FEEDBACKS TO EC
Sustainable Finance Initiative - MiFID II suitability requirements

AMAFI Feedbacks

Association française des marchés financiers (AMAFI) is the trade organisation working at national, European and international levels to represent financial market participants in France. It mainly acts on behalf of credit institutions, investment firms and trading and post-trade infrastructures, regardless of where they operate or where their clients or counterparties are located. AMAFI has more than140 members operating for their own account or for clients in equities, fixed-income products and derivatives. Nearly one-third of its members are subsidiaries or branches of non-French institutions.

AMAFI welcomes the opportunity to give feedbacks on European Commission proposed amendments to delegated acts under MiFID 2 to include ESG considerations into the advice that investment firms offer to individual clients. Indeed, AMAFI pays particular attention to the development of ESG criteria in the financial markets and welcomes this objective to develop sustainable investments which are vital for our future.

In that context, AMAFI supports the proposal to require investment firms to take into account, when doing the suitability assessment as provided by MiFID 2, the clients' ESG preference, in order to provide them with the most appropriate investment advice service.

This is why AMAFI read attentively the Commission proposal of amending Regulation (EU) 2017/565 in application of MiFID 2 and would very much like to outline the following general points before suggesting slight changes in the wording.

1. Implementation schedule. The implementation schedule of such new delegated regulation, notably the date of application, should be carefully considered. Indeed, AMAFI considers that a cost-benefit analysis approach should be taken, between (1) the relative emergency of such measures to be enforced and (2) costs for investment firms to implement additional new requirements:

(1) If developing sustainable finance is clearly an important and urgent issue, we would like to outline that MiFID 2, through Product Governance requirements[1], already consider "*green*" and "*ethical*" investments as possible investment objectives to take into account into target market definition of financial instruments. This ESG consideration is therefore included in the new commercialization framework post MiFID 2 of financial instruments by both, manufacturer and distributors.

(2) Investment firms subject to MiFID 2 have just ended tremendous work in implementing the reform, including review all clients on boarding process in line with new requirements that apply since only 6 months ago. The changes incurred by the amendments contemplated will oblige to partially redesign procedures, process and IT systems developments.

[1] « *The firm should specify the investment objectives and needs of target clients that a product is designed to meet* […]. *For example, a product may be designed to meet the needs of a specific age demographic, to achieve tax efficiency based on clients' country of tax residence, or be designed with special product features to achieve specific investment objectives such as "currency protection",* ***"green investment", "ethical investment",*** *etc., as relevant.* » (*ESMA Guidelines on MiFID II product governance requirements, 2 June 2017, ESMA35-43-620*).

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That explains that we urge the Commission to consider giving a sufficient and reasonable period of time before amending MiFID 2.

Furthermore, the sequencing of publication especially in relation to other regulatory proposals within the sustainable finance agenda of the European Commission has to be carefully considered. Since the regulation proposal amending MiFID 2 itself refers to the Taxonomy, it seems essential, in any cases, that the Taxonomy should be finalized and published before any changes in Suitability requirement of MiFID 2 enter into force.

2. Best effort logic for firms, especially for professional clients. Another important point in our view is that it seems absolutely essential to maintain for investors the possibility of *not* having ESG objectives or considerations. It shall not be seen as a requirement, for the client, to indicate ESG preferences. Symmetrically, the investment firm should be in “best effort” logic for determining ESG considerations of the client. It could be required from the firm to ask for information on that aspect but it should not be required to actually getting it. When a client does not have ESG consideration or does not wish to disclose its preferences, this should not prevent the investment firm from providing him advisory or portfolio management services.

This is particularly crucial where the client is a professional client. In accordance with article 54.3 of Regulation 2017/565, a firm is not required to assess, for a professional client, his level of experience and knowledge nor his financial situation. The firm, however, is required to assess his investment objectives to ensure that the service provided is suitable with those. Therefore, any requirement that concern investment objectives may apply in relation with professional clients (provided that, of course, an investment advice is actually provided). Firms have generally more difficulty to collect “personal” information from professional clients and in some context; ESG considerations might not be relevant at all for those professional clients where acting on their own behalf.

