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Frankfurt,
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BVI[1] comments to the ESMA Consultation Paper "Guidelines on certain aspects of the MiFID II suitability requirements" (ESMA35-43-2998)

The market for products with sustainability-related features is experiencing an unprecedented growth in Germany and EU-wide. In 2021, German retail investors invested net EUR 60 bn in funds with ESG features which represents an increase by nearly 200 percent compared to 2020. Integration of sustainability preferences in the investment advice process under MiFID and IDD shall further contribute to mainstreaming sustainable investments and shifting capital flows to sustainable activities and projects.[2] Therefore, we welcome the opportunity to comment on the ESMA proposed approach for adaptation of the MiFID II suitability guidelines.

As it stands, the market for sustainable products operates on the basis of the SFDR classification in "Article 8" and "Article 9" products and is now evolving to incorporate the relevant product features specified under MiFID and IDD. Currently there are basically no "Article 8" products in the market that already meet one or more criteria for sustainability preferences under MiFID and IDD as binding elements of their investment strategy. "Article 9" products provide per se for a certain (high) proportion of sustainable investments and consideration of principal adverse impacts that are relevant for clients with sustainability preferences. However, given that "Article 9" funds generally have a targeted focus on sustainable sectors or projects (e.g., renewable energies), they are in most cases not sufficiently risk-diversified in order to be suitable as stand-alone investments for average retail investors.

Investment strategies of "Article 8" funds are currently being adapted by the providers, but these adaptations face **several challenges in legal, factual and timing terms**:

- There is **effectively no possibility to commit to a meaningful proportion of Taxonomy-aligned investments in broadly diversified funds** due to (1) the **early stage of development** of the EU Taxonomy that pertains only to a few sectors, in particular energy and transport, (2) the **lack of reported or otherwise reliable data** for assessing investments against the Taxonomy and (3) the **limitations under the draft SFDR RTS for referring to other than data of equivalent quality** as proxies for Taxonomy-alignment. Moreover, it is important to understand that Taxonomy-alignment in case of equity investments pertains not to the company as a whole, but only to that **relevant fraction of turnover** (or alternatively Capex/Opex) by a company that is directly related to economic activities fulfilling the technical criteria under the EU Taxonomy (e.g., in case of car manufacturers, to the proportion of turnover from production of electric vehicles). **High proportions of Taxonomy-aligned investments in diversified equity funds will therefore remain unrealistic in the coming years**, even in case the data availability will improve.

[1] BVI represents the interests of the German fund industry at national and international level. The association promotes sensible regulation of the fund business as well as fair competition vis-à-vis policy makers and regulators. Asset Managers act as trustees in the sole interest of the investor and are subject to strict regulation. Funds match funding investors and the capital demands of companies and governments, thus fulfilling an important macro-economic function. BVI's 116 members manage assets of some EUR 4 trillion for retail investors, insurance companies, pension and retirement schemes, banks, churches and foundations. With a share of 27%, Germany represents the largest fund market in the EU. BVI's ID number in the EU Transparency Register is 96816064173-47. For more information, please visit www.bvi.de/en.
[2] Cf. EU Action Plan on Financing Sustainable Growth dated 8 March 2018, section 2.

- **Similar problems arise in relation to commitments for sustainable investments**. We understand that sustainable investments need also to be assessed based on the economic activities of an issuer which means that generally only a **fraction of the entire investment will be classified as sustainable**. The concept of sustainable investments is defined only in loose terms which creates **legal uncertainty for product manufacturers**. In addition, there is also a **significant data problem** since in principle, sustainable investments involve screening of the mandatory indicators for principal adverse impacts to be defined under SFDR RTS. As to date, however, there are still major data gaps that inhibit full coverage of indicators as foreseen in the RTS draft, e.g., on biodiversity, hazardous waste or gender pay gap.

- In view of these problems, we can observe that **many fund managers currently focus on the concept of considering principal adverse impacts (PAIs)** in their implementation projects. Indeed, consideration of PAIs as sustainability features is in general best aligned with the ESG investment approaches most common in Article 8 products such as exclusion-based strategies, best-in-class selection or dedicated ESG engagement. The data gaps with regard to the coverage of the relevant PAI indicators are, of course, also problematic for this option, but can be overcome by focusing on certain PAI themes, e.g., GHG emissions or adherence to international social and governance standards where data availability is already broadly satisfactory.

