DYNAMIC
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MIFID II with Dynamic Planner

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1. MIFID II Summary

The Markets in Financial Instruments Directive (MIFID) is the framework of European Union (EU) legislation which regulates, among others, financial advisers providing investment and pensions advice in the UK.

Since 3 January 2018, MIFID II has been in force, with the FCA having updated its regulatory handbooks in line with the new directive.

This document provides a brief, non-exhaustive look at the key changes in MIFID II and how Dynamic Planner can support advice firms in complying with the new regulatory requirements.

1.1 A summary of key changes

In this document, we will look at a number of the MIFID II requirements and how they can be met with Dynamic Planner.

Assessment of suitability and appropriateness and reporting to clients (Article 25)

While there are no significant changes from the current rules under the FCA COBS section 9.2, MIFID II re-iterates that firms must obtain information from the client such as:

- The client's or potential client's knowledge and experience in the investment field relevant to the specific type of product or service.
- That person's financial situation including their ability to bear losses.
- And that person's investment objectives including risk tolerance.

We will look at how Dynamic Planner's risk profile process provides you with a framework for evidencing investment suitability.

Suitability reports

MIFID II reinforces the need to provide a suitability report to advised clients specifying how the advice given meets the client's circumstances and objectives. Importantly, MIFID II mandates that this report is provided to the client ahead of the transaction being concluded.
We will look at how the reports generated from Dynamic Planner can provide a robust audit in a client-friendly and accessible way.

Client servicing

Many firms now provide an ongoing review service to their clients, charging an ongoing fee for the provision of ongoing servicing and monitoring of the client's portfolio. MIFID II mandates that where ongoing suitability is being monitored, it must be done at least on an annual basis.
We will look at the features of Dynamic Planner to help you provide an efficient suitability review process.
Section 6 of this document provides a brief summary of other notable changes introduced by MIFID II which may be of interest to Dynamic Planner users.

2. Assessment of suitability and appropriateness and reporting to clients

The directive re-enforces many familiar elements of the current rules on assessing suitability, as documented in the FCA COBs section 9.

Specifically MIFID II requires the following information in Article 25, which addresses suitability and client reporting:

> *When providing investment advice or portfolio management the investment firm shall obtain the necessary information regarding the client's or potential client's* ***knowledge and experience*** *in the investment field relevant to the specific type of product or service, that* ***person's financial situation*** *including his ability to bear losses, and his* ***investment objectives*** *including his* ***risk tolerance*** *so as to enable the investment firm to recommend to the client or potential client the investment services and financial instruments that are suitable for him and, in particular, are in accordance with his risk tolerance and* ***ability to bear losses****.*

MIFID II, Article 25 .2

2.1 Evidencing suitability using Dynamic Planner

Breaking down the requirement into its constituent parts, we can look at how Dynamic Planner can support advisers in evidencing suitability as part of the advice process.

2.1.1 Client's knowledge and experience

Dynamic Planner provides an investment experience questionnaire as part of the risk profiling process. This questionnaire has nine questions which explore:

- The types of investment arrangement the client has previously held.
- The client's engagement with their current investments.
- Any other relevant prior experience (educational or professional) which may be relevant to the suitability assessment.

Completing the investment experience questionnaire is good practice. Even where a full review of the client's arrangements is conducted as part of the fact find, prior arrangements which have since been disposed of may not come to light unless explicitly explored.

The questionnaire is asked of each individual within the case, and responses can be imported into future cases as the basis for a suitability review.

2.1.2 Documenting the person's financial situation

When looking at the client's financial situation, a number of common Know Your Client (KYC) data points are pertinent.
The client's personal situation can be documented in the Profile section of Dynamic Planner. In particular, the following would be relevant details to include as a background to a suitability assessment:

- The client's age.
- Marital / co-habiting status.
- The number of and relationship of any financial dependents.

In supporting your KYC requirements, Dynamic Planner does offer a cashflow summary which can be used as a baseline for an assessment of the client's ability to bear losses. This cashflow information could help evidence the size and source of the client's regular income and expenditure. This might be deemed a useful source of additional information, to support MIFID II requirements, while not being mandated.

