but no corporate broker is retained. Brokers and/or corporate finance boutiques are employed as and when required.

SECTION ONE

Introduction

At one time the accepted model for the services offered by a corporate broker was fairly standard. The broker would sponsor a trust's launch at some time in the distant past and continue to advise it throughout the trust's life. No annual retainer was charged.

The broker would make a certain amount of money from dealing commissions and market making and a great deal more from relatively infrequent corporate deals.

In recent years the environment has changed considerably. New players have entered the sector (including a number of corporate finance boutiques) while other brokers have left it. Competition is fiercer. The regulatory environment is more stringent. Boards themselves are coming under greater scrutiny to justify the continuing appointment of their advisers, including brokers. There is a greater need for independent advice. At the same time, transparency of financial transactions and the payment thereof is strongly encouraged.

Mutually beneficial (but sometimes informal) arrangements such as the provision of free research or soft commission deals are now generally considered to be unsatisfactory in corporate governance terms.

Formal written agreements have their advantages in today's environment. Not only do such agreements define what services are being provided – and at what price – but are seen as lessening uncertainty. In so doing they can offer greater protection both for the broker and for the trust, should disputes arise or things go wrong.

As a consequence of these and other developments, there are now several ways in which the boards of investment trusts can obtain the support and specialist advice that they may need.

Background and statutory requirements

All investment trust companies, being companies listed on the UK Stock Exchange, require a UK Listing Authority (UKLA, now subsumed into FSA) approved sponsor "to act as advisers and provide certain services". Just over 80 firms are currently listed as approved sponsors on the FSA's website www.fsa.gov.uk.

Sponsors will normally be corporate brokers but do not have to be so. For example, a firm of solicitors or accountants, or a corporate finance boutique, may become a trust's sponsor provided that the said firm meets the appropriate regulatory requirements and that its name appears on the FSA's register. A list of corporate brokers offering services to investment trust companies is included at Appendix One to this report.

The contact details for a range of advisers can also be found in the AITC Directory of Services for Boards, the first edition of which was published in July 2004.

The above requirements mean that once an investment trust has been launched there is no compulsion for its board to appoint a corporate broker on a permanent footing. This has led some boards to adopt what may be described as the 'DIY option' in which no broker is nominated on a regular basis. Advisory support is instead contracted out (either to brokers or to corporate boutiques) as and when needed. Such an approach has advantages and disadvantages as will be described.

The historical corporate broking model

"There shall be no Broker in the City, except those who are admitted and sworn before the Warden and Aldermen, on pain of imprisonment".

Statuta Civitatis 13
Edward I, 1285

"To prevent [unapproved persons] from abusing the true and honest ancient trade and name of Broking and Brokerage".

Acte against Brokers 1
James 1, 1442

"The Stocks will be made over to the Trust at the prices quoted at yesterday's Official List (18th March 1868) as certified by two eminent Brokers, plus £2 10s. for each £100 of Stock, for which all expenses of the issue, including Stamps, &c., have been undertaken".

Prospectus, Foreign &
Colonial Government Trust
19 March 1868

Investment trusts have existed since the launch of Foreign and Colonial in 1868 but, as the first two quotations above suggest, brokers of one sort or another have had their part to play for very much longer. Broking tends to be described in pocket dictionaries as "buying or selling on behalf of others" but the services and skills required of a corporate broker are a great deal broader than that. Larger dictionaries are nearer the mark, typically defining a broker as an "agent, negotiator, middleman, intermediary, factor or dealer."

A good corporate broker might be expected to be all of these things, and more, as will be described.

The traditional investment trust broking model was informally agreed between board and broker and based upon trust, mutual respect and the ability to negotiate or influence important matters at a personal level often through a process of what would now be called networking.

The situation might be likened to the traditional arrangement whereby a trusted firm of family solicitors would, especially in Scotland, act as a single point of advice to a family, perhaps for generations, on all matters of a legal or financial nature.

This generally worked well at the time but has rather less merit in today's harsh, sometimes complex, commercial world.

Taking the analogy further, family solicitors, however willing and diligent, could scarcely be expected nowadays to provide top-quality advice, totally free, on every aspect of a family's financial needs – purely on the understanding that the next time a sizeable piece of legal advice was needed they would definitely get the job.

