

Response of the Fédération des Banques Françaises (FBF) to the ESMA Consultation « Review of the Guidelines on MIFID II product governance requirements »
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FBF thanks ESMA for this consultation and for the attention that ESMA will give to its responses.

Preliminary remark

FBF is of the opinion that ESMA's requirements on product governance under MIFID II should be completely based on the same data and compatible with the use of the Findatex templates by the investment firms which allow comparisons of financial instruments from one manufacturer to another one, rely on machine readable data and are even used on a voluntary base by non-MiFID manufacturers.

Q1: Do you agree with the suggested clarifications on the identification of the potential target market by the manufacturer (excluding the suggested guidance on the sustainability-related objectives dealt with in Q2)? Please also state the reasons for your answer.

No, we do not agree with all the clarifications in Paragraphs 14 and 19 of the revised guidelines (compared to the current version of these guidelines)

In Paragraph 14, it has been added that manufacturers should take into account analyses of the scenarios and cost structures associated with a financial instrument when defining their target markets.

This clarification does not seem very relevant to us, because this is a mere repetition of article 9 paragraph 10 of the Delegated directive (EU) 2017/593 which provides that *“Member States shall require investment firms to undertake a scenario analysis of their financial instruments which shall assess the risks of poor outcomes for end clients posed by the product and in which circumstances these outcomes may occur”* (see also paragraph 12 of article 9 of the Directive).

In any case, such detailed information is not very useful for distributors and should not lead to additional target market criteria or to any specific disclosure to clients since it would not be understandable for most end investors, especially for retail ones. It should be recalled that the European Commission is currently trying to address the overload of information retail investors are suffering, and we believe that any additional disclosure requirement would run counter to this objective.

Paragraph 14 also specifies that the identification of the potential target market by the manufacturer should not only be based on quantitative criteria but also on "sufficient qualitative criteria".

This is already mentioned in the current version of the guidelines. However, our members are of the opinion that distributors need standardized data that can be easily processed in their IT systems.

Moreover, such qualitative data are not included in the Findatex EET. The production of non-standardized data should therefore be limited, as such data is too subjective and is ultimately not used by distributors (when provided by manufacturers). It is also difficult for distributors to make comparisons between financial products when manufacturers' data are not homogeneous. Once again, when the European Commission is working to enhance product comparability, and to onboard the digital challenge, in particular through the development of machine-readable documentation, the provision of wordy description not comparable from one manufacturer to another one would result extremely time consuming, costly and useless.

In paragraph 19, further details have been added to the five categories of information to be included in the manufacturer's target market (notably in subparagraph e. regarding the holding period of a financial instrument or the investment horizon of an investor).

Generally speaking, we fear that this growing granularity of information to be defined in the manufacturer target market could lead distributors to exclude many clients from their own target market whereas the profile and needs of these investors might have matched the intrinsic features of the relating financial instruments.

This would be in contradiction with the legitimate wish of the ESAs and NCAs to offer retail investors with a sufficiently wide range of investment products.

Furthermore, it seems important that the definition and implementation of the target markets, both by the manufacturer and the distributor of financial instruments, should not substitute for the suitability assessment carried out by the distributor in the context of an advised service provided to its clients.

At last, in subparagraph b, the element *“time period in which clients should have been active in the financial markets”* (see the current version of the ESMA guidelines) is quite questionable (a client may have been “active” for a long time but a long time ago). Finally, this element would be of little or no use to distributors.

Q2: Do you agree with the suggested approach on the identification of any sustainability-related objectives the product is compatible with? Do you believe that a different approach in the implementation of the new legislative requirements in the area of product governance should be taken? Please also state the reasons for your answer.

Yes, we agree with this approach, with the exception of the specification of the focus on environmental, social or governance criteria or a combination of them (third bullet point), which is not information required in article 1 of the delegated regulation (UE) 2021/1253 modifying article 2(7) of the delegated regulation (UE) 2017/565 and is not specified in the Findatex EET.

We believe regulation is already complex enough not to add additional requirements to those already included in it.

Q3: What are the financial instruments for which the concept of minimum proportion would not be practically applicable? Please also state the reasons for your answer.

For most securities (in particular those issued by companies, with the possible exception of green bonds), this concept is not applicable in practice since information on the minimum proportion of issuers' activities invested in sustainable investments as defined in Article 2 point 1 of Regulation (EU) 2020/582 will not be available at the beginning of 2023.

For equities and bonds, the concept of proportion of sustainable investment might be irrelevant. Manufacturers and distributors should therefore be free to define the best methodology to assess how equities and bonds can be considered as sustainable, bearing in mind that even for SFDR products, there is no prescribed methodology to assess how the product contributes to a sustainable investment objective according to the definition of sustainable investment provided by Article 2.17 of this regulation.

More generally, there is little point in defining a target market for equities and bonds, which are mostly non-complex instruments (in practice, distributors define target markets for equities and bonds themselves, without really having any use for the target markets thus defined).

Q4: Do you agree with the suggested guidance on complexity in relation to the target market assessment and the clustering approach? Please also state the reasons for your answer.