In view of this evolving market situation, it is clear that **by August 2022 the ability of investment advisors to cater for all potential sustainability preferences of clients will be rather limited**. At least in the initial phase of implementation, certain product features (e.g., Taxonomy-aligned products or products with a high share of sustainable investments) will be very scarce. In our view, it is **very important to keep this market reality in mind when making specifications for the investment advice**: Clients should not be lured into thinking that they can pick and choose any sustainability features they like if in the end, no matching products will be available. This could lead to potential frustrations and undermine credibility of the overall investment advice process. The ultimate goal of promoting sustainable investments and shifting capital flows to sustainable activities and projects might be at risk.

Therefore, it is crucial that firms remain able to **inform clients about the respective availability of products addressing sustainability preferences** in order to counteract unrealistic expectations and to focus the “know your client” test only on those available product features. It is important to communicate openly with clients and provide them with a clear picture of the real possibilities. Anything else would not be purposeful at the current stage of the transformation process.

Likewise, firms should be able to approach the client’s preferences with regard to a minimum proportion of sustainable investments by **collecting information on possible ranges or sizes also in qualitative terms**. For instance, firms could assign the available products to qualitative categories “low”, “medium” and “high” based on the proportion of Taxonomy-aligned or sustainable investments not in absolute terms, but relative to the market evolvement. Such dynamic “best in market” approach would allow firms to keep their internal selection process up to date and to take into account progress in the offerings of sustainable products on a continuous basis.

Given the lack of a standardised methodology for determining sustainable investments and calculating their share in a portfolio, comparability of outcomes will not be guaranteed. Therefore, the question arises whether it makes sense at all to ask clients for their preferences in terms of a specific minimum share. Instead, clients could be asked about their preferences for sustainable investments in general and information about the share of sustainable investments could be provided in the suitability report.

In case they have no products available that would exactly match a client's sustainability preferences, it should **still be possible for investment firms to recommend products that pass other criteria of the suitability test** and potentially provide for some basic level of sustainability. **Alternatively, adaptations of sustainability preferences, if necessary, should be admitted on a much broader scale**, including a part of the standard procedure, at least in the first years of application. ESMA should in any case seek to avoid situations where firms will be in the end prevented from recommending products to clients because they have been asked about their sustainability preferences in theoretical terms that is disconnected from the market reality.

Lastly, ESMA should be aware **that in the initial phase of application of the MiFID / IDD sustainability preferences, there will be hardly any products available that will offer binding contractual commitments for the relevant sustainability features**. This is because most providers of Article 8 funds are planning to adapt the description of their investment strategy in order to incorporate commitments in terms of sustainable investments or consideration of principal adverse impacts only by the end of 2022, i.e., to meet the deadline for SFDR RTS implementation, since such disclosures shall be part of the standardised ESG annexes foreseen by the RTS. An earlier implementation is hardly possible given that the final rules and the templates for the ESG annexes have still not been published. Nonetheless, most product manufacturers will have implemented the relevant product features by August 2022 in their internal processes, i.e., by adapting the investment policy and any relevant investment limits in order to already comply with the intended commitment in terms of sustainability preferences. It is intended that product manufacturers will inform their distributors about these internally implemented product features by August 2022 via the European ESG Template (EET).

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.

Our understanding is that information about the purpose of the suitability assessment and its scope may be provided in writing by using a standardised format in accordance with the general guideline 1 and that explanations in terms of sustainability preferences shall be part of such information taking into account the level of knowledge and experience of the respective client category. Taking this for granted, we agree with the approach suggested by ESMA.

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 in principle that it is appropriate to explain the distinction between the different elements of sustainability preferences and their underlying concepts as well as between products with and without relevant sustainability features. However, the explanations provided by distributors should not encompass all ESG product features present in the market, but clearly relate to the regulatory understanding of sustainability preferences. Given that governance aspects are not suitable as distinct

sustainability objectives for neither Taxonomy-aligned nor sustainable investments under SFDR, but apply only as minimum safeguards, we believe that mandatory explanations should focus on environmental and social aspects in the first place.

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.