Assets and liabilities should also be documented. Dynamic Planner provides detailed data capture for investment and retirement products, allowing you to provide aggregated views on the client's portfolio (both in terms of value and risk). Dynamic Planner provides a number of valuation integrations to make obtaining this data a quick process – something we will look at further when we discuss ongoing servicing later in this document.

2.1.3 Investment objectives

An understanding of the client's goals and objectives is also required, looking at both soft goals and those that are directly quantifiable in both size and timeframe. Recording the client's objectives in seeking advice, in the client's own words, can also greatly increase the level of personalisation you are able to provide when documenting the recommendations in the final Suitability Report.

Dynamic Planner investment planning module has the ability to capture full details about the objective and purpose of the investment, and in addition, the ability to perform stochastic forecasts to assess the likelihood of meeting the objective given the current risk level, assets and contributions.

2.1.4 Risk tolerance

Dynamic Planner provides three psychometric questionnaires (10, 15 and 20 questions) to ascertain the client's attitude to risk. Each questionnaire ask a series of statements to which the client typically responds to on a standard Likert scale (Strongly agree / Strongly disagree).

The output of the questionnaire provides a risk tolerance score, categorised in Dynamic Planner's 1 – 10 risk profiles. To ensure a full and robust conversation is had, Dynamic Planner provides an inconsistency check, highlighting potentially inconsistent responses from the client.

2.1.5 Ability to bear losses

As an initial start to the conversation, Dynamic Planner provides a capacity for loss questionnaire as part of the risk profiling process. This questionnaire explores three key areas:

- The expected timeframe for the client's investments.
- The client's views on their ability to bear losses from the investments.
- Any liquidity requirements for the investment.

For a full consideration of the client's ability to withstand losses, Dynamic Planner can be used to provide a number of forecasts to demonstrate the client's likelihood of meeting investment objectives under a number of different scenarios.
Additionally, Dynamic Planner supports the recording of a number of key client facts which can be used to support a robust capacity assessment:

- Client's age and intended retirement age.
- Employment status.
- Financial dependents.
- Income / expenditure.
- Available investment / pension arrangements.

3. Suitability reports

MIFID II introduces two key requirements with respect to suitability reports which may require advice firms to review their processes:

- A suitability report should be provided even where no transaction is recommended – e.g. where the advice is to leave the current arrangements as they are.
- The suitability report must be provided prior to any transaction taking place.

> *When providing investment advice, the investment firm shall, before the transaction is made, provide the client with a statement on suitability in a durable medium specifying the advice given and how that advice meets the preferences, objectives and other characteristics of the retail client.*
> *MIFID II, Article 25 .6*

3.1 Dynamic Planner Reports

Dynamic Planner does not provide a suitability report. However, the reports which are generated can form valuable appendices to a suitability report, keeping the main body of the report short and concise.

Risk profile report

The risk profile report documents the rationale for the selected risk profile, including responses to the risk profiling questionnaires and adviser notes.

Financial plan

The financial plan presents the client with a view of their current arrangements and any proposed changes. It shows both the asset allocation and forecasts for both portfolios.

Fact find

The fact find provides a summary of the data captured to support the financial plan and can be provided as the basis for any recommendations to the client.

3.2 AccessAdvice – providing automated advice on Stocks & Shares ISAs

Our digital advice proposition, AccessAdvice, allows advice firms to provide a white labelled ISA investment process via their existing website.

AccessAdvice already complies with the MIFID II requirements, providing a full suitability report prior to any transaction occurring. The report is provided to the client ahead of the adviser reaching out to answer any questions and arrange for the transaction to be completed.

4. Providing an ongoing suitability assessment

Where firms provide a suitability assessment as part of their ongoing services to the client, there are additional requirements regarding the breadth and frequency of the review.

