



FINANCIAL REGULATOR  
*Rialtóir Airgeadais*

**Markets in Financial  
Instruments Directive  
(MiFID)**

Feedback on Discussions of  
Conduct of Business Industry  
Working Group

# INTRODUCTION

MiFID is a comprehensive regulatory regime covering investment services and financial markets in Europe. It applies to both investment firms and credit institutions when providing investment services, and to regulated markets. MiFID was transposed into Irish law on 15 February 2007<sup>1</sup> and will come into effect on 1 November 2007. MiFID will replace the Investment Services Directive (93/22/EC)<sup>2</sup> [ISD] which is the basis on which investment firms are regulated in Ireland and throughout the EU.

MiFID is a Lamfalussy-type Directive. The Lamfalussy process comprises a four-level approach to the preparation of legislation:

- ▶ Level 1: Framework Directive co-decided by the EU Council and the EU Parliament;
- ▶ Level 2: Technical implementing measures to render the Level 1 principles operational, adopted by the EU Commission;
- ▶ Level 3: Provision of non-binding guidance and common interpretations by the Committee of European Securities Regulators [CESR]; and
- ▶ Level 4: Enforcement.

The Level 2 implementing measures comprise two documents, an Implementing Directive and a Regulation. The Level 1 Directive and the Level 2 Implementing Directive have been transposed into Irish law by means of a Statutory Instrument, No 60 of 2007, entitled European Communities (Markets in Financial Instruments) Regulations 2007 [the MiFID Regulations]. The Level 2 Regulation automatically becomes law and does not require transposition. Level 3 guidance has been issued by CESR in relation to two conduct of business issues, inducements and best execution.

## Why the need for MiFID?

The ISD was adopted in 1993 and is superseded by MiFID. There is a need to enhance consumer protection, eliminate barriers to cross-border trading and harmonise conduct of business rules so that the passport is more effective. It is also necessary to expand the services and instruments to take account of developments in financial markets.

## What are the changes?

MiFID utilises the concept of full harmonisation, which means that the same rules will apply across the EU and individual countries can only impose additional requirements in limited circumstances. The range of financial instruments and services for which authorisation is required is expanded. Investment advice is included as a core service which can be passported to other EU countries in its own right. Additional financial instruments include contracts for differences, commodities derivatives, and exotic derivatives such as those relating to climatic variables, emission allowances and inflation rates.

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<sup>1</sup> SI 60 of 2007.

<sup>2</sup> 10 May 1993.

## Who does MiFID apply to?

MiFID applies to investment firms, stockbrokers, credit institutions when providing investment services, firms or market operators running MultiLateral Trading Facilities, many futures and options firms and some commodities firms. It will not apply to those providing services in relation to insurance policies, tracker bonds or PRSAs. It will not apply to Multi Agency Intermediaries or Authorised Advisors. However, existing Multi Agency Intermediaries and Authorised Advisors should ensure they are not engaged in any of the new services or financial instruments that would require a higher level of authorisation.

## Industry Working Group

As part of the preparation for the implementation of MiFID, the Financial Regulator invited industry representatives to participate on a working group dealing with Conduct of Business requirements. The purpose of the working group was to consider issues other than those already being considered by CESR in its consultation process.

The Conduct of Business working group considered issues in relation to client categorisation, the provision of information to clients, suitability and appropriateness, reporting to clients, best execution and client order handling, inducements, investment research, conflicts of interest, complaints handling and personal transactions.

The group's feedback in relation to the issues discussed is set out in this document, in a questions and answers format, under the following headings:

- ▶ Client categorisation
- ▶ Suitability and appropriateness
- ▶ Provision of information to clients
- ▶ Reporting to clients
- ▶ Investment research

As the guidance on inducements and best execution has only recently been issued by CESR, the working group's conclusions on these issues will be published later in the year. No major issues were raised in relation to complaints handling and personal transactions.

The participants on the working group were:

Breda MacNamara and Enda McMahon, representing the Irish Association of Investment Managers, Sinead Flanagan and Paul Cullinane, representing the Irish Stock Exchange, Martin Purdy and Robert Kelly, representing the Irish Banking Federation, Brendan Kelly, representing Financial Services Ireland, Claire Cunneen, representing Nexgen, John Caslin, representing Alder Capital, Terry Murphy, Deirdre Norris and Clive Duignan, representing the Financial Regulator.

Alternates and other occasional participants:

Aoife McGee, representing the Irish Association of Investment Managers, Mary Dolan and Declan Darcy, representing the Irish Banking Federation, Ailish Byrne, representing the Irish Stock Exchange, and Philip Brennan, representing the Financial Regulator.

## Preparation for MiFID

Prior to 1 November, firms should be familiar with the requirements set out in the MiFID Regulations and the guidance issued by CESR.

This document deals with the requirements set out in Part 7 of the MiFID Regulations and with some of the requirements contained in Parts 5 and 12, i.e., Regulations 38, 39, and 151 to 155.

The MiFID Regulations set out detailed requirements in relation to conduct of business and other issues, e.g., the information to be provided to clients, the assessment of suitability and appropriateness, the obligation to take all reasonable steps to obtain the best possible result for clients when executing orders, conflicts of interest and inducements.

When doing business with clients after 1 November 2007, you must comply with the requirements of the MiFID Regulations. For example, the conduct of business requirements include obligations to:

- ▶ assess suitability or appropriateness in providing investment services to clients;
- ▶ obtain the client's consent to your order execution policy when you execute orders, or arrange for execution of orders, on behalf of a client;
- ▶ ensure you provide clients with the information specified in the MiFID Regulations, e.g., information in relation to the firm and its services, costs and charges, and risk information; and
- ▶ ensure you have categorised your clients as retail, professional or eligible counterparty and have notified them of their categorisation if that has changed.

You should also note that you may have further organisation, reporting, record keeping and other obligations under the MiFID Regulations that are not addressed in this document.

## Interpretation

The MiFID Regulations will come into effect on 1 November 2007. We are aware that there may be some revisions to the version of the Regulations issued on 15 February 2007 and the information provided in this document is, therefore, based on our understanding of the intent of the MiFID Directives.

The contents of this document are intended to provide a helpful guide to the provisions of the MiFID Regulations. It does not amount to, and should not be regarded as amounting to, legal advice from the Financial Regulator or any other person or group. It is intended to restate the obligations set out in the MiFID Regulations in a way that may answer some questions that firms may have. The primary obligations remain in the MiFID Regulations and it is the MiFID Regulations to which a firm must turn to consider the full extent of its obligations. If necessary, a firm should seek legal advice in relation to the application of the MiFID Regulations to specific sets of circumstances. It is not possible, nor have we tried, to address all the myriad circumstances that can arise when conducting the business of providing investment services to clients.

When this document refers to 'investment firms', this should be understood to also apply to 'credit institutions' where applicable. Many of the obligations set out in the MiFID Regulations also apply to credit institutions when providing investment services.

# CLIENT CATEGORISATION

The MiFID Regulations set out a three-tier categorisation system classifying parties as a) professional clients<sup>3</sup>, b) retail clients<sup>4</sup> or c) eligible counterparties.<sup>5</sup> The MiFID Regulations attach different levels of regulatory protection and approaches to each party depending on the category he/she falls into.

The MiFID Regulations envisage some flexibility for clients to upgrade or downgrade between categories to obtain more or less regulatory protection.

## Question 1.1

**How do I decide whether a client should be newly classified as Retail, Professional or Eligible Counterparty under the MiFID Regulations?**

### Answer 1.1

- (1) The MiFID Regulations specify that certain entities should automatically be regarded as professional. These include entities authorised or regulated to operate in financial markets, large undertakings, pension funds, collective investment schemes, national and regional governments, and institutional investors whose main activity is to invest in financial instruments<sup>6</sup>.
- (2) All other clients can be defined as a *retail* client and this category offers the highest level of MiFID protection.
- (3) For certain types of services, clients who meet the criteria set out in Regulation 111 of the MiFID Regulations, may be categorised as eligible counterparties. These include investment firms, credit institutions, insurance companies, UCITS funds and their management companies and pension funds and their management companies. The services concerned are executing orders on behalf of clients, dealing on own account and receiving and transmitting orders. Thus, for these services only, certain of the clients who qualify to be treated as professional clients in (1) above, may be treated as eligible counterparties.

