

MiFID II

**Information to clients about
investment advice and financial instruments**

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Key Points

Firms will be required to give additional information to clients about financial instruments, including in relation to:

- the performance of the instrument in different market conditions (both positive and negative);
- the risk of financial instruments involving impediments or restrictions for disinvestment – including information on how a client might exit such an investment and how long that might take;
- the legal nature of financial instruments (in certain situations); and
- guarantees and capital protection.

Firms which give investment advice will be required to disclose:

- whether their advice is independent or restricted; and
- the extent to which they will undertake periodic assessments of that advice.

- (i) whether the advice is provided on an independent or non-independent basis;
- (ii) whether the advice is provided based upon a broad or restricted analysis of different types of financial instrument (following the requirements in Article 24(4) of the MiFID II Directive regarding restricted advice);
- (iii) whether the firm will provide the client with a periodic assessment of suitability of the financial instruments recommended to that client. Where it does provide a periodic assessment, Article 52(5) of the MiFID II Delegated Regulation¹ states that the firm should also disclose:

- the frequency and extent of the assessment (and, where relevant, the conditions that trigger that assessment);
- the extent to which information previously collected will be subject to reassessment; and
- the way in which the updated recommendation will be communicated to the client.

Information regarding advice and financial instruments

Article 24(4) of the MiFID II Directive requires MiFID firms to provide appropriate information in good time to clients or potential clients with regard to the investment firm and its services, the financial instruments and proposed investment strategies, execution venues and all costs and related charges.

MiFID firms are already subject to similar requirements under Article 19(3) of the MiFID I Directive. The MiFID I Implementing Directive also contains detailed provisions in article 30 (regarding information about the investment firm and its services for retail clients) and article 31 (regarding information about financial instruments).

The key differences under the MiFID II regime will be as follows:

- (a) Where investment advice is provided, the firm must notify the client:

¹ Article 52(5) of the Delegated Regulation of 25 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive (the "**MiFID II Delegated Regulation**"). For earlier advice on this issue, see ESMA, Final Report: Technical Advice to the Commission on MiFID II and MiFIR, 19 December 2014 (ESMA/2014/1569) (the "**Technical Advice**"), chapter 2.13.

- (b) When providing investment advice, the firm must also provide specific information² to the client covering:
- (i) the range of financial instruments which may be recommended;
 - (ii) a description of their types;
 - (iii) the range of instruments and providers per type;
 - (iv) the firm's relationship with the issuers or providers of those instruments;
 - (v) whether the range covers the firm's own financial instruments or those from entities with close links to the firm, and where this is the case, distinguishing for each type of instrument the range which are not issued or provided by entities linked to the firm; and
 - (vi) how any independent advice given has:
 - satisfied the conditions for the advice being provided on an independent basis; and
 - taken selection factors into account such as the risk, cost and complexity of the instrument.
- (c) When providing information regarding financial instruments, Article 48 of the MiFID II Delegated Regulation (in addition to ESMA Technical Advice³) guides that in addition to the disclosure requirements currently contained in Article 31 of the MiFID Implementing Directive:
- (i) firms will be required to inform clients about the functioning and performance of financial instruments in different market conditions (both positive and negative);
 - (ii) the description of risks should specifically include any risks associated with insolvency of the issuer, or related events such as bail in;
 - (iii) the description of risks should specifically address the risk of financial instruments involving impediments or restrictions for disinvestment. The information provided should include an illustration of the possible exit methods and consequences of any exit, possible constraints and issues and the estimated time frame for the sale of the financial instrument (before recovering the initial cost of the transaction). ESMA has acknowledged some of the difficulties associated with this obligation and proposes to make further amendments to its Technical Advice in the future;
 - (iv) in describing of the risks of a financial instrument which is composed of two or more different financial instruments or services, firms should provide a description of the "legal nature" of the financial instrument. The ESMA Consultation Paper (but not the ESMA Technical

² For further detail on the specific information required, please see Article 52 (2), (3) and (4) of the MiFID II Delegated Regulation.

³ For earlier advice on this issue, see chapter 2.13, ESMA Technical Advice.

Advice) says that would include: whether the instrument takes the form of equity or debt; whether it is callable by the issuer; whether it is perpetual; conversion terms; the party liable contingencies; ownership of the instrument, etc.; and

- (v) for financial instruments that incorporate a guarantee or capital protection, the information provided should specify the scope and nature of the guarantee or capital protection.

All of the requirements detailed above apply to all types of client – including professional clients and eligible counterparties. However, it will continue to be acceptable for firms to take account of the client's categorisation⁴ and level of knowledge⁵ in determining the content of the information to be provided.

Insofar as sufficient information on costs and charges is contained in a UCITS Key Investor Information Document ("KIID") or a PRIIPs Key Investor Document ("KID"), that document should be sufficient for the purposes of MiFID II. Clients should however be notified of any costs and charges associated with the product which were not included in the KID or KIID, including the costs of providing any related investment services.⁶

MiFID I provided that firms could provide the relevant information in a standardised format. The MiFID II Directive provides that Member States will be permitted to make their own determinations of whether the information can be provided in a standardised format. This raises the possibility that Member States could take a different approach towards the disclosure requirements.

Investment advice provided on an independent basis

Articles 52 and 53 of the MiFID II Delegated Regulation require firms providing investment advice on an independent basis to comply with certain requirements. These include:

- (a) defining and implementing a selection process to assess and compare a sufficient range of financial instruments available on the market.⁷ If this comparison is not possible, the firm should not present themselves as being independent;
- (b) when focussing the advice on certain categories or a specified range of financial instruments:
 - (i) marketing the advice service in a way which intends to attract only those clients with a preference for those categories or range;
 - (ii) requesting clients confirm they only wish to invest in those categories or range; and
 - (iii) prior to providing the service, ensure the service is appropriate for each new client on the basis of their needs and objectives.

Independent and non-independent advice

Articles 52(1) and 53(3) of the MiFID II Delegated Regulation guide firms that their clients should be notified in good time when investment advice is offered or provided on both an independent and non-independent basis, including:

- (a) confirming (in a durable medium) whether the advice in question will be independent or non-independent⁸, and any restrictions which may apply such as

⁴ Article 31(1), MiFID Implementing Directive.

⁵ Article 31(2), MiFID Implementing Directive.

⁶ Article 51, MiFID II Delegated Regulation.

⁷ Article 53(1), MiFID II Delegated Regulation. See Article 24(7)(a) of MiFID II for further requirements as to a sufficient range of financial instruments.

⁸ Further guidance on categorising the advice is given at Article 24(4)(a) of MiFID II.

- the prohibition on inducements when providing independent advice;
- (b) explaining the scope of both services to allow investors to understand the differences between them;
 - (c) not giving undue prominence to independent investment advice services over non-independent investment services when communicating with clients;
 - (d) presenting the firm as independent only with respect to the services for which it intends to provide investment advice on an independent basis; and
 - (e) confirming the firm has adequate controls in place to separate independent and non-independent advisers (a single advisor cannot provide both independent and non-independent advice under this requirement).

Timescales for implementation

The MiFID II Directive and the Markets in Financial Instruments Regulation ("**MiFIR**") came into force on 3 July 2014, and most of their provisions will come into effect in member states from 3 January 2018. Member states have until 3 July 2017 to transpose the MiFID II Directive into national law.

The changes to the MiFID Implementing Directive will be made by way of the MiFID II Delegated Regulation which will become effective by 3 January 2017. The MiFID II Delegated Regulation will have direct effect and the member states will not need to implement these changes into national law.

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