



FEDERATION
BANCAIRE
FRANCAISE

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**ESMA CONSULTATION PAPER ON MiFID REQUIREMENTS
REGARDING THE SUITABILITY OF THE SERVICE PROVIDED**

THE FBF'S RESPONSE

The Fédération Bancaire Française (the French Banking Federation, hereinafter FBF) is the professional organisation that represents the interests of the banking sector in France. It comprises all of the credit establishments registered as banks and doing business in France, i.e. more than 450 commercial and cooperative banks. FBF member banks have 40,000 permanent branches in France, 400,000 employees and 60 million customers.

The FBF thanks the ESMA for consulting with the parties concerned regarding the crucial issue of investment services provision.

We would like to make a few initial remarks:

- **We are concerned about whether it is appropriate today to publish the ESMA's guidelines**, which would clarify the rules set out in 2007 through the initial directives, at the very time that the texts are being revised and there are plans for a delegated act to set out the measures intended to guarantee respect for obligations regarding suitability assessment for the service provided to clients by investment firms. The investments made by investment services providers or ISPs (in IT, for the implementation of changes, employee training etc.) to comply with these guidelines are too significant, long-term and costly to require changes every two years, while the professionals involved have already defined procedures and taken steps to implement the obligation of ensuring the suitability of the service provided. Bringing forward the MiF II text guidelines could lead companies to make changes that might subsequently prove unnecessary or incomplete, and could also generate confusion in the networks.

- **If, despite these concerns, the ESMA decides to publish these guidelines, the latter must absolutely be drawn up on the basis of established law ("à droit constant").** Indeed, we understand that the ESMA guidelines on assessment of the suitability of the service provided apply under the current provisions of the MiF Directive (hereafter MiFID), according to which, "When providing investment advice or portfolio management, the investment firm shall obtain the necessary information regarding the client's or potential client's knowledge and experience in the investment field relevant to the specific type of product or service, his financial situation and his investment objectives so as to enable the firm to recommend to the client or potential client the investment services and financial instruments that are suitable for him." Yet it is mentioned in point 11 of the consultation paper that the investment firm should set up procedures that enable it to fulfil its obligations under

the MiFID on an ongoing, consistent basis.¹ To us, this requirement seems to go well beyond the provisions of current MiF texts and to anticipate a reform that is still under discussion among various European institutions, with the risk of contradiction.

- Moreover, the ESMA guidelines should allow some flexibility and set out broad principles, leaving it to the professionals, based on the characteristics of their clients (professional clients in financing and investment banking [BFI], mass processing in retail banking, individual clients with strong demand for value-added in private banking etc.), as well as on the institution's own organisation (centralised or cooperative or saving banks), to decide on how to organise implementation.

- We understand that the consultation paper is aimed primarily at retail clients, which should be explicitly stated. Indeed, a number of requirements proposed by the ESMA are not suited to the wholesale markets.

While we understand that the ESMA consultation paper is based on shortcomings observed by the national supervisors, it should be emphasised that these problems do not necessarily reflect failings on the part of investment services providers (hereinafter ISPs), given the context of the unprecedented crisis that we are experiencing. In Europe, and in France in particular, no failure of the market has been observed in the marketing of financial instruments to non-professional investors, despite the high volatility of the stock market, the low returns on monetary products and the uncertainty seen on the bond market.

In any case, it should be ensured that the new clarifications considered by the ESMA do not create a windfall effect for clients, especially since they are being applied to an activity that is already highly regulated at European level, whereas other potentially more risky products (products permitting exposure to Forex or gold, for example) are now being sold by unregulated providers using sometimes very aggressive methods.

- Finally, it is imperative that the ESMA sets out deadlines for implementing its policies.

Q1: Do you agree that information provided by investment firms regarding the services they offer should include information on the reasons for assessing suitability? Please also state the reasons for your answer.