Yes, we agree with paragraphs 23 to 30 except on the following points:

- **Paragraph 27** states that *“for certain OTC derivatives or structured products, it is expected that a clustering approach will not be appropriate”*. Considering that some EU investment firms can issue hundreds of thousands of OTC derivatives or structured products each year, among which hundreds have similar characteristics, a clustering approach to define a single target market for these derivatives and structured products is a necessity. Exception to this approach is correctly addressed by the current guidelines which clarify that *“For bespoke or tailor-made products, the target market of the product will usually be the client who ordered the product unless the distribution of the product to other clients is also foreseen.”*
- **Paragraphs 28 and 29** seem to us to be very demanding and cumbersome to implement, since the key factors enumerated in paragraph 28 to be taken into account when clustering products are numerous and most of them are not included in the Findatex EET.

We consider that ESMA should clarify that these key factors are only examples and subsequently replace the "should" at the beginning of the paragraph with "could".

- **Paragraph 26** seems to be a little caricatural when stating that clients investing in CFDs or similar products are “prepared to lose money”. ESMA should consider that these products can be commonly bought by clients who have a sufficient understanding of their functioning and may in particular use them to hedge for their cash position – therefore accepting to pay for the insurance they buy.

Q5: Do you agree with the suggested guidance on the assessment of the general consistency of the products and services to be offered to clients, including the distribution strategies used? Please also state the reasons for your answer.

Yes, FBF agrees with theses guidance with the exception on two points:

- **In paragraph 34**, could ESMA replace "the management body" with "the senior management", as the management body is not directly involved in identifying the actual target markets for financial instruments, although it is responsible for defining the distribution strategies of the firm (in general terms).
- **In paragraph 35**, we believe that the reference to "the needs, characteristics and objectives of the target clients" (already mentioned in the current version of the ESMA guidelines) is confusing as it is not consistent with the provision of reception and transmission of orders or simple execution services. Ensuring compatibility between financial instruments and clients' needs, characteristics and objectives should remain the objective of the suitability assessment alone (in the context of the provision of an advised service). ESMA should delete this part of phrase so as not to confuse investors on the services they are provided.

Q6: Do you agree with the suggested guidance on the identification of the target market by the distributor? Please also state the reasons for your answer?

The second sentence of **Paragraph 42** ("distributors should define the target market on a more concrete level...") seems to imply that a distributor might not rely on the manufacturer's target market or might not use it to define its own target market.

This seems awkward or even contrary to the EU delegated directive (2017/593) whose article 10 (2) nevertheless provides that *"Investment firms shall use the information obtained from manufacturers and information on their own clients to identify the target market and distribution strategy"*

As already answered in question 1 regarding paragraph 19, the definition of the distributor's target market is a different exercise and cannot replace the suitability assessment that is carried out for each client. No ambiguity should be introduced concerning the service provided to the client, and we consider that adding too much granularity in the definition of the target market when in the same time the client is clearly informed that not all the criteria of the target market will be assessed (when he **chooses** to deal under the execution only or appropriateness regime) would be useless and confusing.

Q7: Do you agree with the suggested approach on the determination of distribution strategy by the distributor? Please also state the reasons for your answer.

No, we do not agree with the penultimate sentence of paragraph 56. In the context of the provision of a non-advised investment service, the investment firm asks its (retail) clients only about their knowledge and experience of financial instruments. If a financial instrument is primarily distributed by the firm through a non-advised investment service, the firm will therefore not have reliable evidence on the other 3 categories of criteria of the suitability test and therefore will not be able to determine whether the target market is likely to be reached (since the target market is defined on the basis of 5 categories of criteria close to those of the suitability test, whereas the firm will only has complete information on the "client category" and the "knowledge and experience" criteria).

If this recommendation were ultimately to result in a prohibition on clients subscribing to certain financial instruments, it could also be considered as a refusal to sell a product or provide a service, which is prohibited by national law. Clients might also consider that they are obliged to buy the additional advisory service to be allowed invest in some products, when they do not want to buy it. This would increase costs for clients and could force firms to sell them a service that is considered useless and/or overly burdensome by these clients.

Ultimately, we believe that such a recommendation is too far reaching and goes beyond MiFID II requirements and therefore **should be deleted**.

In paragraph 59, ESMA refers to “more complex products” without defining them; this wording therefore leaves room for interpretation and uncertainty in the application of this guidance.

It is important that distributors take into account the means of communication or media on which their communication on financial instruments may appear, although it may sometimes be difficult to associate a communication channel with a type of investor (e.g. experienced investors may use social networks as well as younger and inexperienced investors).

Q8: Do you agree with the suggested approach on the deviation possibility for diversification or hedging purposes when providing investment advice under a portfolio approach or portfolio management? In particular, do you agree that a deviation from the target market categories “type of client” and “knowledge and experience” cannot be justified for diversification or hedging purposes, neither in the context of investment advice under a portfolio approach, nor portfolio management? Please also state the reasons for your answer.

Yes, we agree with this approach.

Q9: Do you agree with the suggested approach on the requirement to periodically review products, including the clarification of the proportionality principle? Please also state the reasons for your answer.