That is, in effect, the way that some traditional, non-remunerated corporate broking arrangements are expected to work. And even if they do seem to work, the one-time mainstays of fees, namely the primary issuance of securities and the organisation of subsequent share issues are becoming fewer and fewer and in some investment trust sub-sectors have almost disappeared.

For the broking firms, the above situation spells danger.
While management companies can generally forecast a certain level of inward cash flow, a year or two ahead, from their investment trust business, the same does not apply to earnings from corporate broking. Such earnings could in a bad year be almost nil while in a boom year (likely to be one involving new issues) they could soar to several million pounds or more for a single firm.

In the likely absence of such boom years in the near future, pressure on broking firms seems certain to increase. There have already been some high-profile exits from the sector. Four major players – Credit Lyonnais Securities, Credit Suisse First Boston, Deutsche Bank and Merrill Lynch – have all withdrawn or re-allocated their investment trust teams and no longer seek broking arrangements with investment trust companies.

In some cases, teams or individuals leaving one firm may join another, perhaps in so doing creating a 'new entrant' to the broker sector. Notwithstanding this, further consolidation of the sector remains a danger. Were this to take place, it would almost certainly not be to the advantage of trust boards, who could see their trusts suffering from reduced competition, fewer market makers in their shares, wider bid/offer spreads, wider and more volatile discounts and, perhaps, ultimately to corporate take-overs and/or mergers.

This, in turn, could lead not just to the dissolution of the company which they serve but, on a wider scale, to a contraction in the size of the trust sector itself.

The increasingly widespread application of annual retainers for the provision of corporate broking services ought to reduce the reliance by brokers upon infrequent large deals and, perhaps, help justify their departments' existence in a cost-conscious corporate world.

The changing face of the sector

The competitive nature of the broking sector has altered significantly too. The past situation might be likened to a well-stocked private pond, once only used by a few friends but in which the fishing has been thrown open to the licensed public. Now, strangers might actually have the temerity to want to fish in the same pool. Not only that but the newcomers, having invested in modern equipment and resources, and incurring various annual outlays, will obviously want to offer top-quality bait and catch the prize fish themselves.

This is all very good for the clinical efficiency of the fishing process but far less comfortable for those used to the old ways. Worse, those who do not keep on top of the game, or catch up with it, run the risk of having their permits withdrawn. This new, more testing, environment means that the old way of doing things can only survive if it provides its own competitive advantage.

Continuing to stretch the fishing analogy, the 'old stagers' might still be able to win the day – but only if they can demonstrate their unique knowledge, accumulated over time of, say, the directions of underwater eddies and currents, the location of feeding spots – and maybe even offer an insight into what the pike might be up to. In such a situation, traditionalists would argue, all the latest gear in the world would produce an inferior result.

After all (returning to the world of investment trusts), in days gone by it was said that those firms (including brokers) with the right connections could influence entire financial dynasties through the use of a quiet word in a private room somewhere. But whether such blue-chip service can continue to be offered at nil fixed cost for the foreseeable future is another question entirely.

As a consequence of all of the factors described above, several options have evolved as to which corporate advice services may be provided to trust boards, and at what cost.

Other factors for boards to consider

Certain brokers are considered 'full service' while others are more specialist in nature, perhaps providing particular expertise with respect to split capital trusts, in-house research, market making or the use of derivatives.

Brokers also have differing corporate cultures in which, for example, dialogue with arbitrageurs may be encouraged or, on the other hand, virtually forbidden. Similarly the global presence of a large multi-national house which offers broking services to UK investment trusts as part of a far larger operation may be attractive to one type of trust company but less relevant to a small UK niche player.

Boards need to be aware that potential conflicts of interest can occur, as brokers freely admit, particularly in the situation where brokers have an important client relationship with the manager.

In certain situations it may be helpful for a board to obtain additional independent advice from a third party such as a specialist consultancy or a corporate finance boutique. Nor should boards be deterred from listening, without obligation, to new ideas and proposals being put to them by another corporate broker. Though not necessarily attractive to the incumbent broker, this mirrors the way that large corporates now operate in the general market with investment banks/brokers and ensures that boards (and fund managers) are shown new ideas.

Some brokers may be less willing to take on trusts with a market capitalisation below a certain size – £25m or £50m perhaps, or some other figure. Liquidity can be a significant problem at these levels causing some industry observers to offer a variety of suggestions including seeking the necessary approvals for the AIM Listings for small trusts, or even the creation of a central trading platform for all investment trusts.

