

**CESR'S CONSULTATION 09-665:  
UNDERSTANDING THE DEFINITION OF ADVICE  
UNDER MIFID**

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***Response of the AMAFI***

1. AMAFI thanks CESR for providing it with the opportunity to discuss its understanding of the definition of advice under MiFID.

2. AMAFI is keen to provide its view on the subject, especially so since the scope of the new investment advice service introduced by MiFID has been the subject of many discussions amongst its members since November 2007.

For investment firms with activities on the wholesale markets, which constitute most of AMAFI's membership, it is of particular importance to identify when they are providing or not the investment advice service. Only then are they able to put an organisation and some processes around it that work best with their client types but also in terms of competition with their peers nationally, and more importantly, in the European Union. A good understanding of the definition of the service is key for these professionals and the present proposal of CESR to identify situations where investment advice is (and is not) provided, is thus of particular interest for the Association.

3. To a large extent though the proposed paper falls short of meeting these expectations: although client protection is a concern that AMAFI finds absolutely legitimate, the paper's conclusions are of no practical use to firms and, possibly, to regulators as well. They do not help firms in setting up internal organisations that would ensure their compliance with the requirements attached to the provision of the service because they cannot assess ex ante if the service is provided or not. And the regulators are not provided with the criteria they should use to control the ways in which the service is provided by firms, as, according to the paper, their assessment is to be based on the merits of each particular case.

AMAFI therefore wishes to make the general observations set out below (I). Answers to the questions asked in CESR's document are also provided, together with specific comments on sections of the document on which CESR did not explicitly seek comments but that are of special importance to the AMAFI (II).



## I. – General Observations

4. As a preamble, AMAFI wishes to stress that the concern of client protection that the paper seeks to address is one that it considers indisputable, as a critical factor of the effectiveness and success of financial markets. As a consequence, the observations and propositions put forward in this response should not be seen by any means as seeking to downplay this concern.

5. On a more technical note, AMAFI regrets that the time allowed to respond to the consultation was not set to the three-month standard applicable to significant issues (see CESR's consultation policy – CESR/01-009). This is especially so on the counts that:

- The end of year is usually busy, which is especially the case this year both at the national and international levels considering the number of issues being addressed at the moment in our industry; and
- The scope of the investment advice service is a significant issue that has remained unresolved since the implementation of MiFID and has created widespread uncertainty among firms. This is such that the French market authority, the AMF, recently wrote in its conclusions of a survey administered on the subject to firms it regulates: *“Investment advice or information (of a commercial, financial or marketing nature): for many firms, drawing a line between the two is almost impossible except on a case by case basis, for each transaction and each client, which firms do not consider practical. (...) Compliance officers show a true concern in implementing and verifying the rules related to the investment advice service, to the point that they would characterise some services as investment advice, as a regulatory precaution, even if they are not”*<sup>1</sup>.

➤ ***The paper's objective should be to place firms and regulators in a position to get organised to ensure compliance with the requirements inherent to the provision of the service***

6. Professionals expect from CESR positions and guidelines that will enable them to set up internal procedures and processes to conduct their business in compliance with the rules and regulations they are subject to. In addition, they expect that these positions will result in an even playing field, whereby each authority in the EU will be able to assess the firms it has jurisdiction on based on a uniform set of criteria. For CESR to meet its objective of a harmonised implementation of the EU directives in the financial sector, these criteria need to be absolutely clear and precise to allow the various Member States' regulators to adhere to them and be in a position to use them in the most consistent way possible across the EU.

Incidentally, this objective is entirely consistent with the one of the new European authority for financial markets, which is not only to ensure interpretations of regulatory standards are harmonised but also that the controls and sanctions decided by the competent authorities of the Member States do not differ significantly. This objective should already be considered by CESR in the positions it currently draws up.

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<sup>1</sup> AMF, L'exercice du conseil en investissement : analyse des rapports adressés à l'AMF en 2008 par les prestataires de services d'investissement, 9 décembre 2009 ([http://www.amf-france.org/documents/general/9224\\_1.pdf](http://www.amf-france.org/documents/general/9224_1.pdf))

7. In AMAFI's view, this is not the case in the present paper for several reasons:

- The presentation of the legal framework is too short to enable CESR to set out its interpretation of it and, as a result, the paper does not state the main concern it actually addresses, i.e. client protection.
- The five tests that are key to assessing each particular situation are exposed at the outset of the document but not used consistently in the specific cases described in the document. This results in intricate and ambiguous positions (see below §19).
- The position builds upon subjective concepts such as the client's "*feeling*" and its "*reasonable*" nature, which are not backed by an analysis grid that would incorporate more tangible elements and that authorities and firms could use with a lesser risk of divergent interpretations.

8. This is especially disturbing to firms whose challenge is not only to manage their litigation risk but also to be in a position to set up clear organisational guidelines to their various businesses. The provision of the investment advice service is indeed far from neutral from an organisational point of view, as it requires the implementation of robust procedures around collection of client data and suitability requirements.

