

# MiFID II Supervisory briefing

**Appropriateness and execution-only**





European Securities and  
Markets Authority

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# 1 Introduction

## 1.1 Overview

1. ESMA is required to play an active role in building a common supervisory culture by promoting common supervisory approaches and practices.
2. On 19 December 2012, ESMA published a supervisory briefing in relation to appropriateness rules to provide guidance to NCAs in relation to the MiFID I appropriateness rules. This updated version of ESMA's supervisory briefing on appropriateness and execution-only takes into account the new version of ESMA's guidelines on suitability published on 28 May 2018 with respect to aspects also relevant to the appropriateness rules. ESMA's 2012 supervisory briefing in relation to appropriateness and execution-only will consequently be retired as of the date of entry into application of this new supervisory briefing.
3. This supervisory briefing has been designed for supervisors as an accessible introduction to Directive 2014/65/EU<sup>1</sup> (MiFID II) appropriateness rules, and as a useful starting point when deciding on areas of supervisory focus. It summarises the key elements of the rules and also includes indicative questions that supervisors could ask themselves, or a firm, when assessing firms' approaches to the application of the MiFID II rules.
4. The content of this briefing is not exhaustive, does not constitute new policy, and does not promote any particular way of supervising the rules. It has been designed to be used in the way that best fits with supervisors' methodologies (whether distributing the briefings internally, or passing them to external bodies, such as auditors, for example).

## 1.2 Scope

5. This supervisory briefing is aimed at competent authorities (as defined in MiFID II). It is also meant to give market participants indications of compliant implementation of the MiFID II appropriateness provisions.

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<sup>1</sup> Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU.

6. It applies in relation to the application of the following MiFID II provisions:

- Article 25(3) and (4) of MiFID II.
- Articles 55, 56 and 57 of the MiFID II Delegated Regulation<sup>2</sup>.

### 1.3 Status of this document

7. The supervisory briefing is issued under Article 29(2) of the ESMA Regulation which enables ESMA to develop new practical instruments and convergence tools such as supervisory briefings. The purpose of these tools is to promote common supervisory approaches and practices. The content of this supervisory briefing is not subject to any 'comply or explain' mechanism for NCAs and is non-binding.<sup>3</sup>

### 1.4 Purpose

8. The MiFID II appropriateness requirements are set out in Article 25(3) of MiFID II and in Articles 55 and 56 of the MiFID II Delegated Regulation. Article 25(4) of MiFID II and Article 57 of the MiFID II Delegated Regulation cover the 'execution-only' element of the appropriateness regime. The aim of the requirements is to increase investor protection in respect of 'non-advised' services.
9. The way in which the requirements apply depends on the type of service in question, the type of investment product<sup>4</sup> involved (in particular, whether the investment product is 'complex' or 'non-complex'), and the type of client.
10. They apply to firms<sup>5</sup> which provide MiFID investment services other than investment advice and portfolio management (in those cases, the obligation is to assess suitability). Therefore, they apply to firms when providing 'non-advised' services, i.e. investment services other than portfolio management and investment advice.
11. Where the appropriateness test applies, it requires a firm to seek information from a client or potential client about his knowledge and experience (i.e. ability to understand the risks about a specific type of investment product or service). This is to enable the firm to determine whether that investment product or service is appropriate for the client (unlike

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<sup>2</sup> Commission Delegated Regulation (EU) 2017/565 of 25 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive.

<sup>3</sup> Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC.

<sup>4</sup> 'investment product' means a financial instrument (within the meaning of Article 4(1)(15) of MiFID II) or a structured deposit (within the meaning of Article 4(1)(43) of MiFID II).

<sup>5</sup> 'firms' means firms subject to the requirements set out in Articles 25(3) and (4) of MiFID II and include investment firms (as defined in Article 4(1)(1) of MiFID II), credit institutions when providing investment services and activities (within the meaning of Article 4(1)(2) of MiFID II), investment firms and credit institutions (when selling structured deposits), external Alternative Investment Fund Managers (AIFMs) (as defined in Article 5(1)(a) of the AIFMD) when providing the investment service of reception and transmission of orders (within the meaning of Article 6(4)(b) of the AIFMD).

the requirements for suitability, there are no specific requirements to assess the client's financial situation or investment objectives).