That is why AMAFI wish to propose to add “*where relevant*” with “ESG objectives or considerations” in all relevant articles of the draft delegated regulation. Also, future guidance from ESMA on that particular point might be appreciated.

3. Adjusted definitions. Regarding the definitions of « *environmentally sustainable investments* », « *social investment* » and « *good governance investment* », AMAFI would prefer that those latter not to be too specific – at least at this stage – considering the possibility that this relatively “new” issue is not yet totally mature to be able to discriminate or outline some criteria and not others (for example, all criteria developed by United Nation are not taken up by the European Commission even though they are commonly accepted and used[2]).

That is why, at least at this stage, AMAFI would like to propose to delete specific examples given by the Commission in those definitions and only to keep reference to the taxonomy Regulation.

4. No specific suitability questionnaire for each client. Additionally, the Commission should take into account that most firms have to carry out a very high number of suitability assessments. To be properly managed, these assessments must remain most of the time automatable and therefore questionnaires drafted to collect necessary information should not be designed on a case by case basis. That is why, unlike what seems to imply recital 9 with the wording “*on a case by case basis*”, information on ESG objectives or considerations – like any other relevant information for assessing suitability should be asked to each and all clients but not with questionnaire drafted in a way that is specific for each one.

[2] Suistainable development Goals – 17 goals to transform our world (*United Nation* – link).

5. Keep initial objectives of relevant MiFID 2 articles. If AMAFI supports the proposal to take into account ESG investor preference into its investment objectives for suitability purposes, we feel that some of the changes proposed in the draft regulation go beyond that objective.

Indeed, article 48 of MiFID 2 Delegated Regulation is a general requirement of providing the client information about financial instruments that applies for all investment services even where no suitability requirement could apply (meaning, only for portfolio management and investment advice services). It also applies to clients or even potential clients, so a great time before the provision of services. At that very early stage, it makes no so much sense to focus already on ESG characteristics of potential financial instruments. Many of those potential clients would not be provided portfolio management or investment advice services so will not be subject to suitability requirements. There is no use anyway to add this mention in this article 48(1) because it will be done in article 47(3) and 52, respectively on portfolio management services and investment advice services. Therefore, AMAFI would prefer to not make any change in article 48(1).

The proposed amendments of the article 52, paragraph 3, and particularly the point (d), seem to go beyond that adding ESG consideration. Indeed, this provision applies only to investment firms which provide independent investment advice that should provide description on the "*factors taken into consideration in the selection process*". With this new wording, elements required in (d) would apply to both investment advice services: non independent and independent. To avoid such extension, AMAFI would suggest another wording for taking into account ESG consideration: in paragraph 2 instead of paragraph 3.

6. Investment in a broader sense. Finally, AMAFI would like to remind that an investment product could be "ESG" without "directly" invest in an ESG asset. For instance, this could be the case for a structured product that tracks performance of a basket of shares of companies within energy sector selected on the basis of an environmental or green rating. Another example could be a product that replicates the value of a "low carbon benchmark" or a "positive carbon impact" as proposed by the Commission in its amendment of Regulation (EU) 2016/1011. Such investment from the investor point of view, promote environmental standard through general promotion of ESG performances. It could indeed induce companies to reach good ESG rating. Therefore, such "indirect" environmental investment could be considered as suitable for a client that has environmental preference.

AMAFI proposes to slight change the wording of the definitions of article 1.1 to clarify this point.

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To conclude, AMAFI would like to propose the following changes (identified in **bold and underlined** police as being addition and ~~strikeout~~ police as removed) in the proposed delegated regulation and will be happy to discuss those further with the European Commission if needed.

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Recital 9

To enable those investment firms to recommend the most suitable products to the client, investment firms providing investment advice and portfolio management should introduce questions in their suitability assessment that would help identify the client's investment objectives, including ESG preferences. The final recommendations to the client should reflect both the financial objectives and, where relevant, the ESG preferences of that client. Investment firms providing investment advice and portfolio management should consider each client's individual ESG preferences ~~on a case-by-case basis~~. Investment firms should offer those financial products that correspond to the ESG preferences of the client, in accordance with their obligation to act in the best interests of the client.