9. Unfortunately, the resulting CESR's position rests entirely on the need to assess each situation based on its own merit. This factual approach is undoubtedly the one courts will adopt in case of litigation on the characterisation of the investment service provided by a firm to a client. However, this approach is not helpful to competent authorities and firms: it does not provide the former with the objective criteria they should use to determine whether investment advice is indeed provided and it does not give the necessary tools to the latter to ensure that firms do not give their clients the feeling they are providing investment advice when they do not intend to.

➤ ***The investment advice service is a value added service different to a general obligation***

10. The investment advice service is a full fledged and value-added service. When they provide it, firms create value by making sure their advice is suitable to their clients. It means in particular that clients cannot expect to be provided such a service at no cost (be it explicit or implicit).

The paper's position that any opinion expressed by the firm could become investment advice stands in opposition to this understanding of the service. It creates confusion between the service itself and both the duty to provide clear, fair and not misleading information to clients and the one to act honestly, fairly and professionally in accordance with the best interests of a client. Investment advice is a service, not a general duty – this important distinction seems to be lost by CESR in several sections of the paper.

The risk of enlarging so much the scope of investment advice is to denature this service and to eliminate its original purpose, which is to provide actual value added to clients while protecting them.

11. Such a trend, which would obviously be to the clients' detriment, far from the original objective of MiFID, needs to be duly motivated by the necessity of client's protection.

➤ **Client protection is an indisputable concern – but it needs to be looked into thoroughly**

12. Although it is not clearly stated in the paper, it seems that the main objective of CESR is to ensure clients receive protection attached to the investment advice service even when the provision of the service is not explicit. This objective of client protection should be clearly stated and looked into, where at the moment CESR's analysis of the regulatory framework is very brief and cannot be based upon to detail this objective.

13. Client protection is an essential concern and one that AMAFI supports fully, not only at a micro level but also at a macro level since the investment of personal savings into financial markets constitutes a significant challenge for many EU Member States and it cannot flourish without customer's confidence. It is irrefutable that when investment advice is provided, it must be in such a way that it offers some guarantees, which MiFID explicitly states. This is especially so since the service is provided for a fee, be it implicit or explicit.

However the concept of client protection cannot be dealt with in a "one size fits all" manner and CESR should not do without exploring further where the challenges lie (when reading the paper it is apparent that it has been designed with retail clients in mind at least until question 7 but this is not clearly stated ).

➤ **Professional clients ought to be out of the scope of this paper**

14. As stated in Recital 5 of Directive 2006/73/CE, "*as regards investor protection, and in particular the provision of investors with information or the seeking of information from investors, the retail or professional nature of the client or potential client concerned should be taken into account*".

When dealing with client protection, it is therefore important to consider the nature of the client who is to be protected. Unfortunately, CESR's paper fails to perform this analysis, whereas the higher level of guarantees the paper aims at providing is really founded only when the concern of client protection is true. In particular, it cannot be so with regard to two sets of clients:

- Those who are categorised as professionals under MiFID;
- Those who are in a position to know when investment advice is provided even where they are not categorised as professionals under MiFID.

The first ones are categorised as professional clients under MiFID because of their knowledge and experience of the financial markets. As a consequence, "*where an investment firm provides an investment service to a professional client it shall be entitled to assume that, in relation to the products, transactions and services for which it is so classified, the client has the necessary level of experience and knowledge for the purposes*" of the suitability test (*Directive 2006/73/EC, art. 35*)<sup>2</sup>. Also, "*professional clients should, subject to limited exceptions, be able to identify for themselves the information that is necessary for them to make an informed decision, and to ask the investment firm to provide that information*" It follows that these clients are able to assess by themselves if they are provided with an investment advice service or not.

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<sup>2</sup> In addition, "*where that investment service consists in the provision of investment advice to a professional client covered by Section 1 of Annex II to Directive 2004/39/EC, the investment firm shall be entitled to assume for the purposes of paragraph 1(b) that the client is able financially to bear any related investment risks consistent with the investment objectives of that client*" (*Directive 2006/73/EC, art. 35 2*).

The second set of clients includes all clients which, by their very nature, are able or should be able to assess by themselves if they are provided with the investment advice service or not. Those clients are mainly those which are authorised by a competent authority - such as asset managers, portfolio managers or other investment firms<sup>3</sup> - who are therefore supposed to be competent at investing their client's money. For these entities, it cannot be assumed that they could have the "*feeling*" that they have been provided investment advice: they ought to know which service they are seeking and getting. These clients may have chosen not to be categorised as professionals under MiFID for a variety of reasons (for example to take advantage of the extensive and detailed information due to non professional clients) but they are by their very nature in a position to know which service is provided to them.