The suitability review must consider the same key points as when the portfolio was originally recommended as being suitable for the client as part of the initial recommendation. As such, the suitability review must consider, among other things:

- Changes to the client's circumstances (either personal or financial).
- the client's or potential client's knowledge and experience in the investment field relevant to the specific type of product or service.
- that person's financial situation including their ability to bear losses.
- investment objectives including risk tolerance.

No doubt many firms already undertake such a review, although MIFID II acts as a formalisation of this requirement. These requirements, however, may substantially increase the work (or workload) involved by advice firms to provide the ongoing service after January 2018 if they impact the original advice given to the client.

Importantly, this review must be conducted at least annually, if not more frequently.

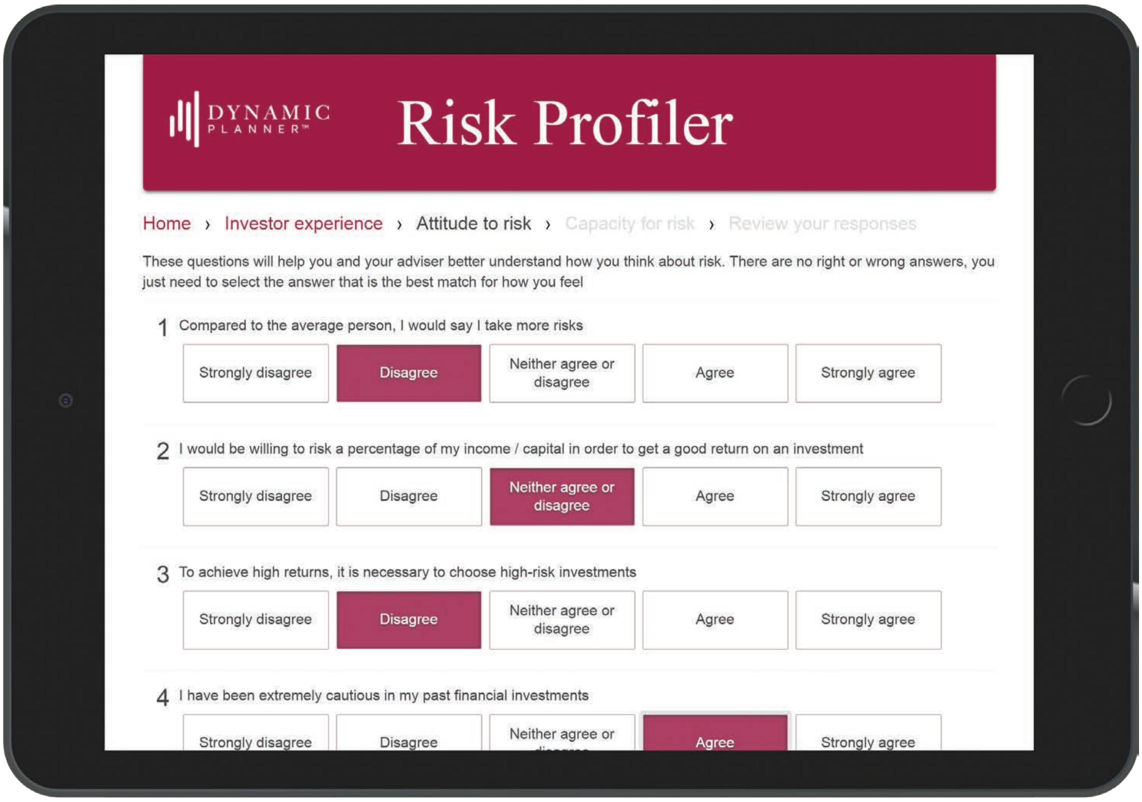
Note – this is only the case where suitability is being assessed on an ongoing basis. It is acceptable for this to not be offered. However, the client must be clear on the nature of the ongoing services being provided at outset.

4.1 Implementing an efficient review process

Dynamic Planner has several features which support firms in providing an efficient suitability review process.

