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The AMF publishes the summary of its short thematic inspections on the suitability of the financial instruments recommended to retail clients

The Autorité des Marchés Financiers analysed the methods for assessing the suitability of recommended financial instruments for the personal circumstances of retail clients in four institutions offering investment advisory services.

When the Markets in Financial Instruments Directive was revised (MiFID II), the investor protection aspect was reinforced by adding requirements concerning the assessment of their personal circumstances. Under MiFID I, a financial institution offering an investment advisory service had to enquire about information on the client's knowledge and experience, objectives and financial situation. The institution also had to perform a suitability test.

Since 3 January 2018 (the date of the entry into force of MiFID II), the collection of information concerning investors' objectives must also include an assessment of their risk tolerance. The information on the client's financial situation must also make it possible to assess their ability to bear losses. Lastly, prior to the transaction, the institution must submit to the client a suitability report specifying the advice given and the extent to which the transaction corresponds to their preferences and investment objectives.

An assessment of compliance with the provisions of MiFID II

Via a series of short thematic "SPOT" inspections (Supervision des Pratiques Opérationnelle et Thématique - operational and thematic supervision of practices) performed last year, the AMF examined the suitability assessment procedures of four inspected institutions. Its investigations covered the period from 3 January 2018 to 16 March 2020.

During these inspections, the AMF focused on:

- the scope and procedures for collecting client information;
- the procedures for implementation of the suitability test;
- verification by the institution of the existence of other equivalent financial instruments which could correspond to the client's profile, taking into consideration their cost and complexity;
- the submission and content of the suitability report summarising the advice given to the client; and
- the control system on the topic of suitability.

In its summary document, while the AMF stresses numerous good practices, it still notes significant shortcomings in complying with the required due diligence regarding suitability.

Collection of information on the client and assessment of their knowledge

Paragraph Regarding collection of the information necessary for an assessment of the ability to bear losses, two institutions estimated this by means of theoretical situation simulations assessing the client's attitude to risk. This methodology reflects a confusion with the concept of risk tolerance.

Among the good practices observed, the summary stresses the fact of providing for measures allowing the client to increase their knowledge concerning a financial instrument while restricting investment in it, temporarily and in the client's interest. The use of scenarios presenting the risk/return ratio, or again the assessment of the client's reaction to a potential market downturn in order to assess their risk tolerance, were also highlighted.

The collection of information on the client's situation is essential in order to provide appropriate advice. It is therefore incumbent on institutions to adopt an instructive approach, explaining to clients the objectives aimed at by the completion of the questionnaire and, more generally, by the suitability assessment.

The suitability test

To assess the institutions' implementation of the suitability test, the regulator tested a sample of transactions performed. In this context, cases of unsuitability were noted. Some of these cases of unsuitability can be explained by late implementation of the MiFID II provisions in the model questionnaires and/or tools used to assess clients.

The suitability report

Although the four institutions do indeed have procedures concerning the submission of a suitability report and the long-term monitoring of suitability, the summary shows that two of them did not always submit this report. Moreover, certain institutions provided no explanation concerning the appropriateness of the investment recommendation for the client's circumstances, considering that this obligation was implicitly fulfilled by carrying out the suitability test. Good practices noted by the regulator include the use of different model suitability reports depending on the type of recommendation issued (investment, arbitrage or holding propositions).

The compliance control system

Regarding the compliance control system, the summary underlines an insufficient coverage of the scope of suitability, for two entities. This can be explained by a failure to verify the quality of the recommendations issued via the IT tool. The existence of a tool dedicated to the recording and traceability of the control results and the possibility of adapting control points marginally depending on the risks identified by the institution, without ever making the control level less demanding, constitute good practices.

About the AMF

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