

MFSA

MALTA FINANCIAL SERVICES AUTHORITY

FEEDBACK STATEMENT

CONDUCT OF BUSINESS RULEBOOK

[MFSA REF: 04/2016 AND 04/2015]

20 December 2017

Feedback Statement

CONDUCT OF BUSINESS RULEBOOK

1.0 Consultation Procedure

Background

On 6 May 2015 the Malta Financial Services Authority (“MFSA”) entered into the first phase of a consultation procedure through the issuance of the “*Consultation document relating to the creation of a proposed Conduct of Business Rulebook*” (**Ref.04/2015**). This consultation procedure followed the previous consultation undertaken by the MFSA regarding the “*Proposed Conduct of Business Rules for the Enhanced Protection of Customers in Investment Services*” (**Ref.03/2014**) which was issued by the MFSA for consultation on 27 January 2014. The first phase of this consultation procedure tackled the topics of: (1) Client Disclosures and Reporting; (2) Product Governance; and (3) Conflicts of Interest.

On 11 April 2016 the MFSA entered into the second phase of the consultation procedure (**Ref. 04/2016**). The purpose of this second phase of consultation was to obtain the industry’s views on the following chapters in the proposed Conduct of Business Rulebook: (1) Selling Process and Practices (including Contractual Agreement with Clients) and (2) Execution of Clients’ Orders.

As indicated in the previous consultations, the Rulebook is addressed to persons licensed under the Investment Services Act (excluding custodians) and to persons carrying on insurance activities in terms of the Insurance Business Act or the Insurance Intermediaries Act (insurance undertakings and insurance intermediaries), and individuals who work with or advise such entities, as well as persons licensed as credit institutions under the Banking which sell or advise clients in relation to structured deposits, where applicable. The Rulebook is aimed at setting out the regulatory requirements of the above –mentioned regulated persons, insofar as their conduct vis-à-vis their clients, is concerned.

Context and Sources of the Rulebook

This Rulebook are mainly a transposition of the relevant requirements set out in the relevant EU directives applicable to Regulated Persons as defined in the Glossary to the Rulebook, as well as any relevant Level 2 and Level 3 measures.

In drafting the Conduct of Business Rulebook, the MFSA has mainly transposed the conduct of business requirements of;

- (i) the Markets in Financial Instruments Directive (MiFID II) together with the MiFID Implementing Directive and Implementing Regulation, as applicable to investment services licence holders, other than AIF managers or custodians; and
- (ii) the Insurance Distribution Directive together with the IDD Implementing Regulation on Conflicts of Interest and Inducements, Assessment of Suitability and Appropriateness, as applicable to insurance undertakings and insurance intermediaries

The MFSA has also taken into account any Guidance and/or Opinions issued by the European Securities and Markets Authority (ESMA) as well as the European Insurance and Occupational Pensions Authority (EIOPA).

Implementation of the Rulebook

With respect to Regulated Persons falling under points (i), (ii) and (v) of the definition of Regulated Person in the Glossary to the Conduct of Business Rulebook, the requirements of the Rulebook will start to apply as from the 3rd January 2018.

With respect to Regulated Persons falling under points (iii) and (iv) of the definition of Regulated Person In the Glossary to the Conduct of Business Rulebook, the requirements of the Rulebook will not be applicable to such entities until further notice. Accordingly, the Conduct of Business Rulebook will be applicable with respect to Insurance Undertakings, Insurance Intermediaries from a date specified by the Authority. With respect to Ancillary Insurance Intermediaries the Rules contained in the Rulebook which would apply to such persons would also be specified at a later date.

The contents of this Rulebook should be read in conjunction with the requirements of the:

- **Investment Services Rules for Investment Services Providers**
- **Insurance Rules**
- **Insurance Intermediaries Rules**

which prescribe the prudential requirements for the Regulated Persons in question and which are also binding on Regulated Persons.

2.0 MFSA’s Feedback to the Consultation Procedures of the 6 May 2015 and 11 April 2016

The MFSA refers to the Consultation Documents on the proposed Conduct of Business Rulebook issued on the 6 May 2015 (Phase 1: **Ref. 04/2015**) and the 11 April 2016 (Phase 2: **Ref. 04/2016**) respectively.