Retail clients may be treated as professional on request and thereby waive some of the protections afforded under the conduct of business regime<sup>7</sup>. The firm must be able to show that the client possesses the market knowledge and experience to make investment decisions and understand the risks involved. The MiFID Regulations specify a test for this, which is that the client must meet **two of the following three criteria**. The client must have:

- a. carried out an average of 10 relevant transactions per quarter over the previous four quarters;
- b. a relevant portfolio exceeding €500,000;
- c. worked for at least one year in a relevant professional position in the financial sector.

In addition to the above assessment, the following procedure must be followed:

- ▶ the client must state in writing that he/she wishes to be treated as a professional client;
- ▶ the firm must give a clear written warning of the protections the client may lose; and
- ▶ the client must state in writing that he/she is aware of the consequences of losing such protections.

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<sup>3</sup> Professional client is required to meet the criteria laid down in Schedule 2 to the Regulations.

<sup>4</sup> Retail client is one who is not a professional client. (Regulation 3).

<sup>5</sup> Eligible counterparty defined in Regulation 111(1).

<sup>6</sup> Paragraph 2 of Schedule 2 of the Regulations.

<sup>7</sup> Paragraph 3 of Schedule 2 of the Regulations.

### **Question 1.2**

**My firm provides investment advice and portfolio management services to clients. I understand that there is a new client category under the MiFID Regulations called eligible counterparty aimed at more sophisticated clients. Will I be able to apply this client categorisation to my clients?**

#### *Answer 1.2*

The MiFID Regulations adopt two main categories of client, retail and professional. There is a separate and distinct third category called eligible counterparty for a limited range of business. As with the existing regulatory regime, the MiFID Regulations attach different regulatory protections to each of these categories. Thus, clients falling into the retail category, deemed to be less experienced, knowledgeable and sophisticated investors, will be afforded a higher level of protection than that afforded to investors in the professional or eligible counterparty categories.

The facility to categorise a client as an eligible counterparty is limited to the following specific types of business:

- ▶ executing orders on behalf of clients; and/or
- ▶ dealing on own account; and/or
- ▶ receiving and transmitting orders.

Since treatment of clients as eligible counterparties is restricted to the above circumstances, if a firm is providing the services of advising and portfolio management a client may not be treated as an eligible counterparty irrespective of how sophisticated he/she may be.

### **Question 1.3**

**What obligations do I have to an eligible counterparty?**

#### *Answer 1.3*

Due to the fact that eligible counterparties are the most experienced type of client they are afforded a lower level of protection under the MiFID Regulations. Specifically, the MiFID Regulations provide for the fact that where an investment firm is providing certain services to an eligible counterparty the general conduct of business and best execution obligations do not apply<sup>8</sup>. An investment firm which enters into a transaction with an eligible counterparty other than those entities that are considered eligible counterparties in accordance with Regulation 111(1) must obtain the express confirmation from the prospective counterparty, either in the form of a general agreement or on a transaction-by-transaction basis, that it agrees to be treated as an eligible counterparty.

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<sup>8</sup> Regulation 111(2).

#### **Question 1.4**

**How do I decide if a corporate client (such as a company or a trust) has "worked for at least one year in a relevant professional position in the financial sector?"**

#### *Answer 1.4*

You should consider the person or persons authorised to carry out transactions on behalf of your client – for example, your client company has a Chief Financial Officer with relevant experience and qualifications and the client's decisions are being made through the authority and expertise of the Chief Financial Officer.

Where a corporate client company has the benefit of expert advisers, you may wish to consider the advisers' experience in deciding the client categorisation. In this situation, you should be satisfied that the expert adviser's experience is relevant to the transactions or services envisaged, and that your client can use the advice received to understand the risks involved in its investment decisions.

#### **Question 1.5**

**Do I have to communicate MiFID categorisations to my clients?**

#### *Answer 1.5*

Customers that are new to the firm after 1 November 2007 as well as those customers whose categorisation has changed under the MiFID Regulations need to be notified of their categorisation.

In addition, clients who requested treatment as professional clients under existing Codes of Conduct and who will continue to be treated as professional clients under the MiFID Regulations must be informed about the conditions for the categorisation of clients, which are set out in Paragraph 3 of Schedule 2 of the MiFID Regulations.

#### **Question 1.6**

**Do I have to inform clients of the possibility of changing their MiFID categorisation?**

#### *Answer 1.6*

Yes. You should advise:

- ▶ retail clients that they may request a change to professional categorisation once they meet the necessary criteria;
- ▶ professional clients that they may request a change to retail categorisation or eligible counterparty categorisation;
- ▶ eligible counterparties that they may request a change to retail or professional categorisation.

You should also inform your clients of the procedures for, and of the main consequences of, such changes.

### **Question 1.7**

**A client is seeking increased protection through a change in categorisation (in general or with regard to a product or transaction). What must I do?**

#### *Answer 1.7*

This situation occurs when a professional client or eligible counterparty requests treatment as a retail client or when an eligible counterparty requests treatment as a professional client. In so doing, clients are exercising a right under the MiFID Regulations.

Your firm does not have to agree to the requests for recategorisation. You may provide the client with the reasons for the refusal, and options available to the client, though the MiFID Regulations do not oblige you to do so. You should retain good records of the request for categorisation change and the reasons for refusal, and pay particular attention to suitability and appropriateness checks in concluding any associated business.

### **Question 1.8**

**A client wants to "upgrade" his/her categorisation to gain access to business terms or services normally reserved for higher classes of clients which will decrease the level of protection afforded them. What should I do?**

#### *Answer 1.8*

Clients may seek upgraded status through a change in categorisation in general or with regard to a product or transaction. This may be to gain access to business terms or services normally reserved for other classes of clients, or to preserve their standing and reputation.

- ▶ If a retail client requests treatment as a professional client with regard to a product or transaction, you should confirm that the client meets the eligibility criteria with regard to that product or transaction and follow the procedure outlined in Question 1.1[3]; if not, you should refuse the request.
- ▶ If a retail client requests treatment as an eligible counterparty, you should always refuse the request.
- ▶ If a professional client, other than those listed in Regulation 111[1], requests treatment as an eligible counterparty, you should obtain express confirmation that the client agrees to be treated as an eligible counterparty, either in the form of a general agreement or on a transaction-by-transaction basis. A professional client who has been categorised as such in accordance with Paragraph 3 of Schedule 2, i.e., "clients who may be treated as professionals on request", may only be permitted to opt up to eligible counterparty status for those services for which he/she has been treated as a professional client.

Your firm does not have to agree to the requests and may decline for good reason. You may provide the client with the reasons for the refusal, and options available to the client, though the MiFID Regulations do not oblige you to do so.

### **Question 1.9**

**Can I accept client furnished information in order to categorise clients under the MiFID Regulations?**

#### *Answer 1.9*

Yes. A firm is permitted to take the information provided by the client, and can use this as the basis for its client categorisation, provided that the firm has acted reasonably in doing so. When considering the criteria for treating a retail client as a professional client, firms can take into account the fact that the client has developed experience through a business relationship with another firm. Of course, the firm should use its own sense of judgment, and if it comes to the firm's attention that certain information appears inconsistent or inaccurate the firm must take appropriate action. The firm should be able to rely on information provided by any other regulated investment firm. The firm may also rely on information provided by a third party acting on behalf of the client provided the firm has no reason to doubt the accuracy of the information.

### **Question 1.10**

**Do firms have an obligation to monitor that clients continue to meet the stated criteria?**

#### *Answer 1.10*

Retail clients do not require monitoring as they hold the highest level of protection afforded under the MiFID Regulations.

The MiFID Regulations require professional clients, including those who have requested treatment as eligible counterparties, to keep the firm informed of any change that could affect their categorisation. As a result, it is not necessary to monitor such clients to ensure they continue to satisfy the criteria. However, firms should draw clients' attention to this obligation in their terms of business and, if the firm becomes aware that the client no longer fulfils the criteria for treatment as a professional client, it must take appropriate action.