The banking industry supports the recommendation that clients need to be clearly and unambiguously informed of the purpose of the suitability test, which is intended to serve their best interests, as well as the recommendation requiring that the client not be misled regarding the responsibilities of each party. Indeed, the bank must not tolerate any ambiguity regarding its own responsibilities for conducting of the suitability test. However, it must also notify clients that they are responsible for the information that they send or fail to send to the bank. The ESMA proposal to go beyond this by explaining to clients how their risk profile is established has, in our opinion, the potential to lead some clients to shape the information they give to their bankers in order to obtain a particular product, which, if they were telling the truth about their wealth or product knowledge, for example, would not be accessible to them.

However, it should be noted that, in the absence of a mandate, the ISP should not make decisions in the client's place, including the final decision on whether or not to purchase a given product. It is therefore up to the ISP to provide clients with

¹ "An investment firm should adopt arrangements that enable it to meet the [suitability] requirements on an ongoing, consistent basis [...]."

comprehensive, appropriate information to enable them to make an informed decision. According to the concept of "empowerment" evoked by the Commission as part of the PRIIP's discussions, the ISP must make every effort to allow a client to make informed investment choices, without taking the client's place in reaching the final decision. The ISP could, for instance, offer several products that it considers appropriate, with clients being able to subscribe to whichever product they desire.

It is important, moreover, not to confuse commercial investment advice and its basic questionnaire and average suitability test with investment advice that is set up as a separate service, paid as such and delivered by BFI and private banks. This presupposes a very detailed questionnaire for assessing the client's financial situation. In other, more "basic" activities, this would be an unnecessary burden for the bank and for the clients, who are the first to challenge the extent and complexity of the information demanded of them.

Q2: Do you agree that investment firms should establish, implement and maintain policies and procedures necessary to obtaining an appropriate understanding regarding both the essential facts about their clients and the characteristics of financial instruments available for these clients? Please also state the reasons for your answer.

The French banking industry can only approve the ESMA recommendation that investment firms must know their clients as well as the products they distribute and must implement procedures that allow for collection of the information necessary to assess the suitability of the service provided.

In France, the distributor's knowledge of the product is ensured by mandatory agreements with the producer that specify, in particular, "the conditions in which [the producers] make available the information necessary to assess the overall financial characteristics of the financial instruments."² This information is to be provided by the producer "possibly in the form of presentation brochures" and must make it possible "for both the investment service provider and the client to appreciate all the financial characteristics of the financial instrument." The producer is also required to keep this information up to date.³

The distributor is thus able to master and to explain to clients the essential characteristics and functioning of the financial instrument (risk, investment horizon, determination of potential gain etc.) without the need to go into detail about the intrinsic "mechanics" (algorithms, calculation formulas etc.) that the client would not understand.

The ESMA guidelines should not, in our opinion, go so far as to require investment firms to establish procedures for matching specific products to a specific client category. This would introduce a level of systematisation and automation that would be unfavourable for both ISPs and clients. Indeed, by definition such procedures can only take into account quantitative factors, even though qualitative factors are often required to assess the suitability of the service provided.

Moreover, the ESMA states in point 22 that the ISP must collect information about the marital status of the client. Issues related to the matrimonial situation are dealt with upstream, at the time the relationship begins or when the client indicates a change in status. The opening of accounts (whether an individual account, joint account or joint and several account, for instance), which is clearly defined legally, has full consequences for the powers of each

² Article L. 533-13-1 of the French Monetary and Financial Code.

³ Article R. 533-15 of the French Monetary and Financial Code.

spouse. Moreover, it should be noted that banking secrecy is opposed to one spouse obtaining information about the accounts and assets of the other.

In any case, it is worth reminding that the ISP should not interfere in its client's life and business.

Q3: Do you agree that investment firms should ensure that staff members involved in the material aspects of the suitability process have the skills and expertise to discharge their responsibilities? Please also state the reasons for your answer.

In France, the AMF has established a certification process to ensure that personnel in investment firms have the knowledge and expertise needed to carry out the suitability test.