The Authority has received a number of comments from members of Malta’s financial services industry and has also engaged in ad hoc meetings on the subject of the Rulebook with various associations representing various industry participant.

A summary of the main comments received in relation to the proposed Conduct of Business Rulebook and the Authority’s position in relation thereto, is provided below. The feedback provided hereunder has been divided in three sections, as per table below. The Authority’s position has been determined after a careful and thorough consideration of the feedback received.

Section A- Applicable to all Regulated Persons

Topic	Respondents’ Comments	MFSA’s Position
General Comments		
Passporting	Respondents queried on the applicability of the provisions of the Conduct of Business Rulebook in so far as Regulated Persons exercising their European passport rights in Malta are concerned.	In so far as passporting activities is concerned the Conduct of Business rulebook will apply to the activities of : <ul style="list-style-type: none"> a) Regulated Persons licensed or otherwise authorised by the MFSA when such persons carry out a cross border activity on the basis of freedom of services and/or freedom of establishment; and b) branches established in Malta of European Investment Firms and European

Topic	Respondents' Comments	MFSA's Position
		Insurance Undertakings in exercise of European passport rights.
Chapter 1 – Disclosures		
<p>Documents to be provided to Clients in both Maltese and English</p> <p>During the Consultation phase, the MFSA had proposed that certain documentation would need to be disclosed in English, or in any other language agreed by the parties; provided that, in the case of Clients resident in Malta, the documents had to be provided both in English and Maltese unless the person to whom the information is to be disclosed specifically chooses to receive such information in either English or Maltese only.</p>	<p>Respondents argued that the operational aspect must be taken into account since where documents are produced directly off IT systems, it is not always possible for the documents to be available in both languages.</p> <p>Another concern of Respondents was that the translation of documents in Maltese will be very onerous and furthermore, Maltese does not have the full technical capacity and is not sophisticated enough to describe certain terms. Extensive reference would still need to be made to the English version in a Maltese translation.</p>	<p>The MFSA considers that the arguments brought forward by the industry are justified and has therefore reconsidered its position, so as not to impose excessive burdensome measures on the market, which might not achieve the intended outcome.</p> <p>In this regard, the relevant rule has been amended to require that information to be disclosed to clients is disclosed in one of the official languages of Malta, or in any other language agreed by the parties; provided that</p> <p>(a) The Statutory Notice to be provided to Clients in terms of the Insurance Business (Long Term Business Contract Statutory Notice) Regulations; and</p> <p>(b) The Statutory Notice required in terms of Insurance Intermediaries Rule 7 – Code of Insurance Selling Practice (Long Term Business Notice).</p>

Topic	Respondents' Comments	MFSA's Position
		are to be made out in both Maltese and English, in the case of clients resident in Malta, as per the existing legislative requirements.
<p>Secure Transmission</p> <p>During the Consultation phases, the MFSA had proposed that Regulated Persons are to ensure that they have in place appropriate arrangements to ensure the security of information they receive from Clients and the secure transmission of any information to their Clients.</p>	<p>Respondents argued that it is not clear whether the requirement for secure transmission of information to customers implies that providers need to encrypt the e-mails addressed to customers.</p>	<p>In this context, MFSA is not imposing a prescriptive approach in that it is leaving it up to Regulated Persons to determine what appropriate action they deem necessary to ensure the secure transmission of any information to clients. Such transmission can be done through encryption or other means.</p>
Chapter 4 – Sales Process and Selling Practices		
<p>Access to financial Services</p> <p>The MFSA had proposed a rule that a Regulated Person shall, inter alia,</p> <p>without prejudice to the pursuit of its legitimate commercial aims, not prevent access to basic financial Services, through its policies, procedures, or working practices.</p>	<p>One Respondent requested clarification on the purpose of this Rule.</p>	<p>On further consideration, the MFSA has decided to delete this Rule.</p>
<p>Signing of declarations</p>	<p>Respondents argued that this Rule places licence holders in the untenable situation of having to prove that the client has indeed understood.</p>	<p>While the MFSA acknowledges the duty of clients to make sure that they fully understand the contents of any document before they sign it, the</p>