### **Question 1.11**

**Our firm's customers, both institutional and corporate, fit comfortably within the definition of professional client. May I categorise any of these clients as an eligible counterparty and what requirements must I fulfil?**

#### *Answer 1.11*

Yes. A client which meets the criteria of professional client may be considered and categorised as an eligible counterparty subject to written notification to the client of eligible counterparty status and, for clients other than those listed in Regulation 111(1), express confirmation of the client's agreement to be treated as an eligible counterparty. The client should also be advised of the right to request higher protection generally or on a product or transaction basis.

### **Question 1.12**

**Under the Code of Conduct for Investment Business Services of Credit Institutions, I automatically treated the following types of customers as professional clients:**

- ▶ **Companies with securities listed on any EEA regulated market**
- ▶ **Non-listed companies with called-up share capital or net assets of at least euro12.5m**
- ▶ **A partnership or unincorporated association with net assets of at least euro12.5m**

**Can I grandfather these clients to professional status under the MiFID Regulations?**

#### *Answer 1.12*

Entities that are automatically considered professional clients under existing Codes of Conduct and are also included in the categories of clients listed in Paragraph 2 of Schedule 2 of the MiFID Regulations can continue to be considered professional clients.

Entities that are automatically considered professional clients under existing Codes of Conduct but are not included in the categories of clients listed in Paragraph 2 of Schedule 2 of the MiFID Regulations cannot automatically be considered professional clients but must be subject to an assessment by the firm and meet the criteria set out in Paragraph 3 of Schedule 2 of the MiFID Regulations.

### **Question 1.13**

**Under the existing Codes of Conduct for Investment Business Services, certain individual clients opted up to professional client status in accordance with the procedures set out in those Codes. Can I treat these clients as professional clients under the MiFID regime?**

#### *Answer 1.13*

Clients who were granted treatment as a professional client in compliance with the existing Codes of Conduct for Investment Business Services may continue to be treated as professional clients under the MiFID Regulations, provided that this categorisation has been granted on the basis of an adequate assessment of the expertise, experience and knowledge of the client which gives reasonable assurance that the client is capable of making his/her own investment decisions and understands the risks involved. Such an assessment is a requirement under the existing Codes of Conduct.

Investment firms must inform such clients about the conditions established in the MiFID Regulations for the categorisation of clients, including the obligation on professional clients to advise the firm of any change that could affect their categorisation.

# SUITABILITY AND APPROPRIATENESS

## Suitability

Suitability tests are required to be conducted by an investment firm to ensure that its investment advice or its portfolio management services are suitable for a potential client (whether a retail or professional client).<sup>9</sup>

Firms must obtain sufficient information about the client to enable them to make an adequate and objective assessment of an investment's suitability. Suitability for these purposes must be based on the client's relevant experience, knowledge, financial situation and investment objectives.

Where a potential client does not provide the required information the investment firm should not recommend investment services or products to the potential client<sup>10</sup>.

## Appropriateness

Sufficient information about the client must be obtained by an investment firm to assess the client's experience and knowledge and ultimately to assess the appropriateness of the investment firm's investment services and activities for the client.

Sufficient information includes an assessment of the types of service and financial instrument with which the client is familiar, the nature, volume and frequency of the client's transactions and the client's level of education and profession<sup>11</sup>.

Investment firms are obliged to warn their client if they conclude that a particular investment service or product is inappropriate<sup>12</sup>. Where sufficient information is not forthcoming from a client the firm must warn the client that it cannot determine whether the service or product is appropriate<sup>13</sup>.

### Question 2.1

#### What is the difference between "Suitability" and "Appropriateness"?

##### Answer 2.1

"Suitability" must be determined where a firm provides investment advice or portfolio management services to a client. A firm may conclude that a product or transaction is suitable for a client where it reasonably determines:

- ▶ that the client is able to financially bear the investment risks (including actual losses or loss of access to funds) in the context of the investment objective/strategy of the client and the type of client;
- ▶ it meets the objectives of the client; and
- ▶ the client can understand the risks involved in the investment.

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<sup>9</sup> Regulation 94.

<sup>10</sup> Regulation 94(6).

<sup>11</sup> Regulation 94(9).

<sup>12</sup> Regulation 76(5).

<sup>13</sup> Regulation 76(6).

"Appropriateness" must be determined where providing services other than portfolio management and investment advice. However, when executing or receiving and transmitting orders in non-complex instruments at the initiative of the client, it is not necessary to determine appropriateness provided the firm has informed the client that it is not required to assess for suitability and that the firm complies with the conflicts of interest obligations<sup>14</sup>. A firm may conclude that a product is appropriate where it reasonably determines that the client understands the risks involved in the investment.

### **Question 2.2**

**Is there a list of the data I have to gather to determine suitability and appropriateness? Is there a standard form?**

#### *Answer 2.2*

As there are many potential investment services, and the appropriate information will vary by service and by client, the MiFID Regulations do not provide a single list of data items that must be collected. The MiFID Regulations do, however, list the types of information you should consider in determining suitability and appropriateness, and says that you should gather the necessary information in the context of the client type and service provided. The types of information required to assess suitability relate to the client's:

- ▶ knowledge and past experience
- ▶ financial situation
- ▶ investment objectives

The information required to assess appropriateness relates to the client's:

- ▶ knowledge and past experience

### **Question 2.3**

**What will need to be obtained in respect of past experience?**

#### *Answer 2.3*

The types of service, transaction and financial instrument with which your client is familiar and the nature, volume and frequency of such relevant transactions as well as the level of education and profession of your client, all form part of your client's experience. Firms may apply their own judgment as to the extent and level of detail that is necessary for the firm to satisfy its obligations in relation to the assessment of suitability or appropriateness.

It would be expected that a client's experience, if any, with your firm would be taken into account. You can accept a client's information on their past activity without requiring production of evidence such as statements of activity with other firms.

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<sup>14</sup> Regulation 99(1).

### **Question 2.4**

#### **What will need to be obtained in respect of education?**

##### *Answer 2.4*

The MiFID Regulations state that relevant information regarding the client's knowledge and experience includes level of education and profession. However, this information only needs to be obtained to the extent appropriate to the nature of the client, the nature and extent of the client's relationship with the firm, the client's general level of professional experience, the nature and extent of the service and the type of product or transaction, including their complexity and the risks involved. Firms can use their own judgement in relation to the extent of information that may be required to satisfy the firm's obligations.

### **Question 2.5**

#### **What will need to be obtained in respect of financial situation?**

##### *Answer 2.5*

The source and extent of a client's regular income, assets, investments and regular financial commitments are all types of financial information that may be relevant to MiFID products or services for a client.

Firms must obtain some financial information but can use their own judgement as to what information is relevant to the products or services under discussion.

### **Question 2.6**

#### **Is it necessary to have all of this information in one document, such as a fact-find?**

##### *Answer 2.6*

No. The information does not have to be in one document. The necessary information can be gleaned and stored in a variety of ways, once it is accessible and can be retrieved when required. For instance, the minutes of a series of meetings could form part of the Know Your Client information record.

### **Question 2.7**

#### **What are the consequences of non-provision of Know Your Client information?**

##### *Answer 2.7*

A firm will generally require some level of Know Your Client information to address other obligations, such as anti-money-laundering requirements. The extent to which you can provide MiFID services depends on the level of information you have about a client, and the services that the client requests.

#### **Investment advice and portfolio management**

The MiFID Regulations<sup>15</sup> set out the specific types of information required before the services of investment advice or portfolio management can be provided. If a client does not provide this information, your firm cannot recommend investment services or financial instruments. However, you may be able to provide such a client with other services, such as reception and transmission of orders.

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<sup>15</sup> Regulation 76 and 94.

## Execution and/or receipt and transmission of orders in non-complex instruments

### (Execution-only business)

Firms may provide services that only consist of execution and/or receipt and transmission of orders without obtaining Know Your Client information, as outlined in Answer 2.2 above, provided the following conditions are met:

- ▶ the service relates to non-complex instruments;
- ▶ it is provided at the initiative of the client;
- ▶ the client has been clearly informed that the firm is not required to assess suitability; and
- ▶ the firm complies with the conflicts of interest requirements.

