Chapter 10

Appropriateness (for non-MiFID and non-insurance-based investment products non-advised services) (non-MiFID and non-insurance-based investment products provisions)
10.1 Application

10.1.1 [deleted]

10.1.2 This chapter applies to a firm which arranges or deals in relation to a non-readily realisable security, derivative or a warrant with or for a retail client, other than in the course of MiFID or equivalent third country business, or facilitates a retail client becoming a lender under a P2P agreement and the firm is aware, or ought reasonably to be aware, that the application or order is in response to a direct offer financial promotion.

10.1.3 [deleted]

Related rules

10.1.4 A firm that is carrying on a regulated activity on a non-advised basis, whether or not the rules in this chapter apply to its activities, should also consider whether other rules in COBS apply.
10.2 Assessing appropriateness: the obligations

10.2.1

(1) When providing a service to which this chapter applies, a firm must ask the client to provide information regarding his knowledge and experience in the investment field relevant to the specific type of product or service offered or demanded so as to enable the firm to assess whether the service or product envisaged is appropriate for the client.

(2) When assessing appropriateness, a firm must determine whether the client has the necessary experience and knowledge in order to understand the risks involved in relation to the product or service offered or demanded.

10.2.2

The information regarding a client's knowledge and experience in the investment field includes, 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, information on:

(1) the types of service, transaction and designated investment with which the client is familiar;

(2) the nature, volume, frequency of the client's transactions in designated investments and the period over which they have been carried out;

(3) the level of education, profession or relevant former profession of the client.

10.2.3

A firm must not encourage a client not to provide information required for the purposes of its assessment of appropriateness.

Reliance on information

10.2.4

A firm is entitled to rely on the information provided by a client unless it is aware that the information is manifestly out of date, inaccurate or incomplete.
Use of existing information

10.2.5 G When assessing appropriateness, a firm may use information it already has in its possession.

Knowledge and experience

10.2.6 G Depending on the circumstances, a firm may be satisfied that the client’s knowledge alone is sufficient for him to understand the risks involved in a product or service. Where reasonable, a firm may infer knowledge from experience.

Increasing the client's understanding

10.2.7 G If, before assessing appropriateness, a firm seeks to increase the client's level of understanding of a service or product by providing information to him, relevant considerations are likely to include the nature and complexity of the information and the client's existing level of understanding.

No duty to communicate firm's assessment of knowledge and experience

10.2.8 G If a firm is satisfied that the client has the necessary experience and knowledge in order to understand the risks involved in relation to the product or service, there is no duty to communicate this to the client. If the firm does so, it must not do so in a way that amounts to making a personal recommendation unless it complies with the rules in COBS 9 (Suitability (including basic advice) (non-MiFID provisions)).

P2P agreements

10.2.9 G (1) When determining whether a client has the necessary knowledge to understand the risks involved in relation to a P2P agreement or a P2P portfolio, a firm should consider asking the client multiple-choice questions that avoid binary (yes/no) answers and cover, at least, the following matters:

(a) the nature of the client’s contractual relationships with the borrower and the firm;
(b) the client’s exposure to the credit risk of the borrower;
(c) that all capital invested in a P2P agreement or P2P portfolio is at risk;
(d) that P2P agreements or P2P portfolios are not covered by FSCS;
(e) that returns may vary over time;
(f) that entering into a P2P agreement or investing in a P2P portfolio is not comparable to depositing money in a savings account;
(g) the characteristics of any:
   (i) security interest, insurance or guarantee taken in relation to the P2P agreements or P2P portfolio; or
   (ii) risk diversification facilitated by the firm; or
   (iii) contingency fund offered by the firm, or
(iv) any other risk mitigation measure adopted by the firm;
(h) that any of the measures in (g) adopted by the firm cannot guarantee that the client will not suffer a loss in relation to the capital invested;
(i) that where a firm has not adopted any risk mitigation measures (such as those in (g)), the extent of any capital losses is likely to be greater than if risk mitigation measures were adopted by the firm;
(j) illiquidity in the context of a P2P agreement or P2P portfolio, including the risk that the lender may be unable to exit a P2P agreement before maturity even where the firm operates a secondary market;
(k) the role of the firm and the scope of its services, including what the firm does and does not do on behalf of lenders; and
(l) the risks to the management and administration of a P2P agreement or P2P portfolio in the event of the firm's becoming insolvent or otherwise failing.
10.3 Warning the client

10.3.1 If a firm considers, on the basis of the information received to enable it to assess appropriateness, that the product or service is not appropriate to the client, the firm must warn the client.

