European Association of Co-operative Banks
Groupement Européen des Banques Coopératives
Europäische Vereinigung der Genossenschaftsbanken

EACB position on ESMA's Consultation paper on Guidelines on certain aspects of the MiFID suitability requirements

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The voice of 4.000 local and retail banks, 51 million members, 181 million customers

EACB AISBL – Secretariat • Rue de l'Industrie 26-38 • B-1040 Brussels
Tel: (+32 2) 230 11 24 • Fax (+32 2) 230 06 49 • Enterprise 0896.081.149 • lobbying register 4172526951-19
www.eurocoopbanks.coop • e-mail : secretariat@eurocoopbanks.coop

General Remarks

The members of the European Association of Co-operative Banks (EACB) are pleased to comment on ESMA's *Consultation paper on Guidelines on certain aspects of the MiFID suitability requirements*.

The European Co-operative Banks generally welcome ESMA's initiative to enhance clarity and foster convergence in the implementation of certain aspects of the MiFID suitability requirements. While most of the financial markets players' attention is focused on the MiFID review currently debated in the European Parliament and Council, it is good to see that ESMA is considering proposals for guidelines, which are based on the current MiFID requirements and are applied by investment firms on a day to day basis.

We are, nevertheless, strongly concerned that the current draft guidelines are too far reaching and create new requirements which go beyond the intended scope of Article 19(4) of MiFID and Article 35 to 37 of the MiFID Implementing Directive.

This tendency of "scope creep" is most easily recognisable in

- the proposal to oblige the investment firm to gather sensitive private information about the client, such as his or her marital status or family situation (Question 2),
- the proposal to require the investment firm to generally mistrust the information provided by the client (Question 5)
- the idea to intermingle the suitability assessments between once-off investment advice and ongoing portfolio management (Question 8).

We therefore would greatly appreciate, if our detailed views and comments are taken into account in the ongoing preparation of the final version of the Guidelines.

Detailed Remarks

Please be aware that our references to paragraphs relate to the main body of the Consultation (Chapter III), if not specified otherwise.

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.

We generally agree with the notion that information provided by investment firms should include information about the reason for assessing suitability but would like to highlight that this additional information should not distract the client from the actual suitability assessment. The only point of contention is that neither Article 19(4) of MiFID nor Art. 35 to 37 of the MiFID Implementing Directive require the investment firm to explain the risk profiles. We therefore would suggest deleting of this requirement.

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.

ESMA's proposal goes much further than either Article 19(4) of MiFID or Article 35(1) of the MiFID Implementing Directive. We believe that especially personal questions about the client's marital status and family situation might, on the one hand, conflict with existing EU data protection regulations, and on the other hand, that this is information clients might be unwilling to divulge to their advisers. We believe that this question is already indirectly covered under the question of his/her general financial situation where the customer is asked to disclose "the source and extent of his regular income, his assets, including liquid assets, investments and real property, and his regular financial commitments"[1]. We therefore would suggest the deletion of the last sentence of paragraph 22.

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.

We generally agree with the proposal.

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.

On a general note, we would like to mention that investment firms are obliged to obtain information before providing certain financial services to clients. At this stage the extent of information collected however, is unlikely to vary, as it is collected prior to providing the actual service. Indeed it is rather difficult to predict what kind of specific information would have to be collected on a given client prior to the suitability assessment being made.

On a more detailed note, we would have some comments with regards to:

- *Paragraph 29(b)*: In practice, it would be difficult for the investment firms to obtain information about conditions, terms, access, loans, guarantees and other restrictions – especially if these products are provided by competing investment firms.
- *Paragraph 32*: The qualifications regarding professional clients lack any justification either under MiFID or its Implementing Directive. Pursuant to Article 35(2) of the MiFID Implementing Directive, an investment firm may generally assume that a professional client is capable to financially bear any related investment risks. We therefore do not understand the rationale for introducing an exception to this rule and believe that the last sentence should be deleted.

[1] Article 35(3) of the MiFID Implementing Directive

- *Paragraph 33*: Pursuant to MiFID Recital 44 it is reasonable to assume that professional clients will be able to identify for themselves the information that is necessary to make an informed decision, and if not, to ask the investment firm to provide that information. We therefore believe that sentence 2 and 3 should be deleted.
- *Paragraph 34*: As already indicated in our answer to Question 2, we believe that such personal information (i.e. age, marital status) should not be part of the suitability test and consequently be deleted.

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.