Topic	Respondents' Comments	MFSA's Position
<p>The proposed Rulebook included a provision prohibiting a Regulated Person from requesting Clients to sign declarations to the effect that s/he has understood and accepts certain features of the product or that s/he is relying on his/her own skill, judgement and expertise in order to make the investment in the Products or Instruments. It is the obligation of the Regulated Person to assess the suitability or the appropriateness of such Products vis-à-vis the Client</p>	<p>Respondents also pointed out that Clients should assume responsibility for his investment decision after understanding and accepting the features and risks of the investment.</p>	<p>Regulated Person cannot in any way be seen to transfer its regulatory obligations onto the client. The Rule in question serves to ensure that especially in the context of investment advice, where, presumably the client has sought the guidance of the Regulated Person in an area in which s/he has little or no expertise, the client is not required to take responsibility for the service given to him by the Regulated Person. In particular, when providing a personal recommendation to the client or when the features of the product are described to a client by the Regulated Person, the client cannot be asked to sign off a declaration stating that in effecting a particular transaction s/he is acting on his/her own skill and judgement.</p>
<p>Gifts One of the proposals included in the COB rulebook was to prohibit Regulated Persons from enticing persons to purchase products or services it offers by giving or promising to give any gifts to any person on condition that such person either purchases a service or a product or fixes an appointment with the Regulated Person to discuss the products and/or services which the Regulated Person offers.</p>	<p>Respondents enquired whether gifts can be provided without being advertised, for example, provided post-sale.</p> <p>Other Respondents agreed that the provision of gifts to entice a person to purchase a product should be prohibited. However they argued that the provision of a gift to fix an appointment should be allowed as it does not represent any regulatory risk.</p>	<p><i>The MFSA is of the view that, in general, licence holders should not entice Clients to purchase products or services it offers by giving or promising to give gifts to such Clients. Having taken into account feedback received the MFSA has revised the proposed rule to allow gifts where these relate to the Product or Service being offered and/or where such gifts enhance the value thereof. Such gifts should however not be of a substantial value. The MFSA has also included guidance on what types of gifts would be acceptable.</i></p>

Topic	Respondents' Comments	MFSA's Position
	<p>In addition, in motor insurance there is the practice that some insurers will give free assistance membership. Clarification was sought as to whether this would be considered as a gift.</p>	
<p>Telephone contact with Clients</p> <p>In the proposed Rulebook there was indicated that a Regulated Person may make telephone contact with a Client who is an existing Client, only if:</p> <ul style="list-style-type: none"> (a) the Regulated Person has, within the previous twelve months, provided that Client with a Product or Service similar to the purpose of the telephone contact; (b) the Client holds a Product, which requires the Regulated Person to maintain contact with the Client in relation to that Product; (c) the Client has given his or her consent to being contacted in this way by the Regulated Person. 	<p>Respondents remarked that the restrictions under this proposed Rule are very onerous making it difficult to contact even existing clients which would ultimately be to the detriment of the general public. One example given by respondents would be when Clients would be contacted as a reminder that their policy is due for renewal, or to discuss developments and the risks that such developments may present and ways to manage them.</p>	<p>Further to comments received by the industry, the MFSA has amended the Rule such that the first two conditions indicated therein would be construed as alternative rather than cumulative, whilst the third condition (client consent) remains mandatory.</p> <p>Further to the above, it would be possible for Regulated Persons to contact clients telephonically in order to remind them that their policy is due for renewal or to discuss developments and the risks that such developments may present and ways to manage them, provided that the client consents to such contact.</p>

Topic	Respondents' Comments	MFSA's Position
<p>Record Keeping Requirements</p> <p>Regulated Persons shall record in written minutes or notes all relevant information related to relevant face-to face conversations with Clients.</p>	<p>Respondents enquired whether this Rule also applies to apply to unsolicited calls/meetings.</p>	<p>The Authority confirms that this Rule shall apply in all cases. The rationale behind this Rule is to keep an audit trail of all meetings with clients.</p> <p>However, Guidance to the Rule has been added to provide that a record of an email exchange with a client reflecting the discussions held in a face to face meeting with a client would also satisfy the requirements of this Rule.</p>
<p>Advice and Non-Advice</p>	<p>Respondents opined that there is a clear thrust towards an “advisory basis” service offering. Respondents stated that the burden of advice will lie too heavily on the licence holder, stifling business and possibly jeopardising interaction with the consumers themselves.</p> <p>Whilst the Respondents agreed that where products exhibit characteristics which render them complex, then the element of advice must be brought in, they failed to see how a service provider can possibly provide a service without touching, even unintentionally, on the provision of advice, based on the propositions of the Rulebook.</p> <p>The Respondents requested the MFSA to consider a broader range of distribution models for retail investment products and that it should provide</p>	<p>The intention of Section 3 – “Advice and Non-Advice” in Chapter 4 – “Sales Process and Selling Practices”, was to provide clarification on circumstances which would constitute advice (i.e. a personal recommendation), not to prohibit non-advised sales. The provisions found in the Rulebook on this matter reflect the requirements of the relevant EU Directives as well as any guidance issued by the relevant ESAs.</p>