In Paragraph 67, the regular review by the manufacturer and the distributor to assess whether products remain consistent with sustainability-related objectives could be difficult to implement by investment firms, especially for shares and bonds for which investment firms have incomplete and non-easily accessible information. We consider that it should be clarified that i) the on-going monitoring of the product should not be in the remit of the firm which has advised the issuer on a specific issue, as they may be no additional link between this adviser and the firms, whose products are freely negotiated on the secondary market with no input or review from the initial adviser; ii) the distributor should only monitor the sustainability-related objectives of the products for which it provides an on-going advice service. Any other requirement would be completely unnecessary as i) there is no negative target market on the sustainability criterion, so there is no reason why the product should become unsuitable for the client on this criterion; ii) as the distributor does not know the sustainability preferences (if any) of the non-advised client, and the target market is not published or disclosed, absolutely nothing would result from this additional work.

In Paragraph 70, we disagree with the second sentence (“Whenever distributors have relevant information to support review by MIFID manufacturers, they should proactively provide it to the manufacturer and not provide such information only at the manufacturer’s request”).

This sentence indicates that distributors should be proactive towards manufacturers and should provide them promptly with any relevant information relating to the distribution/sale of a financial product.

However, it contradicts Article 10 (b) of EU delegated directive 2017/593, which provides that distributors should transmit information on product sales only if manufacturers need it (at their request) (*“Member States shall ensure the investment firm with the direct client relationship has ultimate responsibility to meet the product governance obligations (...). However, intermediary investment firms shall: (b) if the manufacturer requires information on product sales in order to comply with their own product governance obligations, enable them to obtain it”*).

In accordance with the provisions of this article of the delegated directive, many contractual agreements have been signed between manufacturers and distributors which provide for the transmission of sales information by the distributor to the manufacturer, at the latter's request.

Therefore, FBF asks ESMA to delete this sentence which could lead to an undesirable confusion in the respective responsibilities of manufacturers and distributors, in the context of the transmission of commercial information between the two and contradicts the existing regulation.

In Paragraph 72, the FBF asks ESMA to remove the reference to sending a questionnaire to a sample of clients who have purchased financial instruments under non-advised services.

Indeed, it would not make sense to ask clients additional *ex post* questions on their financial situation, their investment objectives including their sustainability preferences when they would not have been asked *ex ante* about these elements since they would be acting in the framework of non-advised services.

This would be extremely confusing, not comprehensible and irritating for clients and it is conceivable that most of them could refuse to answer such a questionnaire. Firms are required to be clear about the investment service they provide to the client and carry out some kind of “ex-post suitability assessment” on non-advised clients would severely impair firms’ compliance with this obligation.

In the last sentence of this paragraph, it will not be possible for distributors to establish that products are too often distributed outside the positive target market, since distributors only collect information on their clients' knowledge and experience, when these clients act in the context of non-advised services. This assessment can only be made on the first two criteria, in accordance with ESMA's guidelines on non-advised services.

Q10: Do you agree with the suggested approach on the negative target market assessment in relation to a product with sustainability factors? Please also state the reasons for your answer.

Yes, we support paragraph 81 which adds welcome clarification to the delegated directive's writing.

Q11: Do you agree with the suggested updates on the application of the product governance requirements in wholesale markets? Please also state the reasons for your answer.

Yes, we agree with these updates.

Q12: Do you have any comment on the suggested list of good practices? Please also explain your answer.

We are surprised that these “good practices” are included in the ESMA draft Guidelines consultation, which scope indicated is that “In accordance with article 16(2) of the ESMA Regulation, this Consultation Paper (CP) sets out for consultation draft ESMA guidelines on certain aspects of the MiFID II product governance requirements”. The good practices are not part of the guidelines, neither listed as a possible tool for ESMA’s task in article 16. Therefore, we believe that they should not be included in this document. In our opinion, would ESMA be mandated to produce “good practices” lists, such views should clearly be identified as being only examples that can "help firms comply with the relevant requirements [of the guidelines]", as stated in Annex IV, and not additional requirements nor part or Annex of a document which legal status (guidelines) is clearly defined.

Q13: Do you have any comment on the suggested case study on options? Please also explain your answer.

Yes, we believe that these case studies cannot be very useful for investment firms.

Indeed, most of the examples of target markets that are supposed to have been defined by a manufacturer are far too narrow to match the client profiles as defined by any distributor.

For example, the information *"client objectives and needs": seeking a capital growth opportunity only in the medium term (six years investment horizon) and expecting that (...) none of the stocks will be worth less than 50% of the initial valuation"* (on page 50 of the CP) is too specific and not realistic, since it would have no chance to match the clients' categories or clients' profiles defined by a distributor.

In addition, since the application of the ESMA product governance guidelines, therefore since almost 5 years, firms have developed the Findatex model, which is i) comparable from one manufacturer to another one ii) machine readable iii) even used on a voluntary base by non-MiFID manufacturers and has not been criticized during the CSA review by any NCAs. Therefore, we do not see actual added value in the provision of case study, as wordy and overly detailed target market description are of no use for distributor, when assessing, selecting and comparing hundreds of thousands of products used by hundreds of manufacturers.