

Ref: ESMA Public Consultation on Guidelines on certain aspects of the MiFID II appropriateness and execution-only requirements

Date: 29 April 2021

Link: <https://www.esma.europa.eu/press-news/consultations/consultation-guidelines-appropriateness-and-execution-only>

INTRODUCTORY EXPLANATIONS (for non-professional readers)

The Markets in Financial Instruments Directive (MiFID II) imposes certain obligations on investment firms offering investment services or products, among which there is the requirement to ensure that the service or product is aligned with the investor profile of each relevant client. This obligation takes two forms, i.e. either the *suitability assessment* (Art. 25(2) MiFID II), which is applicable to any investment firm providing investment advice in relation to an investment service or product. Such services are referred to in EU jargon as “advised services”. The other requirement, which embodies a lower standard of investor protection, is the *appropriateness assessment*, which applies to all services or products that are simply sold, i.e. no investment advice if offered. These services are called in EU jargon “non-advised services”.

In case the client makes a specific and explicit demand for an investment service or product (i.e., execution-only), then the investment firm is not bound to undertake any of the two aforementioned assessments.

The European Securities and Markets Authority (ESMA) is tasked by EU law to develop Guidelines on the application of such obligations. ESMA’s Guidelines are not an official interpretation, nor an implementation act with binding effect, but serve as ESMA’s view on what should be understood and what derives from each provision concerned. However, they are very important as the content of such Guidelines can become directly applicable to investment firms if the national supervisory authorities of EU Member States approve them and transpose them into national law.

This public consultation seeks the opinion of stakeholders on the Guidelines developed by ESMA in reference to the *appropriateness test* and *execution-only requirements* for investment firms.

GENERAL COMMENT

BETTER FINANCE welcomes the initiative of ESMA to clarify certain aspects related to the application of the MiFID II provisions on the *appropriateness test* and requirements for execution-only services. In addition, BETTER FINANCE commends ESMA on adapting the Guidelines on suitability assessment for the appropriateness test as the two procedures are, to a certain extent, substantially the same.

In our view, the appropriateness assessment should also ensure that any investment product or service offered has a reasonable probability to meet the client’s expectations or needs in terms of return over his saving horizon or recommended holding period, or at least a reasonable probability not to erode the purchasing power of his savings or investment over that period.

In addition, the objective of the EU co-legislators and of the European Supervisory Authorities, in this case of ESMA, should be to simplify regulation and administrative procedures for investors, in particular to reduce bureaucracy and documentation that a non-professional client must go through. Evidence from a BETTER FINANCE survey on the implementation of MiFID II reveals that many investors, both experienced and non-experienced, face increasing difficulties at the “point of sale”, claiming “too much bureaucracy” and many hurdles they must undergo before investing.

SPECIFIC COMMENTS

Information to clients about the appropriateness assessment (Q1 and Q2)

BETTER FINANCE recommends ESMA to clarify that all information provided to clients (whether disclosures or warnings) should be simple, concise, and comply with the rule of *fair, clear, and not misleading*, as required by Art. 24(1) MiFID II. In this sense, BETTER FINANCE advises ESMA to:

- a) develop and require standardised templates for disclosure and warnings, to be included in Guideline 1;
- b) clarify that “in good time” means before the provision of the assessment or service in Guideline 1;
- c) BETTER FINANCE agrees with ESMA putting emphasis on practices designed to downplay a warning, to encourage clients taking risky/complex products or to disregard the appropriateness assessment, or to “upgrade” to another service (Guideline 9, para 45);
- d) in light of the latter recommendation, to expressly prohibit practices meant to deviate the purpose of the appropriateness test, to be included in Guideline 9.

In addition, BETTER FINANCE is aware of the data protection issues that stem from such questionnaires required by MiFID II. Therefore, BETTER FINANCE is of the view that ESMA should make explicit reference to the General Data Protection Regulation for the purpose of data collection and processing obligations, in particular to emphasise the principle of data minimisation (Art. 5(1)(c) GDPR) and the principle of “purpose limitation” (Art. 5(1)(b) GDPR).

Arrangements necessary to assess the appropriateness of an investment or else issue a meaningful warning (Q9)

At the same time, BETTER FINANCE advises ESMA to clarify the Guidelines in order to re-enforce the principle that a high standard of investor protection does not come in contrast or at the expense of product availability. BETTER FINANCE’s members have brought evidence from their members (individual, non-professional investors) that the availability and diversity of products at the selling point or with online brokerage platforms have decreased and that investment firms refuse to offer certain products, for example, because of “MiFID II obligations”. In this sense, ESMA should re-ensure product manufacturers and distributors that the stringent rules comprised in the MiFID framework are not meant to reduce the product availability, but only to ensure a high standard of investor protection, and that the product governance and distribution rules are not stronger or weaker depending on the scale of complexity of a product, but are regardless the same. BETTER FINANCE believes, based on our preliminary research and analysis, that these rules are misunderstood, which in practice gives non-professional clients the impression that it is, in fact, the law (MiFID) that expressly prevents them from accessing or buying certain products.

Matching clients with appropriate products (Q15)

BETTER FINANCE agrees with ESMA’s development on the issue of automated tools that perform the appropriateness assessment, in particular the control and regular testing of algorithms (Guideline 8, para 63). In this sense, BETTER FINANCE’s experience with automated investment platforms (which, albeit dealing with the suitability assessment as these provide investment advice, can serve as proper evidence for automated appropriateness platforms) that may have errors or inconsistencies in the algorithms designed to create the investor profile and determine what product or allocation of assets or products would be aligned with the client.

Effectiveness of warnings (Q10)

In relation to Guideline 9, para. 71, BETTER FINANCE advises ESMA to introduce a good practice example by which sellers of financial instruments, whether manufacturers or distributors, should in fact advise the client to:

- a) either advise the client to seek *financial advice*, or
- b) either advise the client that the product can still be bought based on his express, explicit, and prior request,

if the appropriateness assessment dictates that a certain financial instrument or investment service is not appropriate for the relevant client, rather than simply not allowing the client to acquire the product.

Incorporation of sustainability factors and risks (Q16)

BETTER FINANCE agrees that sustainability factors and risks must be incorporated in the product approval process for financial instruments, reason for which ESMA is right to clarify that the client's "*knowledge and experience*" in the field relevant to a certain investment service or product should concern, or extend, also to these finance externalities. In absence of an obligation for investment firms to seek the client's knowledge and experience with the sustainability risks and factors in the field relevant to the product or service offered, the requirement to incorporate the former into the product governance process would be superfluous.