



MiFID Supervisory Briefing

Information and reporting to clients

CESR is an independent Committee of European Securities Regulators. The role of the Committee is to:

- improve co-ordination among securities regulators;
- act as an advisory group to assist the European Commission, in particular in its preparation of draft implementing measures in the field of securities; and
- work to ensure more consistent and timely day-to-day implementation of community legislation in the Member States.

Promoting supervisory convergence

In the run-up to the implementation deadline for the Markets in Financial Instruments Directive (MiFID) on 1 November 2007, CESR devoted a lot of energy to developing recommendations and guidelines to help regulators take a consistent view of MiFID. With MiFID now in force, CESR's focus has shifted to matters of co-ordination and convergence of supervisory outcomes.

As part of its work to promote supervisory convergence, CESR has produced a series of supervisory briefings on the key elements of MiFID. They have been designed for supervisors, summarising the key elements of the rules and explaining the associated objectives and outcomes. The content of these briefings is not exhaustive and does not constitute new CESR policy.

The briefings also include indicative questions that supervisors can use to assess a firm's compliance with the rules. These questions are not intended to be exhaustive or to cover every possible situation, merely a useful starting point in deciding on areas of supervisory focus.

The briefings do not promote any particular supervisory approach and are designed to be used in the way that best fits with a supervisor's own methodology.

CESR believes that promoting convergence of supervisory outcomes can help promote market integrity and market confidence, whilst also minimizing the potential for client detriment and reputational risk, and has designed these briefings to support these goals.

Information and reporting to clients

Information provided to clients plays a crucial role in enabling them to make informed decisions. Accordingly, information provided to clients should take into account their status and their level of knowledge.

The Directives 2004/39/EC (hereinafter "L1 Directive") and 2006/73/EC (hereinafter "L2 Directive") specify the conditions and minimum content of the information to be provided to the client as well as the medium through which it must be provided. All information provided should be 'fair, clear and not misleading' – both in its content and its presentation.

When assessing if a firm is complying with the MiFID information requirements, a supervisor will want to check that the firm's procedures fulfill these requirements and that all the required information is provided via an appropriate medium. Supervisors should also assess whether the information provided is sufficient for the client to make an informed decision in respect of the service being offered. This is especially relevant to retail clients.

This supervisory briefing is designed to help supervisors make these assessments. The document is structured around three headings: (1) setting up arrangements and procedures necessary to be

compliant; (2) types of information to be provided to the client; (3) medium via which the information is provided.

Each heading includes an overview of the desired outcomes, illustrates the issues that supervisors should consider and provides examples of the sort of questions that supervisors could ask to test whether the outcomes are being met by firms.

This briefing focuses on the MiFID information requirements that apply to firms, with the exception of the information requirements regarding best execution, conflicts of interest, inducements as well as suitability, appropriateness and execution-only, which are already covered (or will be covered) in the supervisory briefings concerning those specific topics¹.

1. Setting up arrangements and procedures necessary to be compliant

Article 13 of the L1 Directive establishes the organizational requirements that firms have to comply with to fulfill their obligations. In particular there is an obligation for firms to provide information to their clients and potential clients on an ongoing basis. Those organizational requirements are set out in chapter II, section 1 of the L2 Directive.

In meeting these requirements firms should establish procedures that are appropriate and proportionate to the nature, scale and complexity of their business.

Firms should monitor their procedures to ensure their adequacy and effectiveness.

Key core questions

- What procedures does the firm have to ensure that the information it provides to clients or potential clients fulfills the MiFID requirements regarding content and timing?
- How does the firm ensure that those procedures and arrangements are proportionate and appropriate?
- What measures has the firm put in place to ensure that it will still be able to meet these requirements in the event of an interruption to its systems?
- Does the firm outsource any of the activities related to the provision of information to clients? If yes, how does the firm ensure that the relevant information is being provided?
- What arrangements and procedures has the firm adopted regarding the production of information (e.g. marketing communications)? Do those arrangements and procedures include, for example, sending the information to the supervisor or any independent party to get a pre-approval?
- What are the firm's record keeping procedures and how do they enable a competent authority to monitor the firm's compliance with its information to clients requirements?

Detailed questions

- How do the firm's representatives become and remain aware of these arrangements and procedures? What training/guidance do they receive to make sure they have sufficient knowledge and are able to comply with the information to clients requirements?
- Are the firm's control mechanisms sufficient to ensure the provision of information to clients? Are these mechanisms different depending on the medium used?