Some brokers offer a range of services. They might on the one hand offer a perfectly satisfactory but basic level of advice and support for £15,000 to £20,000 per annum but charge another investment trust a six figure sum for a comprehensive range of services. Once again it is in the board's hands to consider their options and negotiate the most appropriate brokerage arrangement for their company's needs.

The need of flexibility

Where boards are sub-contracting and paying for brokerage services they have every right to require flexibility from their broker. One board might argue, for example, that the traditional method should be varied in which a trust's launch fees are paid in full at the time of a trust's formation. The possibility of spreading these fees over more than one year could (subject to the prior agreement of the company's auditors), be considered as a way of maximising the initial net funds available for investment. Other trust boards might prefer to follow the conventional route and accept the one-off net asset value 'hit'.

Non-executive directors (NEDs) must also be capable of questioning the advice they are being given, for example by the manager when recommending an appropriate benchmark.

AITC categories, or peer group UK investment trusts, may not always provide the most suitable basis for comparison. In a few cases, certain other types of fund, such as unit trusts investing in a similar sector or region, could offer a better benchmark.

The point is that there is no barrier to creative thinking. The implementation of new ideas that emerge should be easier when brokers are aware that the standard of their advice may determine whether they are likely to be appointed – or, indeed, re-appointed, where they already have a client relationship.

SECTION TWO

The services that corporate brokers can provide

The importance of networking ('eyes and ears' of the board)

What might be summarised as the economics of the secondary market are extremely important to an investment trust company and its board.

A good corporate broker can make a real difference in this regard by monitoring the market place, speaking to shareholders and reporting their views back to the board; ensuring the timely and accurate release of statutory announcements; commenting on performance, both absolute and relative to peer group funds; arranging briefings for retail investors and/or IFAs; and spotting developments in the market, not least in regard to the presence (or absence) of arbitrageurs.

The importance of market making

The principal service that a broker can provide which the manager cannot is that of market-making. Indeed it has been argued that one reason alone for the payment of retainers to corporate brokers is to sustain the viability of the investment trust market-making process.

The process of market-making, i.e. making a price and size with the broker's own risk capital, is critical because its effectiveness (or otherwise) has a significant impact on the liquidity, bid/offer spread, discount and discount volatility of an investment trust's shares. The presence of several market-makers in a given trust's stock is also desirable because it introduces competition with the likely benefit of tighter spreads and maybe narrower and less volatile discounts too.

The representatives of integrated houses argue that the presence of in-house market-making is essential because, for example, if there are five sellers for every buyer then this fact would not necessarily be known by an agency broker.

Agency brokers and/or corporate finance boutiques, on the other hand, would argue that they are not constrained by the market-makers' book and have the ability to deal with whoever offers the best terms. However this can only occur if there are a number of market makers prepared to make a price in a given trust's stock.

It should be noted that the payment by a trust of an annual retainer to its broker is not likely to constitute a guarantee that the broker will make a market in a certain size or price in its stock or maintain a particular bid/offer spread.

Market making teams are often willing to facilitate dealings for investment trust savings schemes and ISA schemes. The resultant flow of share purchases, on however modest a scale, can be a useful adjunct to other efforts to improve the liquidity of a trust's shares. (The AITC-commissioned "A report into Secondary Liquidity in the Investment Trust Sector", by Simon Colson, which gives useful guidance in this area, can be downloaded from website www.aitc.co.uk/technical).

The importance of sales

Larger brokers will employ several salespersons and some will provide a dedicated salesperson (and an alternate) as a point of contact for each trust.

Sales teams will typically maintain relationships with a broad range of UK institutions, self-managed/local authority pension funds, the major private client brokers and selected overseas institutions.

Some firms also provide automated dealing services to private client brokers and managers either through remote terminals in client offices or on-line. Enhancements sometimes offered include guaranteed dealing at 'touch' prices, price improvement facilities for larger clients and real time dealing and execution.

It should be noted that sales teams will deal in any stock, irrespective of whether their firm is the broker to the trust. The sales team will often work with the fund manager if they have a line of stock to sell. The fund manager may be able to provide information on which shareholders they have visited recently, identify who is buying and selling and may be able to talk directly to the potential buyer.