As a consequence, CESR's concern over client protection should not be addressed in the same way depending on the type of clients receiving the advice. There may be other issues related to the provision of the investment advice service to these clients, but they are to be addressed with a different angle from the one applicable to retail clients.

**15.** CESR's paper should therefore clearly indicate that the paper targets investment advice provided to retail clients who are not professionals of the financial markets. For these clients, it should be explained how investment firms could avoid giving them the impression that they are providing a service they do not intend to provide and how regulators can assess whether it is the case. To do so, precise criteria should be identified, that both regulators and firms could use. Importantly, these criteria cannot rest on the client's feeling, which can only be assessed from the client's perspective.

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<sup>3</sup> This does not prevent them from seeking investment advice in specific circumstances, in which case this expectation should be clearly stated and documented.

## I. – Specific Observations

### ➤ II – Introduction

- **Considering an investor’s view of whether advice is being given**

16. The statement that the reasonable belief by a client that a recommendation is being provided to him or her is enough to consider that the recommendation is presented as suitable or based on a consideration of the person’s circumstances (i.e. test 3 is fulfilled) is not satisfactory :

- The logic of the investment advice service is turned upside down: it rests on the client’s feeling that the advice constitutes a recommendation and not on the actual provision of the service based on the knowledge of its client by the firm (a pre-requisite to providing the service) and the suitability test it should have performed.
- To base this test on a “*reasonable feeling*” has two drawbacks: first, it creates an opportunity for litigation as any client of bad faith could assert he or she had the feeling that a recommendation was provided to him or her and second, it provides no clear and established regulatory framework within which firms can operate, as no organisation can be built around such a subjective criterion (see above § 8).
- The “*reasonable*” test is one that courts will use but not one that firms (and regulators) can comprehend ex ante: objective criteria should be set instead.

- **Assumptions made in preparing this paper**

17. One can understand the need for protection of clients and potential investors alike. However, such a position that the investment advice service can be provided to potential investors can lead to some aberrations whereby the prospective client would be provided a guarantee for free and the firm would provide the service with no economic purpose.

This can be illustrated by a simple example where a person wishing to purchase a car would seek advice from a car dealer. The car dealer would provide good advice but the price of the car would be too high for the person who would buy the car to another car dealer offering a lower price and no advice. When it happens that the car breaks up every other month, no compensation would be sought from the second car dealer on the basis that the advice on the car’s reliability was provided by the first one, who would be held liable.

This comment is also related to the statement made previously (see above § 10) that the investment advice service is a value added service and should not be seen as being incidentally provided for free.

It may be worth considering this aspect in this section of the document.

18. For the avoidance of doubt, this comment does not preclude considering that the investment advice service is provided when a recommendation is made to a client not to proceed with a transaction, as long as the five key tests are met.

- **Diagram: the five key tests for investment advice**

19. The diagram sets cumulative tests to determine whether investment advice is provided or not. However, the rest of the document considers each test individually to try and provide criteria to assess each of them. This methodology has a major drawback though since the various tests are not considered together and the conclusions drawn seem excessive and partial, as each of the tests is not applied rigorously to each situation considered (see as examples §23 and 25 of this document and §38, 44 and 50 of CESR's paper).

Another consequence of it is that the conclusions are often worded in an ambiguous way (with the use of words such a "may" or "might"), which provides no foreseeable outline which firms can use to organise themselves (see above § 6 to 9).

➤ **III – Part 1: Does the service being offered constitute a recommendation?**

- **What constitutes a (personal) recommendation**

20. Under MiFID a personal recommendation is not qualified as implicit or explicit. As stated in article 52 of Directive 2006/73/CE: "*For the purposes of the definition of "investment advice" in Article 4(1)(4) of Directive 2004/39/EC, a personal recommendation is a recommendation that is made to a person in his capacity as an investor or potential investor, or in his capacity as an agent for an investor or potential investor.*

*That recommendation must be presented as suitable for that person, or must be based on a consideration of the circumstances of that person, and must constitute a recommendation to take one of the following sets of steps:*

*(a) to buy, sell, subscribe for, exchange, redeem, hold or underwrite a particular financial instrument;*

*(b) to exercise or not to exercise any right conferred by a particular financial instrument to buy, sell, subscribe for, exchange, or redeem a financial instrument.*

*A recommendation is not a personal recommendation if it is issued exclusively through distribution channels or to the public."*

The words "implicit or explicit" should therefore be removed from § 8.

21. Similarly, the Directive does refer to personal recommendations and not any other recommendation. Hence, the brackets used in the question should be removed.

- **Q.1. Do you have any comments on the distinction between the provision of personal recommendations and general information?**

22. In AMAFI's opinion, the distinction that the Directive draws when using the concept of "recommendation" to define the investment advice service is not only between "*providing advice and simply providing information*" (see §10 of CESR's paper) but also between investment advice and other types of advice not aimed primarily at investing in financial instruments - like the ones embedded within the remit of other investment or ancillary services – or intended simply to inform the investor – like a statement of opinion on the market conditions for example. This is a critical point, as the investment advice service should not be equated to the general duty of advice that is a rule to any investment firm.

