HMRC - STSM124010 - Introduction

A transaction on a stock exchange or other financial market must be between two members of that exchange - an ordinary person cannot trade stock on an exchange, such trades must be done through a broker.

There a number of different types of brokers and dealers operating in the financial markets, offering a wide variety of services to clients.

The most common of these is a broker (or stockbroker). A broker is a middleman who buys and sells shares on behalf of his clients. He earns his income by taking a commission for the transactions he carries out.

The main services offered by brokers are:

Execution-only dealing - This is the ‘cheap and cheerful’ end of the market. The investor knows what he wants to buy or sell and instructs a broker to carry out the transaction. The broker gives no advice or guidance. The fees paid for this service are likely to be modest, although most brokers will charge a minimum commission.

Advisory service - the broker offers a fuller service which will include advice on which shares to deal in. Investment research carried out by the analysts at the firm may also be available. The final decision on whether to buy or sell will however still rest with the client.

Discretionary service - sometimes described as portfolio management, where the broker manages the investments of clients. The broker will ascertain what the investment objectives of the client are so that he can take the right decisions.

In contrast, a dealer is an individual or firm that buys or sells securities as principal for their own account. This is often referred to proprietary trading.

Many firms act in a duel role as a broker dealer, combining the functions of a broker, with that of a dealer, depending on the transaction.

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