



*MIFID Policy –
Suitability and Appropriateness*

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1. Purpose of the document

The purpose of this document is to demonstrate and describe how EWUB (hereafter “the Bank”) ensures its understanding of the nature, features, costs and risks of investment services and financial instruments selected for its clients and that the Bank assesses, while taking into account cost and complexity, whether equivalent investment services or financial instruments can meet their client’s profile (as per article 54, paragraph 9 of MiFID II Delegated Regulation – 25th April 2016 – Organizational Requirements (Hereinafter referred to as the “**Organizational Requirements**”)).

This demonstration is performed by the implementation of suitability and appropriateness processes.

2. Suitability

A. Definition

The suitability assessment is a process elaborated by the Bank to ensure that investment services such as investment advisory services (in the sense of giving "personal recommendations") or discretionary portfolio management (hereafter “DPM”) services match the client’s investment objectives, financial situation and knowledge & experience (the "Suitability Obligation" as per Recital 87 of the Organizational Requirements).

This assessment obligation applies to all types of clients in respect of MiFID business (including those clients who in relation to the provision of other services would be classified as eligible counterparties), as well as for retail clients.

B. Suitability information capture

In order to make an assessment of the suitability, the Bank needs to obtain the necessary information in relation to the client to evaluate:

- (i) his investment objectives (incl. time horizon and risk tolerance);
- (ii) his financial situation (incl. ability to bear loss);
- (iii) his knowledge and experience.

All the necessary information is captured at the on-boarding of the client via MiFID II Investor Questionnaires for Individuals and for Legal Entities (as per paragraph 2, Article 54 of the Organizational Requirements) and the Suitability Obligation is the full responsibility of the Bank. These questionnaires are mandatory for all clients and cover all types of investment services provided by the Bank. Therefore, the Bank expects to have sufficient information to perform DPM transactions and issue, within a defined investment universe, Advisory recommendations (as per paragraph 8, Article 54 the Organizational Requirements).

Knowledge and experience can be assumed as sufficient for products, services or transactions in respect of which a client has been classified as professional. It cannot be assumed as sufficient for retail clients.

Similarly, it can be assumed that a per se professional client has the ability to financially bear any related investment risks consistent with his investment objectives if the service provided is investment advice (in the form of personal recommendations). This cannot be assumed for retail clients or for "opted-up" professional clients or when providing DPM services to any type of client (as per paragraph 3, Article 54 of the Organizational Requirements).

The Bank has adopted a conservative approach considering that the ability to bear a loss is assessed in the Investor Questionnaire for both Individuals and Legal Entities by means of specific questions. These questions are part of the client risk scoring process whatever is his category (e.g. retail, pro or EC) and cannot be separated from the risk scoring methodology. Therefore, when providing DPM and Advisory service, the ability to bear a loss is part of the suitability assessment for all clients.

In case DPM services involve switching investments, the Client receives an ex-ante costs and charges report which provides him with a transparent picture on possible costs. The reports depict scenarios of an investment gaining and losing in price in order for the Client to be able to assess costs compared to potential benefits from investments (as per paragraph 11, Article 54 of the Organizational Requirements). The Bank does not charge a fee for switching between investments.

C. Suitability client disclosure

The Bank informs its clients that it undertakes the suitability assessment and that the reason for assessing suitability is to enable the Bank to act in the client's best interests. This information is disclosed in the Discretionary Portfolio Management (DPM) agreement and in investor questionnaires (as per paragraph 1, Article 54 of the Organizational Requirements).

D. Suitability framework content

The Bank has designed a suitability framework to ensure that every trade for every client under a DPM or advisory service will be covered by the suitability process in order to provide investments services fitting to client's expectations. For DPM, this framework covers all types of clients (incl. retail) as below:

- Client categorization;
- Client and Portfolio risk level classification;
- Knowledge assessment for retail clients;
- Risk scoring of financial instruments;
- Concentration limit controls;
- Blocking of orders in case of unsuitability.

The suitability framework allows to assess the "Suitability Obligation" both at trade level and at portfolio level to cover both DPM and Advisory services within the same framework.

Thus, it ensures a higher degree of protection for DPM clients because assessing suitability only at portfolio level would mean that a low allocation of a risky product could be equal to high allocation of a riskless product. The Bank considers that a client with a conservative profile shall not hold a risky product whatever is its allocation at any moment.

