

# Guide to investing

## What is ESMA ?

ESMA stands for the European Securities and Markets Authority. It is an independent European Union regulatory authority, and its offices are in Paris.

One of ESMA's objectives is to enhance investor protection in the financial sector.

It does this by ensuring that the rules applicable to the financial sector are adequately implemented across the European Union.

This is aimed at contributing to increased consumer confidence in the financial system as a whole, and at better protecting customers of financial services.



## Why is ESMA issuing this guide?

Even though there are laws in place in Europe to protect investors, helping consumers through education initiatives such as this information guide is an important step towards helping investors to protect their interests themselves.

This guide is for consumers who have invested, or are planning to invest, in financial products.

No matter how much you are planning to invest, it is important that you know what investment options are available to you. There are different investment services and many different products available, so it is important for you to understand and consider the risks and rewards that you face when choosing different investment services and products.

It is also important for you to understand what your rights are, and what you can expect in terms of information required from you, or provided to you, depending on which type of investment service or product you choose.

This guide aims at giving you practical information on investing so that you are better prepared. Existing laws provide consumers with some level of protection, but in order to make informed choices, you also need to take an active role in the investment process.

## What type of investment services are available?

When investing you should think about the type and amount of support you will want from the investment firm, or the investment service provider, so that you can narrow your focus to those firms that can help you to meet your needs.

Having a clear understanding of what you are looking for can prevent you from paying for what you do not really need, or from choosing a firm that cannot provide you with what you need.

The following investment services are available:

**Investment advice:** You are provided with personal recommendations on products. This service is best suited for investors who want to make their own investment decisions, but also want the support and expert advice of financial advisers.

**Investing (or trading) without investment advice:** The investment firm will receive from you, and then transmit or execute, your orders to buy or sell products - without giving you advice. This service is usually best suited for more experienced or self-reliant investors who are able to collect and evaluate, on their own, information on products and who are able to make investment decisions without the help of others. This type of service is increasingly provided through the internet.

**Portfolio management:** Your investments are managed by an investment firm on your behalf, and you are reliant on the firm's decisions and choices. The firm will not communicate with you every time it makes an investment on your behalf. However, the firm is required to report to you, on a regular basis, on its activities carried out on your behalf. This service (portfolio management) is best suited for investors who are comfortable with delegating the choice of investment to others.



## What questions will you be asked when you seek investment advice or portfolio management services?

When you choose advice or portfolio management, you are placing a higher degree of reliance on the investment firm than you would do in the case of non-advised transactions. You therefore need to be comfortable that the firm understands your individual needs and circumstances so that it can recommend, or buy and sell, the right product for you.

It is important for the firm to gather complete and accurate information from you to enable it to recommend, or select, products that are suitable for you. It is in your best interests that you provide the firm with correct, up-to-date and complete information. You should also keep the firm updated regarding any significant changes to your situation. The firm has an obligation to keep all this information confidential.

The firm will need to ask you several questions as part of what is called a **suitability assessment**. These questions are focused on your investment objectives, your financial situation, and your knowledge and experience. The firm will adapt its recommendations according to your answers.

**Your investment objectives:** Questions regarding your investment objectives can include:

- The purpose of the investment. For example, your goals could be to invest for income (regular payments such as dividend or interests), or for growth (increase in the value of your capital at maturity of the investment), or to keep your capital safe. This information also relates to your *risk appetite* and profile.
- The amount of the investment.
- The length of time you wish to hold the investment. This information is especially important when buying products that could be difficult, or costly, for you to sell before their contractual maturity. This information is also important with regard to how certain investments are taxed (for example, taxation may be linked to the retention period of the product).
- Your risk appetite and profile. It is important for the firm to understand whether you wish to limit the risks you take, or to accept a higher level of risk with greater potential for reward, but also possible capital loss.

**Your financial situation:** Information regarding your financial situation may be obtained through questions about matters such as your income, your assets, your debts and any other financial commitments you have. You can therefore expect to be asked questions on the following matters:

- Summary of assets (for example, cash held at a bank, property, or other investments). The firm should, where relevant, also gather information about conditions, terms, access, loans, guarantees and other restrictions, if applicable, to these assets.
- Summary of liabilities and regular financial commitments (for example, rent, school fees, life insurance cover).
- The extent of your regular income and total income, whether it is earned on a permanent or temporary basis, and the source of this income (for example, from employment, retirement income, investment income, rental yields etc).
- Health care plans.
- Retirement planning arrangements.
- Your employment situation.
- Your marital status.
- Your family situation (this may impact your financial situation – for example, in the event of a birth or when your children are at an university going age).

**Your knowledge and experience:** Information regarding your knowledge and experience of financial markets and products may be gathered through questions on:

- The types of services, transactions and products with which you are familiar.
- The nature, volume and frequency of your previous transactions.
- Your level of education.
- Your profession or former profession.



These lists are not exhaustive. You may be asked for other information too. The law requires firms to gather information from you. The extent of information gathered will vary according 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.

Always remember that it is in your best interests to provide the firm with as complete a picture as possible of your personal situation and objectives. This is so that the firm has all the information necessary for it to make a suitable recommendation for you. Of course, data protection laws exist to protect your personal data and privacy.

If a firm providing advice or portfolio management does not, or cannot, obtain the necessary information to assess suitability, then it cannot make a recommendation, or make decisions on your behalf. If you provide only limited or wrong information, this will affect the nature of the service the investment firm will be allowed to provide to you.