23. In §16 of CESR's document, the provision of information based on biased or leading criteria rather than on a balanced basis is given as an example of a personal recommendation. This could indeed be the case, yet for it to constitute investment advice, the other tests should be met (in particular, is the recommendation presented as suitable or based on a consideration of the person's circumstances). In addition, the examples provided in this paragraph do not pertain to the unbalanced nature of the opinion but rather to the multiple step recommendation developed in the following paragraph.

24. More importantly, MiFID sets an obligation on investment firms that "*all information, including marketing communications, addressed by [them] to clients or potential clients shall be fair, clear and not misleading*" (*Directive, 2004/39/CE, art. 19 2.*). This is further detailed in article 27 (2) of Directive 2006/73/CE which states that the information provided to clients "*shall be accurate and in particular shall not emphasise any potential benefits of an investment service or financial instrument without also giving a fair and prominent indication of any relevant risks*" and in particular "*it shall not disguise, diminish or obscure important items, statements or warnings*" and "*where the information compares investment or ancillary services, financial instruments, or persons providing investment (...) the comparison must be meaningful and presented in a fair and balanced way.*"

The risks posed by biased or unbalanced information given to client is therefore already provided for within these general obligations. A breach of these obligations does not need to constitute investment advice to be sanctioned.

In AMAFI's view, confusion is made between two sets of obligations. As a result, equating the imbalanced nature of the information provided to a personal recommendation is inadequate, especially since the other tests to determine whether the investment advice service is provided are not considered. In addition, the concern around the fair and balanced nature of information should be dealt with from the angle of the information duty.

- **Can investment research amount to investment advice**

25. AMAFI agrees with the view that investment research is separate from investment advice (see §19 of CESR's paper). When it is used in conjunction with other elements that meet the five key tests, it could result in the provision of investment advice. However, it is not enough to state that this could be the case when it is used "*in conjunction with other activities of the firm*": again the reference to the five key tests should be explicit to qualify the situation as investment advice.

AMAFI agrees that when research is used to present a recommendation as suitable to the client this could constitute investment advice. However, to avoid subjective and discordant interpretations of the last sentence of paragraph 20, which considers the "*reasonable belief that a recommendation is being made*", examples or criteria should be provided and the concept of "reasonable belief" should be removed. This is important, especially for the wholesale markets, since it is customary for these activities to send research to their clients (e.g. memo sales or sales commentary) who showed an interest in receiving it, without having the intention to make it a personal recommendation. This is especially so since research is developed based on the analysis of an issuer or a set of issuers and not on the analysis of the personal circumstances of the clients it is being sent to.

26. On another note, the conclusion of this section that rests on the merits of each particular case, exemplifies the general observation made § 6 to 8 that subjective interpretations do not enable firms to set up internal procedures that could work for each of their lines of business and, as a result, create uncertainty.



- **Q.2 Do you agree that the limitation that filtered information is “likely to be perceived by the investor as, assisting the person to make his own choice of product which has particular features which the person regards as important.” is a critical criterion for determining whether filtering questions constitutes “investment advice”?**

27. For consistency with the rest of the document, the term “likely” should be replaced by “reasonably”. The criterion proposed by CESR does not raise any observation on AMAFI’s part.

28. As regard generic advice, AMAFI considers that it includes investment research because it does not relate to a particular financial instrument (see also § 25).

#### ➤ **IV. Part 2: Is the recommendation in relation to one or more transactions financial instruments?**

- **Q.3. Do you believe the distinction between general recommendations/generic advice and investment advice is sufficiently clear? Do you have examples of types of advice where the designation is unclear?**

29. In many instances, general recommendations are not addressed randomly to all clients of the firm. An initial filtering of the client base is generally performed to identify a set of clients with similar characteristics to whom more specific information could be targeted (for example, an investment firm may want to target all hedge funds in its client base). The consideration of these characteristics is generally not equal to the consideration of the personal circumstances of each of these clients. Hence, to the extent that the five key tests are not met, this information should not be seen as investment advice and the term “public” should not be restricted to an indistinct group of clients. Generally speaking, the mere fact of sending an email to a client (which is personalised only to the extent that the name of the client is used) can not be considered in itself as constituting a personal recommendation.

30. Another feature of investment advice, worth considering when distinguishing it from generic advice, is the period during which it is valid, which is short by nature because it is based on the one hand, on the personal circumstances of the client that may change and, on the other hand, on financial instruments whose economic interest may vary significantly depending on market circumstances.

31. Finally, generic advice cannot be equated to investment advice, as it is never provided considering the client’s personal circumstances: the rationales supporting generic advice are external to the client (they tend to be product specific instead).