¹ MiFID Supervisory Briefings on conflicts of interest (CESR/08-733), MiFID Supervisory Briefings on inducements (CESR/08-734), MiFID Supervisory Briefings on best execution (CESR/08-735) and the upcoming briefing on suitability, appropriateness & execution only.

- How often does the compliance function of the firm monitor the adequacy and effectiveness of all of the arrangements and procedures mentioned above? How are deficiencies recorded and what is done to ensure that they are appropriately addressed?
- What information does the firm provide to clients about making a complaint?

2. Types of information to be provided to the client

The L1 and L2 Directives require that **different types of information should be addressed to the client** (as detailed below) and that this information must be **fair, clear and not misleading**:

- information to be provided before a client is bound by any agreement for the provision of investment services or ancillary services or before the provision of those services;
- information to be provided prior to some specific events;
- agreement(s) with the client; and
- reports sent to the client.

2.1. The information must be fair, clear and not misleading

Article 19(2) of the L1 Directive states that all information, including marketing communications, addressed by the firm to clients or potential clients shall be fair, clear and not misleading. Furthermore marketing communications shall be clearly identifiable as such.

Article 27 of the L2 Directive details how information addressed to retail clients must be presented in order to be fair, clear and not misleading.

These conditions mainly concern the way the information is presented. In particular, the information must be accurate. The information shall **be sufficient** for, **and** presented in a way that is **likely to be understood** by, the average member of the group to whom it is directed, or by whom it is likely to be received. The way in which the information is presented should not disguise, diminish or obscure important items, statements or warnings.

Specific requirements apply if the information contains the following :

- comparative information;
- information on past performance;
- information on simulated past performance;
- information on future performance;
- information on tax treatment;
- the name of a competent authority.

Art. 27(2) of the L2 Directive requires that information must give a fair and prominent indication of any relevant risks, if any potential benefits of an investment service or financial instrument are emphasized in the information. The comprehensiveness and accuracy of the presentation of risks must be proportional to that of the presentation of benefits. **Examples of typical risks are:**

- issuer default risk
- guarantor default risk
- exchange rate risk
- risk of limited tradability of financial instruments
- risk of further margin calls
- capital guarantees only apply at the end of repayment period

Information contained in a marketing communication shall be consistent with any information the firm provides to its client in the course of carrying on investment and ancillary services². This applies in particular to product information.

Competent authorities are not prevented from pre-approving marketing communications on compliance with MiFID³.

Key core questions

- How does the firm assess if the information provided to clients is fair, clear and not misleading?
- How does the firm ensure that marketing communications are consistent with any information provided by the firm to its clients in the course of carrying on investment and ancillary services, in particular with product information?
- How does the firm ensure that the information provided by means of a website is up-to-date?

Detailed questions

- If the firm provides information edited by a third party, does it check that the information is fair, clear and not misleading? Always? How?
- How does the firm define who is the average member of the group to whom it directs the information or who is likely to receive it? How does it ensure that the information is likely to be understood?
- What further changes has the firm introduced regarding the fair, clear and not misleading character of information to clients since the implementation of MiFID?
- What types of complaints has the firm received from clients or customer organizations regarding the fair, clear and not misleading character of information provided to them? How has the information been changed in consequence?
- In case of pre-approval of marketing communications by the competent authority: how and when does the firm submit its marketing communications for pre-approval? Does it submit all or parts of the marketing communications?

2.2. Information to be provided before a client is bound by any agreement for the provision of investment services or ancillary services or before the provision of those services

Articles 19(3) of the L1 Directive and 29 to 33 of the L2 Directive, require that **appropriate information** be provided to the client or potential client, **in good time before** the client is bound by any agreement for the provision of investment services or ancillary services or before the provision of those services, whichever is the earlier, about:

- the terms of any such agreement;
- information about the investment firm and its services;
- information about financial instruments;
- information requirements concerning safeguarding of client financial instruments or client funds;
- information about costs and associated charges.

This information may be provided in a standardised format and is required so that the client is reasonably able to understand the nature and risks of the investment service and of the specific types of financial instruments that are being offered and is, therefore, able to take decisions on an **informed basis**.

² Article 29(7) of the L2 Directive.

³ Recital 43 of the L2 Directive.

Key core questions

- How and in what documentation does the firm ensure that the required disclosures are being provided?
- How does the firm ensure that those disclosures are provided within the required timescales?
- How does the firm determine what information is needed to enable clients to take investment decisions on an informed basis?
- How does the firm ensure that all the information it provides is up-to-date?