Indeed, the ISP is expected to ensure that the individuals acting under its authority or on its behalf have the appropriate skills and expertise, as well as a sufficient level of knowledge. The AMF defines and verifies the procedures put in place to validate that the minimum knowledge level required has been achieved and that this condition has been met by the ISPs.⁴

Q4: Do you agree that investment firms should determine the extent of information to be collected with regard to the client, taking the features of the service, the financial instrument and the client into account in any given circumstance? Please also state the reasons for your answer.

The banking industry is quite favourable to the possibility, acknowledged by the ESMA, of tailoring the information to be collected to the nature of the service provided. In particular, it seems quite logical that the information required under a portfolio management would be less detailed than that required for a direct investment, as is outlined by the ESMA in point 30 b) of the consultation paper. However, while it seems normal to require clients to understand at least the general risks of the portfolio management arrangement, we feel it is unreasonable to require clients to also understand all the risks associated with each instrument in the portfolio. Indeed, if clients use delegated portfolio management, it is often because they want to delegate management to a specialist. If the manager wants to use more or less complex option strategies to hedge a client's portfolio, it is difficult to require clients to understand how each hedging instrument operates.

Moreover, it is important to remember that the purpose of gathering information is ultimately to allow the ISP to offer clients products tailored to their situation. It does not therefore seem pertinent to require that the information to be collected is determined beforehand by factors specific to the product, even though, by definition, the ISP is still unsure at this stage regarding what products it will recommend to its client. We also note that the retail banking industry is a mass industry and that it is not possible to personalise the questionnaires for collecting the information; the same information is requested from all clients with a given profile.

Finally, the wording of question 4 might indicate that the ISP is required to have the same level of knowledge of its clients as is required for the fight against money laundering, which goes well beyond the MiFID. Furthermore, it is not possible to use the files established for the fight against money laundering for any other purpose unless the client is expressly informed at the time of collection that the information is also being collected for the purposes of investment advice.

⁴ Articles 313-7-1 and 313-7-3 of the AMF General Regulations/Decree of 3 October 2011.

Q5: Do you agree that investment firms should take reasonable steps (and, in particular, those outlined above) to ensure that the information collected on clients is reliable and consistent? Please also state the reasons for your answer.

As we mentioned previously in response to question 1 of the consultation paper, the French banking industry supports the idea that, within the context of compliance with the rules on protection of personal data, the client must be clearly informed regarding the purpose of collecting information and any consequences thereof. It also agrees that the questions posed to the client must be clear.

On the other hand, we believe that assessing the relevance and reliability of the information provided by the client goes beyond the requirements of the MiFID. In addition, some information is not objectively verifiable, and the bank may not have access to the sources needed to verify it.

It should be recalled that **the relationship between the bank and its client is based, above all, on mutual trust, which these requirements would inevitably undermine and which could lift all responsibility from the client's shoulders, a situation that is not acceptable.** The bank must not be mixed up in the affairs of its client.

Moreover, point 40 of the consultation paper seems to suggest that the ISP should go so far as to ask trick questions in order to ensure the reliability of the information provided by the client. Again, this view of the customer relationship is not acceptable and is likely to significantly weaken the confidence that is at the heart of the bank/client relationship. And as we replied to question 1, taking all responsibility away from the client is not healthy and may even lead to devious behaviour.

Article 37.3 of Directive 2006/73/EC also authorises the investment firm to base its judgments on the information provided by the client, "unless it is aware or ought to be aware that the information is manifestly out of date, inaccurate or incomplete."

We therefore do not see any inconvenience for the bank to verify the information provided by its clients whenever it seems clearly erroneous in light of the information known to the ISP, especially with regard to anything that is easily accessible concerning the client's financial situation. In any event, it is up to clients to inform the ISP of any significant change in their personal and/or financial situation. As was noted in response to question 1, it is ultimately up to the ISP to ensure that the client has all the information needed to make an informed decision.

Finally, while this issue might be particularly important for retail clients, it would be quite inappropriate in the case of corporate clients. On this point especially, we consider it important to make it clear that this does not apply to corporate clients.

