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## **CONSULTATION ON THE REVIEW OF THE GUIDELINES ON MiFID II PRODUCT GOVERNANCE REQUIREMENTS**

By means of this letter, the European Financial Market Lawyers Group (EFMLG)<sup>1</sup> wishes to contribute to the above ESMA public consultation.

As you may know, the EFMLG intends to foster the harmonization of laws and market practices in the EU and to facilitate the progress in the Capital Markets Union.

The EFMLG supports the EU sustainable finance strategy including the reorientation of investments towards EU compliance with the Climate Law and ultimately with the Paris Agreement. Investment and financing should indeed be oriented towards more sustainable technologies and businesses and generally towards sustainable growth. An approach which will also contribute to the stability of the financial markets.

From this perspective we want to seize the opportunity of the consultation on the review of the guidelines on MiFID II product governance requirements to reiterate some of our concerns which were already addressed in our letter of 12 April 2022 and stress the importance of consistency. In the interests of both investors as financial institutions it is of the utmost importance that the regulatory sustainable finance framework is consistent and also that the application dates of the different regulations forming part of the framework are aligned and realistic.

### **(i) Consistent regulatory framework – product governance consultation**

We support ESMA's suggestion to align the definition of 'sustainability-related objectives'

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<sup>1</sup> The European Financial Market Lawyers Group is a group of senior legal experts from the EU banking sector dedicated to making analysis and undertaking initiatives intended to foster the harmonization of laws and market practices and facilitate the integration of financial markets in Europe. The members of the Group are selected amongst lawyers of major credit institutions based in the EU active in the European financial markets. The Group is hosted by the Legal Services of the European Central Bank.

with the definition of 'sustainability preferences' according to Article 2(7) of the MiFID II Delegated Regulation as will be detailed further in the ESMA Guidelines on certain aspects of the MiFID II suitability requirements. This should indeed facilitate a consistent implementation across different roles and different stages of the product cycle.

In this respect, we welcome ESMA's call for feedback on the application of sustainability preferences on financial instruments that are not financial products under the Disclosure Regulation. Although as EFMLG we do not want to pronounce ourselves on how different types of financial instruments could meet sustainability preferences, we nevertheless want to stress the importance of a common approach that is not too restrictive. Indeed, we would suggest considering a broad, flexible interpretation. If not, the new sustainability framework would, in practice, limit the range of products that may be recommended to clients. This would or at least could have - in our view – major consequences with direct detrimental impact on the general EU policy goal of increasing/promoting products with sustainability features.

Although, as such not subject of the consultation, we want to highlight that – to date – there is still no common understanding on the definition of 'sustainable investment' or on how to consider principal adverse impacts.

(ii) Aligned and realistic implementation timelines of ESG regulations

For financial institutions to be able to manufacture and distribute financial instruments that could meet clients' sustainability preferences, it is not only necessary to have a minimum level of common understanding (cfr. above) but sufficiently reliable ESG related data also need to be available. However, quantitative data on EU Taxonomy will only become gradually available starting as of January 2023. For the application of the Corporate Sustainability Reporting Directive (CSRD) the financial sector will need to wait until 2025!

Although large corporates will only be subject to transparency requirements at a later stage, certain ESG requirements are already applicable to financial institutions well beforehand.

Manufacturers should provide as of 22 November 2022 information on sustainability-related objectives. However, the consultation on this topic is still running and final guidelines are expected in Q1 2023.

Financial market participants under the SFDR should start disclosing ESG-related information as of 22 November 2022. The RTS in this respect is however only applicable as of 2023. At the same time the ESAs have received two mandates:

- (1) A first one to propose amendments in relation to the information that should be provided about exposure of financial products to investments in fossil gas and nuclear energy activities; and
- (2) A second one to review the indicators for principal adverse impact (PAI) and the financial product disclosures in the SFDR Delegated Regulation. Input has been requested at the latest by 28 April 2023.

The above mandates imply that – most likely – the templates used in Q1 2023 will already need to be revised in the course of 2023.

Timewise distributors are even worse off. They should already have started to consult their clients on their sustainability preferences, so they may be matched with suitable sustainable products as of August this year however:

- (1) There are no final guidelines on certain aspects of the MiFID II Suitability Requirements;
- (2) The feedback received on the consultation on draft Guidelines on integrating the customer's sustainability preferences in the suitability assessment under the Insurance Distribution Directive (IDD) made EIOPA decide to pause its work on issuing Guidelines and focus instead on providing guidance;
- (3) Target markets for financial instruments do not yet take into account sustainability features. Product governance requirements in this respect will only enter into force as of 22 November 2022 and the relevant consultation is pending.
- (4) It is not clear how to apply sustainability preferences to financial instruments that are not financial products under SFDR (cfr. pending consultation).
- (5) There is no precontractual ESG related information available that can be shared with clients (e.g., SFDR RTS will only be applicable as of 2023)
- (6) With regard to ESG ratings, we are currently in the phase of a call for evidence of an impact assessment. A (legislative) initiative will potentially be launched not earlier than in Q1 2023.