- **Is a recommendation to become a client of a particular investment firm investment advice?**

32. The portfolio management service requires in itself, irrespective of the investment advice service, a suitability test of the mandate given to the portfolio manager with respect to the client’s personal circumstances. The second sentence of § 42 in CESR’s document is not clear and seems to complicate this simple obligation with a reference to the existence (or not) of a personal recommendation. AMAFI therefore suggests to clearly states that Recital 60 is implemented as such by article 19 (4) and to remove the last sentence of the paragraph.

➤ **V. Part 3a: Is the recommendation presented as suitable?**

- **Q.4. Is there sufficient clarity as to when an implicit recommendation could be considered as investment advice? If not, what further clarification do you think is necessary?**

33. An example of the implicit nature of a recommendation is provided that is based on the lack of balance of the information provided. Again, such a practice constitutes a breach of the firm's duty to provide clear, fair and not misleading information to clients (see above § 23). It is not as such investment advice based on a personal recommendation, as long as it does not meet the five key tests.

Again, client protection being provided for in such cases by another obligation set by MiFID, the recourse to investment advice to handle such instances of improper information is not useful, especially so since it may not be applicable if the five key tests are not met.

34. Furthermore, the implicit nature of a recommendation raises strong objection with regard to certain types of clients. AMAFI disagrees strongly on the application of such a concept to professional clients and retail clients who are themselves market professionals. As already mentioned (see above §14), these clients have the necessary experience and knowledge to decide whether they want or need investment advice. Hence the provision of the service to them cannot be incidental, it should be totally explicit. As an example, when such clients provide orders on flow products, which are vanilla instruments whose objectives are simple (such as standard stocks, bonds, warrants, certificates of deposits, ...) and whose use is very common amongst this category of clients, there is an assumption from both parts that no investment advice is provided: if it was to be provided, it should be explicitly set (especially since, in some cases, it could slow the execution process, whose speed is often critical to clients).

35. More generally, it is not enough for the information to seek to influence the client's choice to constitute investment advice (with such a view, advertising could constitute investment advice): the five key tests must be met. Considering that any advice or opinion from the firm could constitute an implicit recommendation would widen the scope of investment advice to such an extent that it would become equivalent to a general duty of advice and would no longer present any value-added as a proper investment service (see above §10 and 11).

- **Can a firm avoid providing investment advice using a disclaimer in its communications?**

36. To the extent that the "*feeling of the client*" could become a criterion to judge whether investment advice was provided or not, it is not acceptable that a disclaimer could not be considered as a clear denial of this feeling. To the extent that the disclaimer is clearly written (for e.g. it could state that the views expressed are not based on the examination of the personal situation of the client and does not constitute investment advice) and that it is visible, it should not be possible for a client to assume still that investment advice was provided to him or her.

This distinction is important: whereas MiFID sets a number of obligations to firms with regard to client's information, it cannot be considered that information are mandatory in certain cases (based on the assumption that clients read them) but that in other cases they have no value (assuming that clients do not read them). CESR's position needs to be balanced in this respect if the logic of the directive is to be maintained.

The statement that “if the disclaimer does not change the nature of a communication, meaning that the communication would still create a reasonable expectation by the client that he is being advised, the firm may be viewed as providing investment advice” is not acceptable as such because it is too vague. It should mention that if the facts show that despite this disclaimer, the firm did provide investment advice (meeting the five key tests), obviously the disclaimer is of no value: but this conclusion would be drawn from actual facts and not from the client’s feeling. And the ability of the firm to set up systems and controls to place some of its activities out of the scope of the investment advice service would be safeguarded (except for exceptional circumstances).

➤ **VI. Part 3b: Is the recommendation based on a consideration of the person’s circumstances?**

- **What do we mean when we talk about a person’s circumstances?**

37. The elements that a firm should consider to base its recommendation in order to make it suitable are defined in article 35 of Directive 2006/73/CE: the investment objectives of the client, their financial capacity to bear the risk of their investments and their experience and knowledge. These elements constitute the person’s circumstances and are further detailed in (3) and (4) of the same article and in article 37:

*“3. The information regarding the financial situation of the client or potential client shall include, where relevant, information on the source and extent of his regular income, his assets, including liquid assets, investments and real property, and his regular financial commitments.*

*4. The information regarding the investment objectives of the client or potential client shall include, where relevant, information on the length of time for which the client wishes to hold the investment, his preferences regarding risk taking, his risk profile, and the purposes of the investment.”*

*(Directive 2006/73/CE, art. 35)*

*“1. Member States shall ensure that the information regarding a client’s or potential client’s knowledge and experience in the investment field includes the following, to the extent appropriate to the nature of the client, the nature and extent of the service to be provided and the type of product or transaction envisaged, including their complexity and the risks involved:*

*(a) the types of service, transaction and financial instrument with which the client is familiar;*

*(b) the nature, volume, and frequency of the client’s transactions in financial instruments and the period over which they have been carried out;*

*(c) the level of education, and profession or relevant former profession of the client or potential client.*

*(...)”*

*(Directive 2006/73/CE, art. 37)*

The list that CESR provides should build on these three elements and include the data provided by the directive: as proposed, it lacks structure and is incomplete.