Detailed questions

- Is the information provided to clients in a comprehensible form? Will it enable clients to:
 - ✓ understand the nature and risks of the investment service and the specific type of financial instrument?
 - ✓ take investment decisions on an informed basis? and
 - ✓ make an informed choice between the different products and services offered by the firm?
- Can the firm evidence that it:
 - ✓ provides information about itself and its services as required by the directive?
 - ✓ provides information about financial instruments as required by the directive?
 - ✓ meets the directive's information requirements concerning safeguarding of client financial instruments or client funds?
 - ✓ discloses information about costs and associated charges and that it does so in accordance with the relevant directive requirements?
- When providing a portfolio management service, how does the firm establish an appropriate method of evaluation and comparison so that the client for whom the service is provided is able to assess the firm's relative performance?
- How does the firm provide clients with information about costs and associated charges? Does this include the total price to be paid by the client, including all related fees, commissions, charges and expenses, taxes, or, if the exact price cannot be indicated the basis for the calculation of the total price? Are any commissions charged by the firms itemized separately?
- What types of complaints has the firm received from clients or customer organizations concerning the form, content, or timing of disclosures that have to be provided before the provision of a service? What remedial measures has the firm taken as a result of those complaints?

2.3. Information to be provided prior to some specific events

Besides the information to be provided before a client is bound by any agreement for the provision of investment services or ancillary services, or before the provision of those services, there are other types of information that must be provided to the client:

- information regarding client categorisation⁴; and
- information regarding use of client financial instruments⁵.

⁴ Article 28 of the L2 Directive.

⁵ Articles 19 and 32(7) of the L2 Directive.

Key core questions

- How does the firm inform its new and existing clients of their categorisation as a retail client, a professional client or an eligible counterparty ?
- When a firm requests the prior express consent of a client to the use of its financial instruments, how does it
 - ✓ inform that client about the specified terms governing the use of these instruments? and
 - ✓ provide the retail client with clear, full and accurate information about the obligations and responsibilities of the firm with respect to the use of those financial instruments, including the terms for their restitution, and the risks involved?

Detailed questions

- Does the firm inform its clients about any right they have to request a different categorisation? If so, how has the firm informed its clients about this right as well as about any limitations to the level of client protection that it would entail ?
- What arrangements and procedures has the firm set up to obtain a client's prior express consent to the use of its financial instruments ?

2.4. Agreement with the client

Article 39 of the L2 Directive requires investment firms that provide investment services other than investment advice to retail clients to enter into a **written basic agreement** with the client setting out the essential rights and obligations of the firm and the client⁶.

Key core questions

- What arrangements and procedures has the firm set up in order to ensure that it enters into a written agreement with its clients before providing any investment service other than investment advice?
- How does the firm ensure that the terms of the agreement include - directly or by reference to other easily accessible documents - all the relevant information regarding the service to be provided and the rights and obligations of the firm and the client?

Detailed questions

- Which parts of the agreement incorporate by reference other documents and/or legal texts?
- Does the firm's client agreement set out the rights and obligations of the parties and the other terms on which the firm will provide services to the client? When and how does the firm provide the client with this document?
- Is the agreement signed by the client and the firm's representative?
- Does the agreement refer to the specific investment service(s) provided to the client or does it refer to all the investment services the firm is authorized to provide?
- Does the firm's portfolio management agreement allow the firm to invest in financial instruments not admitted to trading on a regulated market, in derivatives, or in illiquid or highly volatile instruments, or to undertake short sales, purchases with borrowed funds, securities financing transactions, or any transactions involving margin payments, deposit of collateral or foreign exchange risk? If so, how does the firm make a retail client aware of this?⁷

⁶ See also Article 19(7) of the L1 Directive.

⁷ Recital 51 of the L2 Directive

- In what durable media does the firm establish basic agreements?
- What arrangements and procedures has the firm set up to update the agreements signed with its clients?
- What types of complaints has the firm received from clients or customer organizations regarding the agreement that must be entered into with the client? What measures has the firm taken as a result of those complaints?

2.5. Reporting to the client

The client must receive from the firm **adequate reports** on the service(s) it has been provided with. These reports shall include, where applicable, the costs associated with the transactions and services undertaken on behalf of the client⁸.

The L2 Directive specifically distinguishes four types of reporting⁹. These regard :

- execution of orders other than for portfolio management;
- portfolio management;
- additional reporting for portfolio management or contingent liability transactions; and
- client financial instruments or client funds.