12. The MiFID II appropriateness rules give firms a certain degree of flexibility regarding the information to obtain about the client's knowledge and experience: the information to be collected should be the information necessary with regard to the nature of the client, the nature and extent of the service to be provided and the type of investment product or transaction envisaged, including their complexity and the risks involved (proportionality principle). In most circumstances, supervisors will have to assess the adequacy of a firm's arrangements on a case-by-case basis, having regard to the proportionality principle and a firm's operational framework.
13. This supervisory briefing is designed to help supervisors make the above-mentioned judgements, and is structured around the following elements:
  - determining situations where the appropriateness assessment is required;
  - obtaining information from clients;
  - assessment of appropriateness;
  - warnings to clients;
  - qualification of firm's staff; and
  - record-keeping.
14. Each element refers to the relevant legislation as well as provides examples of the sort of questions that supervisors could ask to test whether the outcomes of the appropriateness rules are being met by firms.

## 2 Supervisory briefing

### 2.1 Determining situations where the appropriateness assessment is required

15. In accordance with Article 25(3) of MiFID II, when providing MiFID investment services other than investment advice or discretionary portfolio management services, firms must ask the client or potential client to provide information regarding that person's knowledge and experience in the investment field relevant to the specific type of investment product or service offered or demanded to assess whether the investment service or product envisaged is appropriate for the client in question.
16. However, Article 25(4) of MiFID II (together with Article 57 of the MiFID II Delegated Regulation) provides for an optional exemption from the appropriateness test for certain types of 'execution-only' business, where a number of conditions are met. To assess whether such conditions are met, firms are likely to need processes (i) to distinguish between "complex" and "non-complex" investment products; (ii) to identify whether contact with the firm is at the initiative of the client; and (iii) to ensure that necessary warnings have been provided.
17. Relevant legislation: Article 25(3) and (4) of MiFID II and Article 57 of the MiFID II Delegated Regulation.
18. Other: ESMA Guidelines on complex debt instruments and structured deposits dated 4 February 2016<sup>6</sup> and Q&A1 in relation to appropriateness/complex financial instruments.
19. Questions

#### *General*

- How do the firm's arrangements and procedures guide, track and record the interaction between staff and clients, having regard to the distinction between 'advised' and 'non-advised' services?
  - What measures has the firm adopted to decide whether the services offered by its employees and agents are advised or not? What controls has the firm put in place to ensure that the distinction it has set up between 'advised' and 'non-advised' services is complied with?
  - How does the firm communicate this distinction clearly to its staff and other agents? How does it monitor this?

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<sup>6</sup> ESMA/2015/187. The document CESR/09-559 on MiFID complex and non-complex financial instruments for the purposes of the Directive's appropriateness requirements is also relevant.

- How does the firm ensure that it is clear towards the client about the type of services to be provided, in particular whether these are advised or not and the corresponding level of protection?
- What kind of safeguards are in place in order to avoid any advised service being provided inadvertently without a suitability assessment being performed?
- What kind of safeguards are in place in order to ensure that the use of an electronic system does not hinder the firm's capacity to detect where an appropriateness assessment should be carried out?

#### *Execution-only*

For the avoidance of doubt, the below questions would only be relevant where a firm intends to use the 'execution-only' exemption (under Article 25(4) of MiFID II).

- Where an appropriateness assessment is not envisaged, what kind of internal systems and controls are in place in order to ensure that the services given can only amount to "execution-only" business?
- How do the firm's arrangements and procedures guide, track and record the interaction between staff and clients, having regard to the distinction between business falling within the 'execution-only' exemption and other non-advised transactions?
- What policies and processes has the firm set up to identify which of its investment products may be regarded as "complex" for the purposes of the appropriateness requirements? Are such policies and processes regularly updated or reviewed?
- Is the firm maintaining a list of automatically non-complex investment products and all others will be categorised as complex unless they have been assessed against and have met all the criteria in Article 57 of the MiFID II Delegated Regulation?
- If the firm maintains a list of automatically non-complex investment products, how is the firm constructing its list of automatically non-complex investment products:
  - in relation to investment products referred to in the first indent of Article 25(4) of MiFID II<sup>7</sup>? For instance, how is the firm assessing which shares embed a derivative (what are the criteria used)?

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<sup>7</sup> Shares admitted to trading on a regulated market or on an equivalent third-country market or on a MTF, where those are shares in companies, and excluding shares in non-UCITS collective investment undertakings and shares that embed a derivative.