38. In addition, two pieces of the information mentioned are irrelevant as such because they pertain to the client’s identity (whose verification is performed for anti-money laundering purpose, irrespective of MiFID): the client’s address and the marital status. The knowledge of a client’s address is of no value to the firm to gain knowledge of its financial capacity, its objectives or its knowledge and

experience. At best, one could in a few cases, assess its financial capacity but this assessment would be of no value and very questionable ethically. Similarly, if some investment objectives could be inferred from the marital status, still they should be explicitly stated by the client.

- **When will a firm be viewed as basing a recommendation on a consideration of a person's circumstances?**

39. The statement that the possession by the firm of information on the client's circumstances creates a reasonable expectation that the information will be used to provide recommendation raises several concerns.

Firstly, if the definition of personal circumstances is as wide as the one proposed and includes KYC information, then the firm would be deemed to be in a position to provide personal recommendation to all its clients, which is obviously inadequate.

Secondly, in wholesale markets, the possession by the firm of the information is not enough to infer that investment advice will be provided: the information should be used for the advice to be considered as a personal recommendation, i.e. the suitability test should be performed and, more generally, the five tests should be met. In these markets, investment advice is provided in relation to a specific transaction that is tailored to meet the client's objective. As a result, the objectives of the client are not collected once and for all (and updated from time to time): they are discussed again for each transaction because they may differ significantly depending on the transaction foreseen. This observation strengthens AMAFI's view that the paper should clearly target the clients it is trying to enhance the protection of and scope out professional clients and retail clients who are professionals of the financial markets.

- **Q.5. Are the circumstances where "it is clear the firm is making a personal recommendation" sufficiently clear? Would further clarification be helpful?**

40. See comments above § 37 to 39. The statements provided are not helpful in AMAFI's view for the reasons explained above § 19.

#### **➤ VII. Part 4: Is the recommendation issued otherwise than exclusively through distribution channels or to the public?**

- **Q.6. Are there other criteria you believe should be considered when determining whether messages to multiple clients constitute investment advice?**

41. To the extent that a message sent to a set of clients is neutral in tone, i.e. it does not give the impression that it is based on the client's circumstances (example of a commercial document sent to a large set of clients), it should not be seen as a personal recommendation. For example, in wholesale markets, opinions are often provided without the intention that they be perceived as (or expected to be) personal recommendations.

In addition, as mentioned before (see above § 29), the fact that these messages are addressed to a set of clients (and not to a larger public) does not change the nature of the message. This is reinforced by the fact that investment advice does not go well with the notion of multiple clients, since the purpose of the service is to consider the personal circumstances of each individual and not the common feature shared by a group of people.

Also, best products lists that are product-specific rather than client specific should be treated as generic advice (see above §31).

➤ **VIII. Part 5a: Is the recommendation made to a person in his capacity as an investor or potential investor?**

- **Q.7. What information would be helpful to assist in determining whether or not what firms provide constitutes investment advice or corporate finance advice?**  
**Q.8. Are there specific examples of situations you would like considered, where it is difficult to determine the nature of the advice?**

42. According to MiFID, investment advice means “*the provision of personal recommendations to a client, either upon its request or at the initiative of the investment firm, in respect of one or more transactions relating to financial instruments*”.

Article 52 of the Implementing Directive indicates that a recommendation may be deemed to be personal only if it is made “*to a person acting in his capacity as an investor or potential investor*”.

When trying to identify what does that mean, CESR suggests that “*where an investment firm makes a recommendation to a person to buy or sell a financial instrument, it should be assumed that the person is an investor or potential investor unless particular circumstances clearly demonstrate otherwise*”.

At the same time, CESR indicates that the provision of “*advice to undertakings on capital structure, industrial strategy and related matters is not investment advice because such advice will not involve investment in financial instruments*”.

The combination of these two statements gives the impression that the key criterion to distinguish “*investment advice*” from “*corporate finance advice*” (this term is used here to designate the ancillary service referred to in Section B(3) of Annex I of MiFID) is whether or not the advice given leads to the sale or purchase of a financial instrument.

AMAFI disagrees with this analysis simply because both “*investment advice*” and “*corporate finance advice*” lead eventually to the sale or purchase of certain financial instruments. Indeed, when advice is given on the capital structure or industrial strategy of an undertaking, it is not a purely theoretical exercise. Most of the time, this advice leads to a form of recommendation to buy or sell the whole or part of the capital of the undertaking in question i.e. strictly speaking to buy or sell some financial instrument.

This shows that the criterion to distinguish “*investment advice*” from “*corporate finance advice*” cannot be whether or not the advice involves the investment in financial instruments – at least not, if the term “*investment*” is intended to mean “*buying or selling financial instruments*” because in both cases, there is eventually the purchase or the sale of financial instruments.