Key core questions

- What arrangements and procedures has the firm set up to ensure that it complies with the reporting obligations in respect of the investment services it provides to its clients?
- What arrangements and procedures has the firm set up to ensure that it complies with the reporting obligations in respect of execution of retail clients orders other than for portfolio management?
- Does the firm adopt the same arrangements and procedures regardless of the categorization of the client? If not, what are the differences?
- What arrangements and procedures has the firm set up to ensure that it complies with the reporting obligations in respect of portfolio management?
- Does the firm adopt the same arrangements and procedures regardless of the categorization of the client? If not, what are the differences?
- When providing portfolio management services or operating retail client accounts that include an uncovered open position in a contingent liability transaction, how does the firm ensure that the losses exceeding the predetermined threshold agreed with the client are promptly and appropriately reported to the retail client? In what document is this threshold agreed?
- What arrangements and procedures has the firm implemented in order to ensure that it provides a statement of the financial instruments and/or clients funds held for the client at least once a year?
- Can the firm evidence that reports it sends to its clients contain all the specific elements required by the directive and that they are sent in accordance with the timescales set out in the directive?

Detailed questions

Reporting in respect of execution of orders other than for portfolio management

⁸ Article 19(8) of the L1 Directive.

⁹ Articles 40 to 43 of the L2 Directive.

- Regarding the notice confirming the execution:
 - ✓ how does the firm ensure that it sends it within the required time?
 - ✓ how does the firm ensure that it contains the information required in article 40(4) of the L2 Directive?
- Does the firm use standard codes for the reporting purposes? If so, does the firm provide the retail client with an explanation of the codes used?
- When the order is executed in tranches, does the firm supply information about the price of each tranche or about the average price?

Reporting in respect of portfolio management

- How does the firm determine the frequency of the reporting in respect of portfolio management? How does the firm inform the retail clients that they have the right to request quarterly provision of the periodic statement on portfolio management activities?
- How does the firm ensure that it complies with the reporting obligations when a retail client chooses to receive information about executed transactions on a transaction by transaction basis?
- How does the firm ensure that the periodic statement of the portfolio management activities provided to retail clients includes all the information required in article 41(2) of the L2 Directive?
- In which cases is the statement provided by another person according to article 41(1) of the L2 Directive? In those cases, how does the firm ensure that the client is correctly informed about the portfolio management activities carried out by the firm?

Statement of client financial instruments or client funds

- How does the firm ensure that the statement of client assets includes the relevant information of article 43(2) of the L2 Directive? In particular:
 - ✓ what details of the financial instruments held by the firm for the client at the end of the period covered by the statement are reported to the client?
 - ✓ does the firm include the market valuation of each financial instrument held as one of the details of the financial instruments? If so, what information does the firm provide if the market value is unavailable?
 - ✓ in cases where client financial instruments or client funds have been subject to securities financing transactions, how does the firm satisfy itself that it complies with the reporting obligations?

3. Medium via which the information is provided

The L2 Directive specifies when the information to the client must be provided via a durable medium and when a non-durable medium can be used as well as the conditions to be met in order to be allowed to use one medium rather than another¹⁰.

Key core questions

- How does the firm determine which types of medium it uses and how does it control that it uses the appropriate medium to fulfill its information obligations?

Detailed questions

- When the firm offers to provide information in a durable medium other than paper and the client elects to receive it in this way, can the firm provide evidence of the client's choice?
- Where a firm is allowed to provide information to its clients by means of a website and that information is not addressed personally to the client, which measures has the firm taken to obtain the client specific consent to the provision of that information in that form as well as to notify the client of the address of the website and the place on the website where the information may be accessed?

This note has been prepared by the CESR MiFID Level 3 Expert Group chaired by Mr Jean-Paul Servais, Chairman of the Executive Management Committee at the CBFA, and by its sub-group on Intermediaries, chaired by Mrs María José Gómez Yubero, Director at the CNMV. For more information on this document or on CESR activities regarding intermediaries please contact Diego Escanero at descanero@cesr.eu.

The contents are merely illustrative and do not constitute legal advice. The MiFID legal texts are available at

http://ec.europa.eu/internal_market/securities/isd/index_en.htm

¹⁰ Regarding the medium through which information must be provided to clients, the situation can be summarized as follows :

Article(s) concerned (of the L2 Directive)	Durable medium	Durable or non-durable medium	Medium not specified
26 (inducements)			X
28 (client categorisation)	X - Article 28(2)		X - Article 28(1)
29-33 (information to clients)		X	
39 (retail client agreement)	X		
40, 41 and 43 (reporting to clients)	X		
42 (additional reporting)			X

Reference should also be made to Article 3 of the L2 Directive regarding the conditions applying to the provision of information.