- in relation to investment products referred to in the second<sup>8</sup>, third<sup>9</sup> and fifth<sup>10</sup> indents of Article 25(4) of MiFID II? For instance, how is the firm assessing i) which debt instruments embed a derivative or incorporate a structure making it difficult for the client to understand the risk or ii) which structured deposits incorporate a structure which makes it difficult for the client to understand the risk of return or the cost of exiting the investment product before term? Is the firm taking into account ESMA's Guidelines on complex debt instruments and structured deposits dated 4 February 2016?<sup>11</sup>
- in relation to investment products referred to in the fourth<sup>12</sup> indent of Article 25(4) of MiFID II? For instance, how is the firm assessing which UCITS shall be understood as UCITS which provide investors, at certain predetermined dates, with algorithm-based payoffs that are linked to the performance, or to the realisation of price changes or other conditions, of financial assets, indices or reference portfolios or UCITS with similar features (structured UCITS)?.
- If the firm maintains a list of automatically non-complex investment products, is it updated and at which frequency?
- Are the firm's policies and processes clear that the investment products expressly excluded from the list of automatically non-complex instruments of Article 25(4)(a) of MiFID II<sup>13</sup> should not be nonetheless assessed against the criteria set out in Article 57 of the MiFID II Delegated Regulation to potentially be categorised as non-complex investment products for the purposes of the appropriateness test?
- What policies and processes has the firm set up to identify which of its investment products may be deemed non-complex in accordance with Article 57 of the MiFID II Delegated Regulation?
  - To do so, is the firm maintaining a list of investment products falling within Article 57 of the MiFID II Delegated Regulation?
  - If the firm maintains a list of investment products falling within Article 57 of the MiFID II Delegated Regulation, is such list updated and at which frequency?

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<sup>8</sup> Bonds or other forms of securitised debt admitted to trading on a regulated market or on an equivalent third country market or on a MTF, excluding those that embed a derivative or incorporate a structure which makes it difficult for the client to understand the risk involved.

<sup>9</sup> Money-market instruments, excluding those that embed a derivative or incorporate a structure which makes it difficult to understand the risk involved.

<sup>10</sup> Structured deposits, excluding those that incorporate a structure which makes it difficult for the client to understand the risk of return or the cost of exiting the product before term.

<sup>11</sup> ESMA/2015/1787.

<sup>12</sup> Shares or units in UCITS, excluding structured UCITS as referred to in the second subparagraph of Article 36(1) of Regulation (EU) No 583/2010.

<sup>13</sup> For instance, shares in non-UCITS collective investment undertakings, shares embedding a derivative, structured deposits incorporating a structure which makes it difficult for the client to understand the risk of return or the cost of exiting the investment product before term.

- What policies and processes has the firm set up to identify whether the service is being provided at the initiative of the client?
  - Is the firm able to trace whether a client's demand is made in response to a "solicitation" by the firm? What types of general solicitations, advertisements or other form of general communications initiated by the firm (or a third party on its behalf) towards the public or a group/category of clients is the firm considering as not disqualifying for the purposes of the execution-only exemption?

## 2.2 Obtaining information from clients

- 20. In accordance with Article 25(3) of MiFID II and Article 56 of the MiFID II Delegated Regulation, firms shall determine whether a client has the necessary experience and knowledge to understand the risks involved in relation to the investment product or service offered or demanded when assessing whether an investment service (other than investment advice or portfolio management) is appropriate for a client.
- 21. Relevant legislation: Articles 25(3) of MiFID II, Articles 55 and 56 of the MiFID II Delegated Regulation.
- 22. Other: ESMA Guidelines on certain aspects of the MiFID II suitability requirements dated 28 May 2018 (in relation to the knowledge and experience aspects).
- 23. Questions

### *General*

- Are the questions asked by the firm to determine a client's knowledge and experience covering all factors set out in Article 55(1) of the MiFID II Delegated Regulation?
- How is the firm articulating the relationship between knowledge and experience? For instance, could a lack of experience be compensated by sufficient knowledge when the firm assesses whether the investment service or product being offered or demanded is appropriate for the client?
- Is the firm requiring that its client meet certain thresholds in relation to certain or all factors set out in Article 55(1) of the MiFID II Delegated Regulation? Are such thresholds tailored to the types of investment services and investment products offered or demanded?
  - If the firm has set up thresholds as described above, are these thresholds considered as minimum requirements that a client needs to meet or as guidance for the firm's staff and other agents when assessing a client's knowledge and experience?