Topic	Respondents' Comments	MFSA's Position
	<p>more flexibility between advisory and non-advisory services since this strict categorisation was likely to lead to customer detriment.</p>	
<p>Suitability Statement</p> <p>A Regulated Person when providing Advice or, in the case of MiFID firms, Portfolio Management Services to a Client shall, before the transaction is made, provide the Client with a suitability statement.</p>	<p>Respondents noted that the inclusion of a Suitability Statement for each transaction, particularly in the case of clients who transact on a regular basis (weekly/monthly) is very onerous. Respondents consider that the case of discretionary mandate, providing the client with a suitability statement ahead of each trade would be impractical.</p>	<p>The requirement to provide clients with a suitability statement when providing advice, prior to the conclusion of a contract, emanates from MiFID II and IDD. The respective directives do not provide an exemption from providing suitability statements to clients who transact on a regular basis or in the case of discretionary mandates. To note however, that a suitability statement is only required when advice or portfolio management services are provided. Transactions which are not done on an advisory basis or in the context of portfolio management services do not require a suitability statement to be issued in their respect.</p>
<p>Suitability and Appropriateness Assessment Tools/Questionnaires</p> <p>A 'tick-box' approach should not be used either to collect Client information or to assess suitability or appropriateness. Suitability and Appropriateness is not about collecting irrelevant information but such information as is necessary to achieve the intended outcome, which, in the case of the</p>	<p>Respondents sought clarification on the interpretation of this guidance, namely whether it should be understood that the assessment as a whole, should involve a thought process in arriving at a final determination, and not simply a tick-the-box exercise in its entirety.</p>	<p>The purpose of the guidance is to highlight that care must be taken to ensure that the Regulated Person analyses all the relevant aspects and asks all the necessary questions before taking action by, inter alia, proving a personal recommendation.</p>

Topic	Respondents' Comments	MFSA's Position
<p>provision of Advice, is a suitable recommendation.</p>		
<p>Persuasion to surrender or cancel a Product or Service</p> <p>One of the requirements set out in the proposed Rulebook was that a Regulated Person shall not persuade or attempt to persuade a Client to surrender or cancel any Product or Service which such Client may have already purchased.</p>	<p>One Respondent pointed out that there are instances where brokers give advice to cancel or surrender a product if it is in the best interest of the client, so the reason for this rule was not clear.</p>	<p>The Authority has taken note of the comments by the industry and has inserted a clarification that such a provision would apply only when the surrender or cancellation is not in the best interest of the client.</p>
<p>Chapter 5 – Execution of Clients' Orders</p>		
<p>Organisational Requirements</p>	<p>The Respondents remarked that the rule relating to retention period of records would need to give a clear indication of the warning to be given by MFSA when records are to be kept – such as at least 6 months prior to the end of the 5 year period.</p>	<p>The discretion of the MFSA to request an extension of the retention periods is an important supervisory tool that allows the MFSA to effectively exercise its statutory supervisory powers. The circumstances surrounding such requests, such as investigations of possible wrongdoing, do not always allow the MFSA giving advance notice of such extension in the retention period of records.</p>