As highlighted elsewhere, therefore, the ideal situation is one in which board, broker and manager are all working together within a framework of mutual support and trust.

Boards have the right to ask for what they want and some have found it useful to invite their dedicated salesperson to give them a personal briefing, perhaps quarterly, on liquidity issues involving their company.

The importance of research

Research may be conducted at various levels and some brokers expend a great deal of effort providing daily, weekly and monthly commentaries including sector reports and stock recommendations.

Many trusts also issue daily, or certainly weekly, net asset values and most fund managers now have web sites updated monthly with comments on performance, strategy, sector allocation, stock selection gearing and outlook. The AITC site www.aitc.co.uk itself provides not just a great deal of information and statistics, but specific guidance documents on such matters as Treasury Shares. It is important, therefore, that the research provided by brokers adds value and insight to the plethora of 'open source' data already available.

Brokers can do this by publishing regular analyses of key events; reviews (including peer group reviews) of management and investment styles; tailored data sheets and performance reports for inclusion with board papers and one-off research documents covering key industry issues (such as the valuation of debt at par or at market and the effects of trust discounts thereupon).

Brokers' company research may also be made available on-line to investors, using a log-in and password access system.

The importance of corporate advice to the board

The broker must be prepared to provide corporate advice to the board not just by acting as a 'springboard' for new ideas but by maintaining a watching brief on virtually all aspects of a trust's wellbeing and proposing remedies to problems whether already present or foreseen.

The sorts of advice that may be offered include reviews of the mandate and objectives of the trust; capital structure; gearing; strategy, for example with regard to share buy-backs and their implementation; corporate governance matters and ways to expand the trust by share issues (including 'C' share issues where appropriate). Alternatively, it may be recommended that cash be returned to shareholders via tenders to buy back large tranches of shares; the potential for (or dangers of) mergers and acquisitions may be examined, and options for restructuring the trust may be considered. In extreme cases, the winding-up of the trust may even be suggested, as a means of giving shareholders an exit at close to net asset value.

As stated earlier, the broker's mind is likely to remain a great deal more focused on providing a given trust with the best possible level of advice when it is aware that boards can and will look elsewhere if they are dissatisfied with the service they are receiving. In recent years a growing number of boards have done just that, arranging 'beauty parades' from among the broking community with a view to appointing replacement advisers, contracted on new terms.

The biggest beneficiaries of this trend have been those brokers that have set themselves up to win brokerships by offering a high level of service and addressing the difficult issues of the day.

Before a broker takes on a new trust, however, it is usual to ask the chairman of any existing trusts being advised whether there is any objection to the new arrangement. This is particularly important where the 'new' trust has a similar mandate (such as UK smaller companies) to that of the existing trust being advised.

The role of the investment manager

Many fund management groups now have their own investment trust management teams who may already be providing boards with some of the services that a broker intends to offer. It is not unusual for the manager to organise regular meetings with institutional shareholders and private client managers following, for example, the announcement of annual or half-yearly figures.

In addition managers may arrange a number of presentations around the country over the course of a year, either on their own or with the support of the AITC or a specialist financial marketing organisation. Feedback from these events may be passed back to boards on a regular basis.

Company secretarial departments are often well used to issuing statutory announcements of a routine nature and there may be little that brokers can add to the process. However brokers are often accustomed to advising on more specialist announcements and documentation and working with the UKLA. It is likely that this type of advice would be subject to a separate contract owing to the specific nature of the work.

Most fund managers have their own performance measuring teams or the means of calculating the investment returns of their trusts. The results may be provided in regular board papers and produced in interim and full-year accounts. Fund managers may also have access to daily performance data showing comparison with peer group funds. Many fund management groups also analyse their shareholder lists very closely and may receive additional reports from specialist providers who 'look through' nominee accounts to identify the underlying holders of the shares.

In summary, some fund managers already provide boards with a good deal of the information which brokers may offer. The key for the broker is to be seen, therefore, as willing to work closely with the manager to enhance the overall standard of the services and advice received by trust boards. In some cases, too, shareholders may be more open with the broker about their concerns than they would with the manager.

Most trusts aim to keep their shareholders up to date either (in the case of larger shareholders) through personal visits or via information despatched by post or promulgated on the internet. Brokers can enhance this service by writing reports and by giving recommendations.