- When collecting information from a client, does the firm make it clear that a lack of answer to certain questions or to a certain number of questions, or that the provision of insufficient information, prevents the firm from assessing the client's knowledge and experience and, consequently, from carrying out the appropriateness test? How?
- How is the firm assessing the types of services, transactions and investment products with which the client is familiar?
  - For instance, is the firm asking questions about the client's past transactions, level of education (in the relevant field) and profession or former profession?
- When collecting information about a client's level of education and profession or former profession:
  - which education fields/professions are considered relevant by the firm?
  - Is the level of education or professional experience considered appropriate by the firm tailored to the complexity of the investment product offered or demanded?
  - Is the information requested by the firm about educational qualifications and professional experience sufficiently granular?
- If the firm uses questionnaires (also in a digital format) to collect information about the client's knowledge and experience, are they designed in a clear, exhaustive and comprehensible way (using layman's terms, where possible and appropriate) avoiding misleading, confusing, imprecise and excessively technical language?
- If the firm uses questionnaires (also in a digital format) to collect information about the client's knowledge and experience, are they designed to gather the necessary information and in an accurate manner?
  - For instance, is the questionnaire presented as a battery of questions (collecting information on a series of items through a single question)?
  - Are the questions asked sufficiently detailed to collect the necessary information about the client's knowledge and experience?
  - Is the level of details of the questions tailored to the complexity of the relevant services, transactions or investment products? Do they get more specific and complex where the investment products offered or demanded get more complex as well?
  - How leading are the questions? Could answers be directly deductible from information available from the firm's website?

- is some customer service/client support (such as remote interaction via emails or mobile phones) available to the client when responding to the questionnaire (if in a digital format) in case the client needs clarity or is seeking further information?

### *Proportionality*

- How does the firm assess the extent of the “necessary” information that should be collected with respect to clients’ knowledge and experience?
  - Is the firm using different questionnaire versions (depending on the features of the service provided, the type and characteristics of the investment products to be considered, the channel through which the service is provided, the characteristics of the client, etc.)? What are the main differences between the different versions? Do they all enable the firm to gather the necessary information?
  - In order to assess the appropriateness of complex investment products, how does the firm ensure that the information collected about the client’s knowledge and experience is sufficiently detailed and granular, including the specific investment product to be traded and the relevant underlying class (as the case may be)?
  - For investment products with an underlying, is the firm asking specific questions to identify the relevant experience and knowledge of the client in relation to the investment product itself but also the relevant underlying asset and market? Where the investment product is sufficiently diversified (e.g., a well-diversified fund), is the firm asking specific questions about the relevant underlyings’ types and markets?
- What policies and guidance has the firm formulated for its employees and agents about the level of information that it regards as acceptable in determining appropriateness (without which a warning that the firm is not in a position to determine whether the investment product or service envisaged is appropriate for the client would be issued)?

### *Reliability*

- Are clients asked to make any degree of ‘self-assessment’ in respect of their knowledge and experience? Is the self-assessment counterbalanced by objective criteria?
  - Are the tools used by the firm to collect the necessary client information designed to allow the firm to check any self-assessment by the client against objective criteria (e.g. open-ended questions related to the client’s understanding of risk-return trade off and diversification or the client’s knowledge and experience)? How?

- For instance, if a client declares that it is familiar with certain types of services, transactions and investment products but does not provide any other information such as his or her past transactions, level of education or profession, would the firm rely solely on the client's declarations to carry out the appropriateness assessment, even for complex and risky products? Or would the firm declare that it is not in a position to determine whether the investment product or service envisaged is appropriate for the client (and therefore issue the relevant warning to the client)?
- What steps have been taken by the firm to address inconsistencies in the client's responses? Does the questionnaire itself contain some design features to alert clients when their responses appear inconsistent? Or does the firm carry out an ex-post review of the client's responses? If inconsistencies are identified, how does the firm resolve them? Does the firm make use of automatic inconsistency checks when working with online questionnaires?
- What arrangements and procedures has the firm set up to address the risk that clients may tend to overestimate their knowledge and experience?
- Is the firm allowing its clients or prospective clients to answer the questionnaire several times in a row (even without any training) if the firm considered, on the basis of the client's initial answers, that such client did not have the required knowledge and experience? If so, does the firm make use of an alternative questionnaire? If not, for how long is such client not allowed to answer the questionnaire again?