The approach suggested by ESMA is **overly complex** and will likely **overstrain advisors and investors likewise.**

It needs to be taken into account that in the initial phase of implementation, there will be certainly no sufficient products to match all sustainability preferences of clients. As explained above, most products that currently classify as Article 8 under SFDR and are sufficiently risk-diversified to pass the suitability test for average retail investors do not currently provide for the product features relevant in terms of sustainability preferences. Investment strategies of these Article 8 funds are currently being adapted by the providers, but these adaptations face several challenges in legal and factual terms as described above. It is hence quite likely that by August 2022, there will be no risk-diversified investment funds with any relevant proportion of Taxonomy-aligned investments or with high share of sustainable investments.

Consequently, distributors should be allowed to limit the "know your client" process to those products that are available in the market and that they can offer as part of their product range in order to avoid asking clients about their preferences for only theoretical product features. This would only cause frustrations for clients and lead to a situation where subsequent adaptation of the individual sustainability preferences, if required, might be considered a standard case and thus, would contradict the general expectation by ESMA (cf. para. 81 of the draft guideline).

In case the relevant product range does not encompass all sustainability features of products that are generally available in the market, advisors should be allowed to inform the client that their product offer does not include certain options without being obliged to ask for client preferences in relation to these excluded options. Furthermore, it should be noted that investment firms are generally free to choose the products they offer their clients. They should not be obliged to offer all available products. This can also lead to a situation where the product range does not include products that are suitable for clients with sustainability preferences. Of course, the customers must be informed about this circumstance.

With regard to the approach for testing client's preferences for consideration of PAIs as outlined in the second last bullet point in para 26, **we fully support the suggested first stage of such testing based on the families of PAI indicators**. In our view, such exploration of client's preferences with a possible focus on environmental, social and/or governance aspects by referring to the relevant indicator categories already involves elements of qualitative consideration. A more extensive qualitative evaluation based on the approaches for PAI consideration as part of the investment strategy, as envisaged by ESMA, would however likely overstrain an average retail investor. Market soundings indicate that many products will combine different approaches for PAI consideration depending on the relevant indicator or on the level of adverse impacts which would make such strategy-based selection very cumbersome.

In addition, we would like to stress that the text of MiFID II delegated regulation makes reference to qualitative or quantitative elements of PAI consideration that shall be determined by clients, not to both as implied in the consultation paper.

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

We see no need for further, more specific guidance for assessing sustainability preferences. It is crucial to keep the process viable and to focus on product features that are relevant for the client. Sustainability preferences have to be assessed not in an abstract manner, but in the context of the overall client profile and in particular against the background of his or her financial needs.

Flexibility is also particularly important in order to match the level of detail prescribed for other elements of the "know your client" process. Under the current ESMA guidelines, there is no standardised approach either for customer exploration in the market. It must be possible to integrate sustainability preferences into the existing internal processes, also in order to foster competition.

Against this background, **it would be helpful not to specify the sequence of questions to keep the process flexible**. It should also be made very clear that the approach outlined in paragraph 26 is to be seen only as an example of good practice and that the actual supporting guideline is confined to paragraph 25 (the current wording "should" in para. 25 and "could" in para. 26 indicates this distinction, but it should be emphasised more clearly for proper understanding).

Consequently, **exploration of a client's focus on either environmental, social or governance aspects of sustainability as suggested in para. 26 should be optional as well** since such differentiation is not required by the MiFID rules. A sole focus on governance issues is very unlikely for funds and other SFDR products and in any case, must not pertain to either Taxonomy-aligned or sustainable investments, since a positive contribution to a governance-related objective is not considered sufficient under either concept. Moreover, in the initial phase of implementation, i.e., before end 2022, there will be in many cases no sufficient information for distributors to establish the relevant focus of an investment strategy, given that products will allocate shares of investments contributing i.e. to social and environmental objectives only when implementing ESG disclosures in line with the upcoming SFDR RTS.

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?

We think that **it should not be mandatory to ask clients about their preferences for possible combinations of product features**, also against the background of the evolving market situation with only a limited range of relevant products becoming gradually available (cf. our introductory remarks).

If a client expresses a preference for more than one relevant product feature, firms should in our view look for possible combinations in their product offer as a first step. However, in case there is no possibility to offer a product that matches the exact combination preference of a client but provides for

at least one relevant feature in line with his or hers individual specifications, this should be considered as sufficiently adequate and no adaptation of individual sustainability preferences should be required.

ESMA could review this approach after an initial phase of application, e.g., two years, in terms of appropriateness, after having analysed the situation in the market.

