



April 27, 2022

Positions of the Association of Foreign Banks in Germany

regarding the

ESMA's draft Guidelines on certain aspects of the MiFID II suitability requirements (ESMA35-43-2998, "Draft Guidelines")

Q1 Do you agree with the suggested approach on the information to clients about the purpose of the suitability assessment and its scope? Please also state the reasons for your answer.

We agree with the suggested approach on the information to clients about the purpose of the suitability assessment and its scope.

Regarding our comments to marginal number 16 of the Draft Guidelines, please see our answer to question 2.

Q2 Do you agree with the new supporting guideline in relation to the information to clients on the concept of sustainability preference or do you believe that the information requirement should be expanded further? Please also state the reasons for your answer.

We agree that there must be a general explanation of the concept of "sustainability preferences" in order to fulfil the suitability assessment and the new requirements of the Delegated Regulation (EU) 2021/1253. However, from our point of view, it should be just a general explanation in the meaning of Art. 2 Number 7 a) to c) of the Delegated Regulation (EU) 2017/565 as amended by the Delegated Regulation (EU) 2021/1253; i.e. a general explanation of the term and the distinction between the different elements of the definition of sustainability preferences under a) to c). These explanations should also be designed in such a way that they can be reused for every client.

Moreover, the requirements in the sentence

"Firms should also explain what environmental, social and governance aspects mean."

should be further specified, in particular the extent of the explanation requirements seem to be too vague. We would recommend outlining in detail what firms are required to explain regarding the "environmental, social and governance aspects".

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Q3 Do you agree with the suggested approach on the arrangements necessary to understand clients and specifically with how the guideline has been updated to take into account of the clients' sustainability preferences? Please also state the reasons for your answer. Are there other alternative approaches, beyond the one suggested in guideline 2, that you consider compliant with the MiFID II requirements and that ESMA should consider? Please provide examples and details.

We welcome the approach of using questions to obtain the necessary information, as described in marginal number 25 of the Draft Guidelines. However, from our point of view, the described approach in marginal number 26 of the Draft Guidelines seems to be drafted unclearly. For example: Marginal number 26, point 1 para. 2 of the Draft Guidelines states the following:

*“When doing so, firms could also assess whether the client would only prefer one certain degree of sustainability-related expectation or whether more or all of them should be part of its preferences. This aspect could be assessed through **closed-ended yes/no-questions.**”*

In this respect it is not clear what kind of questions are meant in this respect. Therefore, examples of questions would be very helpful.

In general, it should be made clearer which questions, processes and procedures ESMA expects. In this respect, model templates should be included as annexes to the draft guidelines.

Q4 Do you believe that further guidance is needed to clarify how firms should assess clients' sustainability preferences?

We are of the opinion that there is no further guidance needed.

Q5 Where clients have expressed preference for more than one of the three categories of products referred to in letters a), b) or c) of the definition of Article 2(7) of the MiFID II Delegated Regulation, do you think that the Guidelines should provide additional guidance about what is precisely expected from advisors when investigating and prioritizing these simultaneous / overlapping preferences?

From the current point of view, we do not believe that additional guidance is necessary in this respect.

Q6 Do you agree with the proposed approach with regard to the assessment of ESG preferences in the case of portfolio approach? Are there alternative approaches that ESMA should consider? Please provide possible examples.

We have no comments in this regard.

Q7 Do you agree with the suggested approach on the topic of 'updating client information'? Please also state the reasons for your answer.

We agree with the suggested approach in marginal number 55 of the Draft Guidelines.

Q8 Do you agree with the suggested approach with regards to the arrangements necessary to understand investment products? Please also state the reasons for your answer.

We agree with the suggested approach in marginal number 70 of the Draft Guidelines.

Q9 Do you believe that further guidance is needed to clarify how firms should take into consideration the investment products' sustainability factors as part of their policies and procedures? Please also state the reason for your answer.

We are of the opinion that there is no further guidance needed.

Q10 Do you agree with the additional guidance provided regarding the arrangements necessary to ensure the suitability of an investment concerning the client's sustainability preferences? Please also state the reasons for your answer.