E. Suitability transaction scope

The suitability process is performed for each decision to buy or sell under DPM services for all clients without any exemptions, and for any type of recommendation under Advisory service.

New suitability requirements apply starting from 03/01/2018. Therefore, any previously acquired instruments held in clients' portfolios on this date which would be qualified as unsuitable both at trade and at portfolio level for DPM service will be subject to disposal taking into account the best interest of the client.

F. Suitability process description

The Investor Questionnaire is composed of mandatory questions filled by the client with regards to necessary information to be collected (e.g. suitability information capture section). Each answer is subject to a dedicated scoring leading to a consolidated result.

The result is then compared to the risk level classification table in order to identify types of DPM portfolios and instruments that are suitable to the client:

- **for DPM portfolios** – DPM portfolios of a risk level corresponding to the client’s score and of all lower risk levels are suitable for the client;
- **for advised instruments** – instruments of a risk level corresponding to the client’s score and of all lower risk levels are suitable for the client.

RISK LEVELS

Risk Level borders differ for individuals and legal entities and questionnaires contain different sets of questions and result in a different total maximum score.

Risk Level Codification	DPM Strategy	Instruments Risk Class for Advisory	Individuals		Legal Entities	
			Score (from)	Score (to)	Score (from)	Score (to)
R1	0% Equity + IG	1	0	14	0	16
R2	0% Equity + HY	2	14	28	16	32
R3	25% Equities + IG	3	28	42	32	48
R4	25% Equities + HY	4	42	56	48	64
R5	50% Equities	5	56	70	64	80
R6	75% Equities	6	70	84	80	96
R7	100% Equities	7	84	98	96	112

The scoring methodology is detailed in the *Scoring Manual for the Investor’s Questionnaire*.

Each instrument belonging to the DPM investment universe will be risk-scored between 0 and 6 by the Asset Manager in accordance with the Instrument Scoring Procedure.

In the process of managing a portfolio, the Asset Manager takes a decision to buy or sell a financial instrument based on his investment strategy. Prior to entering the order into T24, the Asset Manager initiates a “DPM Assessment Form” document (the “DAF”) with the respective parameters of the instrument.

Then the PAM performs the suitability test which consists to compare the instrument risk profile with the portfolio risk level whatever is the type of client.

For retail clients, there is an additional control on client’s Knowledge & Experience. The PAM controls that the client has the required knowledge based on the client’s answers in the investor questionnaire. The knowledge is compared with the instrument details provided in the DPM Assessment Form.

If assessments are positive (suitability test + knowledge for retail clients), then the PAM is empowered to conclude that the investment is suitable and notifies the AM that the trade can be processed in T24 system.

The suitability process has been designed to control the asset allocation at the inception of the order by the Asset Manager and the suitability control will be performed at trade and portfolio level. The rationale is that:

- The Knowledge and Experience is assessed in the same questionnaire than the financial situation and investment objectives leading to a global score. Assessing all of them at trade level does not create more difficulty and it guarantees a higher level of control;
- The Bank considers this process of suitability check as a whole for both DPM and Advisory services to standardize this flow (and automatize it more easily).

In addition, when both tests on asset allocation and at trade level are successful, the order is inputted in T24. T24 will automatically process controls on asset allocation. This provides for a double check of the Asset Manager’s evaluation against the IT system of the Bank (as per recital 81 from Suitability Guidelines).

G. Suitability result

Unsuitable result:

When providing DPM and Advisory services, the Bank shall not recommend or decide to trade where none of the services or instruments are suitable for the client (as per paragraph 10, Article 54 of the Organizational Requirements); this is the reason for the suitability framework to contain a block of the order execution if:

- The security is not in the approved list for DPM;
- The asset allocation exceeds limits defined;
- The knowledge and experience of the retail client is not sufficient to invest in this product;
- The product is not suitable to the risk profile of the client;

However, the firm could proceed on a non-advised, execution only basis in relation to that instrument if:

- a. the client had wished to do so and
- b. had confirmed this in writing, and
- c. that doing so was consistent with the firm's obligation to act in the client's best interests.

The firm will need to check if there is an obligation to test appropriateness when providing the non-advised service.

In some cases, there may be no obligation to test appropriateness if the instrument is a non-complex instrument and if the client is not retail. This is detailed in the next section “*Appropriateness*”.

Suitable result:

If the result of the suitability process is positive, then the order is processed and executed.

