

BVI¹ response to the ESMA Consultation Paper Guidelines on certain aspects of the MiFID II appropriateness and execution-only requirements (ESMA35-36-2159)

Q3: Do you agree with the suggested approach on the extent of information to be collected from clients? Please also state the reasons for your answer.

We do not agree with ESMA's statement of the differentiation between more complex or risky products and less complex or risky products.

Citing from ESMA on that matter: *"referring to complexity as a relative term"* (p. 10, No. 26). This leads to many uncertainties.

First, the requirements of Art. 25 (4) MiFID II are clear and exhaustive. An appropriateness assessment is not necessary for the mentioned products. These products are not complex. For all other products an appropriateness assessment is mandatory. Further gradations are not foreseen and cannot be done on a Level 3. It is important to keep the same understanding of complexity across the different regulatory requirements.

Second, this proposal does not take into account that the appropriateness assessment is an elaborate technical process. It is not possible to review financial instruments with respect to different grades of complexity which are not even defined. If distributors should be obliged to do so, this would massively reduce the range of financial products offered to clients. The distributors would focus on a small group of products for which they classify the complexity. This would not be in the interest of the clients using non-advised services who are interested in a broad range of investment products. Furthermore, an open definition of complexity would lead to a non-uniform approach because each distributor would have its own understanding.

Q5: Do you agree with the suggested approach on the reliability of client information? Please also state the reasons for your answer.

We agree in general that the information provided by investors must be reliable and consistent. However, it is important to draw a clear line between the requirements for the suitability assessment and the appropriateness assessment. For instance, clients who opt for advice get in touch with the distributors directly. Clients who make their own decisions and opt for the "non-advised services", on the other hand, are doing this mostly online. There is often no face-to-face contact between the client and the distributor. While the information provided by clients must be reliable and consistent, it must also be clear that investment firms cannot check all the information they get from their clients. They

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have to rely on the clients and the information they receive from them. Art. 55 (3) Delegated Regulation 2017/565 points this out explicitly. The final Guidelines must be brought in line with this.

Q6: Do you agree with the suggested approach on relying on up-to-date client information? Please also state the reasons for your answer.

We do not agree with ESMA's statement that particular attention should be given to the update of information for more vulnerable clients (e.g. such as older clients). This is an undue discrimination of those clients who would not be considered "more vulnerable". Furthermore, it is not clear how distributors should define vulnerable clients.

We agree that there should be arrangements to ensure that information is updated. Sending a questionnaire to clients, as foreseen in Guideline 5, No. 43, is not suitable for non-advised services.

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

We have concerns with this approach. See also our answer to Q 3.

Even though ESMA indicates that the criteria and principles of MiFID II should be taken into account for graduating the level of complexity (Guideline 7, No. 53), ESMA mentioned also that "complexity is a relative term". Such a statement leads to legal uncertainties. ESMA should concentrate on the legal basis of Art. 25 (4) MiFID II.

Q10: Do you agree with the suggested approach on the effectiveness of warnings? Please also state the reasons for your answer.

We agree with the approach in general, but not with ESMA's statement in Guideline 9, No. 71. ESMA proposes to define situations under which a client would not be allowed to process a transaction after having received a warning. This is not foreseen in Art. 25 (3) MiFID II/ Art. 56 Delegated Regulation 2017/565 and cannot be done on Level 3.

Q14: Do you agree with the suggested approach on determining situations where the appropriateness assessment is needed? Please also state the reasons for your answer.

Yes, we agree.

In this context we would like to emphasise another topic. We consider ESMA's assessment incorrect that all alternative investment funds ("AIFs") are obligatory complex without recourse to an individual complexity test (see ESMA MiFID II / MIFIR Investor Protection Q&A, Section 10, Question 1). ESMA refers to Recital 80 of MiFID II, according to which AIF "shares" are generally to be regarded as complex. However, this and the relevant rule in Art. 25(4)(a)(i) MiFID II, which explicitly mentions AIFs, only prevent shares in AIFs from being considered as non-complex solely because they are listed on a stock exchange. Otherwise, the legislator would not only have spoken of "shares in AIF" but – as



elsewhere – of "shares or units in AIF". Moreover, the legislator would have structurally transformed this regime into a regime together with that applicable to UCITS and not into that applicable to listed shares. This is because listed shares in AIFs are in practice rather the exception than the rule. In effect, the blanket classification is also inappropriate. The category of AIFs covers a wide variety of fund vehicles, ranging from strictly regulated and supervised mutual funds which differ from UCITS investment policies only in certain details (e.g. so called „Gemischte Sondervermögen“ under the German investment law (“Kapitalanlagegesetzbuch”)), to funds for professional investors which are not subject to investment restrictions (including hedge funds). In order to take account of this diversity and not to bring AIFs in a worse position than investment products without risk spreading and prudential supervision, but with issuer risks (e. g. equities), AIFs should have access to the complexity test under Art. 57 of the MiFID II Implementing Regulation. This would allow an individual classification based on the characteristics of the respective product.

Q16: When providing non-advised services, should a firm also assess the client’s knowledge and experience with respect to the envisaged investment product’s sustainability factors and risks? If so, how should such sustainability factors and risks be taken into account in the appropriateness assessment? Please also state the reasons for your answer.

We fully understand that sustainability is a topic that is becoming more and more important for both issuers and investors. Since there are many different aspects, we want to clarify that we understood that ESMA doesn’t want to take into account the ESG preferences of clients in the appropriateness assessment, but “only” the understanding of sustainability factors and risks. From our point of view this approach is proper and should be maintained. The ESG preferences are taken into account in the process of investment advice on a later stage. In the appropriateness assessment, however, it is required to find out if the client has understood (i.e., his knowledge about) the service to be provided, the type of the product and the complexity and risks that are involved (Art. 55, 56 Delegated Regulation 2017/565). Specific preferences relating to product features are not part of these requirements so far – this should be retained.

There is a need for a common understanding that a sustainability risk is not a separate risks type. It is important to understand that the concept of an assessment of sustainability risks as part of the risk management process is not a new stand-alone risk element, but rather a specific subset of other relevant financial risks. Otherwise, a distinction from other risk types would be extremely difficult. To put it differently: sustainability risk is risk inherent in a portfolio due to sustainability factors. Therefore, as it stands, sustainability risk in investment funds is in general not identified and measured separately from other risks. Rather, it is included into the exposure to other relevant risks or considered part of the price valuation of portfolio assets. It is necessary to have this in mind, should sustainability factors and risks be taken into account in the appropriateness assessment. Furthermore, should the latter happen, their inclusiveness in the appropriateness assessment should be proportional.