Brokers can follow developments in the trust sector and give boards a steer as to the likely effect, if any, on the trust. They can also help to 'manage' a share register, especially where there are large lines of stock available to the market and can look for help from the manager in placing that stock with a good long-term investor.

SECTION THREE

The four basic options for obtaining corporate advice

Nil retainer - the traditional model

Nil retainer. Usually a relatively informal arrangement in which the broker makes no fixed annual charge. The broker mainly relies for funding purposes upon market making, dealing commission from, for example, share buy-backs, and periodic sizeable fees from corporate deals. Charges may also be levied for additional tasks such as the provision of one-off advice on a specific issue.

Note: the above traditional broking model was once predominant but is becoming less widespread. A number of brokers will now only take on a new client if the trust's board is prepared to pay an annual retainer. Existing clients are in some cases also being persuaded to move to a fixed retainer agreement.

Standard retainer

Standard retainer (typically of £20,000 to £30,000 per annum per trust). A set menu of agreed tasks, detailed in a formal written agreement, is provided within the standard retainer; extra charges can be made for out of the ordinary tasks; and revenues from dealing commission on share buy-backs and/or fees from corporate deals may be off-settable against the retainer. An example of a list of agreed tasks is given later in this report.

Bespoke broking model

Bespoke retainer (which might vary from as little as £15,000 to as much as £125,000 or more per annum). Agreed on a one-to-one basis between a trust's board and the corporate broker; tailored menu of agreed tasks to be provided within the retainer; charges by negotiation for additional work; revenues from dealing commission on share buy-backs and/or fees from corporate deals may be off-settable against the retainer.

The DIY option

A sponsor is appointed for a trust's launch but no corporate broker is retained.

Instead, corporate finance boutiques, brokers or other specialist advisers – each offering differing types and levels of service – are employed as and when required for specific tasks.

This route has been followed by certain trusts that have been launched in recent years and typically managed by small, relatively 'boutique' investment management companies. It is likely to remain less attractive to older trusts and management houses with a long-established system of relationships and divided responsibilities between board, manager and broker in place.

Particularly at the time of a trust's formation, the 'DIY' route option can be cheaper than the traditional route, perhaps resulting in a higher post-launch net asset value than would otherwise be the case. A counter-argument to this approach might be that trusts without the retained services of a corporate broker lack the comfort of knowing that someone is not just acting as their 'eyes and ears' in the market place, but is ready to fight their corner should difficulties arise.

The formal corporate brokerage agreement

Typically an agreement between a broker and a trust board will be formalised in a document which sets out both the terms under which the broker will provide corporate services and financial advice and the level of remuneration for their provision.

It is likely that the agreement will have a clause, which will state that the annual fee will be offset against any significant corporate fees that the trust incurs in the financial year. In addition if a brokerage charge is deducted on any buy-backs, this commission may also be offset against the annual retainer.

Some brokers will expect to be reimbursed for any travel and out of pocket expenses in relation to any of the services provided to the trust.

A typical agreement is likely to describe the provision of the following services:

- Provide a point of contact at a senior level on the corporate finance side to maintain contact with the board. Points of contact will also be provided for the board and manager who should monitor activity, on a day-to-day or regular basis, in the shares and feed back comments from shareholders.

- Provide advice and comments on statutory announcements including annual and interim statements and any other types of shareholder announcements and documents.

- Arrange meetings for the board with major shareholders if appropriate.

- Attend board meetings at least once a year and update directors on developments in the market in general and any points which are specific to the trust.

- Attend the AGM.

- Liaise with major shareholders if appropriate in relation to any corporate activity.

- Make a market in the shares.
- Help to market the shares to existing and potential shareholders.
- Provide research for publication on the trust in relation to performance, comparisons with peer groups funds, strategy and objectives.
- Provide a regular health check on all aspects of the trust including performance, capital structure, buy-backs (including Treasury Shares), corporate governance, composition of the board, changes to the share register, views of shareholders, gearing, and any other developments which are likely to have an impact on the trust.
- Provide technical advice in relation to the share listings and any ongoing obligations with the UKLA and any stock exchange where the shares are listed.

Formal agreements – other points

A significant part of the agreement will cover the legal and regulatory conditions under which the broker will provide the services and highlight what can and cannot be done under the formal arrangement.

The document will often specify that if the broker provides any advice in relation to a particular corporate action, then this will be subject to a separate agreement and engagement letter.