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 agree that in case of portfolio management, the client's sustainability preferences should be determined with a comparable level of granularity and should relate to the portfolio level. However, ESMA should keep in mind that clients of portfolio management services are often quite experienced and bring along their own, sometimes very detailed ideas about sustainability and implementation in their portfolio. In these circumstances, a standardised query may not be able to do justice to the individual preferences of clients. Therefore, it is also necessary to provide for more flexibility in the survey of sustainability preferences.

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 and consider it feasible. In particular, we support ESMA's suggestion that in ongoing client relationships exploration of sustainability preferences should be expected in the course of the next regular update of client information or during the first meeting with client, whichever takes place first after the entry into force of the MiFID II Delegated Regulation.

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 have identified no objections in this regard.

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 fully agree that firms should be able to rank or group products in their internal systems according to certain features relevant for sustainability preferences of clients. In this regard, it is **important that such ranking or grouping can be based on a relative "best in market" approach having regard to the current offering of products with sustainability features in the market** rather than on absolute values. For example, we assume that the proportion of Taxonomy-aligned investments in funds pursuing sustainable investment strategies will increase over time due to a variety of factors, i.e., further development of technical criteria for Taxonomy-aligned economic activities, enhanced reporting by companies and increasing progress in transition. Funds that hold for instance 10 percent of Taxonomy-aligned assets might be ranked "high" compared to their peers today but will be likely classified as "medium" in a few years' time. The internal arrangements for assessing sustainability factors of products should thus be able to keep up with the market evolvement and rely on qualitative ranking features rather than hard quotas that will be subject to continuous changes.

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.

We very much support the additional guidance provided in para. 79 as regards the sequencing of the suitability testing that makes clear that **identification of products matching the sustainability preferences of a client should take place only as a second step** once the range of suitable products with regard to the financial suitability criteria has been identified.

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 strongly disagree with the proposed requirement to limit a firm's ability to recommend a product that does not meet a client's sustainability preferences to instances where the client has subsequently adapted his or her individual preferences for the purpose of suitability testing.

Our understanding of the provision in Art. 54 (10) second and third subparagraph of MiFID II Delegated Regulation is that it **does not ban recommending financial instruments to clients in case the individual sustainability preferences cannot be met**. Rather, in this case the advisor must not recommend a product as meeting the relevant sustainability preferences, but he is still allowed to make a recommendation. Indeed recital 8 clarifies that *"it is necessary to clarify that financial instruments that are not eligible for individual sustainability preferences can still be recommended by investment firms, but not as meeting individual sustainability preferences."* Adaptation of a client's sustainability preferences should be thus relevant to cases where a client wishes to change his sustainability profile in order to receive recommendations that match his or her individual preferences. A practicable approach would also be, among other things, if a client consciously chooses a product that does not coincide with his or her sustainability preferences, to assume this choice as an implied adaptation of sustainability preferences.

In case ESMA does not follow this interpretation, it will be nevertheless **absolutely necessary to abstain from the requirement of adapting sustainability preferences only for the sustainability assessment or investment advice in question**. Otherwise, there is a high risk of frustration on the part of investors. Given that the market environment will not change overnight and products with new sustainability features or increased level of ambition will need to evolve over time (also in view of the availability of reliable ESG data that will only gradually improve), it is **crucial to allow for updates of sustainability preferences of clients to be conducted at regular intervals, e.g., annually**. Clients seeking investment advice more frequently would be then spared from rediscussing their individual sustainability preferences over and over again.

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Moreover, we have **serious concerns with ESMA's proposal in para. 81 that a client's sustainability preferences may not be adapted as part of a "standard procedure"**. First, this interpretation is not consistent with recital 8 of the MiFID II Delegated Regulation which does neither stipulate nor even imply such limitation. Second, in combination with the proposed approach to the "know your client" testing under general guideline 2, firms will have no other choice than to provide for the possibility of adapting the individual sustainability preferences of clients in order to be able to recommend suitable products at least in the initial months and years of application.
As explained in our introductory remarks, it is clear that by August 2022 the ability of investment advisors to cater for all potential sustainability preferences of clients will be rather limited. At least in the initial phase of implementation, certain product features (e.g., Taxonomy-aligned products or products with a high share of sustainable investments) will be very scarce. For average retail clients with a rather conservative risk and reward profile, it is likely that in most cases only products with consideration of PAIs, if any, will pass the suitability test.