Q6: Do you agree that where an investment firm has an ongoing relationship with a client, it should establish appropriate procedures in order to maintain adequate, updated information about the said client? Please also state the reasons for your answer.

The MiFID requires ISPs to keep the available information on its clients up to date. Arrangements for the update process may differ, depending upon the type of client concerned (BFI, private banking, retail client) and the way in which the institution is

organised (centralised or cooperative or saving banks). ISPs thus need to maintain full discretion in establishing the appropriate procedures for their updates.

However, the French banking industry considers that the guidelines proposed by the ESMA, insofar as they require ISPs to ensure the suitability of the service over time (which refers to the notion of “ongoing advice”), to go beyond the requirements currently imposed by the MiFID and to anticipate reform of the Directive, which is far from being finalised. Under existing law, this constant checking by ISPs can only be required if it has been agreed with the client at the outset that this particular service is to be provided.

Q7: Do you agree that, with regard to client information for legal entities and groups, the investment firm and the client should agree on how the relevant client information is to be determined and that, at minimum, information should be collected on the financial situation and investment objectives of the beneficiary of the investment advice or portfolio management services (the ‘end client’)? Please also state the reasons for your answer.

It is imperative to clarify whether this issue applies only to retail markets and not to wholesale markets, as the problems encountered with the two types of client involved are not at all the same. Applying these requirements to the wholesale market would inevitably lead to many refusals to answer the questionnaire developed by the ISP.

Moreover, it must be remembered that, as regards legal entities, the assessment depends upon the existing relationship with the client. Frequently, only a single assessment is made involving the CFO, who then allows or disallows a delegation of authority for placing orders to another person in the company. This delegation engages the responsibility of the delegator. In other situations, if the client so desires, it may happen that two or more corporate officers are assessed. In any case, no schema should be imposed in this area, which is intimately related to the bank/client relationship and to the size of the legal entity (SA/EURL).

Finally, knowledge of the client can never extend to ‘end clients’ if the ISP does not know them. In particular, when the client is an investment fund, it is important to clarify that the ‘end client’ is the fund in question and not its holder(s).

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? Please also state the reasons for your answer.

We broadly agree with the guidelines advocated by the ESMA on this point, and in particular with the fact that “tools should be designed so that they take into account all of the relevant specificities of each client and financial instrument.”

On the other hand, we do not agree with the statement that “tools that classify clients or financial instruments broadly would not be fit for purpose.”⁵ Indeed, the assessment tools are necessarily designed to handle a mass of information that, to some extent, requires the classification of clients.

⁵ Point 45 of the consultation paper.

Moreover, the obligation that would be placed on the ISP to take into account in the suitability test all information regarding the client is inconsistent with point 31 of the consultation paper, according to which the level of detail required by the ISP can vary, depending upon the extent of the service provided to the client. The current provisions of the MiFID also provide that the ISP must obtain from its client any information **necessary for and relevant to** the specific type of product or service concerned.

Q9: Do you agree that investment firms should establish and maintain record-keeping arrangements that cover all relevant information regarding the suitability assessment? Please also state the reasons for your answer.

It is indicated that investment firms should retain the documents obtained as part of the suitability test "through all stages of the process." It seems to us disproportionate and unnecessary to require the archiving of all stages of the suitability test. In any event, a record of every stage of the interview would involve very significant costs for the institutions involved without this being necessary for the achievement of the given objective. Indeed, certain steps in the process (including rollbacks) can be explained by simple data-entry errors. In our opinion, recording should only be done at the end of the process (closure of the suitability test). **Only the final situation confirmed by the client needs to be retained.**

Furthermore, contrary to what is stated in point 48, it would not seem practical to store the adviser's interpretation of the information regarding the client, as the decision process is not fully computerised and involves a qualitative approach.

Finally, ISPs do not have the means to sort through the information collected via the process of assessing the suitability of the service provided so as to identify information that is "relevant" and should, as such, be preserved. As we have said, it is the final situation confirmed by the client that needs to be retained.