We would like to stress that investment firms should in general be able to trust the information provided by the client. This is mentioned in Article 37(3) of the MiFID Implementing Directive, in which an investment firm shall be entitled to rely on information provided by its clients or potential clients unless it is aware or ought to be aware that the information is manifestly out of date, inaccurate or incomplete. The implementing directive does not consider a specific requirement for the investment firm to establish special procedures to ensure that the client is telling the truth. Besides, it should be stressed here that it also lies within the client's responsibility "to provide correct, up-to-date and complete information" (Paragraph 37), as the suitability assessment is a co-operative effort between investment firm and client. We therefore believe it to be unreasonable for the investment firms to ensure that all information collected is reliable.

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 are of the opinion that the Guideline and paragraph 42 practically force the investment firms to verify that the information obtained from the client is up to date. Yet this is again at odds with Article 37(3) of the MiFID Implementing Directive which entitles investment firms to rely upon information it obtained from its clients or from its potential clients. There is but one exception, as already state above: The investment firm is aware or ought to be aware that the information is manifestly out of date, inaccurate or incomplete. In our view, therefore, concerning the ascertainment that said information is up to date, the following organisational arrangements would be sufficient:

1. Asking the client to notify the investment firm in a timely manner of any changes to the information previously provided.
2. Ensuring that appropriate organisational arrangements are in place that information received within one organisational unit (i.e. lending desk) will also be made available to the advisers.

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.

Firstly, on the subject of paragraph 43 (when no specific representation for a group of natural persons is chosen) we feel that this should not only be limited to the approach chosen by ESMA. Another possibility (practised in some Member States) is to allow each group member their own suitability test, and therefore their own investment decisions, if this is requested by the client.

Secondly, we would like to propose a small clarification with regards to how the relevance of client information is negotiated between the investment firm and the client ("agree on how the relevant client information will be determined"). The first sentence stating that "the investment firm and the client should agree on how the relevant client information will be determined" could be replaced by the phrase "specialities have to be taken into account" in order to account for the second sentence starting with "As a minimum".

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.

Our main concern with this point is that the suitability assessments between the once-off investment advice and the ongoing portfolio management are mixed up both under the Guideline (III.VIII. and Annex III paragraph 41) and also in the subsequent explanations (esp. paragraph 46 and Annex III paragraph 44).

Regarding investment advice the financial instrument specifically recommended needs to be suitable on the basis of the information provided by the client (see Article 19(4) MiFID). Hence under the Directive there is no mandatory obligation to take the client's total portfolio (including the asset allocation within that portfolio) into account. In particular we would like to point out that a client's portfolio might also feature assets that the client may have acquired independently from the investment firms (i.e. on their own account and without any prior investment advice by the investment firm or through another investment firm). This might lead to a situation in which the investment firm is unable to gather sufficient data on those products to render a suitable assessment.

With regards to portfolio management the situation is somewhat different. Here, taking into account the overall portfolio is common practice. Yet, also when it comes to portfolio management services, during an investment decision it will only be possible to consider portfolios for which portfolio management services are being rendered. The current proposals should include a clarification to this effect.

In order to align with the objectives of MiFID we would therefore suggest the deletion of the first point of the Guideline (and corresponding Annex III paragraph 41) as well as paragraph 46(a) (and corresponding Annex III paragraph 44(a)). As a minimum, we

would expect that there should be clarification that the requirements shall only be applicable to portfolio management services and that the appropriate degree of risk diversification is linked to many factors (such as portfolio size, risk management policies, nature and characteristics of investment products, decreasing reliability of rating agencies).

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.

Our main point of contention is that paragraph 48 envisions the record-keeping of both the actual interpretation of the client's information and the reasons about a change in information of financial instruments accessible to the client. All relevant information about the client's suitability is already documented in its entirety. Supervisors can already assess whether the specific advice given was suitable for the client. Furthermore, as the client is free to change his information at any point in time without having to state any reasons, keeping a record thereof thus becomes impossible for the investment firm.

We therefore would suggest deletion the two parentheses in paragraph 48.

Contact

The EACB trusts that its comments will be taken into consideration. Should there be any need for further information any questions on this paper, please contact:

Ms. Marieke VAN BERKEL
Head of Retail Banking, Payments and Financial Markets
m.vanberkel@eurocoopbanks.coop

Mr. Andreas STEPNITZKA
Adviser for Financial Markets
a.stepnitzka@eurocoopbanks.coop