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London, 24 February 2012

Re: Consultation paper on certain aspects of the MiFID suitability requirements

Dear Sir, Madam,

We welcome the opportunity to respond to the ESMA Consultation Paper entitled "Guidelines on certain aspects of the MiFID suitability requirements."

We support most of the guidelines proposed in the paper, but we are concerned that some requirements are ambiguous, or do not take into account a clear division of responsibilities between an investment firm and its clients. The text seems at odds with our general understanding that, if a client has been sufficiently informed and warned, he is ultimately responsible for making his own investment decisions. Some statements in the guidelines could lead to the impression that an investment firm takes investment decisions on the client's behalf. The client should decide their investment aim or risk appetite; it is not the responsibility of the firm to establish, decide or correct a client's investment aim or risk appetite.

We also note that the consultation paper mostly addresses the conduct of suitability tests. We would also suggest addressing relevant internal policies, systems and controls.

Some of our comments do not relate to the specific numbered questions posed in the Consultation Paper, but rather, the material contained in the Background section and Appendices to the document. Thus, in the pages below, we have also inserted comments according to the sections of the Consultation Paper to which they relate.

We trust you find these comments useful. Please let us know if we can provide further information.

Yours sincerely,

A blue ink signature, likely of Andrew Procter, consisting of a stylized 'A' followed by a horizontal line.

Andrew Procter



Guidelines on certain aspects of the MiFID suitability requirements

Section II – background

Although we generally agree with the description, we believe there should be a clearer distinction between investment advice and portfolio management. In the case of investment advice, the financial instruments that are recommended should be suitable for a client, whereas in the case of portfolio management it is also key that a recommended investment strategy is suitable.

With regard to paragraph 11, we note the description that requirements need to be met “on an ongoing and consistent basis for any client”. It is not clear what firms are required to do on the basis of this text. Neither MiFID1 (nor the proposal for MIFID2) contains a similar obligation. We would suggest deleting this phrase.

In the same paragraph, the phrase “irrespective of the distribution channel used” may create some confusion between the responsibilities of investment firms that act in an advisory capacity (and thus have to carry out suitability tests) and those that only manufacture a product.

Q.1 Do you agree that information provided by investment firms about the services they offer should include information about the reason for assessing suitability? Please also state the reasons for your answer.

We are concerned about paragraph 17 and the associated Annex III, paragraph 10, which states that a firm should recommend “the most suitable product or service”. ESMA has no delegated power to require that firms recommend the “most suitable” product or service. Investment firms may, when providing advice, discuss a range of suitable products and may suggest that some align more closely than others to the clients' objectives. Imposing a requirement to specify the “most suitable” product is unduly onerous and may prevent the firms from fully discussing a range of products which may all be equally suitable for a particular client.

In paragraph 19 we feel a better balance should be achieved between the responsibilities of an investment firm and of clients. MiFID requires investment firms to decide if a recommendation or product is suitable for a client’s investment objectives, risk appetites, etc. However, the decision to buy a product can only be made by the client himself. If an investment firm warns a client not to buy a product or take a service, but the client decides to buy the product nonetheless, this decision is and remains the sole responsibility of the client.

Thus, for the avoidance of doubt and in order to ensure that investment firms are not exposed to legal liabilities for clients’ decisions in these areas, the text should be clarified to state that: (a) investment firms must ensure that the products they recommend are suitable, but are not responsible for the product which the client ultimately acquires; and (b) clients must provide investment firms with sufficient information on their investment objectives and risk appetite.

Q.2 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? Please also state the reasons for your answer.

We agree.

- Q.3 Do you agree that investment firms should ensure that staff is involved in material aspects of the suitability process have the skills and the expertise to discharge their responsibilities? Please also state the reasons for your answer.**

We agree.

- Q.4 Do you agree that investment firms should determine the extent of information to be collected about the client taking into account the features of the service, the financial instrument and the client in any given circumstances? Please also state the reasons for your answer.**

Although in situations where large numbers of clients are serviced a certain level of procedural standardisation is needed, we agree that in specific circumstances (for example when a retail client wants to buy a bespoke financial instrument) it will be appropriate to request more information to ensure this product is suitable for this specific client.

With regard to paragraph 36 (and Annex III, guideline 31) we note that if an investment firm has not obtained sufficient information to make a suitable investment recommendation, MiFID prohibits the firm from providing the recommendation, but not from executing a trade that the client demands. Thus, the text should focus on a firm's provision of the recommendation, not on the execution of a service required by the client.