H. Suitability reports

Although MiFID does not expressly require firms who have to assess suitability to provide the client with a suitability report, it does require the provision of adequate reports on the service provided (as per paragraph 12, Article 54 of the Organizational Requirements). For Advisory, a dedicated ex-ante report with the results of the suitability assessment (the “Suitability Statement”) will be issued to inform the client of the suitability of his investment before the trade occurs. The Suitability Statement is generated on the basis of a pre-order/advice. The frequency will be ad-hoc / event-based – issued in respect of each relevant log entry.

As part of the suitability process, the Suitability Test executed in respect of DPM should result in an ex-post Suitability Report (based on the logged suitability tests performed during the reporting period) to inform the client that a suitability test has been performed in respect of DPM investments and containing the results of such tests. The frequency will be quarterly (issued in respect of the logged suitability tests performed during the past quarter) for DPM (as per paragraph 13, Article 54 of the Organizational Requirements).

3. Appropriateness

A. Definition

The appropriateness assessment is a process elaborated by the Bank to ensure that investment services **other** than investment advisory (in the form of personal recommendations) and DPM are in line with the **retail** client’s knowledge & experience when a product is deemed to be classified as **complex**.

The Bank assumes that a professional client has the necessary knowledge and experience in order to understand the risks involved in relation to the particular products or services for which he has been classified as a professional client.

A product is deemed to be **complex** when:

- it incorporates a structure which makes it difficult for the client to understand the risk of return or the cost of exiting the product before contractual term;
- it incorporates a clause, condition or trigger that could fundamentally alter the nature or risk of the investment.

B. Appropriateness information capture

For such services, the Bank requires all clients to provide information about their knowledge and experience in the investment field relevant to the specific type of product or service offered or demanded in order to enable the Bank to assess whether the product or service envisaged is appropriate for them in the sense that they have the necessary experience and knowledge in order to understand the risks involved in relation to the product or service (as per paragraph 1, article 56 of the Organizational Requirements).

The knowledge and experience is captured at the client's on-boarding via the investor questionnaire (mandatory for both Individuals and legal entities) for all types of investment services provided by the Bank and related to the following products:

- Fixed-term deposits
- Equities
- Simple bonds
- Complex bonds
- UCITS funds
- Complex funds such as hedge funds and alternative ones
- Structured products
- Derivatives (hedge)
- Derivatives (speculation)
- Commodities

Therefore, the Bank expects to have sufficient information to perform the appropriateness test at trade level. Warnings will be only generated if the result of the knowledge assessment is negative.

C. Appropriateness framework content

The Bank has designed an appropriateness framework to ensure that every trade for every retail client under an execution-only service will be covered by the appropriateness process in order to warn the client if his investments do not fit his knowledge. This framework contains the following:

- Client categorization;
- Instrument classification;
- Knowledge assessment for retail clients;
- Warning generation.

D. Appropriateness assessment scope

The appropriateness process is performed for each client order to buy or sell financial instruments received by the PAM under execution-only services, with a dedicated knowledge assessment for retail clients.

E. Appropriateness process description

The Investor Questionnaire contains the client's knowledge information to be collected.

If the client is retail, then the PAM will check the complexity of the security based on the classification between complex and non-complex provided by an independent financial data provider as contracted by the Bank.

If the product is deemed to be complex, then the PAM must compare the client's knowledge mentioned in the related Investor Questionnaire with the type of instrument the client is intending to buy or sell. This is the appropriateness test.

F. Appropriateness result

Inappropriate result:

If the result of the knowledge assessment is negative, the PAM will notify the Client by generating a warning via a communication channel approved for communication with that client and classified as durable medium. The warning will explain that the security which the Client intends to buy or sell, is not appropriate for him based on his knowledge and that trading it may put the Client at a significant risk (as per paragraph 2, article 56 of the Organizational Requirements).

If a client is provided with a warning but still wishes to proceed, the PAM must receive the confirmation from the client that he is willing to trade and confirm by e-mail to the Trader that the trade can be done.

If the client does not provide such a confirmation, it means he wishes to cancel the order. In this case the process is stopped. The cancellation must be received via a channel of communication defined in the client file (in case confirmation is received via a recorded line, a call report is prepared).

In case a client is unreachable within 5 working days, this is logged and the order request is automatically cancelled.

Appropriate result:

If the appropriateness test is positive, then the PAM confirms by e-mail to the Trader that the trade can be done. Then the order is processed and executed.