### Other services

The firm must warn the client that the non-provision of sufficient information regarding his/her knowledge and experience will not allow the firm to determine whether the product or service is appropriate<sup>16</sup>.

### **Question 2.8**

**The MiFID Regulations detail certain criteria that a financial instrument must meet in order for it to be considered non-complex (in addition to those instruments included in Regulation 99). What should I do in order to classify an instrument as non-complex?**

### *Answer 2.8*

The MiFID Regulations state that in order for a financial instrument to be considered non-complex, it must meet the following criteria<sup>17</sup>:

- ▶ The instrument in question is not a derivative,
- ▶ The instrument is highly liquid,
- ▶ The instrument does not involve an actual or potential liability which exceeds the cost of acquiring the instrument, and
- ▶ Adequate information on the instrument is publicly available and easily comprehensible.

A firm must assess whether or not a financial instrument is non-complex in light of the above criteria. Any such decision should be well documented and contain the reasons for determining that the instrument meets the criteria set out in the MiFID Regulations. For example, shares that are listed on the Irish Enterprise Exchange (IEX) do not automatically fall within the scope of non-complex instruments as listed in Regulation 99. However, if any shares listed on IEX meet the criteria listed above, a firm may determine that these instruments are non-complex for the purpose of the MiFID Regulations. Similarly, if shares listed on the Alternative Investments Market (AIM) and shares listed on US regulated markets meet the criteria a firm may determine that these instruments are non-complex.

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<sup>16</sup> Regulation 76(5) and (6).

<sup>17</sup> Regulation 95.

### **Question 2.9**

**How do the obligations to perform suitability and appropriateness checks differ between retail and professional clients?**

*Answer 2.9*

#### **Assessment of suitability**

##### **Retail:**

As this category of client is afforded the highest level of protection, a firm must obtain all relevant information required by the MiFID Regulations depending upon the services offered.

##### **Professional:**

Some of the information required by the MiFID Regulations can be assumed in the case of professional clients, i.e.,

- ▶ When providing **investment advice or portfolio management services** to a professional client, a firm can assume that the client has the necessary level of knowledge and experience for the product or service for which the client has been categorised as professional.
  
- ▶ When providing **investment advice** to a client that automatically meets the criteria of a professional client (as defined in Paragraph 2 of Schedule 2 of the MiFID Regulations) a firm can also assume that the client is able to financially bear the risks in respect of the product recommended by the firm<sup>18</sup>.

The assumption that a client may financially bear the risks involved may never be made in the case of retail clients or for portfolio managed services to professional clients.

#### **Assessment of appropriateness**

##### **Retail:**

As this category of client is afforded the highest level of protection, a firm must obtain all relevant information required by the MiFID Regulations depending upon the services offered.

##### **Professional:**

A firm can assume a professional client has the necessary knowledge and experience to understand the risks involved in relation to a particular product, service or transaction<sup>19</sup>.

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<sup>18</sup> Regulation 94(3).

<sup>19</sup> Regulation 94(8).

### **Question 2.10**

**What other factors should I take into consideration when relying on my client's categorisation as a professional in determining the level of Know Your Client information required?**

#### *Answer 2.10*

In relying on your client's professional categorisation, you should ensure that the categorisation remains correct. For example:

1. If your professional client has used only non-complex instruments in the past and wants now to use complex instruments, you should ensure that the client still meets the criteria for *professional* categorisation with regard to these instruments. If not, your client may become a *retail* client for the purpose of these products or transactions.
2. If your professional client is trading in familiar instruments but significantly increases the volume or value of trades, you should ensure that the trading remains suitable in the light of the client's investment objectives.

### **Question 2.11**

**As regards the suitability and appropriateness obligations, can I rely on information already held for existing clients?**

#### *Answer 2.11*

Under the appropriateness test (applicable to all services except for investment advice, portfolio management or certain transactions in non-complex instruments) a service or instrument can be deemed to be appropriate for a client, if you have information showing that the client has previously used the service/instrument (i.e., prior to 1 November 2007)<sup>20</sup>.

However, under the suitability obligations (required in relation to investment advice or portfolio management) the firm is required to obtain the appropriate information for the client as set out in the MiFID Regulations.

### **Question 2.12**

**Does this Know Your Client information have to be gathered again from scratch?**

#### *Answer 2.12*

No. If you believe your existing Know Your Client information to be accurate and up to date, you can use it in suitability and appropriateness assessments. If you believe you require additional information to complete these assessments, you should gather it separately.

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<sup>20</sup> Recital 59 of MiFID Level II Implementing Directive.

### **Question 2.13**

**If a client employs a consultant or a professional advisor, whose remit it is to retain portfolio managers or seek investment advice (e.g., a pension fund employing a consultant, a company employing an accountant, or a personal client using the services of a regulated financial advisor) can a firm rely on the information provided by the consultant/advisor (even if the consultant is not regulated) for the suitability or appropriateness assessments?**

#### *Answer 2.13*

Where information, such as the Know Your Client information specified in Regulation 94, is provided by a third party on behalf of a client, a firm can rely on such information provided the firm has no reason to doubt its accuracy.

A firm can rely on a recommendation made by another investment firm.

In all other cases, firms must obtain the necessary information, as outlined in Regulation 94, either from the client or from a third party acting on behalf of the client, to enable the firm to recommend an investment service or financial instrument that is suitable.

Where a professional firm (such as a law firm, accountancy firm or actuarial consultant) refers a client to an investment firm for discretionary portfolio management services and the professional firm has suggested a certain strategy for the portfolio, it will generally be reasonable for the discretionary portfolio management firm to manage the portfolio in accordance with the instructions without being obliged to check whether the proposed strategy is suitable for the client. Of course, the investments recommended or decided upon by the investment firm in such circumstances must themselves be suitable in the context of that strategy.

Where a client is subject to legal restrictions on investment, as in the cases, for example, of trustees of a pension fund or credit unions, information in relation to such restrictions will be relevant when performing the assessment for suitability. A firm cannot assume that all legally permissible investments are suitable and must ensure that the proposed investment is suitable having given due consideration to the client's knowledge and experience, financial situation and investment objectives.

Of course, the circumstances will vary in individual cases and the Financial Regulator will take into account all of the relevant facts that are available, or that reasonably should have been available, to an investment firm when considering compliance with the obligations of suitability and appropriateness. It is not possible to prescribe precise steps for all given cases as the circumstances of each case may dictate or require differing consideration, and will depend on the facts of any given case.

### **Question 2.14**

**Can firms rely on existing client information and knowledge to meet the 'knowledge and experience' requirements of the MiFID suitability and appropriateness tests?**

#### *Answer 2.14*

Yes. Firms may rely on existing client information and knowledge for the purpose of meeting the 'knowledge and experience' requirement under suitability and appropriateness tests. Firms are not obliged to re-confirm this information as part of any fact-find exercise, provided they are satisfied that the information is sufficiently accurate and up to date for this purpose.

### **Question 2.15**

**Where appropriateness has been established for a client for given MiFID categories of investment services and/or financial instruments, is there any obligation to re-establish appropriateness for subsequent transactions in those same categories?**

#### *Answer 2.15*

There is no need to re-establish appropriateness for subsequent transactions within the same category of investment services and/or financial instruments, unless the client advises the firm of a material change to their circumstances which would impact on the firm's existing determination of appropriateness.

A firm may decide to establish appropriateness for certain product types at the start of the relationship so that the firm does not need to establish appropriateness for each new transaction in those product types.

### **Question 2.16**

**If a firm has obtained the information required to determine appropriateness, is the firm under an obligation to update this information where the client does not transact in a complex instrument immediately?**

#### *Answer 2.16*

The MiFID Regulations do not specify when the information should be sought prior to providing the service so firms need to decide this for themselves. However, where information has been obtained significantly in advance of the provision of the service, a firm may need to consider whether the information should be updated<sup>21</sup>.