43. AMAFI believes therefore that the key criterion to distinguish “*investment advice*” from “*corporate finance advice*” should be the objective pursued by the client when seeking advice from a professional firm. On that basis, two situations corresponding to two entirely different objectives can be distinguished:

In the first situation, the client has a “patrimonial” objective, i.e. he is looking for (or receiving at the initiative of the firm) a personal recommendation concerning the type of investment he should make to have the sort of return on his investment that he expects. Very simply, the client has some money and wants to invest it into some type of financial instruments that will give him a return on his investment. It may also be that the client wants advice as to whether he should sell certain financial instruments that he holds – still with the objective of making money (or at least losing as little money as possible, depending on the surrounding economic circumstances of the matter). In both cases, whether the client is receiving advice as to whether he should buy or sell certain financial instruments, the advice he is given may be characterised as **“investment advice”** provided that the other criteria of such service are met.

In the second situation, the client has an “industrial / strategic / entrepreneurial” objective. In that case, he is looking for **“corporate finance advice”**. The identification of the client in this context is particularly important. The client in that case is generally the main shareholder of the undertaking<sup>4</sup>. It may also be the management of such undertaking (president, manager or board depending on the form of the company). Very often, particularly in small or medium size - and certainly in family-owned - undertakings, the main shareholder and the management is the same person. In larger companies, they can be different and have different objectives although both do have an industrial/entrepreneurial objective when seeking corporate finance advice<sup>5</sup>.

The “industrial or entrepreneurial” objective is easy to understand and does not require a lot of explanations. At the basis of it, there is always an industrial motivation: to expand the company’s business, to find new partners, to find new ways of financing the current activity of the company or to develop new activities, new products, etc...<sup>6</sup> If the objective is to sell, it can be, for instance for an aging client, to sell its company or its business to somebody who will be able to pursue it and maintain the workforce, etc...In all these cases, the key difference with the purely “patrimonial” objective is that the search for a profit is not the only motivation. Naturally, the corporate finance client also wants preferably to make a profit but it is not the sole objective and not the primary objective.

**44.** The reason why the objective pursued by the client must be the key criterion to distinguish “investment advice” from “corporate finance advice”, rather than whether the advice leads to the sale or purchase of financial instruments, is the following. Let’s take an example:

Client A – majority shareholder and president of the board of directors of company X - wants to find a new partner to develop the activity of the latter. His motivation is clearly industrial/entrepreneurial. He seeks “corporate finance advice” possibly to look for such new partner (he may already have identified a new partner B) and surely to advise him as to the best way to bring B into his capital. The professional firm which advises him gives him two options to consider in order to achieve his objective:

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<sup>4</sup> In some cases, the “corporate finance advice” mandate is also signed by the minority shareholders, generally family members who are “linked” to the main shareholder and want to take an active part in the acquisition or selling process. By signing the mandate, they demonstrate that they wish to be part of the “entrepreneurial” process and receive the “corporate finance advice” which is going to be given to the main shareholder.

<sup>5</sup> In larger companies, particularly when they are listed, some minority shareholders, holding a significant minority interest in the company, may also seek “corporate finance advice”.

<sup>6</sup> To achieve this objective, in addition to “corporate finance advice”, the client also requires - most of the time - from other competent professionals, accounting, tax and legal advice. The addition of these different services is another distinctive feature of the “corporate finance” objective and therefore of the fact that the service rendered is “corporate finance advice”. In case of doubt, the fact that accounting/tax/legal advice was also provided to the client in connection with the operation which was the subject matter of the initial “corporate finance advice” would be an additional indication of the fact that the service concerned is “corporate finance advice” and not “investment advice” for which such additional services are never provided.

One option is for him to sell part of his shares to B. In that case, the recommendation will be eventually for him to sell, say 20% of his shares in X, to B. It will therefore result in a recommendation to sell a specific financial instrument.

The second option is to increase the share capital of X and reserve part or the whole of such share capital to B so that by subscribing to such newly issued shares, B eventually holds 20% of the share capital of X. In that case, there will be no “sale” of financial instrument but the “issuance of new instruments” to which B will subscribe.

In practice, A will most likely choose between these two options, which both achieve his entrepreneurial objective, depending on the respective cost of implementing one or the other option, taking into account primarily their respective tax consequences.

Yet, if we were to follow CESR’s reasoning expressed in § 74<sup>7</sup> and 72<sup>8</sup> of the CP, then we would say that the first option would be deemed to constitute “investment advice” whereas the second option would not. Clearly that does not make sense. The two options in question are simply two different “technical” ways of achieving the same objective which is entrepreneurial in both cases. It would not make any sense to give them a different legal characterisation with all the consequences attached to each characterisation just because the “legal” technique is different.

This example shows that the only possible criterion to draw a line between “investment advice” and “corporate finance advice” is the objective pursued by the client.