This means that in the initial phase of implementation, investment firms will **need to manage the gap between potentially very demanding expectations of clients, e.g., in terms of high proportions of Taxonomy-aligned or other sustainable investments, and the range of products available in the market**. In order to make this part of suitability testing feasible and to avoid situations where firms will be in the end prevented from recommending products to clients because they have been asked about their sustainability preferences in theoretical terms, we see the need for the following adaptations of the draft guidelines, also in line with our suggestions made above:

- Investment firms should be able to **focus in the "know your client" testing on product features that are available in the market and that form part of their current product range** in order to avoid exploration of client preferences being detached from the market reality. This more focused approach would significantly reduce the need for subsequent adaptations of individual sustainability preferences and prevent potential frustrations on the part of clients.

- [Assessment of sustainability preferences should be **embedded in the overall evaluation of the client profile** and in particular, should be conducted with due regard to his or her financial needs.]

- Investment firms should be **allowed to rank or group products according to a "best in market" relative approach and present the options to clients in a qualitative manner** (e.g., by differentiating between products with high, medium and low proportion of Taxonomy-aligned or sustainable investments).

- In case there are no products that would exactly match a client's sustainability preferences, it should **still be possible for investment firms to recommend products that pass other criteria of the suitability test** and potentially provide for some basic level of sustainability (for more details, cf. our reply to Q13 below). **Alternatively, adaptations of sustainability preferences should be admitted on a much broader scale**, including a part of the standard procedure, at least in the first years of application.

It is indeed crucial that ESMA improves the practicability of integration of sustainability preferences into the advice process along our suggestions outlined above in order to actually support, not inhibit, reorientation of capital flows towards investments in sustainable activities and projects as foreseen by the 2018 EU Action Plan.

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.

Please refer to our reply to Q11 above.

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 situations where firms cannot offer any financial instruments that fully meet the client's sustainability preferences, the client must of course be informed of this outcome. As explained in our introductory remarks, we assume that there will be difficulties in selecting suitable products, especially in the initial phase of the new sustainability preferences assessment, given that the market is continuously evolving. As a fallback solution, however, we believe it should also be possible to explain to the client that the firm has currently no financial instrument that meets his/her preferences and to document this outcome in the suitability report. In a second step the firm could then alternatively offer financial instruments that do not meet the requirements of Art. 2(7) MiFID II Delegated Regulation and hence are not compatible with the individual sustainability preferences of the client, but which nevertheless provide for certain features with relevance to sustainability.

In Germany, associations representing distributors and manufacturers of financial products, including BVI, have agreed on a common concept that represents a relevant market standard for implementation of sustainability-related target market criteria under MiFID (cf. https://www.bvi.de/service/muster-und-arbeitshilfen/mindeststandard-zur-zielmarktbestimmung/). Here we have foreseen two product categories that could be used as fallback options in such circumstances:

- First, so-called ESG strategy products: For investment funds, these comprise products with a dedicated ESG strategy according to Article 8 SFDR
- Second, so-called basic products: For investment funds, these are products that provide for a systematic integration of ESG risks and opportunities in the investment process and as part of engagement without including binding commitments for ESG criteria to be followed in the investment strategy ("Article 6+ products")
- For both product categories, there is the requirement for product manufacturer to take into account UN PRI as a recognised industry standard

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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 do not understand why the product's sustainability features shall still be explained or further mentioned to clients that either do not answer the question on sustainability preferences or even declare specifically no interest in suitability. The supporting guideline in para. 83 should be revised.

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.

Yes, we agree with the explanations in the case of portfolio management in para. 82. In our opinion, the approach to ongoing investment advice with a portfolio approach is also appropriate.

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?

As explained in our reply to Q11 above, we have **serious concerns with ESMA's proposal in para. 81 that a client's sustainability preferences may not be adapted as part of a "standard procedure"**. First, this interpretation is not consistent with recital 8 of the MiFID II Delegated Regulation which does neither stipulate nor even imply such limitation. Second, in combination with the proposed approach to the "know your client" testing under general guideline 2, firms will have no other choice than to provide for the possibility of adapting the individual sustainability preferences of clients in order to be able to recommend suitable products at least in the initial months and years of application.
It is clear that by August 2022 the ability of investment advisors to cater for all potential sustainability preferences of clients will be rather limited. At least in the initial phase of implementation, certain product features (e.g., Taxonomy-aligned products or products with a high share of sustainable investments) will be very scarce. For average retail clients with a rather conservative risk and reward profile, it is likely that in most cases only products with consideration of PAIs, if any, will pass the suitability test.