Section B- Applicable to Regulated Persons falling under points (i) and (ii) of the definition of Regulated Person in the Glossary Topic	Respondents' Comments	MFSA's Position
Applicability to Fund Managers	One respondent requested clarification on the extent to which AIFMs, de minimis AIFMs and UCITS management companies will be subject to the provisions in the CoB Rulebook or other MFSA Rules where they provide investment services.	The Authority would clarify that Fund Managers offering MIFID Services shall only be subject to the Conduct of Business Rulebook provisions in the context of those services.
Chapter 4 – Sales Process and Selling Practices		
Definition of Eligible Counterparty	Clarification was sought on the interpretation of the definition of “Eligible Counterparty”.	The wording of this section reflects verbatim the definition in MIFID II. In the absence of guidance from ESMA on the interpretation of this provision, the MFSA is not in a position to issue its own interpretations.
<p>Personal Recommendation</p> <p>A Regulated Person shall be deemed to provide Advice for the purposes of these Rules if it provides a Personal Recommendation relating to Products to Clients or their agents.</p>	Respondents argued that the notion of a general recommendation was not seen in the Rulebook. For instance, a research report with a general recommendation which is distributed via distribution channels should not constitute a personal recommendation.	The Authority would like to clarify that any recommendation which does not fall within the definition of a personal recommendation is a general recommendation and does not qualify as investment advice. A general recommendation which is distributed via distribution channels does not constitute a personal recommendation. This position is already the prevailing one under the current MIFID I regime.
Regulated Persons providing both Independent and Non-Independent Advice	Respondents stated that this requirement is impractical for small firms and those offering a discretionary portfolio management service to clients.	This is a MIFID II Requirement emanating from the Delegated Regulation from which no derogation is possible.

<p>In the proposed rules, a Regulated Person must ensure that a staff member does not provide both independent and non-independent advice.</p>		<p>Furthermore MIFID Implementing Regulation very clearly states in Article 53(3)9c) “<i>The investment firm shall not allow a natural person to provide both independent and on-independent advice.</i>” The context of this requirement is that the investment firm’s set up should be such that it is very clear to the client who of the Regulated Person’s staff provides advice and who does not.</p>
<p>Complex Products</p> <p>The Financial Instruments indicated in points (i), (ii), (iii), (v), (vii), (viii), (ix), (xi), (xii), (xiii), (xv) and (xvi) in Appendix 3 to these Rules may only be sold to Retail Clients on an advisory basis, that is, after the satisfactory conclusion of a suitability assessment in terms of this Rulebook.</p>	<p>Respondents commented that point (viii) of the Appendix (“Debt instruments the return of which is subordinated to the reimbursement of debt held by others”) is written in such a way as to suggest that unsecured debt could fall in this category.</p>	<p>Please Refer to Dedicated Section in this Feedback statement below.</p>
<p>Vulnerable Clients</p> <p>The MFSA had proposed the inclusion of guidance on the manner in which MiFID firms are to deal with vulnerable clients as well as guidance on which type of clients should be deemed vulnerable.</p>	<p>Respondents stated that care must be taken not to generalise. Persons listed in the guidance note need not necessarily be vulnerable. Moreover, requesting service providers to proactively identify vulnerability is excessively onerous and time consuming, especially since the benchmark is a “non-exhaustive list” of circumstances that will always create a doubt as to whether there may be other vulnerabilities which were not identified.</p>	<p>The MFSA is in favour of taking on board the industry’s suggestion to remove the non-exhaustive list of examples, which creates the impression that all people falling in these categories are by default vulnerable.</p> <p>The Authority has therefore amended the guidance to favour a principle based approach to define “vulnerable clients” as a natural person who:</p> <p>a. has the capacity to make his or her own decisions but who, because of individual circumstances, may require assistance to do so</p>

		(for example, hearing impaired or visually impaired persons); and/or b. has limited capacity to make his or her own decisions and who requires assistance to do so (for example, persons with intellectual disabilities or mental health difficulties).
Chapter 5 – Execution of Clients’ Orders		
Order execution policy In addition to differentiation by class of Financial instrument, it is recommended that a Regulated Person distinguish its policy by Client or order type.	The Respondents queried the meaning of “order type”.	“Order type” refers to whether the order is being received in the context of the service of reception and transmission of orders or whether that order relates to an execution-only transaction.

Section C- Applicable to Regulated Persons falling under points (iii) and (iv) of the definition of Regulated Person in the Glossary

Topic	Respondents’ Comments	MFSA’s Position
General Comment		
Distinction between Professional and Retail Clients	Respondents argued that the distinction between retail and professional is mostly limited to investment expertise. Respondents noted that in the context of insurance, it is not clear whether the distinction between a professional client and retail client applies to customer seeking cover under general insurance contracts or long term insurance contracts linked to investment products. One Respondent suggested	Given that the Rulebook will not immediately apply to Regulated Persons falling under points (iii) and (iv) of the definition of Regulated Person in the Glossary, the MFSA is further analysing the feedback received from the industry in this respect, bearing in mind the requirements of the IDD.

