

**EFAMA PRELIMINARY RESPONSE TO
THE CONSULTATION CONCERNING ESMA GUIDELINES
ON CERTAIN ASPECTS OF THE MIFID SUITABILITY REQUIREMENTS**

EFAMA is the representative association for the European investment management industry. EFAMA represents through its 27 member associations and 57 corporate members approximately EUR 14 trillion in assets under management of which EUR 8 trillion was managed by approximately 54,000 funds at the end of 2011.

EFAMA strongly supports ESMA's guidelines which aim to enhance clarity and foster convergence in the implementation of the MIFID suitability and organizational requirements related to the compliance function.

Although EFAMA agrees with many of the ESMA's guidelines, we are concerned that the proposed guidelines seem to be based on the assumption that investment firms are obliged to prevent clients from acquiring unsuitable investment products. However, MiFID does not contain such an obligation. Investment firms have to perform a suitability test and they are not allowed to advise any investment product which, according to the result of the test, is not suitable for the client. It is then up to the client to decide whether he follows the test result (and the given advice) and acquires a suitable product, or if he ignores the test result and invests in an unsuitable product.

The suitability regime applies to all clients, both retail and professional. There is a very different relationship between investment firms and professional per se clients and between investment firms and the mass retail market. Typically, a per se professional client will give an investment manager discretion over a specified segment of their assets and request that they are managed in accordance with investment restrictions as detailed in the relevant investment management agreement. Such clients are of course entitled to suitability. However, in such circumstances the service requested by the client itself limits the extent to which suitability can be framed. We would therefore urge ESMA to make this distinction clearer as to the extent to which the guidance applies to per se professional clients.

Against this background, we wish to submit the following answers and comments to the consultation.

Guidelines on certain aspects of the MIFID suitability requirements

Questions and Answers

Q1 Do you agree that information provided by investment firms about the services they offer should include information about the reason for assessing suitability?

EFAMA agrees that the reasoning for assessing suitability should be provided to the client. However, the way to inform the client should be left to the discretion of the investment firm (general terms and conditions, posted on the web site or on the questionnaire). In addition, the information should not have to include the way a risk profile is established. What is important is that clients should be informed about which type of risk and what level of risk a petite is determined. Information on the methodologies to identify how a risk profile is established could be too technical and therefore non-comprehensible to the client.

Q2 Do you agree that investment firms should establish, implement and maintain policies and procedures necessary to be able to obtain an appropriate understanding regarding both the essential facts about their clients, and the characteristics of financial instruments available for those clients?

EFAMA agrees that the suitability assessment process should be implemented and maintained with clear policy and procedures. Investment firms should have policies capable of achieving an appropriate knowledge of their clients and of the characteristics of financial instruments available for those clients.

Q3 Do you agree that investment firms should ensure that staff involved in material aspects of the suitability process have the skills and the expertise to discharge their responsibilities?

EFAMA agrees that staff involved in material aspects of the suitability process should have proper skills and expertise to establish and perform the suitability test. Those skills and expertise should be adapted to the task performed by the relevant staff. Each step of this assessment process may not be implemented by the same person, and the required skills and expertise at each stage may therefore vary. In addition, concerning the service of investment adviser, the correct relation between the client's need and the recommended financial instruments should be assessed only at the time when such advice is provided.

Q4 Do you agree that investment firms should determine the extent of information to be collected about the client taking in to account the features of the service, the financial instrument and the client in any given circumstance?

EFAMA agrees that the extent of information to be collected should take into account some features such as the type of the service provided. For example, pension schemes often use consultants which provide recommendations or "advice" on asset allocation, manager choice and overall strategy. Such

“advice” on asset allocation is not regulated in Europe. A manager will be asked to compete for the award of a mandate of € hundreds of millions and that mandate will have been framed by the consultant and client to cover perhaps only equities or fixed income and then only one-half or one-third of all the equities. It is important to note that in such circumstances the service requested by the client itself limits the extent to which suitability can be framed as if applying to the client overall rather than the service given to that client.

As regards retail clients, investment advisers usually should first collect information from clients and as a second step, determine the type of financial instruments that shall be recommended.

Recommendations do not form part of the suitability test, but should be provided on the basis of the results provided by the suitability assessment. Therefore, it seems not appropriate to differentiate the extent of information depending on the type of financial instruments as suggested in guideline 22.

Preliminary differentiation should rather be performed in accordance with the investment objectives of the client (long-term/short-term, conservative or more risk-inclined etc.).

There are also some practical difficulties related to the information to be gathered according to the draft guidelines. EFAMA’s members have noticed that in general clients are not willing to disclose information such as total income, assets and regular financial commitments. As a result, those clients would prefer investment firms that ask the “least intrusive” questions, resulting in an un-level playing field. In the ESMA’s guidelines it is not clear how those requirements of gathering more and more in-depth information are to be implemented in practice. ESMA does not provide any guidance concerning the approach and methodologies to be used to collecting all those information from the clients.

Consequently, EFAMA proposes to ESMA to develop an approach and a methodology for the different levels of information to be gathered which must be applied by all investment firms, resulting in a level playing field and an adequate protection of clients across the European Union.

