Press Release **23 November 2015**

Central Bank inspection finds 75% of CFD clients lost money

- **Consumers should be made fully aware of the high risk nature of CFDs**
- **Key risk is potential loss of more than their initial CFD investment**
- **Inspection of firms found issues with appropriateness and marketing**
- **Formal supervisory requirements have been imposed on offending firms**

Consumers have been advised by the Central Bank that they need to be fully aware of the high-risk and complex nature of Contracts for Difference (CFDs) before making investment decisions.

Mr Bernard Sheridan, Director of Consumer Protection, said: "One of our key priorities for 2015 was to examine the sale of investment products which may pose a risk to consumers.

"One such product is a CFD and, following a themed inspection of the CFD market, we identified several issues in relation to execution-only sales. It is our view that CFDs are unsuitable for investors with a low-risk appetite.

"This is due to the volatile nature of the CFD market, coupled with the potential for a consumer to lose more than the initial investment. Consumers need to be made fully aware of the high-risk and complex nature of CFDs before making investment decisions," he said.

The themed inspection covered retail clients who invested in CFDs during 2013 and 2014.

Over 39,000 retail clients, of which almost 5,000 were Irish Resident, invested in CFDs with Irish-based investment and stockbroking firms during this period. The main findings were:

- 75% of clients made a loss, of which the average loss was €6,900.
- Criteria used for assessing appropriateness varied among firms. Although some firms went over the requirements, the Central Bank determined that in others, the client's knowledge and experience may have been overestimated;
- Most firms were in compliance with regulatory requirements on complaints handling, however some failed to maintain up-to-date records; and
- Marketing material was not always constructed and presented in a sufficiently-balanced way to outline both the risks and benefits of CFDs.

Where the Central Bank has identified risks to consumers, due to the issues outlined above, formal supervisory requirements have been imposed on the relevant firms. The Central Bank has also sent a letter to all MiFID firms, detailing the findings of this inspection together with recommendations to enhance their compliance arrangements, where relevant.

Notes to editors

About CFDs

- CFDs allow a client to take a position on the movement in the price of financial instruments such as shares, share indices, currencies and commodities without owning the underlying instrument. It offers retail clients access to the gains and losses of financial markets that would traditionally be limited to institutional and professional investors. CFDs are a leveraged product and can magnify clients' potential losses.
- A CFD is a prescribed financial instrument under European Communities Markets in Financial Instruments Regulations 2007 (MiFID) and therefore the requirements for firms authorised to provide services in relation to CFDs are limited to the MiFID Regulations, which is based on a maximum harmonisation model.
- Firms which provide financial services in relation to CFDs are authorised as Investment Firms and must comply with MiFID and, where relevant, the Consumer Protection Code 2012 (Code).

About the themed inspection

- The themed inspection consisted of a desk based review of all active Investment and Stockbroking firms providing CFD products (including spread betting) which are regulated by the Central Bank or operating in Ireland on a branch basis (nine firms). The desk based review was followed up by onsite inspections in four firms.

Issues identified

Assessment of Appropriateness

Firms offering complex financial instruments such as CFDs are required to carry out an 'appropriateness' assessment of all clients to ascertain the clients' knowledge and experience in order to determine if the product / service is appropriate for the client. If a client does not have sufficient knowledge and experience, the firm is required to inform the client of the risks prior to opening the account and provide specific warnings that the product may not be suitable.

The inspection identified that the criteria used for assessing appropriateness varied among the firms reviewed. The criteria used by some firms went above the requirements, however, improvements are needed in other firms, where the Central Bank has determined that the processes and procedures used in these firms may have overestimated their client's knowledge and experience.

Complaints Process

Complaints handling, when dealt with in an open, fair and timely way, can represent a real opportunity for firms to restore confidence in their consumer relationships. This includes the identification of root causes of issues to ensure that the whole problem is solved rather than solely focusing on the individual complaint. Firms are required to meet the complaints handling requirements of the MiFID Regulations and expected to meet the requirements of the Consumer Protection Code, 2012 (Code).

Most firms were found to be in compliance with regulatory requirements, but some firms have not incorporated all of the requirements of the Code, such as failure to maintain up-to-date and comprehensive records, and failing to provide the consumer with regular updates on the status of their complaints.

Marketing Material
Firms are required to ensure that all marketing material is sufficiently balanced and does not disguise, diminish or obscure important information, statements or warnings for a consumer.

Marketing material was not always constructed and presented in a sufficiently balanced way to outline both the risks and benefits associated with CFDs. Furthermore, risk warnings were not always sufficiently prominent as required under MiFID Regulations.

MiFID

MiFID is a comprehensive regulatory regime covering investment services and financial markets in Europe and introduces common standards for investor protection throughout the European Union. It applies to both investment firms and credit institutions when providing investment services, and to regulated markets. MiFID came into effect on 1 November 2007.

The MiFID Regulations set out a three-tier categorisation system classifying parties as a) professional clients, b) retail clients or c) eligible counterparties. Different levels of regulatory protection are afforded to each category, with Retail clients receiving the highest level of MiFID protections.

MiFID is currently being revised to improve the functioning of financial markets in light of the financial crisis and to strengthen investor protection. MiFID II is due to come into effect in 2017.

Consumer Protection Code

The Consumer Protection Code 2012 is imposed under Section 117 of the Central Bank Act, 1989. This revised Code was published on 19 October 2011 and came into effect on 1 January 2012.