

ALFI COMMENTS AND RESPONSES TO ESMA'S CONSULTATION PAPER ON GUIDELINES ON CERTAIN ASPECTS OF THE MiFID SUITABILITY REQUIREMENTS

ALFI is the representative body of the 2.1 trillion Euro Luxembourg fund industry. It counts among its members not only investment funds but also a large variety of service providers of the financial sector. There are 3,845 undertakings for collective investment in Luxembourg, of which 2,427 are multiple compartment structures containing 11,876 compartments. With the 1,418 single-compartment UCIs, there are a total of 13,294 active compartments or sub-funds based in Luxembourg.

According to September 2010 EFAMA figures, Luxembourg's fund industry holds a market share of 30.9% of the European Union fund industry, and according to 2009 Lipper Hindsight data, 76.2% of UCITS that are engaged in cross-border business are domiciled in Luxembourg. As one of the main gateways to the European Union and global markets, Luxembourg is the largest cross-border fund centre in the European Union and, indeed, in the world.

ALFI welcomes ESMA's initiative to consult the public and the financial industry on certain aspects of MiFID suitability requirements.

As a general comment, we would recommend to take into account the fact that investment firms can only rely on the information provided by their clients and that it is those clients' responsibility to give true and reliable information as well as to communicate any relevant changes in his personal situation. Overall we think that current rules are adequate and that any new regulation in this regard should be of real value-added to the suitability process and not constitute a mere additional administrative burden.

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Comments on Section III

(Q1) Information to clients about the suitability requirements - Do you agree that information provided by investment firms about the services they offer should include information about the reason for assessing suitability?

ALFI agrees that the reason for assessing suitability should be provided in a consistent and clear wording. However we do not see the need to always document this on a specific material support. It would be sufficient in our view that general information in this regard be posted on the firm's website, and that documents such as summary or minutes of the client meeting document the fact that the reasons for suitability have been addressed. In addition, the information should not include the way a risk profile is established, we deem important to inform the clients about which type of risk is determined. Information on the methodologies

to identify how a risk profile is established could be too technical and non-comprehensive for the client.

(Q2) Arrangements necessary to understand clients and investments – 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? Please also state the reasons for your answer.

ALFI is of the view that current rules are already appropriate in this regard, these aspects being covered by risk profile questionnaires and other intake forms.

It should only be noted that the collection of personal data is only applicable to individual clients / natural persons (e.g. age, marital status, family situation, employment situation etc.), so paragraph 22 should indicate this.

(Q4) Extent of information to be collected from clients - 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 circumstance? Please also state the reasons for your answer.

In article 28, ESMA refers to the MiFID Implementing Directive definition of complex or risky financial instruments. It must be noted that the EU Commission's proposed MiFID regulation is suggesting a differentiation of UCITS into complex and non-complex instruments – based on criteria that raise our concern, as UCITS have been designed for distribution to retail investors with very strict risk mitigation rules (ALFI's concerns in this regard were detailed in our response to the European Parliament's questionnaire on the proposal for a review of MiFID - http://www.alfi.lu/sites/alfi.lu/files/files/Publications_Statements/Statements/questparl20120113fin.pdf).

We agree that the extent of information to be collected about the client should be taking into account the features of the service and the client – provided the service provided is an investment service and not a post-investment decision service, as provided by Transfer Agents, Processing Agents, Execution Only Platforms, etc. where the investor would have taken his investment decision before submitting his transaction. 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. Investment advisers 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 a distortion of competition. 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.

(Q5) Reliability of client information – 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.

ALFI is of the view that the investor has to take full responsibility of providing accurate information – investment firms cannot be expected to verify that all information provided by the client is correct, as this could be considered by their clients as an unreasonable violation of their privacy. The same applies when ensuring that the questions and investment products discussed are understood. When asking clients what types of instruments they are familiar with, investment firms must be able to place reliance on responses given by their clients. However, ALFI wishes to make clear that investment firms do need to be able to protect themselves against the possibility of loss-making investors asserting, at a future point in time, (potentially wilfully) that they answered certain questions incorrectly. There needs to be a reasonable balance between the extent to which an investment firm can be expected to ensure reliability of the information collected and the exposure an investment firm can face with clients exploiting such “loopholes” in the suitability investor protection mechanism in case of unsuccessful investment.

(Q6) Updating client information – 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.

ALFI is of the view that it is necessary for institutions to review the client’s risk profile if that client informs them of an important new element in his/ her situation. However clients have no legally binding obligation to fully disclose any information to investment firms. It would therefore not be justified to expect firms to take full responsibility for ensuring all client information is reviewed on a regular basis and is up to date. We would also like to draw attention to what should be required for subsequent investment decisions taken at the initiative of the client: For investors having e.g. savings plan arrangements agreeing to an automated investment for a limited or unlimited period at a pre-defined frequency, investor profiling should be performed when the initial arrangements are agreed and put in place. However for later investments or savings plan arrangements the investor is making potentially at his own initiative, one should raise a question as to whether such update should be considered at that point in time.

(Q8) Arrangements necessary to ensure the suitability of an investment – 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.

A client profile usually does not normally change on a permanent basis, unless a request is made by the client themselves. Therefore, we are of the view that the investment firm should base its assessment on the current knowledge about its client. The expectation towards the investment firm to ensure that the client is able “to finance his investments at any moment” cannot be fulfilled at all. The investment adviser is not obliged to perform an ongoing

monitoring of the complete financial situation of the client at any time. Besides the problem of a possible violation of the client's privacy (please see above Q5), the investment advice is given at the certain moment of the meeting with the client and on the information basis at that time. ESMA should not try to introduce a comprehensive liability of investment firms for "wrong" client decisions by means of interpretative Level 3 guidelines, as such liability is not provided for in the Level 1 Directive.

The reference to "bear any loss" in paragraph 46c seems to go well beyond what is needed and required in our opinion.

(Q9) Record-keeping – 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.

The term record-keeping arrangement is used for various types of systems – ALFI would recommend to specify more clearly that in this context it refers to the investment advisor's record keeping. To avoid any confusion with the record-keeping system of a Transfer Agent, Processing Agent, Execution Only Platform, etc., we therefore suggest to use the term "investment advisor records". The detection of failures regarding the suitability assessment and access to records in this context clearly refers to the records of investment advisors, as they are the ones performing the suitability assessments. We further 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.