#### *Updating client information*

- What are the arrangements used to keep the information about the client's knowledge and experience updated? Do these appear appropriate?
- Under what circumstances might the firm amend the information collected about the client's knowledge and experience? Has the risk of unjustified updates been considered (for example, to avoid the situation where the firm may have an interest in selling some investment products which do not match the client's characteristics); and how is it managed?

## **2.3 Assessment of appropriateness**

24. In accordance with Article 56(1) of the MiFID II Delegated Regulation, firms shall determine whether a client has the necessary experience and knowledge to understand the risks in relation to the investment product or service offered or demanded when assessing whether an investment service (other than investment advice or portfolio management) is appropriate for a client.
25. Relevant legislation: Article 25(3) of MiFID II and Article 56(1) of the MIFID II Delegated Regulation.

26. Other: ESMA Guidelines on certain aspects of the MiFID II suitability requirements dated 28 May 2018 (in relation to the knowledge and experience aspects).

27. Questions

- Has the firm adopted robust and objective procedures for the assessment of the investment products offered under the appropriateness regime? Are these procedures subject to periodic review?
  - Does the firm categorise investment products according to their complexity when carrying out the appropriateness assessment? Does this categorisation appear reasonable?
  - Is the information used as a basis for the investment products' assessment reliable, accurate, consistent as well as regularly reviewed and updated, where necessary?
- How do the firm's arrangements and procedures ensure that the appropriateness of a transaction is assessed against the client's knowledge and experience?
  - By which means is the appropriateness test carried out (online, face-to-face, over the telephone)?
  - If the firm uses algorithm(s) underpinning the appropriateness test, does it regularly monitor and test this/these algorithm(s) to ensure they are neutral and objective?
- Is the firm attributing any weight to the information collected about the client's knowledge and experience and the answers provided by the client? If so, how is the weighting attributed?
- At what stage in the sales process is the appropriateness test carried out?
- Has the firm defined a clear policy on how the assessment should be conducted in relation to groups of two or more clients?
- How are relevant facts regarding knowledge and experience (ability to understand the relevant investment product and in particular the risk to be taken) assessed and used to determine appropriateness?
- What degree of discretion is given to relevant staff when assessing appropriateness? Is this degree of discretion reasonable?
- What are the firm's procedures and arrangements to ensure that any automated tools used in the conduct of the appropriateness assessment (even if the interaction with the client does not occur through automated systems) do not hinder the consistency and reliability of such appropriateness assessment?

## 2.4 Warnings to clients

28. In accordance with Article 25(3) of MiFID II, a firm shall warn its client or potential client where it considers, on the basis of the information received in relation to the client's knowledge and experience, that the investment product or service is not appropriate to the client or potential client. In addition, when clients or potential clients did not provide the requested information about their knowledge and experience, or when they provided insufficient information, the firm shall warn them that it is not in a position to determine whether the investment product or service envisaged is appropriate for them.
29. In addition, under Article 25(4) of MiFID II, when a firm chooses not to test appropriateness for all non-advised transactions and to use the "execution-only" exemption, it shall ensure that the client or potential client has been clearly informed that, in the provision of the corresponding service(s), the firm is not required to assess the appropriateness of the investment product(s) or service(s) provided or offered and that, therefore, he does not benefit from the corresponding protection of the relevant conduct of business rules.
30. Relevant legislation: Articles 24(1), 25(3) and (4) of MiFID II and Article 56(2) of the MiFID II Delegated Regulation.
31. Questions

### *General*

- What systems are in place to ensure that warnings are given where required?
- What warnings does the firm have in place:
  - to warn the client that insufficient information has been provided so the firm is unable to judge appropriateness;
  - to warn the client that the investment product/service is inappropriate;
  - to warn the client that in the provision of the execution-only service the firm is not required to assess the appropriateness of the instrument or service provided or offered and that therefore the client does not benefit from the corresponding protection of the relevant conduct of business rules?
- Are these warnings clear? By which means are these warnings provided to clients (such as face-to-face meeting, by telephone, email, pop up boxes)? Is clients' attention sufficiently drawn to them?
- In cases where the assessment of appropriateness indicates that the investment product or service is not appropriate or where insufficient information is available to assess appropriateness, what are the measures adopted by the firm to ensure that the warning is effective and to avoid presenting the appropriateness



assessment as a box ticking exercise (i.e. meant by the firm as a mere administrative burden that both firm and client can get over hastily and in a superficial manner)