## What questions will you be asked when you do not ask for investment advice?

When you want a firm to buy or sell an investment without providing you with advice or portfolio management services, the firm will need to verify what is called the **appropriateness** of the product for you. You should understand what the implications are, and the level of risk, in this sort of service.

The firm will need to ask you questions on your knowledge and experience relating to the specific investment in order to assess whether that product is appropriate for you. The sorts of questions that you may be asked include:

- The types of services and products with which you are already familiar.
- The nature, volume and frequency of your previous transactions.
- Your level of education.
- Your profession or former profession.

It is important for you to understand that a key objective of these questions is to verify whether you have the necessary experience and knowledge in order to understand the risks involved in relation to the specific investment.

If the firm concludes that you have the necessary knowledge and experience to understand the risks involved, then the firm may go ahead with the transaction you selected.

Alternatively, you will receive a warning from the firm saying that either the firm does not regard the proposed transaction as appropriate for you, or that the information is not enough to enable it to determine the appropriateness. If you insist on going ahead with the transaction anyway, you do so at your own risk.

## What questions should you ask yourself and the firm?

It is important to ask questions before you make any decision regarding your investments (advised or non-advised). Do not feel intimidated. Remember that it is your money.

A firm must provide you with certain information, including information on who regulates it and the services it is authorised to offer. This information is aimed at helping you to understand the nature of its services, the types of products on offer and the risks involved. Do not hesitate to check this information. If anything is unclear, or you do not understand, or you feel you need more information, ask for it.

### Ask questions to help you understand the products and the risks associated with them

As it is you who makes your investment decisions, you should be sure you understand the relative advantages, disadvantages, and risks of different types of investments. You will receive information explaining the nature, risks and costs of products. This information includes, for example, a description of a product's risks and whether prices/values may fluctuate. The amount of information will depend on the type of product, its complexity and risk profile.

Remember that all investments involve some level of risk: taking higher risks increases the likelihood that you may lose some or all of your initial investment. It's important to understand what your investment choices are and how different types of investments put your money to work. Risks and potential returns vary greatly from investment to investment.

### Ask about fees, costs and charges

Investment advice and portfolio management services are not free. When you ask for advice or portfolio management services, ask the firm how much it will charge you at the start and in the future.

It is important to understand how the firm is paid for its services, so ask the firm to explain this. For instance, does it receive fees or commission or other benefits from the manufacturers of the products that it is recommending or is investing in on your behalf? This will also help you to evaluate the firm's independence when making investment recommendations or investing on your behalf.

- Different products have different costs and charges. For some products, such as stocks and bonds, it is likely that you will be asked to pay a one-off commission for buying or selling the product.
- For other products, such as mutual funds, some fees are charged at specific times, based on actions you take, and some are charged on an on-going basis. Fees are described in detail in each fund's prospectus, which you should read before investing.
- In addition, the holding by firms of most investment products is likely to generate some additional fees called *custody fees*. These fees are payable by you.

### Ask for information about the firm

Firms need to be authorised to provide services. If a firm is not authorised to provide investment services and activities, it is not allowed to provide them.

Always check if the firm is authorised in your country on <http://www.esma.europa.eu/page/Investment-Firms> or on the website of the firm's national regulator.

### **Information on portfolio management**

Where you have asked a firm to manage investments on your behalf (portfolio management), you should receive information including a description of the management objectives, the related level of risk, what types of products or transactions may be included in your portfolio, and information about the valuation method and the frequency of valuations of your investments. You should also ask how the performance of your portfolio will be calculated.

### **Ask about the progress of your investments**

Ask for information on how frequently you will receive statements and on their content. This will make it easier for you to understand the statements once they arrive. During your relationship with the firm, always ask for updates on the return of your investments and consider, or even discuss with the firm, whether they are meeting your expectations and goals. Are those investments performing as you were led to believe?

### **Ask about the firm's execution policy**

To complete the purchase or sale of products, your firm is required to achieve the best possible result for you. The firm's execution policy will include information on how and where the firm executes orders, and the factors affecting the choice of execution venue.

### **Ask for the firm's policy on conflicts of interest**

Firms are required to act in your best interests. In order to do this, they are required to have effective arrangements in place to prevent conflicts from adversely affecting your interests.

### **Other information**

Before investing, it would be sensible for you to make sure that you know what the arrangements are if you need to make a complaint about the firm or to seek redress.

A list of investor compensation schemes (or investor complaints mechanisms) is also available on the ESMA website (<http://www.esma.europa.eu/content/Welcome-Investor-Corner>), and the FIN-NET network website ([http://ec.europa.eu/internal\\_market/fin-net/index\\_en.htm](http://ec.europa.eu/internal_market/fin-net/index_en.htm)).

Remember that all information provided by the firm must, by law, be fair, clear and not misleading. The information provided should not disguise, diminish or obscure important items, statements or warnings. If you do not understand the information provided to you, ask for more information.

Take notes of all discussions with the firm, and on all questions and answers. Also write down what you decided to do. If something goes wrong, and you make a complaint, your notes can help to establish what was said.

### **Conclusion**

Every investor starts with the basics. Before you decide on how to invest your money, you must identify your main financial needs and goals. Help your investment firm to understand what you want to invest for, what your financial situation is and your experience and knowledge of financial products and markets.

No matter how much or how little money you have, the important thing is to educate yourself about your opportunities and your rights. Always remember: if you have any doubts, ask questions.