Article 1

1. In Article 2, points (7), (8) and (9) are added:

(7) 'ESG preferences' means a client's or potential client's preferences for environmentally sustainable investments, social investments or good governance investments;

(8) 'ESG considerations' means a consideration related to environmentally sustainable investments, social investments or good governance investments';

(9)'environmentally sustainable investment' means an investment, **direct or indirect**, in an economic activity that contributes to an environmental objective, and in particular an environmentally sustainable investment as defined in Article 2 of [insert reference to taxonomy Regulation]

(10) 'social investment' means an investment, **direct or indirect**, in an economic activity that contributes substantially to a social objective**;** ~~and in particular an investment that contributes to tackling inequality, an investment fostering social cohesion, social integration and labour relations, and an investment in human capital or economically or socially disadvantaged communities;~~

(11) 'good governance investment' means an investment, **direct or indirect**, in companies following good governance practices**;** ~~and in particular companies with sound management structures, employee relations, remuneration of relevant staff and tax compliance.~~";

2. In Article 47(3), point (d) is replaced by the following:

"(d) the types of financial instrument that may be included in the client portfolio, based on the client's investment objectives, including any ESG preferences **where relevant**, and the types of transaction that may be carried out in financial instruments, including any limits;."

~~3. In Article 48(1), the first sentence is replaced by the following:~~

~~"Investment firms shall provide clients or potential clients in good time before the provision of investment services or ancillary services to clients or potential clients with a general description of the nature and risks of financial instruments, taking into account in particular any ESG considerations and the client's categorisation as either a retail client, a professional client or eligible counterparty."~~

4. Article 52, paragraph **2** ~~3~~ is replaced by the following:

2. Investment firms providing investment advice, on an independent or non-independent basis, shall explain to the client the range of financial instruments that may be recommended, including, where relevant, any ESG considerations and its relationship with the issuers or providers of the instruments.

~~3. "Investment firms shall provide a description of:~~

~~(a) the types of financial instruments considered;~~
~~(b) the range of financial instruments and providers analysed per each type of instrument according to the scope of the service;~~
~~(c) when providing independent advice, how the service provided satisfies the conditions for the provision of investment advice on an independent basis;~~

~~(d) the factors, taken into consideration in the selection process used by the investment firm to recommend financial instruments, such as risks, costs and complexity of the financial instruments or, where relevant, ESG considerations."~~

5. Article 54 is amended as follows:

(a) in paragraph 2, point (a) is replaced by the following:

"(a) it meets the investment objectives of the client in question, including the client's risk tolerance and**,** **where relevant,** any preferences~~, including~~ **in** environmental, social and governance considerations";

(b) paragraph 5 is replaced by the following:

"5. The information regarding the investment objectives of the client or potential client shall include, where relevant, information on the length of time for which the client wishes to hold the investment, his or her ESG preferences~~,~~ if any, his or her preferences regarding risk taking, his risk profile, and the purposes of the investment".

(c) paragraph 9 is replaced by the following:

"9. Investment firms shall have in place, and be able to demonstrate, that they have in place adequate policies and procedures to ensure that they understand the nature, features, including costs, risks of investment services, and financial instruments selected for their clients, including any environmental, social and governance considerations~~,~~ **where relevant,** and that they shall assess, while taking into account cost and complexity, whether equivalent investment services or financial instruments can meet their client's profile."

(b) **the first paragraph of**[3] paragraph 12 is replaced by the following:

"12. When providing investment advice, investment firms shall provide a report to the retail client that includes an outline of the advice given and explains how the recommendation provided is suitable for the retail client, including how the recommendation meets the client's objectives, including ESG preferences~~,~~ if any, and personal circumstances with reference to the investment term required, the client's knowledge and experience, and client's attitude to risk and capacity for loss."

[3] This addition is made to correct what we consider a typo.