- For instance, in cases where the appropriateness assessment indicates that a complex and risky investment product is not appropriate for a client, is the warning delivered by the firm overly generic and/or vague?
  - To the contrary, is the firm delivering overly long warnings that obscure the key message that the client has failed to demonstrate the necessary knowledge and experience for the investment product or service?
  - Is the firm using different warnings depending upon the level of complexity and riskiness of the investment products?
  - For instance, for speculative products such as CFDs, is the firm including a mandatory “cooling-off” period after the provision of a warning (to demonstrate that the client has considered the information presented in the warning before deciding whether to proceed)? How long is any “cooling-off” period?
  - Is the firm, for speculative products such as CFDs, requiring the client to sign and return a form or to respond to a separate email such that the client does not have the option to proceed immediately? Do such form or email include the relevant warning that the client must separately acknowledge its receipt and content?
  - Is the firm including in its warnings language specifically designed to encourage the client to agree to a disclaimer and proceed with the transaction?
  - Are the warnings delivered by the firm presenting the confirmation by the client that he/she has the intention to proceed as the first logical next step?
  - By which other means is the firm making sure that the warnings delivered are effective?
- Does the firm maintain records of data showing the ratio of instances where clients decide to proceed with a transaction despite receiving a warning from the firm that such transaction may not be appropriate (compared to the number of instances where such warnings were issued)? Is the firm using such data (if available) to assess whether such warnings are effective? Is such assessment made regularly?
  - Does the firm maintain records of data showing the ratio of instances where clients decide to proceed with a transaction despite receiving a warning from the firm that insufficient information is available to assess appropriateness (compared to the number of instances where such warnings were issued)? Is the firm using such



data (if available) to assess whether such warnings are effective? Is such assessment made regularly?

*Relationship with the firm's obligation to act in the best interest of its clients*

- Where the appropriateness assessment indicates that an investment product or service is not appropriate for a client, and such client has been warned accordingly but nonetheless wishes to proceed, does the firm have in place policies and procedures to deal with this situation and, as the case may be, decide whether it allows the client to proceed with the transaction?
  - For instance, if the firm is in possession of information that indicates potential vulnerability (due to age and/or financial situation) of a retail client who is willing to invest in a speculative investment product (such as, for instance, a CFD), is it considering the client's best interest before deciding to allow the client to proceed? On this basis, has the firm previously refused to let a client proceed? Is the firm able to show records of past instances where it refused to let a client proceed?
  - In cases where a client wishes to proceed with a transaction notwithstanding the warning issued by the firm and the latter allows the client to do so, is the firm nonetheless considering whether the investment product or service to be offered to the client should be adapted (e.g., limiting the level of leverage available to a client, limiting the sum that a client can invest in any one transaction and/or for a period of time)? Is the firm able to show records of past instances as described in the foregoing?
  - Do the firm's policies in this respect take into account cases where there is a heightened risk of conflicts of interest because the firm is selling its own investment products (or investment products issued by entities of the same group) or actively marketing investment products from within the firm's range?
- Does the firm maintain records of data showing the ratio of instances where clients asked to proceed with a transaction despite receiving a warning from the firm (that such transaction may not be appropriate or that insufficient information is available to assess appropriateness) and the firm accepted the client's request (to proceed)? If available, how is the firm using such data?

## **2.5 Qualifications of firm's staff**

- 32. In accordance with Article 21(1)(d) of the MiFID II Delegated Regulation, firms are required to employ personnel with the skills, knowledge and expertise necessary for the discharge of the responsibilities allocated to them.
- 33. Relevant legislation: Articles 16(2) and 25(1) of MiFID II and Article 21(1)(d) of MiFID II Delegated Regulation.