### **Question 2.17**

**Where a firm determines, on the basis of sufficient information from the client, that a proposed transaction or service is not appropriate to that client, and having warned the client in the prescribed format, can the firm complete the transaction on the customer's instruction?**

#### *Answer 2.17*

Yes. Where a client requests the firm to proceed with a transaction and the firm has provided the required warning, it may proceed on the client's instruction.

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<sup>21</sup> Regulation 94(11).

# INFORMATION TO CLIENTS

Prior to making an investment decision, clients must receive adequate information to assist them in making an informed decision. For example, retail clients must receive general information about the investment firm and the services which it provides<sup>22</sup>. Clients must also receive sufficiently detailed information about the specific type of financial instrument<sup>23</sup> and information about the costs and charges involved<sup>24</sup>.

## **Question 3.1**

### **Initially what information should firms send to retail clients?**

#### *Answer 3.1*

One of the key changes introduced under MiFID is the significant increase in the volume of information which must be given to retail clients. As retail clients are provided with a greater amount of protection they are required to be provided with more detailed information in order to assist them in making their investment decisions. One of the new information requirements under the MiFID Regulations is the obligation to notify new clients and clients whose categorisation has changed of their client categorisation<sup>25</sup>. Other information requirements include providing retail clients with general information about your firm and its service<sup>26</sup>, information about the specific type of financial instrument, the terms of their agreement with you, the nature and risk of the product they are buying and the costs and charges that the retail client has to pay.

A table of the key information requirements under the MiFID Regulations for retail and professional clients is contained in Appendix 1. Please note that this table is provided to assist you in identifying your obligations and is not intended to be exhaustive.

## **Question 3.2**

### **Initially what information should firms send to professional clients?**

#### *Answer 3.2*

Professional clients are perceived as being more sophisticated investors. They are regarded as being equipped with the relevant knowledge, experience and expertise to take an investment decision and properly assess the risks that it incurs. Less detailed information is therefore required to be given to professional clients.

For more information, see tables in Appendix 1.

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<sup>22</sup> Regulation 82.

<sup>23</sup> Regulation 84.

<sup>24</sup> Regulation 92.

<sup>25</sup> Regulation 81(1).

<sup>26</sup> Regulation 82.

### **Question 3.3**

#### **What information do I need to provide to my existing clients under the MiFID Regulations?**

##### *Answer 3.3*

The information to be communicated to a firm's existing clients may vary depending on your client's categorisation and the services that the firm provides. However, in general a firm must be able to demonstrate that the following information has been provided to its existing clients. Industry practice may vary as to whether such information will be provided in a single communication or as a series of separate communications.

- ▶ Supplementary Terms of Business/Management Agreement
- ▶ Notification of client categorisation (where applicable)
- ▶ Order Execution Policy/Execution Policy as applicable (depending on whether the firm is an entity that executes client orders or transmits/places orders for execution)
- ▶ Summary of conflicts of interest policy to retail clients

Firms should be conscious that the obligation to provide information to its clients may overlap with other MiFID obligations such as record keeping. The Financial Regulator will draw up a list of minimum records that will assist investment firms in determining which records they will be required to maintain<sup>27</sup>.

### **Question 3.4**

#### **Post MiFID, what information do I need to send to new clients that are classified as eligible counterparties?**

##### *Answer 3.4*

The full conduct of business rules and the detailed information disclosure provisions do not apply to eligible counterparties. Under Regulation 81 of the MiFID Regulations a firm must only notify these clients of their categorisation as eligible counterparties and any rights which they may have to request a different categorisation. Eligible counterparties typically would include capital market participants such as investment firms and banks.

### **Question 3.5**

#### **Must I send all my information to my client by post? Can I provide information by another means, for example, directing him/her to a webpage?**

##### *Answer 3.5*

The MiFID Regulations require certain information to be provided in a durable medium. This may include provision via a website where the website qualifies as a durable medium according to the criteria in the MiFID Regulations<sup>28</sup>.

The MiFID Regulations also allow some information to be provided by means of a website that does not qualify as a durable medium, as long as the website satisfies certain other criteria<sup>29</sup>.

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<sup>27</sup> Regulation 40(5).

<sup>28</sup> Regulation 3.

<sup>29</sup> Regulation 77(2).

Information that must be provided in a durable medium includes information about conflicts of interest policy, information concerning client categorisation, and periodic statements. Information that may be provided by means of a website (where that does not constitute a durable medium) includes information to retail clients about the firm and its services, financial instruments and execution policy.

A durable medium is defined as "any instrument which

- a) enables a client to store information addressed personally to that client in a way accessible for future reference and for a period of time adequate for the purposes of the information, and
- b) allows the unchanged reproduction of the information stored".

Where information must be provided in a durable medium, it may be provided in a durable medium other than paper if that medium is appropriate and if the client, when offered a choice between paper and that other medium, specifically chooses that medium.

Where information may be provided by means of a website and that information is not addressed personally to the client, firms must ensure that this is an appropriate medium in the context of the business to be carried out. A firm can electronically notify and direct clients to a relevant website address. However, clients must specifically consent to receive the information in this manner and the information has to be up to date and continuously available on the webpage to ensure that the client may access it.

### **Question 3.6**

#### **When should information be given?**

#### *Answer 3.6*

Retail clients must be given adequate information before they make an investment decision, to enable them to make a decision on an informed basis<sup>30</sup>. As retail clients are regarded as being less experienced they are given more detailed information. They must also be given such information 'in good time', before the provision of services so that they have sufficient opportunity to read and understand the specific information provided before taking an investment decision. Industry practice will vary as to what 'in good time' will entail, depending of course on the nature of the product and the client and what is reasonable in the circumstances.

On occasion, the nature of the transaction may require flexibility in the timing of the provision of information. An investment firm may provide the required information after a contract has been concluded in limited circumstances. Typically, this would occur where a client has specifically requested that the contract be concluded via electronic means. The use of distance communication may prevent the firm from providing the information at an earlier stage<sup>31</sup>.

For example where a client wants to buy shares immediately in a listed company on an execution-only basis, there is no requirement for a firm to wait until a certain period has elapsed in between providing information to the client and trading for the client. However, this approach may not be appropriate in all cases and is dependent upon the nature of the product and service being offered by the firm. It is up to each firm to take a reasonable approach as to the appropriate interpretation of this requirement.

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<sup>30</sup> Regulation 81.

<sup>31</sup> Regulation 81(7)(b)(i).

### **Question 3.7**

**Must I change my advertising practices under the MiFID Regulations? What will I be required to do? Does it only apply to retail clients?**

#### *Answer 3.7*

The MiFID Regulations provide that any marketing communications should be clearly identified as such<sup>32</sup>. Although advertising is not an investment or ancillary service under the MiFID Regulations, firms must be careful to ensure that the content of its advertising complies with the requirement that information must be fair, clear and not misleading.

An investment firm is under an obligation to act in the best interests of its clients<sup>33</sup>. Regulation 76(2)(a) provides that: "All information, including but not limited to marketing communications, addressed by an investment firm to clients or potential clients is fair, clear and not misleading"<sup>34</sup>.

Clients in this instance, means all clients (including potential clients) and not merely retail clients. However, there are specific requirements in place in relation to the provision of marketing communications to retail clients<sup>35</sup>. Many of these requirements should already be familiar to firms from existing legislation, codes and industry practice. Regulation 152(1) provides for certain restrictions in relation to advertising whereby firms should not advertise for services where the provision of such services would be in breach of Regulation 7, i.e., a firm advertises the provision of services for which it does not hold the appropriate authorisation under the MiFID Regulations. A due diligence exercise should be conducted to review existing business practices with respect to advertising and sale of products and services as MiFID provisions have higher level requirements than those under the ISD.

### **Question 3.8**

**Our firm transacts both MiFID and non-MiFID business. Does this mean that we should have separate "Terms of Business" documents?**

#### *Answer 3.8*

It is not necessary to have separate "Terms of Business" documents given the common areas which exist under the MiFID Regulations and the Consumer Protection Code. A single Terms of Business document must meet the relevant requirements of both the MiFID Regulations and the Consumer Protection Code.

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<sup>32</sup> Regulation 76(2)(b).

<sup>33</sup> Regulation 76(1).