**45.** This criterion is also helpful to distinguish the situation of the majority shareholder/manager of a company (envisaged above) from that of the other minority shareholders. Clearly, as mentioned above, the objective of the former is entrepreneurial. The minority shareholders, on the other hand, may have a similar objective but not necessarily.

In practice, the advice is given by the professional firm to the manager/majority shareholder. It is very rarely given to the minority shareholders<sup>9</sup>. If the corporate finance advice given to A is, for instance, to sell the whole of the share capital of company X to B, most of the time, in family owned businesses, A will deal with the minority shareholders himself and ensure, vis-à-vis B, that he will be in a position to sell 100% of the share capital, minority shares included. The reality is that in that very common situation, the minority shareholders receive no professional advice (only the personal advice of the majority shareholder) regarding the sale of their shares<sup>10</sup>.

If the minority shareholders however want to receive professional advice separate from the advice given to the majority shareholder, then, depending on their objective, the type of advice they will seek could be

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<sup>7</sup> “Advice given to an undertaking for example to acquire the control of another company by purchasing all or a substantial portion of its shares, or to dispose of a subsidiary, would, if the other elements of the definition of investment advice are satisfied, be investment advice”

<sup>8</sup> “Advice to an undertaking to issue securities is not investment advice”.

<sup>9</sup> Only in the case mentioned in footnote 1 above where the minority shareholders directly linked to the main shareholder decide to sign the corporate finance advice mandate alongside the main shareholder or possibly in the case, mentioned in footnote 2, of minority shareholders holding a significant minority interest.

<sup>10</sup> This situation cannot be confused with that referred to in article 52 of the Implementing directive which includes in the definition of « investment advice » the personal recommendation given to « a person in his capacity as an agent for an investor or potential investor ». In the situation described in paragraph 45, the management/majority shareholder may be deemed to be acting as agent for the minority shareholders but in the context of the « corporate finance advice » that he receives (not in the context of any « investment advice »).

either “corporate finance advice” if they have an industrial motivation (as minority shareholders, they could still have such an objective) or “investment advice” if their objective is purely patrimonial.

Therefore, it is true to consider that in the context of a corporate operation of M&A, both types of advice could be rendered, but they will never be rendered simultaneously to the same client. In that sense, investment advice and corporate advice, in AMAFI’s view, are mutually exclusive. To the main shareholder/manager described above, because the objective is entrepreneurial, the service could only be “corporate finance advice” (at a later stage, the seller of a business having sold pursuant to corporate finance advice could seek “investment advice” regarding the way to invest the proceeds of the sale<sup>11</sup>). To the minority shareholder concerned by the same operation, it could be “investment advice” in a limited number of cases.

**46.** AMAFI certainly agrees that there is a need to clarify the respective scope of each of these two types of advice and that the wording used by MiFID is confusing. It believes however that in doing so, the regulators should be guided by the original intention of the European legislator, which was clearly to have two different services, one investment service regulated under MiFID and one ancillary service, such duality calling for a clear differentiating criterion. In this connection, the feeling that a given party in a given operation might be in need of protection and that, in that case, as suggested by CESR, in the event of a doubt as to the nature of the advice, it would be preferable to opt for the most protective approach (i.e. consider that the investment advice characterisation is more protective because it implies the implementation of the suitability test) cannot serve as an appropriate criterion.

AMAFI believes that if the need to protect certain categories of people is identified, it is up to the legislator/regulator to issue the appropriate regulation to ensure sufficient protection. But the existing regulation cannot be bent and interpreted just for that purpose. A legal characterisation must be based and can only be based on the objective application to a given situation of the criteria set by the legislator, criteria which of course should be clear or clarified if necessary.

In this connection, it should also be recalled that clients who seek corporate finance advice are not left without legal protection. They generally enter into a very detailed contract with the professional firm rendering such service. Such contract (or “mandate”) defines quite specifically the objectives of the client (which are therefore perfectly known by the professional firm) the scope of the service sought by the client and the terms and conditions under which the service will be rendered. Therefore, the client benefits from a certain degree of protection.

**47.** In conclusion, AMAFI believes that vis-à-vis a given client, the “investment advice” and the “corporate finance advice” are mutually exclusive. To determine which type of advice is involved in a given situation, one should look exclusively at the main objective of the advice sought by the client or given to him at the firm’s initiative: if the objective is patrimonial, then the advice may be “investment advice”. If on the other hand, the objective is entrepreneurial / industrial, then the advice can only be “corporate finance advice”.



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<sup>11</sup> Likewise, during the life of the company, the management may seek « *investment advice* » regarding the best way to invest the excess cash it may hold: in that case, the same client (the management of the company) may receive “*investment advice*” and simultaneously “*corporate finance advice*”, if at that moment it is involved in some “entrepreneurial” project, but it will not be in connection with the same operation, the two types of advice corresponding clearly to two separate objectives.