

# MFSA

---

## MALTA FINANCIAL SERVICES AUTHORITY

### **Circular addressed to the investment services industry regarding ESMA opinion on MiFID practices for firms selling complex products**

The European Markets and Securities Authority (ESMA) has recently issued an opinion on the marketing and sale of complex products, in particular to the retail investors category.

By way of background, securities regulators, including the MFSA, are concerned that alternative and more sophisticated investment strategies are being made available to retail clients. This trend poses certain risks for retail investors as they may not be able to understand the risks involved.

ESMA has published an opinion which sets out the expectations of securities regulators in this area. The opinion can be accessed as follows: [https://www.mfsa.com.mt/pages/readfile.aspx?f=/files/LegislationRegulation/regulation/securities/MiFID/ipisc\\_complex\\_products\\_-\\_opinion.pdf](https://www.mfsa.com.mt/pages/readfile.aspx?f=/files/LegislationRegulation/regulation/securities/MiFID/ipisc_complex_products_-_opinion.pdf)

The underlying objective of the opinion issued by ESMA is to improve supervisory convergence in the area of conduct of business (as defined in the Markets in Financial Instruments Directive ‘MIFID’). Licensed entities should act in accordance with the provisions set out in ESMA’s opinion when selling complex products on an advisory and non-advisory basis.

ESMA’s opinion discusses the following MiFID practices for investment firms selling complex products: [i] Organisation/Internal control; [ii] Suitability; [iii] Appropriateness; [iv] Disclosure (including marketing communications); [v] On-going monitoring (compliance risk assessment) and [vi] Execution of client orders.

Licensed entities engaged in the distribution of complex products should consider the issues as explained in each of the above-referred sub-sections. In carrying out its supervisory duties, MFSA will examine the extent to which the licensed entity has adopted ESMA’s minimum expectations.

ESMA’s opinion should also be viewed in conjunction with the following feedback statement: “*MiFID complex and non-complex financial instruments for the purpose of*

*the Directive's appropriateness requirements*” as issued in November 2009 [ref. CESR/09-559].

#### Clarification on callable bonds

ESMA opinion classifies callable bonds as a complex product. In broad terms, callable bonds give the issuer of the bond the right to redeem the bond at par or at any other pre-determined price prior to the maturity date, under certain conditions. The definition of callable bonds captures many locally issued corporate bonds as they contain such an early redemption feature. Therefore in relation to callable bonds, the licensed entity would need to conduct and document the appropriateness test assessment, as detailed in SLCs 2.21 and 2.22 of *Part B1 – Standard Licence Conditions applicable to Investment Services Licence Holders which qualify as MiFID firms*.

#### Clarification on complex products

The MFSA is of the view that complex products exist in a spectrum of complexity. Therefore previous investment in a certain type of complex product (such as “callable bonds”) does not necessarily mean that the client concerned has the knowledge of and experience in all other complex products. Complex products have many different features and structures, which affect the intrinsic level of risk associated with the product.

ESMA in its opinion notes that prior to a sale of a complex product, firms should consider whether the retail client has experience from past transactions regarding the same or similar complex product. In line with duty of care obligations, firms are to ensure that the sale of complex products meets clients’ expectations and that any product documentation is fair, clear and not misleading.

## **Contacts**

Should you have any queries regarding the above, please do not hesitate to contact: Mr. Christopher P. Buttigieg, Tel: 25485229; [cbuttigieg@mfsa.com.mt](mailto:cbuttigieg@mfsa.com.mt); or Ms Sara Antonia Borg, Tel: 25485451; [saborg@mfsa.com.mt](mailto:saborg@mfsa.com.mt) .

**Communications Unit**  
**Malta Financial Services Authority**  
**4<sup>th</sup> March 2014**