



**ESMA Consultation paper on
Guidelines on certain aspects of the
MiFID suitability requirements**

TEST-ACHATS contribution

About Test-Achats

Test-Achats /Test-Aankoop is an independent association dedicated to the promotion of the interests of consumers. We are entirely funded by our approximately 350,000 members, who are subscribers to our consumer information magazine. Test- Achats /Test-Aankoop is a member of the executive board of the European Consumers' Organisation (BEUC), and a member of Consumers' International (CI) and International Consumer Research and Testing (ICRT).

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General remarks:

1. Test-Achats welcomes the ESMA initiative to improve the quality of investment advice through a better compliance with the MiFID suitability requirements.
2. Test-Achats confirms the problems mentioned by ESMA in its background analysis¹. The quality of suitability tests is effectively quite variable among the Member states and among banks / investment firms.
3. Improving the regulation on suitability test, including the collection of client's information, is an important step to ensure a better quality of investment advice among all EU countries. But the guidelines to be published will have their full impact only if they are enforced by the local supervisors. Not all national competent authorities are controlling the investment firms's compliance with the MiFID conduct of business rules, even if article 17 of MiFID provides that it should be the case :
"1. Member States shall ensure that the competent authorities monitor the activities of investment firms so as to assess compliance with the operating conditions provided for in this Directive. ..."
ESMA should act to promote the compliance of all EU Member States with this provision.
4. The quality of investment advice is also impacted by other parameters than the quality of suitability test regulation or guidelines. Employee representatives tell us that sales targets and, where it applies, variable remunerations creates conflicts of interests that are detrimental to correct suitability test. Insufficient training and high productivity levels have also a high negative impact on the advice quality and should also be addressed.
5. The appropriateness test to be carried for other investment services than investment advice is not of a better quality than the suitability test addressed by the ESMA draft guidelines. For instance, experience with a structured product is sometimes interpreted as experience with derivatives; or highly complex and speculative products like CFDs are promoted and made accessible to retail investors without due assessment and warnings. Test-Achats asks ESMA to draft guidelines for MiFID appropriateness requirements.

¹ See Consultation paper; especially points 13 and 14 on page 7.

Information to clients about the suitability assessment

Q1: 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.

Too often suitability assessment is told to be just some red paper “from Brussels” or “from EU” to minimize its importance and the time given to it.

Test-Achats fully agree that an investment firms should take steps to ensure that the client understands the relationship between risks (volatility, liquidity, counterparty...) and return on investments, and should inform the client about how a risk profile is established.

Test-Achats agrees that the suitability test is the responsibility of the investment firm. Therefore, a special attention should be given to questionnaire published online to determine the clients’ profile. The client should not have the possibility to start and start again the questionnaire to reach the investor profile he wants in place of his true profile.

Arrangements necessary to understand clients and investments

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? Please also state the reasons for your answer.

Test-Achats considers that a consistent quality among all employees in contact with clients cannot be achieved if policies and procedures are not implemented into the investment firm. Both aspect of the suitability assessment, client’s needs and product’s characteristics should be addressed.

Qualifications of investment firm staff

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? Please also state the reasons for your answer.

The employee must be able to carry the suitability test and therefore he must have the needed skills to assess the needs and circumstances of the client, and be able to understand the financial instrument to be recommended. How could he proceed to the suitability test if those conditions are not met?

Even if the advice is electronically assisted, the employees that are in contact with client, by phone or face to face, must be able to explain the advice given and to answer the client’s questions.

Extent of information to be collected from clients (proportionality)

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? Please also state the reasons for your answer.

Test-Achats considers that the client's needs must be correctly assessed to allow the investment firm to give a suitable advice. At least all information necessary to understand the essential facts about the client as provided by Article 35.1 of the MiFID Implementation Directive (Commission Directive 2006/73/EC) should be collected.

Point 28 of the consultation paper mentions that *"When providing access to complex (as defined in MiFID) or risky financial instruments, firms should bear in mind the need to collect more in-depth information about the client in order to be able to assess the client's capacity to understand, and financially bear, the risks associated with such instruments."*

Due to the current MiFID dogma considering all UCITS as non-complex, referring to the definition of complex investment provided by MiFID is not satisfactory. Retail investors are not able to sufficiently understand all UCITS. Maybe will the MiFID review, when adopted, make this definition more conform to the reality but as long as it is not the case ESMA should avoid referring to it.

We are not sure of point 28 refers to the appropriateness test (*providing access to ...*) or to the suitability test related to financial advice. Test-Achats would certainly agree with point 28 if it is related to the appropriateness test.

Test-Achats agrees with the fact that when risky or complex products are not in range to answer to the client needs, detailed questions related to the client's capacity to understand and correctly react to risky investments is not needed.

Point 29 mentions that *"For example, for risky or illiquid financial instruments, the 'necessary information' to be gathered will include information on the length of time for which the client is prepared to hold the investment and ..."*.

The concept of risky or illiquid financial instrument is not very clear. Savings account protected by a deposit guarantee, preferably in a good rated country, can generally be considered as a liquid and non-risky investment or saving. Every other investment carries some risk like illiquidity risk, interest rate risk, counterparty risk, volatility risk...

