

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 **R** [deleted]

10.1.2 **R** (1) This chapter applies to a *firm* which *arranges or deals* in relation to a *non-readily realisable security, speculative illiquid security, derivative or 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*.

(2) Where a *rule* in this chapter applies to a *firm* which *arranges or deals* in relation to a *speculative illiquid security*, the *rule* also applies to:

- a *TP firm* (to the extent that the *rule* does not already apply to such a *TP firm* as a result of ■ GEN 2.2.26R); and
- a Gibraltar-based firm (having the same meaning as in the *Gibraltar Order*) to the extent that the *rule* does not already apply to such a Gibraltar-based firm as a result of ■ GEN 2.3.1R).

10.1.3 **R** [deleted]

Related rules

10.1.4 **G** 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 **R** (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 **R** 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 **R** A *firm* must not encourage a *client* not to provide information required for the purposes of its assessment of appropriateness.

- 10.2.4 **R** **Reliance on information**
 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 **R** (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 **R** (1) 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 **G** 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

R

- (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 **R** 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 **R** [deleted]



10.5 Assessing appropriateness: guidance

The initiative of the client

- 10.5.1 **G** 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 **G** 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 **G**
- (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 **G** [deleted]

Independent valuation systems

- 10.5.5 **G** 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 the *United Kingdom*.



10.6 When a firm need not assess appropriateness

10.6.1 **G** 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 **G** [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.