Confidentiality issues may be spelt out in detail. The conditions under which either party can break the agreement, and at what notice period, may be described.

Different investment trusts and their boards may have widely differing needs in respect of the services expected of their corporate broker. On the one hand, a trust may have a highly experienced board of directors with a close understanding of the dynamics of corporate finance and UK equities. In such a case then the full bespoke services of a corporate broker would add less value than they would in the case of, for example, an overseas-based company entering the UK closed-ended sector but needing guidance at almost every stage.

The future of the corporate broking sector - conclusions

As highlighted in the main body of this report, there has already been significant consolidation in the investment trust corporate broking sector and future exits by large integrated houses cannot be ruled out. It has even been suggested that, to a global, multi-disciplined financial house, UK investment trust companies are "an unimportant and relatively unprofitable asset class."

Some numbers bear these concerns out. Where at one time the trust sector was capitalised at more than 10% of the entire FTSE All-Share Index, this figure is now under 2%. Moreover the entire investment trust sector is smaller in capitalisation terms than each of the largest five companies in the FTSE-100 Index. Yet there are over 600 individual securities for analysts to consider within the trust sector. For brokerage firms, this can put pressure on revenues generated on a departmental 'per-person' basis.

Experienced brokers point out that while management companies can generally predict their cash flows at least a year or two ahead, and budget accordingly, this is not usually the case in the broking world.

On the other hand trust management houses can and do reward brokers by using them to implement equity transactions on their behalf and this can generate sizeable sums over the course of the year. That does not alter the fact that brokers, some employing quite large teams, have long been used to a cyclical 'feast and famine' existence and to looking ahead for the next 'big thing'. The 'next big thing' is a little hard to predict at the moment, though some now hold high hopes for the UK Government's recent initiative to launch property investment funds (PIFs) loosely based upon US-style Real Estate Investment Trusts (REITs).

Meanwhile, deal flow from trust launches and rollovers has slowed to a trickle. This is why brokers may not feel that they can retain substantial multi-disciplined teams, to await the next bull market or a major development – such as the launch of PIFs – on the basis of small (or nil) retainers plus a flow of dealing commissions charged at 0.2% or even less.

One way ahead – for brokers and trust boards alike – may well be a formally retained, properly remunerated, corporate broking sector. However, the investment trust industry has re-invented itself many times over the last century and more. It is not inconceivable that the industry could develop its own market should external providers fall by the wayside. In the end, the market will decide.

Appendix One

Corporate Brokers – contact details

Note: the following data has been provided by the brokers thenselves, in response toresearch for this report. contact details may differ from those nominated in the less frequently updated UKLA sponsors list (of c.80 firms) that can be found on the FSA's web site, www.fsa.gov.uk.

Broker	Contact 1	Contact 2
ABN AMRO Hoare Govett Limited 250 Bishopsgate London EC2M 4AA Tel: 020 7678 8000 Fax: 020 7678 7702 Website: www.abnamro.com	Bob Cowdell Tel: 020 7678 7509 e-mail: bob.cowdell @uk.abnamro.com	Hugh Field Tel: 020 7678 1902 e-mail: hugh.field @uk.abnamro.com
Arbuthnot Securities Arbuthnot House 20 Ropemaker Street London EC2Y 9AR Tel: 020 7012 2000 Fax: 020 7012 2001 Website: www.arbuthnot.co.uk	James Steel Tel: 020 7012 2100 e-mail: jamessteel @arbuthnot.co.uk	Tom Griffiths Tel: 020 7012 2129 e-mail: tomgriffiths @arbuthnot.co.uk
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Appendix Two

About the AITC

The AITC is the non-profit making trade body of the investment trust industry and was formed in 1932. Contact details:

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About the Author

John Newlands set up his own Edinburgh-based consultancy in January 2003 before which he was investment trust analyst at the London stockbroking firm of Williams de Broë Plc. Investment analysis was his second career after leaving the UK Royal Navy in 1994.

In addition to his work as an analyst he has written two hardback books about the sector. The first, Put Not Your Trust in Money, the official history of the UK investment trust industry, was published in 1997. His second book, F&C - A History of Foreign & Colonial Investment Trust, written jointly with Neil McKendrick, Master of Gonville & Caius College, Cambridge, was published in 1999.

Both books can be ordered via website www.newlandsfr.co.uk.

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