<sup>34</sup> Regulation 76(2).

<sup>35</sup> Regulation 80.

### Question 3.9

**In general what types of information should I consider providing to my clients prior to the provision of MiFID services?**

#### Answer 3.9

This will depend both upon the client's categorisation and the services provided. In general, prior to the provision of MiFID services a firm should provide the following information to retail and professional clients:

Content	Retail	Professional
Written agreement <sup>36</sup>	✓	N/A
Inducements and fees paid to third parties <sup>37</sup>	✓	✓
Client's categorisation under MiFID <sup>38</sup>	✓	✓
The firm and services to be provided <sup>39</sup>	✓	N/A
Nature and risks of financial instruments <sup>40</sup>	✓	✓
Safeguarding of clients instruments <sup>41</sup>	✓	✓
Costs and associated charges <sup>42</sup>	✓	N/A
Conflicts of Interest: - Disclosure of conflicts <sup>43</sup> - Description of policy <sup>44</sup>	✓ ✓	✓ N/A
Order execution policy <sup>45</sup>	✓	✓

A more detailed table has been included at Appendix 1 to assist firms in understanding their obligations under the MiFID Regulations in respect of the provision of information to clients.

### Question 3.10

**I wish to send promotional material related to a MiFID complex instrument to my clients. Do I have to assess appropriateness prior to provision of the material?**

#### Answer 3.10

No. The promotional material must meet the obligations detailed in Regulation 80. The appropriateness test must be conducted prior to the completion of the transaction or entering into the service, not prior to sending the promotional material itself. A firm will need to consider whether promotional material (in complex or non-complex instruments) is personalised as this may constitute investment advice.

<sup>36</sup> Regulation 94(12).

<sup>37</sup> Regulation 78(2).

<sup>38</sup> Regulation 81.

<sup>39</sup> Regulation 82 and 83.

<sup>40</sup> Regulation 84.

<sup>41</sup> See separate Financial Regulator's Client Money Requirements.

<sup>42</sup> Regulation 92.

<sup>43</sup> Regulation 74(2).

<sup>44</sup> Regulation 82(h).

<sup>45</sup> Specific Best Execution obligations vary depending on whether the firm is "executing orders" or providing "portfolio management/RTO" services.

### **Question 3.11**

**I provide portfolio management services managing portfolios in accordance with mandates given by clients on a discretionary and non-discretionary basis. Do the MiFID Regulations make a distinction in respect of the information that I am required to provide the client about the nature of the agreement between us?**

#### *Answer 3.11*

Unlike the present Codes of Conduct for investment services, the MiFID Regulations do not distinguish between discretionary and non-discretionary clients in relation to the provision of a Terms of Business or Investment Management Agreement document. Rather the requirements under the MiFID Regulations are set out on the basis of whether the client is a retail or professional client and the nature of the service being provided.

Thus, the MiFID Regulations do not expressly require firms to provide client agreements to professional clients. Nor do the MiFID Regulations expressly require an agreement in situations where the firm is only providing investment advice, although in both instances a firm may choose to do so for commercial reasons.

The MiFID Regulations require firms that provide services other than investment advice to retail clients to provide them with a written agreement setting out the essential rights and obligations of the firm and the client. They also include requirements to retain records of documents that set out the terms on which the firm will provide services to its clients for at least the duration of the relationship and in any event for at least five years.

### **Question 3.12**

**What should firms do, when providing the service of portfolio management, to establish an appropriate method of evaluation and comparison to enable the client to assess the firm's performance?**

#### *Answer 3.12*

Where possible, a range of appropriate indices should be used to benchmark portfolios. In the case of complex instruments, an appropriate method of evaluation should be agreed in advance with each individual client.

# REPORTING TO CLIENTS

Clients have a right to be informed on a regular basis and in sufficient detail of the type of service that is provided to them. There are three main reporting requirements to clients under the MiFID Regulations, namely reporting obligations in the case of portfolio management<sup>46</sup>, reporting obligations other than portfolio management<sup>47</sup> and reporting obligations relating to financial instruments or funds belonging to clients<sup>48</sup>.

Firms should be advised that the reporting obligations in relation to client funds are outside the scope of this paper. Accordingly, firms should familiarise themselves with the Financial Regulator's Client Money Requirements.

## **Question 4.1**

**What ongoing client reporting obligations do I have to my clients under the MiFID Regulations?**

### *Answer 4.1*

Reporting obligations are set out in Regulations 96 and 101. The obligations differ according to client categorisation (i.e., whether the client is a retail or professional client) and type of service provided (i.e., whether the service being provided to the client is portfolio management or the service relates to the execution of clients orders other than for portfolio management).

### **Execution of Orders other than for Portfolio Management**

Where the service being provided is the "execution of orders other than for portfolio management", the primary obligation is to provide contract notes in respect of each transaction. If the service is provided to retail clients, the contract notes must contain all of the information specified in Regulation 96(6) [which is set out in Appendix 2] and they must be sent to the client within a specified time period (as soon as possible and no later than the first business day following execution or receipt of the confirmation from a third party). If the service is being provided to professional clients then the firm must provide the client, in a durable medium, with the essential information concerning the execution of the order.

### **Portfolio Management**

If the service being provided to the client is "portfolio management" then the primary obligation is to provide the client with a periodic statement in a durable medium. The content and frequency is not prescriptive in the case of professional clients and industry practice may vary.

In the case of retail clients the periodic statement must include the information listed in Regulation 96(10). If the retail client has elected to receive contract notes containing the information required by Regulation 96(6) on a transaction-by-transaction basis, this information does not have to be provided again in the periodic statement. For example, a firm which currently provides its clients with contract notes may decide to continue providing information about executed transactions to its portfolio managed clients in this way rather than in periodic statements.

Regulation 96(11) requires that periodic statements must be provided to retail clients at a minimum of once every 6 months. However, where requested the periodic statement must be provided once every 3 months<sup>49</sup> and a firm must inform its retail clients that they have the right to make this request.

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<sup>46</sup> Regulation 96(9) to (17).

<sup>47</sup> Regulation 96(1) to (8).

<sup>48</sup> Regulation 96(18) to (22).

<sup>49</sup> Regulation 96(11)(a).

If the retail client has elected to receive contract notes containing the information required under Regulation 96(6) on a transaction-by-transaction basis and the client does not trade in derivatives, the periodic statement need only be provided once every 12 months. However, if the retail client authorises the firm to manage a leveraged portfolio in its agreement then the periodic statement must be provided once a month.

#### **Question 4.2**

**I provide a service in respect of the execution of orders other than for portfolio management and I provide my retail clients with contract notes containing the information required under Regulation 96(6). Do I also have an obligation under the MiFID Regulations to send my clients a periodic statement?**

#### *Answer 4.2*

No. There is no obligation under the MiFID Regulations to send a periodic statement to clients where the service provided is in respect of the carrying out of an order other than for portfolio management. However, where the firm holds client financial instruments or funds there are additional periodic reporting requirements. These are contained in the Financial Regulator's Client Money Requirements.

#### **Question 4.3**

**My firm provides portfolio management services. Do I have an obligation under the MiFID Regulations to send my clients contract notes?**

#### *Answer 4.3*

No. However, your clients may elect to be provided with contract notes. If a retail client elects to be provided with contract notes, they must include the information required under Regulation 96(6). The contract notes must be provided within the timescales stipulated in the MiFID Regulations. If a professional client elects to receive contract notes on a transaction-by-transaction basis, they must be provided promptly and contain the essential information concerning the transaction in a durable medium.

#### **Question 4.4**

**The MiFID Regulations require that information regarding fees and charges must be detailed in the periodic statement, including details in relation to the costs associated with execution. I currently provide my clients with detailed information regarding costs such as ITP levy, stamp duty and commissions in the contract note. Do I need to repeat this information in the periodic statement?**

#### *Answer 4.4*

No. Where this detailed information has already been provided to the client there is no need to provide it again as this would be a duplication of information already provided. Instead, a firm should detail any costs and charges in the periodic statement not previously provided to the client and include an explanation that a more detailed breakdown of charges had already been provided on the individual contract notes.