(2) This warning may be provided in a standardised format.

10.3.2 If the client elects not to provide the information to enable the firm to assess appropriateness, or if he provides insufficient information regarding his knowledge and experience, the firm must warn the client that such a decision will not allow the firm to determine whether the service or product envisaged is appropriate for him.

(2) This warning may be provided in a standardised format.

10.3.3 If a client asks a firm to go ahead with a transaction, despite being given a warning by the firm, it is for the firm to consider whether to do so having regard to the circumstances.
10.4 Assessing appropriateness: when it need not be done

10.4.1 (1) A firm is not required to ask its client to provide information or assess appropriateness if:
   (a) the service only consists of execution and/or the reception and transmission of client orders, with or without ancillary services, it relates to particular financial instruments and is provided at the initiative of the client;
   (b) the client has been clearly informed (whether the warning is given in a standardised format or not) that in the provision of this service the firm is not required to assess the suitability of the instrument or service provided or offered and that therefore he does not benefit from the protection of the rules on assessing suitability; and
   (c) the firm complies with its obligations in relation to conflicts of interest.

(2) The financial instruments referred to in (1)(a) are:
   (a) [deleted]
   (b) money market instruments, bonds or other forms of securitised debt (excluding those bonds or securitised debt that embed a derivative); or
   (c) [deleted]
   (d) other non-complex financial instruments.

(3) A financial instrument is non-complex if it satisfies the following criteria:
   (a) it is not a derivative or other security giving the right to acquire or sell a transferable security or giving rise to a cash settlement determined by reference to transferable securities, currencies, interest rates or yields, commodities or other indices or measures;
   (b) there are frequent opportunities to dispose of, redeem, or otherwise realise the instrument at prices that are publicly available to the market participants and that are either market prices or prices made available, or validated, by valuation systems independent of the issuer;
   (c) it does not involve any actual or potential liability for the client that exceeds the cost of acquiring the instrument; and
   (d) adequately comprehensive information on its characteristics is publicly available and is likely to be readily understood so as to
enable the average retail client to make an informed judgment as to whether to enter into a transaction in that instrument.

10.4.2 If a client engages in a course of dealings involving a specific type of product or service through the services of a firm, the firm is not required to make a new assessment on the occasion of each separate transaction. A firm complies with the rules in this chapter provided that it makes the necessary appropriateness assessment before beginning that service.

10.4.3 [deleted]
10.5 Assessing appropriateness: guidance

The initiative of the client

10.5.1 A service should be considered to be provided at the initiative of a client (see COBS 10.4.1 R (1)(a)) unless the client demands it in response to a personalised communication from or on behalf of the firm to that particular client which contains an invitation or is intended to influence the client in respect of a specific financial instrument or specific transaction.

10.5.2 A service can be considered to be provided at the initiative of a client notwithstanding that the client demands it on the basis of any communication containing a promotion or offer of investments made by any means that by its very nature is general and addressed to the public or a larger group or category of clients.

Personalised communications

10.5.3 (1) Communications to the world at large, such as those in newspapers or on billboards, are likely to be by their very nature general and therefore not personalised communications.

(2) Communications addressed to a client (such as, for example, an email, telephone call or letter), may or may not be personalised depending on the content.

(3) A communication is not personalised solely because it contains the name and address of the client or because a mailing list has been filtered.

(4) If a firm is satisfied that a communication does not contain any personalised content, it may wish to make clear that it does not intend the communication to be personalised and that the personal circumstances of the recipient have not been taken into account.

10.5.4 [deleted]

Independent valuation systems

10.5.5 The circumstances in which valuation systems will be independent of the issuer (see COBS 10.4.1 R (3)(b)) include where they are overseen by a depositary that is regulated as a provider of depositary services in a EEA State.
10.6 When a firm need not assess appropriateness

10.6.1 A firm need not assess appropriateness if it is receiving or transmitting an order in relation to which it has assessed suitability under COBS 9 (Suitability (including basic advice)).

10.6.2 [deleted]
10.7 Record keeping and retention periods for appropriateness records

10.7.1 G A firm is required to keep orderly records of its business and internal organisation, including all services and transactions undertaken by it. The records may be expected to include the client information a firm obtains to assess appropriateness and should be adequate to indicate what the assessment was.

10.7.2 R The firm must retain its records relating to appropriateness for a minimum of five years.