MORNINGSTAR®

Adapting Your Advice for MiFID II

How our tools can help you deliver suitable advice to your clients

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Financial firms throughout Europe are rethinking their advice processes as they approach the January 2018 implementation deadline for MiFID II. The directive requires all advisers to make sure that the portfolios and advice they offer are suitable to investors' needs.

To do this, firms will need to:

- Determine which groups of investors they are serving and how.
- Assess each investor's needs based on risk tolerance, financial experience and ability to bear losses.
- Illustrate how the investment recommendation is suitable.
- Ensure that advice is delivered consistently across the business.

A New Look at Client Segmentation

As a first step, firms are evaluating the investments they offer across the firm, how they are serving their clients and whether those services align with their clients' needs.

MiFID II prohibits independent advisers from receiving commissions and rebate payments. Non-independent advisers can continue to receive commissions, but they must be upfront about how investors benefit from the products they recommend and how those products will help them achieve their goals. As a result, firms need to explore how fee-based services could change their business and what opportunity they present to serve new clients.

Morningstar can help firms standardise their advice processes while navigating MiFID II changes.

"We're seeing that a lot of firms want to ensure some level of consistency no matter which segment an investor fits into, because that investor will potentially move across segments."

Know What Suits Your Client

Advisers must correctly capture a client's investment knowledge and experience, financial situation, objectives, time horizon, attitude toward risk and ability to bear losses to deliver suitable recommendations. Risk-tolerance questionnaires and other ways of evaluating risk will help firms adhere to the regulation.

> "Advisers really need to understand an investor's situation before offering any type of advice."

The investment recommendation must fit the client's profile. And while advice and investments must be suitable, they should also be good quality. Firms may want to create model portfolios that are ready-made for various levels of risk in order to be consistent and efficient across their business.

Morningstar can help firms develop these model portfolios using our independent research and breadth of data. We also can provide portfolio risk tools that show investors how close they can get to their goals based on their risk tolerance and objectives.

"There is often a mismatch between the goal someone needs to meet and the risk they're willing to take—or the amount they're saving or their time horizon. Our tools allow advisers to play with different scenarios to get investors the result they need."

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Finding the Right Fit

Technology can help firms gather the relevant information for each client, make sure the right investment goes to the right person and provide the appropriate documentation at the point of advice in a suitability report. The report collates the steps advisers have taken with a client from the assessment process to the investment recommendation in one easy-to-understand document.

Many firms have systems that can only do some of these things, yet they will need to do them all after January 2018. Firms will need flexible solutions that also will help them modernise their business and address the industry trends driving the regulation.

Some firms may choose to work with third parties to integrate new data, additional research and meet the directive's fee transparency requirements. "A lot of firms want to have ownership of the client experience. The benefit of working with Morningstar is that the firm can own that customer experience, or the interface their users see, but we will run all the calculations."

Consistency Across the Company

Firms that offer investment guidance within their home countries or across borders will want a repeatable advice process that their advisers can easily follow and adopt. As firms roll out their new process, advisers will need to have clear information, appropriate training and ongoing support during the transition.

"There are challenges around maintaining consistency and quality of advice, and technology can really help you."

Firms will want to take a company-wide view of suitability to help their business leaders and compliance teams identify potential areas of concern. Morningstar's risk scoring can be mapped to a firm's own risk framework, so that the firm can monitor suitability on an ongoing basis across all its locations.

We know that managing regulatory change isn't easy. As a global company with on-the-ground local expertise, we supported UK and Dutch advisers during the Retail Distribution Review, or RDR, when business models shifted from commission-based to fee-based services. We are supporting efforts in the US and elsewhere to address regulation driven by industry trends that include a preference for low-cost investing, outcome-oriented solutions and automated advice.

"We know the impact this type of regulation has on firms and we can help to address it."

"MiFID II is about creating better investor protections and a better experience for investors. We know the impact this type of regulation has on firms and we can help to address it. After all, these principles align perfectly with our work as an advocate for investors for more than 30 years."

Morningstar has the experience and vision to lead firms through the MiFID II compliance process with solutions that address product governance, research unbundling, fee transparency, and suitability and advice. To find out more:

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