	<p>to consider all commercial entities as professional clients.</p>	<p>Respondents should be guided by Recital 51 of the IDD which states that “There is less of a need to require that such information be disclosed when the customer is seeking reinsurance or insurance cover <u>for commercial and industrial risks</u>, or solely for the purposes of distributing insurance-based investment products, when the customer is a professional client as defined in Directive 2014/65/EU”.</p>
<p>Chapter 1 – Disclosures</p>		
<p>Disclosure of Contract Terms</p> <p>A Regulated Person must provide each Client with the terms and conditions attaching to a product or service, in a durable medium, before the Client enters into a contract for that Product or Service.</p>	<p>One Respondent noted that the internationally accepted practice with tailored covers such as commercial lines policies where slips, summaries or cover notes are typically used at inception to order to attach cover whilst the policy terms are being drafted in accordance with customer requirements should not be removed.</p>	<p>The Authority would clarify that it is not the intention to remove such practice in so far as commercial lines policies are concerned.</p> <p>The Authority considers that, in all cases, clients should be in a position to know the terms and conditions of the contract prior to their being bound by it. The Authority is of the view that even in the case of cover notes and slips, the general terms and conditions of the policy would also be provided to the client and at no time would cover be bound prior to the client’s acceptance of the relative terms and conditions.</p> <p>In the light of the above, the Authority will be retaining this requirement.</p>

<p>Chapter 2 – Product Governance</p>		
<p>Distributors and Manufacturers</p>	<p>One Respondent requested clarification on the circumstances in the context of insurance under which a distributor would be considered to be acting as manufacturer.</p>	<p>Article 3 of the IDD Implementing Regulation, provides that insurance intermediaries shall be considered manufacturers where an overall analysis of their activity shows that they have a decision making role in designing and developing an insurance product of the market.</p> <p>Further details as to when such a decision making role is assumed are also given in Article 3(2) of the said Regulation.</p> <p>This Regulation also specifies that personalisation of and adaption of existing insurance products in the context of insurance distribution activities for individual customers as well as the design of tailor-made contracts at the request of a single customer, shall not be considered manufacturing.</p>
<p>Chapter 3 – Conflicts of Interest</p>		
<p>Applicability</p>	<p>Respondents requested clarification on the applicability of Chapter 3 (Conflicts of Interest) to Regulated Persons in the context of insurance distribution.</p>	<p>Regulated Persons falling under paragraph (iii) and (iv) of the definition of Regulated Person in the Glossary, shall only be required to adhere to requirements set out in Chapter 3 in so far as they carry out the distribution of insurance-based investment products.</p>
<p>Chapter 4 – Sales Process and Selling Practices</p>		

<p>Personal visits and contact with Clients</p> <p>The Regulated Person shall avoid providing Services and Products in the home of the Client except in cases where the Client’s mobility or other circumstances prohibit the Client from going to Regulated Person’s offices.</p>	<p>Respondents noted their concern with the introduction of this Rule, since in the context of insurance, sales are sometimes completed in the Client’s home at the request of the Client.</p>	<p>This Rule has been updated such that only “unsolicited visits” are not permitted. That is, it should be the client him/herself who should request a home visit from the Regulated Person. Conversely, Regulated Persons will not be allowed to cold call potential clients with a view of setting up appointments for home visits to sell Products or Services.</p> <p>This Rule has now been updated to clarify that Regulated Persons are required to obtain informed consent before the visit and to maintain a record of such consent.</p> <p>By way of Guidance, it is also clarified that this Rule shall not apply by visits carried out by Regulated Persons on the client’s premises for commercial purposes (e.g. in order to carry out a broker’s survey).</p>
<p>Chapter 5 – Execution of Clients’ Orders</p>		
<p>Application</p>	<p>The Respondent enquired on the exclusion of application of this Chapter to Tied Insurance Intermediaries and persons falling under paragraph (iii) of the definition of Regulation Person.</p>	<p>Applicability to Regulated Persons in so far as insurance is concerned was limited to those persons falling under part (iv) of the definition of Regulated Person in the Glossary (excluding TIIs) since the source of the rules was IIR 4, which is applicable to insurance brokers, agents and managers. IIR 4 is not applicable to TIIs or to insurance undertakings.</p>