#### **Question 4.5**

**I manage leveraged portfolios on behalf of my retail clients; does this affect the frequency of reporting?**

##### *Answer 4.5*

Yes. The MiFID Regulations require that where a retail portfolio managed client holds a leveraged portfolio the periodic statement must be provided monthly.

#### **Question 4.6**

**A number of our retail clients have authorised the firm in their agreements to manage a leveraged portfolio on their behalf. However, while we have the discretion to manage their portfolios on a leveraged basis, we have not as yet availed of this discretion. Do we have to provide these clients with a monthly statement or can we provide a six-monthly statement until such time as we avail of our discretion to use leverage?**

##### *Answer 4.6*

Where an agreement between a firm and a retail client authorises a leveraged portfolio but the firm has not yet exercised that authorisation, the periodic statement may be provided once every six months provided the firm has strict controls in place and:

- ▶ the client is notified in advance that the firm intends to exercise the authorisation, and
- ▶ periodic statements are provided monthly once the authorisation has been exercised.

#### **Question 4.7**

**I currently send my portfolio managed clients contract notes. What additional reporting obligations do I have under the MiFID Regulations?**

##### *Answer 4.7*

In the case of retail portfolio managed clients you also have an obligation to send the client a periodic statement containing the information required under Regulation 96(10). If the contract notes contain all of the information listed in Regulation 96(6), are provided in accordance with Regulation 96(1)(b), and do not relate to derivatives, then the periodic statement must be provided at least once every 12 months. Otherwise, it must be provided once every six months although the client may request a statement every three months. However, if the portfolio is leveraged, the retail client must be sent a monthly statement irrespective of whether or not he has been provided with contract notes on a transaction-by-transaction basis.

If the firm holds financial instruments or funds on behalf of its clients, then the firm has additional reporting obligations under the Financial Regulator's Client Money Requirements. These obligations apply to professional clients as well as retail clients.

#### **Question 4.8**

**I currently send my execution-only clients contract notes. What additional reporting obligations do I have under the MIFID Regulations?**

#### *Answer 4.8*

If the firm holds financial instruments or funds on behalf of its clients, the firm has additional reporting obligations under the Financial Regulator's Client Money Requirements. These obligations apply to professional clients as well as retail clients.

#### **Question 4.9**

**I currently provide my clients with periodic statements/contract notes in electronic form; can I continue to provide the information in electronic form under the MiFID Regulations?**

#### *Answer 4.9*

Yes. The MiFID Regulations permit the provision of information in a durable medium other than paper where the provision of the information in that medium is appropriate, for example, where the client has an e-mail address and where the client has chosen to receive the information in that medium. If you currently provide your clients with this information electronically then you must be satisfied that the client has already chosen this method of communication.

#### **Question 4.10**

**If a client advises in writing that he/she does not wish to receive contract notes or wishes to receive them on a periodic basis only, can I disregard the MiFID requirements in respect of contract notes in order to comply with my client's request?**

#### *Answer 4.10*

Under the MiFID Regulations, where a firm is executing transactions other than for portfolio management, essential information must be provided promptly to professional clients and in the case of retail clients the detailed information listed in Regulation 96(6) must be sent no later than the first business day following execution (if the confirmation is received by the investment firm from a third party, no later than the first business day following receipt of the confirmation from the third party). There is no scope or flexibility to agree a different timescale with your clients.

If your client is a portfolio management client there is no requirement to provide contract notes. However, clients may elect to receive information from a portfolio manager on a transaction-by-transaction basis and if a retail client opts to receive contract notes he/she must be provided with the detail required under Regulation 96(6) within the timeframe set out above.

#### **Question 4.11**

**I provide services to retail clients in respect of the receipt and transmission of orders in collective investment schemes only. Do I have an obligation under the MiFID Regulations to provide a contract note no later than the first business day following execution?**

#### *Answer 4.11*

Under the MiFID Regulations retail client orders for units or shares in collective investment schemes which are executed periodically must comply with the detailed information requirements in respect of contract notes either upon every execution or at least once every six months.

# INVESTMENT RESEARCH

## Question 5.1

**Investment research and marketing material are subject to certain requirements under the MiFID Regulations. The Market Abuse Regulations (MAD Regulations) also impose certain requirements on investment recommendations. How do the MiFID and MAD Regulations interact with each other?**

### Answer 5.1

Regulation 155 of the MiFID Regulations applies where a firm produces *investment research*<sup>50</sup> that is intended or is likely to be subsequently disseminated to the public. *Investment research* is a sub-category of *recommendations* as defined in the MAD Regulations. It is intended that the MiFID and MAD Regulations will operate together and therefore both sets of rules must be considered by the firm and applied where relevant. It should be noted that Part 3 of the MAD Regulations applies only to recommendations issued in respect of financial instruments admitted to trading on an EU regulated market (or for which such an admission has been sought) whereas the MiFID Regulations apply to investment research issued in respect of financial instruments (regardless of whether admitted to trading or not). For the purposes of the MiFID Regulations, material will not fall within the scope of *investment research* unless it is clearly labelled as objective and does not constitute investment advice.

*Recommendations* within the meaning of Part 3 of the MAD Regulations (which do not meet the requirements of *investment research* in the MiFID Regulations) will be treated as marketing material for the purposes of the MiFID Regulations and therefore they must be clearly identifiable as marketing material and contain a clear statement that the material has not been produced in line with the MiFID requirements designed to ensure objectivity. A firm must be aware of its obligations under the MiFID Regulations in respect of the management of conflicts of interest<sup>51</sup> and if the *recommendation* is distributed to retail clients there are specific requirements to ensure that the information is fair, clear and not misleading<sup>52</sup>.

## Question 5.2

**How do I decide whether a piece of written material constitutes investment research, in order to apply the related obligations<sup>53</sup>?**

### Answer 5.2

The term *investment research* is designed to capture research material that contains a substantive analysis of one or more financial instruments. The publication of general material, for example, the analysis of a sector or commentary on the economy is not likely to fall within the definition of *investment research*. In order to determine whether more generic material falls within the definition of *investment research* a firm should consider whether the material is likely to influence an investor in respect of a particular financial instrument (i.e., is an investor likely to trade on the basis of the material?).

The issuance of sales notes and short term trading ideas internally within a firm and/or expressed to clients, which are not likely to become publicly available, do not fall within the definition of a *recommendation*<sup>54</sup> (and therefore do not constitute *investment research*).

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<sup>50</sup> Regulation 151.

<sup>51</sup> Regulation 74 and 75.

<sup>52</sup> Regulation 76(2) and 80.

<sup>53</sup> Regulation 154(2) and 155.

<sup>54</sup> Recital 3; Commission Directive 2003/125/EC.

### Question 5.3

**What are the requirements contained in the MiFID Regulations where a firm produces "investment research"?**

#### Answer 5.3

If your firm produces *objective investment research* publications, there are specific obligations that apply which are outlined in Regulation 155. In addition to these specific obligations, consideration must be given to the firm's general obligations in respect of the management of conflicts of interest<sup>55</sup> and if the *investment research* is available to retail clients there are specific requirements to ensure that the information is fair, clear and not misleading<sup>56</sup>. If your firm produces what is commonly referred to as *non-objective investment research*, this will be treated as a marketing communication for the purposes of the MiFID Regulations.

### Question 5.4

**The MiFID Regulations state that a financial analyst and other relevant person must not trade in a financial instrument where they have knowledge as to the likely timing or content of investment research<sup>57</sup>. Does this always prevent employees from dealing in financial instruments where they possess such knowledge?**

#### Answer 5.4

The obligation contained in Regulation 155(2)(a) is there to ensure that financial analysts and relevant persons may not trade in financial instruments in the event that they have knowledge as to the **content** or **timing** of research which cannot be readily inferred from publicly available information until the recipients or intended recipients of the research have had a reasonable opportunity to act on the research.

The rule relates to exclusive knowledge and not to market knowledge or general market expectations as to the timing or content of research. For example when considering whether a relevant person has knowledge as to the timing of research, the market may expect the publication of research in line with broker regular reporting dates or the financial reporting dates of a company. The rule does not prevent relevant persons of the firm from dealing merely because they expect (on the basis of generally available information) a firm's analyst to produce a piece of research which coincides with such dates.

