Technical standards and guidelines on certain aspects of the MiFID suitability requirements. July 2012.

ESMA has published, on the 6 of July 2012, technical standards and guidelines on certain aspects that MiFID imposes for assessing the suitability of the financial product or service when the advisory service is provided in the field of investment or discretionary management of portfolios. These standards are issued under article 16 of the Rules of ESMA. Article 19.4 of MiFID sets out that when providing such services, investment firms will obtain the necessary information about the knowledge and experience in the field investment corresponding to the specific type of product or service, financial situation and investment objectives of the client, so that the entity may recommend the investment services and financial instruments that best suit it. The guidelines focus primarily on the need for institutions, taking into account their nature and circumstances, to have policies and procedures that allow them to obtain the necessary information from their customers to make an appropriate assessment of appropriateness of financial products or services (suitability assessment). Technical standards are composed of a general rule and several (explanatory) supporting standards, and are as follows:
Guideline 1: Information to be provided to customers on the suitability assessment.

Investment firms must inform customers clearly and simply that the reason why the suitability assessment is made is to allow the entity to act in the best interest of its clients. Entities must not create any ambiguity or confusion about their responsibilities in the evaluation process.

Guideline 2: Measures necessary to know customer and financial instruments.

Investment firms should adopt suitable policies and procedures that allow them to understand the their customers' essential data and the characteristics of the financial instruments available to these customers.

Guideline 3: Qualifications of investment firm personnel.

Investment firms are required to check that employees involved in material aspects of the suitability assessment process have an appropriate level of knowledge and experience.

Guideline 4: Extension of information to collect from customers. (Proportionality).

Investment firms must determine the extent of customer information to seek taking into account all the features of the service to be provided (investment advice or discretionary portfolio management). The scope of information required about the client can vary depending on the type of financial instrument (complexity and risk level), the nature and extent and nature of the service, the customer's needs and circumstances.

Guideline 5: Reliability of customer information.

Investment firms must take all reasonable measures to ensure that the information collected from customers is reliable; for example, to ensure that questions asked of the investor are easy to understand. In particular, entities: a) should not rely solely on the assessment that the client makes of its knowledge, experience and financial condition; b) must ensure that all tools used in the suitability assessment process are appropriately designed (for example, that issues are formulated in such a way that they will lead the customer to a specific type of investment), and c) must take steps to ensure consistency in customer information.

Guideline 6: Update client information.

When an investment firm has a continuing relationship over time with a client, it must set out appropriate procedures to maintain complete and adequate information about the client.

Guideline 7: Customer information when regarding legal persons or groups.

If the customer is a legal person, two or more persons or one or more natural persons represented by another, in

order to identify who should undergo a suitability assessment, the investment firm must first comply with the provisions of the applicable legal framework. If the applicable legal framework does not offer sufficient guidance on this issue, particularly where a single representative has not been designated (as may be with the case of a marriage), the investment firm, based on a policy it had designed previously, it should agree with the relevant people (representatives of legal persons, people belonging to the group or represented legal persons) who should undergo suitability assessment and how this assessment will be made in practice, specifying who will obtain the information about knowledge, experience, financial situation and investment objectives. The entity shall keep a record of such agreements.

Guideline 8: Measures to ensure the suitability of the investment.

To give customers suitable financial instruments or services, investment firms must set out policies and procedures to ensure that they consistently take into account: a) all available information about the client that it may be relevant to assessing whether the investment is suitable including its current portfolio (and the composition of the portfolio's assets) and b) all the characteristics of the instruments taken into account in assessing adequacy including all relevant risks and costs (including indirect ones) for the client.

Guideline 9: Maintenance and record keeping.

Investment firms must as a minimum: a) maintain a suitable recording and conservation system to ensure the orderly and transparent recording of that which touches on the suitability assessment, including any investment advice provided and all investments (or disinvestments) made; b) ensure that measures to maintain and preserve records are designed to detect any failure in the suitability assessment (for example, inappropriate sales); c) ensure that the saved files are accessible to people relevant in the entity and competent authorities; and d) have appropriate processes to mitigate any deficiencies or limitations of maintenance procedures and record keeping.

It may be recalled that ESMA guidelines bind its members in a quasi-compulsory manner since, according to articles 16.3 and 16.4 of Regulation 716/2010 of the Council and EU Parliament (ESMA Regulation), competent authorities have two months to decide and inform ESMA and the market if they meet the guidelines or, if not, to report the reasons for not following the recommendations. ESMA shall report to the Parliament, Council and European Commission on decisions taken by national competent authorities on the implementation of the guidelines, and the means that ESMA has to verify such compliance.

If you want to read the full document, click on: http://www.esma.europa.eu/system/files/2012-387.pdf