- Q.5 Do you agree that investment firms should take reasonable steps (and, in particular, those outlined above) to ensure that the information collected about clients is reliable and consistent? Please also state the reasons for your answer.**

Generally, we believe that increasing the complexity of the client on-boarding process by asking open-ended questions such as the client's familiarity with financial instruments and provision of factual information on their financial situation (as required in paragraph 38) is, in our view, likely to be expensive and time-consuming to implement and likely to yield unclear and unreliable information.

We also note that, if a product includes a capital guarantee for securities – for example -, a client may not be aware of the risk of insolvency of the guarantor. Therefore, the client would be unlikely to describe it when asked about it according to example c of paragraph 38. To avoid confusion, firms should set out the risks of a product clearly. We believe that the approach in point c of paragraph 38 (and Annex III, guideline 34) could be confusing to clients.

- Q.6 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? Please also state the reasons for your answer.**

We agree.



- Q.7 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')? Please also state the reasons for your answer.**

Although we agree that in the circumstances described under III.VI (and Annex III, guideline 39) a firm should agree with the client how the suitability test will be carried out, we feel there should not be a reference to "beneficiary". The term "beneficiary" is often used in the context of civil law and can therefore have different meanings. It may also be unclear or uncertain who the beneficiaries of a financial product are. Where a client is a trust, for example, a firm may not be able to obtain sufficient information about the beneficiaries to carry out a suitability test.

We would suggest that the reference to beneficiaries be removed and that the suitability test be based on the official representatives of the legal entity.

With regard to paragraph 43, we believe that an obligation to assess the knowledge and experience of a group of natural persons in order to gauge who has the least knowledge, would come close to requiring a suitability test for all those individuals. Therefore, it may be more appropriate to assess which person in the group has the lowest risk appetite, and base the suitability test on this person.

Furthermore, we suggest that a firm should be able to use a different approach than the one outlined in paragraph 43 if this meets the objectives of the suitability test better.

- Q.8 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? Please also state the reasons for your answer.**

We broadly agree with the proposals. One helpful clarification would be to change paragraph 44 from "investment firms that rely on tools in the suitability assessment process" to "investment firms that *solely* rely on tools in the suitability assessment process".

With regard to paragraph 46 (a) we would add "unless a client has specifically instructed the firm not to".

We would also note that the ongoing disclosure requirements, in particular the requirement to ensure that a client can "finance his investments at any moment and to bear any possible losses resulting from his investments" may be very onerous and may limit long-term debt and investment in ventures such as start-ups.

- Q.9 Do you agree that investment firms should establish and maintain record-keeping arrangements covering all relevant information about the suitability assessment? Please also state the reasons for your answer.**

We agree.



Annex III, paragraph 11

MiFID requires firms to inform clients about the risks of a product. We note that where the guideline recommends informing a client about *how* a risk profile is established, goes beyond the obligations of MiFID.

Annex III, paragraph 41.

In line with our comments above we would suggest the following amendment:

General guideline

*41. In order to match clients with suitable investments, investment firms should establish policies and procedures to ensure that ~~they~~ **their recommendations** consistently take into account:*

(a) all available information about the client. ~~including his current portfolio of investments (and asset allocation within that portfolio), that is likely to be relevant in assessing whether an investment is suitable.~~

(b) all characteristics of the investments considered in the suitability assessment, including all relevant risks and any direct ~~or indirect~~ costs to the client.

Annex III, paragraph 24 and 44

The financial circumstances of a client may vary over time and it will be extremely difficult for an investment firm to monitor a client's personal financial commitments. The guidelines should reflect information that firms can realistically and objectively obtain. We would suggest the following amendments:

Paragraph 24:

b) the client's assets, including liquid assets, investments and real property, which would include what financial investments, personal and investment property, pension funds and any cash deposits, etc. the client may have ~~(the firm should also gather information about conditions, terms, access, loans, guarantees and other restrictions, if applicable, to the above assets that may exist).~~

c) The client's regular financial commitments, which would include ~~ascertaining what financial commitments the client has made or will be making within a timeframe that would affect any investment the client wished to make (or that the firm wished to recommend or enter into in the course of providing a portfolio management service).~~

Paragraph 44

Policies and procedures established by the firm should enable it to ensure inter alia that:

*a) The advisory and portfolio management services provided to the client take into account an appropriate degree of risk diversification, **unless the client specifically requests otherwise.***

b) The client has an adequate understanding of the relationship between risk and return, i.e. he understands that the remuneration of risk free assets is necessarily low, and the impact of costs on his investments;

c) ~~The financial situation of the client allows him to finance his investments at any moment and to bear any possible losses resulting from his investments;~~

d) ...