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<p>Insurance Requirements of Clients The Regulated Person shall..</p> <p>(b) Have printed on the receipt, the full name and business address of the Regulated Person</p>	<p>One Respondent suggested the addition of “on the receipt <i>or the invoice</i>”.</p>	<p>The Authority has decided to take on board this suggestion and has amended the Guidance accordingly. The necessary corresponding amendments have also been effected to Chapter 4 – Sales Process and Selling Practices.</p>
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Sale of Complex Financial Instruments

MFSA’s Proposals

In its first Consultation, the MFSA has indicated two options setting out the regulatory obligations of Regulated Persons when these are selling complex financial instruments (as defined in MIFID and the relevant Level 2 Measures) as follows;

Option 1: Regulated Persons would only be allowed to sell complex financial instruments (as defined in MIFID and the relevant Level 2 measures) on an advisory basis. This means that the Regulated Person would have to assess a prospective client’s suitability vis-à-vis a complex product and provide a personal recommendation to the client in this regard prior to the purchase of such instrument by the said client.

Option 2: This option recognises that not all complex instruments are equally complex. Accordingly, some complex financial instruments have more complicated and non-transparent structures which render them more difficult for retail clients to understand than other products which although considered to be “complex financial instruments” in terms of the MIFID Implementing Directive, may not be too complicated for some retail clients to understand. Under this option, the sale of “particularly or highly” complex financial instruments to retail clients would be prohibited. On the other hand, the sale of other complex instruments (which are not highly complex) will only be permissible if sold on an advisory basis.

In this Consultation, the Authority had initially indicated that it favoured Option 1.

MFSA's Final Requirements

In considering feedback received, the Authority in Phase 2 of the Consultation proposed an approach wherein it indicated a number of instruments in relation to which transactions could only be executed on an advisory basis. Hence, with respect to other complex instruments which were not indicated in the Rules for this purpose, Regulated Persons could effect transactions only on the basis of an appropriateness test, in line with MIFID Requirements.

The Authority has taken into consideration of the additional feedback received from the industry further to its proposed position above and has now decided to take the following approach with respect to the sale of Complex Financial Instruments which will be reflected in R. 4.xx et seq:

Before providing a service to a client with respect to a Complex Instrument, the Regulated Person would be required to consider whether that Complex Instrument is to be provided to such client on an advisory or on a non-advisory basis (subject to an appropriateness test), and shall only provide services to clients on the basis of this consideration.

In effecting the above consideration, the Regulated Person will be required to, *inter alia*:

- (a) ensure that its categorisation of these clients is robust and regularly monitored and that it correctly reflects the status of each client such that retail clients are not incorrectly categorised as professional clients;
- (b) Consider the possibility of conflicts of interest especially where the Regulated Person is the issuer of the instrument or acts as a counterparty in the transaction, or is otherwise involved in the issue of the instrument. In this context the Regulated person shall specifically assess whether incentives (i.e. inducements/remuneration) are more lucrative for complex instruments than for those of more standard instruments.

Accordingly, in terms of this Rule, it will be the responsibility of the Regulated Person to ensure that before providing a service to a client with respect to complex instruments, it considers whether that Complex Instrument should be provided to such client on an advisory or on a non-advisory basis (subject to an appropriateness test). Furthermore, the Regulated Person shall only be allowed to provide services to clients on the basis of this consideration.

- (a) The level of complexity of the instrument in question;
- (b) The categorisation of the client as retail or professional;
- (c) The level of sophistication of retail investors and any aspects of vulnerability which they may have.

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Regulated Persons are expected to carry out this assessment on a per client basis, where a client requests to purchase a complex financial instrument. A general policy taken by a Regulated Person in this regard would therefore not be appropriate. Regulated Persons will be expected to retain documentation to support their decision to sell a particular complex product to a particular client on an advisory basis or otherwise, as applicable.

Accordingly, MFSA will not accept a situation where, for example, transactions in complex instruments, are systematically carried out by the Regulated Person on the basis of an appropriateness test.

Contacts

Should you have any queries regarding the above, please do not hesitate to send your queries on: csu@mfsa.com.mt.

