

MFSA

MALTA FINANCIAL SERVICES AUTHORITY

11th February, 2009

Securities Unit

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Dear Sirs,

**Re: Circular letter regarding sale of complex financial instruments by
Investment Services Licence Holders**

The MFSA has been monitoring the development, promotion and sale of certain investment products whose underlying assets comprise insurance policies such as traded endowment policies or life insurance policies. These investment products are generally packaged as collective investment schemes or asset-backed bonds. Moreover, these products are generally characterised by redemption restrictions in the form of: **[a]** lock-up periods of around two to five years, **[b]** redemption gates and **[c]** absence of a liquid secondary market where they may be sold.

Given the characteristics of the investment products referred to above, investment in these financial instruments may involve substantial risks, in particular significant liquidity risk, and may therefore not be suitable for all types of investors. Indeed, in view of their characteristics, these products are generally considered suitable only for experienced investors and should be classified as 'complex' financial instruments for the purpose of Part B of the Investment Services Rules for Investment Services Providers and they are therefore only suitable for investors who have the necessary experience and knowledge in order to understand the risks involved. To assess experience and knowledge, investment services licence holders are required to comply with SLC 2.22 of Part B of the Investment Services Rules for Investment Services Providers.

The MFSA is concerned that complex financial instruments such as the above-mentioned may have been sold to certain retail clients who may not have the knowledge and experience to understand how these complex financial instruments work and the relevant related risks. The sale of complex financial instruments does not fall within the parameters of the exemption from the appropriateness test set out in SLC 2.25 of Part B of the Investment Services Rules for Investment Services Providers. Accordingly, irrespective of the manner in which complex financial instruments are sold, the client should always be subject to a test which establishes whether the product is appropriate for such client.

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Licence holders should ensure proper compliance with the client profile requirements set in Part B of the Investment Services Rules for Investment Services Providers and with the relevant Guidance Notes. In addition, as required in terms of the record keeping requirements set in same Rules, Licence holders should maintain proper records of the services provided to clients including a copy of the relevant client fact find. These records should be available for inspection during compliance visits or upon request by the MFSA, in terms of its statutory powers.

Investment services licence holders will be retained responsible for any mis-selling of complex financial instruments.

Should you have any queries with respect to the above, please do not hesitate to contact Mr. Christopher P. Buttigieg or the undersigned.

Yours faithfully,

Cristina Parlato Trigona
Director