We understand the urgency of the EU Sustainable Finance project, which, as indicated, we do support, but we also do believe that it can only be successful if there is a solid sustainability regulatory framework whereby the implementation timeline is coherent with the ESG related reporting and transparency regulations. If not, instead of clients being guided towards more sustainable investing, in practice, there is the risk that clients will be overwhelmed by the complexity of the subject, that moreover is rapidly changing<sup>2</sup>, and disappointed because high expectations cannot be met. As a result, we may face the undesired scenario whereby clients turn their back on sustainable products whilst financial institutions still incur – involuntarily – reputational and compliance risks.

Yours faithfully,



Fernando Conledo,  
Vice Chairman, EFMLG

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<sup>2</sup> In annex is a revised overview of the most important regulatory initiatives whereby the changes vis-à-vis our overview of April 2022 are highlighted to illustrate how volatile and fragile the regulatory sustainable finance framework is.

## Annex

### EFMLG LETTER: ESMA CONSULTATION ON THE REVIEW OF THE GUIDELINES ON MIFID II PRODUCT GOVERNANCE REQUIREMENTS

Date	Regulatory changes - Application date	Impact
1 January 2022	Article 8 Taxonomy Delegated Act – partially applicable	Only quantitative reporting on the proportion of taxonomy eligible activities.  Non-financial undertakings to disclose the proportion of taxonomy-eligible economic activities.  Limited disclosures by financial undertakings
2 August 2022	Application of the Delegated Regulation (EU) 2021/1253, Delegated Regulation (EU) 2021/1257	The suitability assessment will need to include the new sustainability preferences regime.
Q3-Q4 2022	Final ESMA guidelines on suitability	Pending
8 July 2022	ESMA guidelines on product governance	Consultation – Request for input on application of sustainability preferences to products with sustainability factors that are not in scope of the SFDR and/or the Taxonomy Regulation.  Final guidelines: expected Q1 2023.
On hold	EIOPA guidelines on the integration of the customer's sustainability preferences in the suitability assessment under IDD	On hold – only guidance.
30 September 2022	ESAs Final Report on SFDR amendments for nuclear and gas activities: proposed amendments to the SFDR RTS to include transparency on investments in fossil gas and nuclear energy activities	Impacts on SFDR templates – application date left to the Commission: unknown yet.
22 November 2022	Application of the Delegated Directive (EU) 2021/1269	The target market will need to include any sustainability related objectives that the financial instrument is compatible with + information on sustainability factors.
30 December 2022	Application of SFDR Article 7 (Transparency of adverse	Updates needed to reflect the following:

	sustainability impacts at financial product level)	<ul style="list-style-type: none"> <li>• Clear and reasoned explanation of whether, and, if so, how a financial product considers principal adverse impacts</li> <li>• Statement that information on principal adverse impact is available in periodic reports</li> </ul> <p>In the preamble of the first draft MiFID amendment ((2020)2955205 the European Commission recognized the issue and stated that '[as of 30 December 2022], <i>investment firms should be able to increasingly recommend also those products as suitable in terms of client's sustainability preferences after that date.</i>'</p>
1 January 2023	Application of the SFDR RTS	<p>Pre-contractual templates need to be added to existing pre-contractual documents.</p> <p>This will include the percentage of sustainable investments under SFDR and the disclosure of the percentage of the products' Taxonomy alignment for Article 8 products with sustainable investments and all Article 9 SFDR products.</p>
1 January 2023	Full application of the Article 8 Taxonomy DA to non-financial undertakings	<p>First quantitative taxonomy reporting on taxonomy alignment for non-financial undertakings subject to NFRD for the 2022 reporting period.</p> <p>Before this date, no taxonomy data will be available on investee companies.</p>
By 28 April 2023	ESAS are requested to review the indicators for principal adverse impact (PAI) and the financial product disclosures in the SFDR Delegated Regulation	Impact on SFDR templates – quid impact on advisory – application date: unknown.
1 January 2024	Full application of the Article 8 Taxonomy DA to financial undertakings.	Financial undertakings falling under NFRD/CSRD start quantitatively reporting their entity's taxonomy alignment levels (some information only as of 1 January 2026).
[Financial years starting on or after 1 January 2023] [Listed SMEs 3 years later: 1 January 2026]	CSRD (still to be published)	<p>[Sustainability Reporting Standards for SMEs at the latest by 31 October 2023].</p> <p>Probably postponed with an additional year. Not yet published. No final standards.</p>

?	Extension of taxonomy classification (delegated acts) to (i) environmental objectives other than climate and climate change and (ii) social and governance.	
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