This means that in the initial phase of implementation, investment firms will need to **manage the gap between potentially very demanding expectations of clients, e.g., in terms of high proportions of Taxonomy-aligned or other sustainable investments, and the range of products available in the market**. In order to make this part of suitability testing feasible and to avoid situations where firms will be in the end prevented from recommending products to clients because they have been asked about their sustainability preferences in theoretical terms, we see the need for certain targeted adaptations of the draft guidelines in line with our suggestions made in response to Q11 above.

These adaptations should include **a revision of the proposed approach that adaptations of the sustainability preferences should not be part of the standard procedure**, at least in the first years of application. ESMA should in any case seek to avoid situations where firms will be in the end prevented from recommending products to clients because they have been asked about their sustainability preferences in theoretical terms that is disconnected from the market reality.

More generally, adaptations of the sustainability preferences must remain possible, not only in case of a specific recommendation, but also subsequently the issue of sustainability is still new for many clients, and social perceptions are evolving, sometimes even changing rapidly (as sadly demonstrated by the current discussion about qualification of activities relating to military hardware or weapons in general as sustainable following the Russian invasion in the Ukraine). Therefore, it is also to be expected that clients will wish to change their personal attitude to sustainability (if necessary, even several times).

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

Yes, we agree. Clients can thus better understand the advantages of a switch. Costs are regularly of great importance, especially for private clients, so more transparency is desirable.

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 have no objections with regard to the proposed additional guidance.

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

We agree with the additional guidance on record keeping. As regards adaptation of a client's sustainability preferences, however, we would like to stress once again that such adaptations, if required at all, should be admitted on a much broader scale, including by way of a standard procedure, in order not to inhibit recommendations of products that would have otherwise passed the suitability test.

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.

Yes, we agree.

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

As indicated in our introductory remarks, it is of **key relevance for the market to find a workable solution for the initial phase of application**, i.e., before implementation of SFDR RTS by end 2022.

Given that the RTS under SFDR do not apply until January 2023, most funds will not have included commitments to the relevant product features, such as minimum proportion of sustainable investments or consideration of PAIs, in their pre-contractual documents by 2 August 2022. Instead, they will provide such commitments in a standardised manner by implementing the ESG annexes to their sales prospectuses as prescribed by EU regulation by end 2022. An earlier implementation is hardly possible given that the final rules and the templates for the ESG annexes have still not been published. In the meantime, i.e., by August 2022, any information on the relevant product features can only be given on

the basis of internal evaluations by product manufacturers. It is important that this approach is accepted as an interim solution.

In addition, it is clear that ESMA's final guidelines will only be published either too close to the start of the application date of the MiFID II Delegated Regulation or even afterwards – leaving fund managers and other investment firms with the prospect of starting practical application based on not yet finalised guidelines. In order to allow for an orderly phasing-in and not to interfere with the currently running implementation process, we urge ESMA to foresee a **12-month transition period for implementation of the final guidelines in the supervisory practice following their publication**.
Further complexity is added by the fact that consultation of the revised product governance guidelines catering for integration of sustainability factors is still outstanding. We understand that ESMA expects to build upon the outcomes of the current consultation in order to introduce consistent concepts and requirements for both suitability and product governance guidelines. While fully supporting this notion in principle, we must nonetheless point out **that this staggered consultation process will likely further delay full operationality of the final guidelines**, given that implementation of the suitability process needs to be built upon the target market information to be still defined.

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

So far, we have no comments in this regard.

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 major impact in terms of costs and other resources is being caused by amendments to the MiFID II Delegated Regulation. Nonetheless, the level of complexity proposed by ESMA for the "know your client" exploration and for subsequent adaptations of sustainability preferences might further add to implementation efforts in both financial and operational terms. We thus reiterate our requests for streamlining integration of sustainability preferences in line with our response to Q11.

Significant further costs will be driven by the uncoordinated sequencing of regulatory changes and the Level 3 guidelines building upon them that will effectively require subsequent adaptations of the processes for suitability testing to be implemented by August 2022.