Test-Achats considers that the first step in the financial advice process is having a sufficient picture of the situation and needs of the client before considering of risky or complex investments could be suitable. At least all information necessary to understand the essential facts about the client as provided by Article 35.1 of the MiFID Implementation Directive (Commission Directive 2006/73/EC) should be collected. Based on the first analysis of collected information, more detailed information should be needed if risky or illiquid financial instruments are in range to

answer the needs of the client. However, Test-Achats considers that the investment horizon, the length of time for which the client is prepared to hold the investment is a key element to understand the needs and objectives of the client and should always be asked by the investment firm.

Point 31 provides that *"the extent of the service requested by the client may also impact the level of detail collected about the client. For example, firms would need to collect more information about clients asking for investment advice covering their entire financial portfolio than for clients asking for specific advice on how to invest a given amount of money."*

Test-Achats can agree with the principle that the level of detail can be impacted by the extent of the service requested for so far that the information needed in accordance with Article 35.1 of the MiFID Implementation Directive are collected by the investment firm.

About the example of an advice related to a part of his portfolio, Test-Achats considers however that if there is a risk that the advice related to a part of the client's portfolio could be unsuitable when considering the complete client's situation. If the client discloses the existence of other assets without giving the key information necessary to assess the risks attached to those assets, the suitability of the advice to the client's situation can simply not be assessed. How to assess the risk repartition if only a part of the assets is taken in account? The advisor who provides advice based on only a part of the needed information would not comply with the duty to act honestly, fairly and professionally in accordance with the best interests of its clients (Article 19.1 of MiFID) and he could be responsible in case of damages due to a unsuitable advice.

ESMA should also take in account the fact that a broad application of the proposed guideline could allow advisors to give partial advice in order to be able to recommend investment products they have interest to promote. This should be prevented. As long as all discussions leading to investment advice are not recorded, clients will not be able to prove that they did not take the initiative to restrict their demand to a part only of their portfolio.

An exception could be foreseen for sophisticated investors who have the knowledge and experience to understand the risks taken and to take the appropriate decisions when needed. But MiFID does not permit such an exception for retail investors.

Reliability of client information

Q5: 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.

Test-Achats fully agrees with the proposed guideline. The reliance of the answer given by the client is strongly influenced by the way the questions are asked. Questions may induce answers and self-assessment is quite sensitive to the

behavior bias (like overestimating his own knowledge and experience or overestimating chances to make profit and underestimating risks or costs...). Therefore the investment firm should draft the questions in a way that self-assessments are minimized and validated by objective criteria.

Updating client 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? Please also state the reasons for your answer.

We hear sometimes that it is the client's responsibility to warn his advisor when something relevant has changed regarding his investor profile. Test-Achats considers that the client is not always in the position to evaluate the impact of events on his investor profile; the advisor is the professional who should regularly make the client aware of the need to update his profile. Test-Achats agrees that the investment firm should establish appropriate procedures to maintain adequate and update information about its clients.

Client information for legal entities or groups

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')? Please also state the reasons for your answer.

Test-Achats considers that the suitability of the advice to the needs (financial situation and objectives) of the real owners of the assets must be assessed. After control of the validity of the mandate (in a married couple, one partner could also give an express mandate to his/her partner for common assets), the advisor may take the knowledge and experience of the representative in account.

Arrangements necessary to ensure the suitability of an investment

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.

Test-Achats agrees with the guideline proposed by ESMA. Too often on one hand the client's investor profile is a medium one and on the other hand the categorization of financial instrument is as broad as possible. The result is that a maximum of products can be recommended to a maximum of clients. Too often a same product is personally recommended to all clients belonging to the same

investor category without any other assessment of the advice suitability. The investor profile is in that case more a license to sell than a guarantee of quality of investment advice. Those wrong approaches of the suitability test must be improved.

Record-keeping

Q9: 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.

To better protect consumers, there is a need of recording communications and increase the shelf life of records. Test-Achats supports recording when the contact with the consumer leads or could lead to giving personal recommendations (financial advice) or collecting orders. We understand that Article 13.6 of MiFID provides that it should be the case.

Test-Achats considers that the record should be accessible to the client in case of dispute and that the conservation period should be equal to the investment period plus one year.

This can be justified by the following reasons:

- Recording helps to prevent conflicts between retail clients and investment firms. When conflicts are not prevented, recording helps to solve them in the respect of the rights of all parties. It happens too often that consumers trapped in a conflict with a bank are unable to lift the burden of evidence about the information or the advice that was given before the investment decision. Nowadays, when conversations are recorded by a firm, records are only used by the firm if it is in its own interest.
- This is the only way to avoid abuses of financial advice given by telephone and followed by a recommendation to give the transaction order through the execution only platform of the firm.
- Recording is also a good means to detect insider trading when information is given by telephone without collecting the order at the same moment.
- The records and documents should be stored at least as long as the consumer cannot face the real consequences of the investment he has been advised on. A period of three years is definitely too short. Investments are generally made for a longer period than 3 years and the return of some products, like structured products, remains uncertain until the very end of the investment. In Denmark and Belgium, where BEUC members are represented in alternative dispute resolution bodies in charge of financial services, it has been observed that consumers who file a complaint about their litigious investments have generally been advised more than three years before realising that financial advice they received was wrong.

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