In respect of marginal number 79 of the Draft Guidelines, we fully agree with the suggested approach that sustainability preferences should only be addressed once the suitability has been assessed in accordance with the criteria of knowledge and experience, financial situation and other investment objectives.

In respect of marginal number 80 to 84 of the Draft Guidelines, please see our answers to Q11 to 16.

Q11 Do you agree with the approach outlined with regards to the situation where the firm can recommend a product that does not meet the client's preferences once the client has adapted such preferences? Do you believe that the guideline should be more detailed? Please also state the reasons for your answer

We recommend that marginal number 80 (1) of the Draft Guidelines should be deleted or alternatively amended as follows:

"A firm can still ~~Where a firm intends to~~ recommend a product that does not meet the initial sustainability preferences of the client in the context of investment advice as referred to in Recital 8 of the MiFID II Delegated Regulation, ~~it can only do so once the client has adapted his/her sustainability preferences.~~ In order to allow for further recommendations to clients or potential clients, where financial instruments do not meet a client's sustainability preferences, the client should have the possibility to adapt information on his or her sustainability preferences. The firm's explanation regarding the reason to resort to such possibility as well as the client's decision should be documented in the suitability report."

Reasons

Marginal number 80 (1) of the Draft Guidelines states the following:

*"Where a firm intends to recommend a product that does not meet the initial sustainability preferences of the client in the context of investment advice as referred to in Recital 8 of the MiFID II Delegated Regulation, it can only do so **once the client has adapted** his/her sustainability preferences."*

We are of the opinion that this rule is contrary to recital 8 of the Delegated Regulation (EU) 2021/1253, which states that

*„it is necessary to clarify that financial instruments that are not eligible for individual sustainability preferences **can still be recommended** by investment firms, (...)”.*

Recital 8 thus clearly states that the recommendation for other financial instruments must be possible at all times, even if they do not meet the sustainability preferences. However, marginal number 80 (1) of the Draft Guidelines restricts this possibility and allows a recommendation for financial instruments that do not meet the sustainability preferences only after the client has adjusted his or her sustainability preferences. This regulation is thus not in line with the principle of "*acting in the best interest of the client*" according to Art. 54 (1) of the Delegated Regulation (EU) 2017/565 (Art. 25(2) of Directive 2014/65/EU). For this reason, we would recommend - as proposed above - an adjustment of marginal number 80 (1) of the Draft Guidelines.

Q12 Do you agree with the approach outlined with regards to the situation where the client makes use of the possibility to adapt the sustainability preferences? Please also state the reasons for your answer.

We recommend that marginal number 81 sentence 1 of the Draft Guidelines should be deleted.

Reasons

Marginal number 81 sentence 1 of the Draft Guidelines states the following:

*“With regards to the possibility for the client to adapt the sustainability preferences referred in Article 54(10) of the MiFID II Delegated Regulation, firms are reminded that this possibility **should not be the standard procedure.**”*

In this respect, it should be clarified as to what is meant by the term "*this possibility **should not be the standard procedure.***"

We are of the opinion that this rule of marginal number 81 sentence 1 of the Draft Guidelines is contrary to Art. 54 (10) of the Delegated Regulation (EU) 2021/1253 which states the following:

“When providing the investment service of investment advice or portfolio management, an investment firm shall not recommend or decide to trade where none of the services or instruments are suitable for the client.

(...)

Where no financial instrument meets the sustainability preferences of the client or potential client, and the client decides to adapt his or her sustainability preferences, the investment firm shall keep records of the decision of the client, including the reasons for that decision.”

Art. 54 (10) of the Delegated Regulation (EU) 2021/1253 does not specify that a firm should follow a particular chronology when recommending financial instruments. Rather, the firm is obliged to recommend only financial instruments to the client that are suitable. If, however, the firm cannot recommend a financial instrument that corresponds to the client's sustainability preferences, it is obliged to inform the client of this and also to allow him or her to adjust his or her sustainability preferences. If the firm did not do so, this would be a violation of Article 54 (10) subparagraph 1 of the Delegated Regulation (EU) 2021/1253. Enabling the customer to adjust his or her sustainability preferences can therefore not be understood as a "standard process". In this respect, sentence 1 of marginal number 81 of the Draft Guidelines should be deleted.