4.1.1 Risk profiling clients

Many firms are now adopting Risk Profile Invites. This feature ensures the firm to send clients an electronic version of the risk profile questionnaires, allowing the adviser to quickly and efficiently assess if there are any changes which need to be considered.



When used as part of a servicing process, Risk Profile Invites can reduce the need for face to face meetings with the client (where desired) and reduce the time taken to gather risk profile responses from the client.

4.1.2 Analysing the client's current portfolio

Another key element of the review process is to look at any changes to the client's current portfolio.

Dynamic Planner streamlines this through electronic valuation integrations with many platforms and providers. These allow the client's current holdings to be updated at the touch of a button, ensuring that the fund holdings and values are up to date.

Aggregated portfolio information is then available through the asset allocation and valuation reports, showing the value and risk associated with the current portfolio. This can be used to identify if any rebalancing is required to re-align the portfolio to the selected risk profile.

4.1.3 Ability to meet financial objectives

Where a financial objective has been recorded, its feasibility can quickly be re-assessed once updated portfolio values have been obtained. The forecasts within Dynamic Planner will use the latest portfolio values along with the latest market assumptions (provided by Dynamic Planner on a quarterly basis) to re-forecast the client's investments. The outcome of the forecast can quickly identify if any changes are required to the client's contributions or objectives.

4.1.4 Managing service levels and activities

While stopping short of a full diary management system, Dynamic Planner's features for Service Levels and Activities can help small and large advice firms plan and manage their obligations for client servicing.

By defining service levels, you can set out a periodic set of activities which must be undertaken within the year. Each activity is recorded, assigned to a member of staff and can be tracked.

5. Dynamic Planner MIFID II Checklist

Criteria	Feature to explore
Types of service, transaction and regulated investments with which the client is familiar	Investor Experience
Nature, volume, frequency of the client's transactions with regulated investments	Investor Experience
Level of education, profession or (if relevant) former profession of the client	Investor Experience
The source and extent of the client's regular income	Fact Find
The client's assets, including liquid assets, investments and real property	Fact Find
The client's regular financial commitments	Fact Find
The ability to bear losses	Capacity - Capacity for loss
The client's investment horizon	Capacity - term
The client's risk preferences, risk profile and risk tolerance	Attitude to risk
Invest for income or growth (with liquidity or not) or keep his/her capital safe and avoid any risk or accept a low risk so as to aim to achieve some level of a profit or accept an appropriately higher level of risk because the client has a higher profit expectation	Capacity for risk

6. Other notable changes

There are a number of other changes introduced in MIFID II, which while Dynamic Planner may not directly help with are still relevant to our users.

Independent / restricted status

MIFID II requires that each individual adviser either provides Independent or Restricted advice. This is a change to the current requirements, where an adviser can set out the nature of advice provided on a client by client basis.

Disclosure of costs and charges

MIFID II brings greater focus on transparency of client charges, for advice, products and funds. Charges should be set out clearly, both in monetary and percentage terms. This is required both ex-ante (pre-sale) and ex post (e.g. as part of an ongoing review service).

Legal Entity Identifiers

If you advise Charities, Trusts or Corporate entities, you may need to investigate if they have a Legal Entity Identifier (LEI). These will be required prior to entering into certain types of financial transaction after MIFID II.

Notifying clients of falls in value

MIFID II requires clients to be notified if their portfolio falls in value by 10% or more. This applies to discretionary managers, but also to advisers with discretionary permissions offering a portfolio management service. If the client is operating on an advised basis then this is not a portfolio management service.

Replacement business

MIFID II introduces explicit requirements for firms providing advice or discretionary investment management which involves switching investments to demonstrate that the benefits outweigh the costs.

Telephone recording

MIFID II requires firms to record transactions with clients which are intended to lead to an investment transaction taking place. This can be in the form of written records but covers a wider (more in-depth) scope of recording.

Recording of calls does, however, apply to discretionary managers or advisers with discretionary permissions offering a portfolio management service. If the client is operating on an advised basis then this is not a portfolio management service and they do not need to physically record the call. However, it could be deemed best practice to record calls.

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