Q5 *Do you agree that investment firms should take reasonable steps or ensure that the information collected about clients is reliable and consistent?*

EFAMA agrees that investment firm should take reasonable steps to ensure that the information collected about client is reliable and consistent. However, as explained in article 37(3) of MiFID 2006/73/CE, “An investment firm shall be entitled to rely on the information provided by its clients or potential clients unless it is aware or ought to be aware that the information is manifestly out of date, inaccurate or incomplete.”

ESMA should state in the guidelines that an investment firm cannot be held responsible if the client provides out-of-date, inaccurate or incomplete information.

Q6 *Do you agree that where an investment firm has an ongoing relationship with the client, it should establish appropriate procedures in order to maintain adequate and updated information about the client?*

EFAMA agrees that this should be a good practice but it would not be useful to update information about a client for whom the firm will not undertake any further work. This procedure should be required to be established only where appropriate given the relationship with the client. In addition, the client should be obliged to inform the investment firm about all changes that may affect the service that is provided on an ongoing basis. Investment firms cannot be aware of such changes.

Q7 *Do you agree that regarding client information for legal entities or groups, the investment firm and the client should agree on how the relevant client information will be determined and, as a minimum, information should be collected on the financial situation and investment objectives of the beneficiary of the investment advice or portfolio management services ('end client')?*

EFAMA agrees with ESMA that regarding client information for legal entities or groups, the firm and the client should agree on how the relevant client information will be determined and that minimum information on the financial situation and investment objectives of the beneficiary of the services should be collected.

Q8 *Do you agree that in order to match clients with suitable investments, investment firms should establish arrangements to ensure that they consistently take into account all available information about the client and all characteristics of the investments considered in the suitability assessment?*

EFAMA considers that the final objective of the suitability test is to match a client's needs and a suitable investment. As a consequence, this assessment should ensure that it takes into account available information about the client and all characteristics of the financial instrument.

Q9 *Do you agree that investment firms should establish and maintain record-keeping arrangements covering all relevant information about the suitability assessment?*

We agree that investment firms should establish and maintain record-keeping arrangements. These arrangements should be an integral part of any investment firm's business activity. This is particularly relevant in the event of any dispute or complaint, when accurate records need to be referenced.

We note that the guideline proposes that the record keeping arrangements are designed to enable the detection of failures such as mis-selling. We agree that the records should be capable of identifying consumer detriment in that way. However, such activity seems to imply an active process rather than the passive activity of keeping information as records. This would seem to be an unnecessarily burdensome requirement and we would not see the need for keeping the records under constant review as being efficient or necessary in a competent and well-run investment firm.

Proposed Amendments

Draft Guideline No. 9

The second sentence of No. 9 should read as follows:

"At no stage during the suitability assessment process, or when informing clients, should investment firms create any ambiguity or confusion about **which responsibilities have to be borne respectively by them and by the client** in the process."

It should be clear that the investment firm is not responsible for every aspect of the process. The client is responsible for the correctness of the information provided by him, and also for the decision whether to follow the test result (and a warning by the investment firm) or to choose an unsuitable product. His final decision may not be part of the suitability assessment process, but is closely linked to it.

Draft Guideline No. 11

The guideline should be deleted.

In our view, the investment firm is only obliged to gather information about the financial knowledge and education of the client. It is not responsible for improvement of these skills. The investment firm has to find out to what extent the client understands the relationship between risk and return or the set-up of a risk profile. But there is no duty to educate clients on these points. A client's poor understanding has only to be taken into consideration as part of the suitability test.

Draft Guideline No. 31

In case investment firms do not obtain sufficient information from clients, they should refrain from recommending investment services or financial instruments, but are not generally prevented from performing investment services as such (Article 35 para. 5 of MiFID L2 Directive). This is important in terms of portfolio management where it should be possible to provide management services on a cautious basis even if the client objects to disclosing some aspects of the relevant information. Thus, the wording of guideline 31 should be amended in "it must refrain from **recommending investment services or financial instruments** to that client".

Draft Guideline No. 32 (a) should read as follows:

"In particular, firms should **only rely on the client's self-assessment if it is based on clear and objective criteria**";. The second sentence in **Guideline No. 33** should be deleted and the first sentence in **No. 34** should start as follows:

“Investment firms should try to lead the client to a self-assessment that is rather based on objective criteria than on opinions or estimations. For example: ...”

No. 32 (a) actually indicates that self-assessment should not be used at all, which is not in line with Nos. 33 and 34. In many cases, investment firms have to rely mainly on clients' self-assessment because there is no other source of information available. As stated in No. 33, it is the client's responsibility to provide correct and complete information. Investment firms may only support clients with this task, for example by asking for facts rather than for estimations. However, if the client's self-assessment turns out to be wrong, the investment firm shall not be liable.

Draft Guideline No. 44 (c) should read:

"the **actual** financial situation of the client allows him to finance his investment and to bear any possible losses resulting from his investments;"

Investment firms may not always have information about investments and disinvestments made by their clients (e.g. in case of pure investment advisers maintaining no client accounts).

Draft Guideline No. 47

The wording shall be amended to read "information about financial instruments **recommended** to the client". Financial instruments are generally "accessible" to clients at their own initiative, regardless of the results of the suitability test.

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