G. Appropriateness reports

There is no specific appropriateness report under the MiFID II regulation. Only the trade confirmation will be circulated to the client after the trade has been processed.

The Bank shall maintain records of the results of appropriateness assessments. The following information must be stored as evidence:

- Confirmation that the Client has received a warning that the instrument is not appropriate (an e-mail with a warning attached sent via a channel of communication as defined in the client file).
- Confirmation from the Client that he is willing to trade received via a channel defined in the client file (in case confirmation is received via a recorded line a call report is prepared);

4. Suitability and Appropriateness within the investment services framework

Suitability and Appropriateness processes are an integral part of the investment services framework of the Bank (as summarized in Exhibit 1) and as such are embedded into all the workflows related to any existing or future service which results in an investment (or a termination of such) on the part of any client of the Bank. As such, Suitability and Appropriateness procedures shall always be performed to the level of completeness, in the exact sequence and in respect of the complete set of events a provided for by the regulations of the Bank.

5. Applicable controls for EWUB investment activities

A. 1st level controls

1st level controls will be performed in 2 steps.

The **first step** will be conducted by the PAM at the account opening and reviewed at least on an annual basis or ad hoc in case of change of client classification or profile, or when information required for the suitability & appropriateness processes is received by the PAM.

The Suitability & Appropriateness 1st level controls will be:

- Ensuring completion of the Investor Questionnaire (incl. client's knowledge),
- Ensuring client classification has been performed,
- Ensuring client risk level has been defined,
- Ensuring portfolio risk level has been defined.

The **second step** will be conducted at trade level.

The Suitability 1st level controls will be:

- Ensuring assessment of the retail client's knowledge has been performed,
- Ensuring assessment of the instrument suitability has been performed,

The Appropriateness 1st level controls will be:

- Ensuring instrument complexity has been established,
- Ensuring assessment of the retail client's knowledge has been performed,
- Ensuring client has received a warning and has provided his consent to trade if the appropriateness test had shown an investment to be inappropriate,

Please note that all controls with regards to Suitability and Appropriateness are described in detail in the related procedures / manuals.

For suitability, some additional controls will be performed by the Asset Manager to ensure the instrument he intends to buy or sell is part of the DPM approved list of instruments at trade level.

For Appropriateness, some additional controls will be performed by the Trader to ensure that the Client has received a warning that the instrument is not appropriate and that he is willing to trade.

B. Compliance 2nd level controls

Compliance:

The Compliance Officer will perform ad hoc spot checks with a minimum of frequency of once per annum (the frequency will be defined based on the number of clients) on the 1st step of controls to ensure the PAM had fulfilled his responsibilities at the account opening in respect of the collection, completion and coherence of the investor questionnaire and deriving the client risk profile.

The Compliance Officer will also perform ad hoc spot checks with a minimum of frequency of once per annum (the frequency will be defined based on the volume of trades) on the 2nd step of controls to ensure the PAM, the Asset Manager and the trader involved in the S&A processes have duly assessed client's knowledge, instrument suitability, complexity and client's consent to trade.

Spot checks will be based on S&A manual forms, e-mail exchanges and all documented durable mediums. Thus, the Compliance Officer will use T24 queries extracting the MiFID and transaction-related data to cross-check accuracy of information provided.

On top of these spot checks, the Compliance Officer will control on an ad hoc basis with a minimum frequency of once per annum the correct storage of all the documentation related to S&A controls performed to ensure an audit could be performed accordingly.

Escalation to Head of Department is possible, in accordance with Escalation Policy provisions.

Risk Management:

Please note that the Appropriateness and Suitability on-going controls are performed at the portfolio level by Risk Management as described in the DPM procedures.

6. Policy non-compliance consequences

The S&A processes are in scope of the CSSF (National Competent Authority) review and will be covered by on-site inspections of the regulating authority starting from 2018.

In case an on-site inspection reveals a breach of the processes and controls, the consequences could be (depending of the significance of the non-compliance of the Bank):

- Findings for remediation leading to a law reminder;
- Administrative fines with the publication of employees and /or the Bank's name on the CSSF website with formal notice to make the processes compliant;

This is part of the annual CSSF report published on their website:

http://www.cssf.lu/fileadmin/files/Publications/Rapports_annuels/Rapport_2016/CSSF_RA_2016.pdf

The sanctions for non-respect of MiFID II requirements have not yet been defined and there is no precedent or benchmark yet.