Q13 Could you share views on operational approaches a firm could use when it does not have any financial instruments included in its product range that would meet the client's sustainability preferences (i.e. for the adaptation of client's preferences with respect to the suitability assessment in question/to the particular transaction and to inform the client of such situation in the suitability report)?

In the case that a firm cannot recommend a financial instrument that meets the client's sustainability preferences, the firm should first communicate this to the client. It should also document this. In addition, the firm should allow the client to adjust its sustainability preferences in accordance with Art. 54 (10) of the Delegated Regulation (EU) 2021/1253. The firm may also recommend other financial instruments to the client in accordance with recital 8 of the Delegated Regulation (EU) 2021/1253, even if these do not meet the sustainability preferences.

Q14 Do you agree with the proposed approach for firms to be adopted in the case where a client does not express sustainability preferences, or do you believe that the supporting guideline should be more prescriptive? Please also state the reasons for your answer.

We are of the opinion that it should be possible for clients not to indicate sustainability preferences. Such customers should not be highlighted, for example as "sustainability neutral". Moreover, from our point of view, if the client says "no" it should be clear that there is no need that the firm's product offer should be explained to the client with a mention of the products/portfolio's sustainability features. Answering the question on sustainability preferences with "no" already clearly indicates that the client does not want more intensive advice on this. Therefore, we recommend that marginal number 83 of the Draft Guidelines should be deleted.

Q15 Do you agree with the proposed approach with regard to the possibility for clients to adapt their sustainability preferences in the case of portfolio approach? Do you envisage any other feasible alternative approaches? Please provide some possible examples

We agree with the suggested approach in marginal number 82 of the Draft Guidelines.

Q16 What measures do you believe that firms should implement to monitor situations where there is a significant occurrence of clients adapting their sustainability preferences? What type of initiatives do you envisage could be undertaken to address any issues detected as a result of this monitoring activity?

From our point of view, there is no need that firms should implement measures to monitor situations where there is a significant occurrence of clients adapting their sustainability preferences. Article 54 (10) of the Delegated Regulation (EU) 2021/1253 allows clients to adapt their sustainability preferences if no financial instrument of a firm meets their sustainability preferences. According to Art. 54(10) of the Delegated Regulation (EU) 2021/1253, there is just an obligation that the investment firm keep records of the decision of the client, including the reasons for that decision.

Q17 Do you agree with the proposed amendment to supporting guideline 10? Please also state the reasons for your answer.

We agree with the suggested approach in marginal number 97 of the Draft Guidelines.

Q18 Do you agree with the additional guidance regarding to the qualification of firms' staff or do you believe that further guidance on this aspect should be needed? Please also state the reasons for your answer.

We agree with the suggested approach in marginal number 104 of the Draft Guidelines.

Q19 Do you agree on the guidance provided on record keeping? Please also state the reasons for your answer.

We agree with the suggested approach in marginal number 109 of the Draft Guidelines.

Q20 Do you agree on the alignment of the two sets of guidelines (where common provisions exist for the assessment of suitability and appropriateness)? Please also state the reasons for your answer.

We agree with the alignment of the two sets of guidelines. A harmonisation of different guidelines is always welcome in order to avoid differences in regulation and evaluation.

Q21 Do you have any further comment or input on the draft guidelines?

We have no further comments.

Q22 Do you have any comment on the list of good and poor practices annexed to the guidelines?

We have no comments on the list of good and poor practices.

Q23 What level of resources (financial and other) would be required to implement and comply with the guidelines (organisational, IT costs, training costs, staff costs, etc., differentiated between one off and ongoing costs)? When answering this question, please also provide information about the size, internal organisation and the nature, scale and complexity of the activities of your institution, where relevant.

The amendments in the Delegated Regulation (EU) 2021/1253 that have been made to MiFID II cause high cost regarding organizational, IT and staff issues. Especially the date of entry into force of the Delegated Regulation (EU) 2021/1253 and the associated very short implementation period should be emphasised here. This has caused a lot of uncertainty among market participants, as it has not been clear and unambiguous to what extent the new regulations are to be implemented and how the new processes are to be designed. Against this background, we also expect high costs in the implementation of these Draft Guidelines.