34. Questions:

- How has the firm ensured that its staff and other agents are clear about the services it is offering and whether these are advised or not?
  - In the case of customer-facing staff providing 'non-advised' services, how are they trained on the risk of inadvertently i) giving a personal recommendation on a given investment product or ii) giving the client the impression (or let the client think) that a personal recommendation was given?
- How are relevant staff trained on the appropriateness assessment? How does the firm ensure that all staff involved in material aspects of the appropriateness process have an adequate level of skills, knowledge and expertise?
  - How are relevant staff trained on the way to obtain relevant information from the client?
  - How are relevant staff trained on the importance of the collection of information from the client for the appropriateness assessment?
  - Do relevant staff understand the conditions where an appropriateness assessment is not required (execution-only)?
  - Do relevant staff understand the role they play in the appropriateness assessment process and do they possess the skills, knowledge and expertise necessary, including sufficient knowledge of the relevant regulatory requirements and procedures, to discharge their responsibilities?
  - Is the firm training its staff involved in the appropriateness assessment on the relationship between the appropriateness assessment and the firm's obligation to act in the best interests of its clients (where clients asked to proceed with a transaction despite receiving a warning from the firm (that such transaction may not be appropriate or that insufficient information is available to assess appropriateness))?
  - With respect to staff that does not directly face clients but is involved in the appropriateness assessment in other ways (such as setting up the questionnaires, defining algorithms governing the assessment of appropriateness, working on the automated tools used in the appropriateness assessment...), how is the firm ensuring that they have the necessary skills, knowledge and expertise?
- What are the firm's procedures and arrangements to review its staff training and to ensure that staff involved in material aspects of the appropriateness process have an adequate level of skills, knowledge and expertise to fulfil their obligations in accordance with the relevant appropriateness requirements applicable to the firm?

## 2.6 Record-keeping

35. In accordance with Article 16(6) of MiFID II, firms shall arrange for records to be kept of all services, activities and transactions undertaken by it which shall be sufficient to enable the competent authority to fulfil its supervisory tasks and to perform the enforcement actions under MiFID II, MIFIR<sup>14</sup>, Directive 2014/57/EU<sup>15</sup> and Regulation (EU) No 596/2014<sup>16</sup>, and in particular to ascertain that the firm has complied with all obligations including those with respect to clients or potential clients and to the integrity of the market. In addition, Article 56 of the MiFID II Delegated Regulation provides for a number of record-keeping obligations which are specific to the assessment of appropriateness.
36. Relevant legislation: Articles 16(2) and (6) and 25(5) of MiFID II, Articles 56, 72, 73, 74 and 75 of the MiFID II Delegated Regulation.
37. Questions
- Has the firm established adequate record keeping arrangements in relation to all material aspects of the appropriateness assessment process, irrespective of the distribution channel used, including at least:
    - the result of the appropriateness assessment;
    - any warning given to the client where the investment service or product was assessed as potentially inappropriate for the client, whether the client asked to proceed with the transaction despite the warning and, where applicable, whether the firm accepted the client's request to proceed with the transaction; and
    - any warning given to the client where insufficient information is available to assess appropriateness, whether the client asked to proceed with the transaction despite this warning and, where applicable, whether the firm accepted the client's request to proceed with the transaction?
  - Has the firm established adequate record keeping arrangements in relation to all other material aspects of the appropriateness assessment process, irrespective of the distribution channel used, such as:
    - the collection of information from the client (including how that information is used and interpreted to define the client's knowledge and experience); and

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<sup>14</sup> Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) NO 648/2012.

<sup>15</sup> Directive 2014/57/EU of the European Parliament and of the Council of 16 April 2014 on criminal sanctions for market abuse (market abuse directive).

<sup>16</sup> Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse (market abuse regulation) and repealing Directive 2003/6/EC of the European Parliament and of the Council and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC.

- on which basis an appropriateness assessment was not carried out.
- How is the firm tailoring its record-keeping arrangements to the means by which the appropriateness assessment is carried out? For instance, how is the firm accurately recording all material elements of appropriateness assessments carried out during face-to-face meeting?
- Is the firm keeping records of any changes made to the client's knowledge and experience profile and types of investment products that fit that profile (including the reasons for such changes)?
- Are the record-keeping arrangements established by the firm designed to enable the detection of failures regarding the appropriateness assessment? Please explain how.
- Are the records kept by the firm with respect to the appropriateness assessment accessible for the relevant persons in the firm (such as the compliance and audit functions, the persons involved in the appropriateness process...)? And competent authorities?
- Does the firm have adequate processes designed to mitigate any shortcomings or limitations of its record-keeping arrangements?