### Question 5.5

**How will the prohibition on dealing ahead of research impact upon my market-making obligations?**

#### Answer 5.5

The MiFID Regulations provide for the fact that a firm can trade in the ordinary course of its market-making activities. A firm may also trade on behalf of another person where executing an unsolicited client order<sup>58</sup>.

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<sup>55</sup> Regulation 74 and 75.

<sup>56</sup> Regulation 76(2) and 80.

<sup>57</sup> Regulation 155(2)(a).

<sup>58</sup> Regulation 155(2)(a)(ii).

## Appendix 1

Information to be Provided to Clients prior to Provision of Service		
Written Agreement	Retail	Professional
<p>A firm that provides an investment service other than investment advice shall enter into a written basic agreement in a durable medium with the client setting out the rights and obligations of the firm and the client.</p> <p><i>Regulation 94(12)</i></p>	✓	N/A
Inducements		
<p>When applicable, firms must disclose in summary form the essential terms of the arrangements it has in place regarding a fee, commission or non-monetary benefit. The firm must provide further details on request.</p> <p><i>Regulation 78(2)</i></p>	✓	✓
Client Categorisation		
<ul style="list-style-type: none"> <li>▶ Firms must notify new clients, and existing clients that the firm has newly categorised under the MiFID Regulations, of their categorisations as a retail client, professional client or eligible counterparty.</li> <li>▶ Firms must inform clients in a durable medium about any right that client has to request a different categorisation and about any limitations to the level of client protection that would entail.</li> </ul> <p><i>Regulation 81</i></p>	✓	✓
Information about the Firm and Services to be Provided		
<p>Firms must provide retail clients or potential retail clients with the information listed in Regulation 82, including:</p> <ul style="list-style-type: none"> <li>▶ General information about the firm (name, address, method of communication, authorisation, etc).</li> <li>▶ Nature and frequency of reports on performance of service.</li> <li>▶ Details of any relevant investor compensation scheme.</li> </ul> <p><i>Regulation 82</i></p>	✓	N/A
<p>When providing the service of portfolio management, a firm must provide retail clients or potential retail clients with the information listed in Regulation 83(2) including details of any delegation of the discretionary management of all or part of the portfolio and a specification of any benchmark against which the performance of the portfolio will be compared.</p> <p><i>Regulation 83</i></p>	✓	N/A

<b>Information to be Provided to Clients prior to Provision of Service</b>		
<b>Information about Financial Instruments</b>	<b>Retail</b>	<b>Professional</b>
Description of the nature and risks of financial instruments taking into account the client's categorisation as either retail or professional. <i>Regulation 84</i>	✓	✓
<b>Safeguarding of Client Financial Instruments</b>		
Where an investment firms holds financial instruments or funds belonging to a retail client, or potential retail client, the firm shall provide them with certain information regarding the safeguarding of client instruments (refer also to the Financial Regulator Client Money Requirements for the relevant requirements). <i>Regulations 88 to 91</i>	✓	N/A
Professional clients must receive in good time certain specific information related to the safeguarding of client financial instruments or client funds (refer also to the Financial Regulator Client Money Requirements for the relevant requirements). <i>Regulations 89/90</i>	N/A	✓
<b>Conflicts of Interest</b>		
Where there is a potential risk of damage to client interests, the firm must disclose the general nature and/or sources of conflicts of interest to a client before undertaking business on the client's behalf. <i>Regulation 74(2)</i>	✓	✓
In the case of retail clients a description of the conflicts of interest policy must be provided which may be in summary form. <i>Regulation 82(h)</i>	✓	N/A
<b>Costs and Associated Charges</b>		
Detailed information in respect of the costs and associated charges of MiFID services provided by the firm. <i>Regulation 92</i>	✓	N/A

Information to be Provided to Clients prior to Provision of Service		
Best Execution	Retail	Professional
<p>Appropriate information on the firm's execution policy must be provided to clients. The nature of the information to be provided will vary depending on whether the firm is deemed to be executing orders or simply receiving and transmitting orders for execution by another entity. <i>Regulations 98(3)(d) and 106(3)</i></p>	✓	✓
<p>Where the firm is providing portfolio management services and/or receiving and transmitting orders, retail clients must be provided with the information listed in Regulation 98(6) in good time prior to the provision of services. <i>Regulation 98(6)</i></p>	✓	N/A
<p>Firms that execute client orders must obtain prior consent from clients to their order execution policy and must obtain express prior consent if an order is executed outside a regulated market or MTF. <i>Regulations 106(3)(c) and 106(4)</i></p>	✓	✓

## Appendix 2

<b>Contract Notes</b>		
<b>Orders Other Than for Portfolio Management</b>	<b>Retail</b>	<b>Professional</b>
An investment firm must promptly provide the client, in a durable medium, with the essential information concerning the execution of that order.	✓	✓
In the case of a retail client, the firm must send the client a notice in a durable medium confirming execution of the order (i) as soon as possible and no later than the first business day following execution, or (ii) if the confirmation is received by the investment firm from a third party, no later than the first business day following receipt of the confirmation from the third party.	✓	N/A
Contract Notes for retail clients must contain <sup>59</sup> (a) the reporting firm identification; (b) the name or other designation of the client; (c) the trading day; (d) the trading time; (e) the type of the order; (f) the venue identification; (g) the instrument identification; (h) the buy/sell indicator; (i) the nature of the order if other than buy/sell; (j) the quantity; (k) the unit price; (l) the total consideration; (m) a total sum of the commissions and expenses charged and, where the retail client so requests, an itemised breakdown; (n) the client's responsibilities in relation to the settlement of the transaction, including the time limit for payment or delivery as well as the appropriate account details where these details and responsibilities have not previously been notified to the client; (o) if the client's counterparty was the investment firm itself or any person in the investment firm's group or another client of the investment firm, the fact that this was the case unless the order was executed through a trading system that facilitates anonymous trading.	✓	N/A
<b>Portfolio Management</b>		
If a client elects to receive contract notes on a transaction-by-transaction basis, they must comply with requirements set out above including in the case of retail clients the timescales for remitting the contract note and contents requirements set out in Regulation 96(6).	✓	✓

<sup>59</sup> Regulation 96(6).

## Appendix 3

Periodic Statements		
Portfolio Management Services Only	Retail	Professional
An investment firm which provides the service of portfolio management to clients shall provide each of them with a periodic statement in a durable medium of the portfolio management activities carried out on behalf of that client, unless such a statement is provided by another person.	✓	✓
Periodic reports for retail clients must contain certain specified information contained in Regulation 96(10).	✓	N/A
In the case of retail clients, the periodic statement must be provided once every 6 months, except in the following cases: <ul style="list-style-type: none"> <li>▶ where the client so requests, the periodic statement must be provided every 3 months (Firms must inform retail clients that they have the right to make requests for reports to be provided every 3 months);</li> <li>▶ where the client has elected to receive contract notes containing all of the information listed in 96(6), the periodic statement can be provided on a 12 monthly basis. <b>N.B.</b> This exception does not apply in the case of transactions in complex instruments.</li> <li>▶ where the agreement between an investment firm and a retail client for a portfolio management service authorises a leveraged portfolio, the periodic statement must be provided at least once a month.</li> </ul>	✓	N/A
All Services		
Where an investment firm - <ul style="list-style-type: none"> <li>(a) provides portfolio management transactions for retail clients, or</li> <li>(b) operates retail client accounts that include an uncovered open position in a contingent liability transaction,</li> </ul> the firm shall report to the retail client any losses exceeding any predetermined threshold, agreed between the firm and the client, no later than <ul style="list-style-type: none"> <li>(i) the end of the business day in which the threshold is exceeded, or</li> <li>(ii) in a case where the threshold is exceeded on a non-business day, the close of the next business day.</li> </ul>	✓	N/A
Where an investment firm holds client financial instruments or client funds there are specific reporting requirements including a list of items that must be included in such reports. Firms should refer to the Financial Regulator's Client Money Requirements for details.	✓	✓



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