Amafi ASSOCIATION FRANÇAISE DES MARCHÉS FINANCIERS

FINANCIAL MARKET PROFESSIONALS

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ESMA CALL FOR EVIDENCE
IMPACT OF THE INDUCEMENTS AND COSTS AND CHARGES DISCLOSURE REQUIREMENT UNDER MIFID II

AMAFI comments

INTRODUCTION

- ### About AMAFI

***Association Française des Marchés Financiers* (AMAFI)** is the legal trade organisation representing financial market participants in France. AMAFI members are investment firms and credit institutions (French, European and global firms), operating in and/or from France (corporate and investment banks (CIBs), brokers-dealers, market infrastructures, exchanges and private banks). AMAFI has been extremely active on MiFID II issues. We are involved in all regulatory matters that concern commercialization of financial instruments. As far as financial products are concerned, we mostly represent all issuers/manufacturers of products (CIBs) but, through our private bank members, distributors as well. AMAFI has more than 140 members operating in equities and fixed-income and interest rate products, as well as commodities, derivatives and structured products for both professional and retail clients.

- ### Executive summary

- **Inducements**

Considering:
- The absence of legal basis for applying Article 24(9) of MiFID II in the context of placing activities (whether relating to Debt or Equity Capital market) as described below; and
- The negative effect of such an approach on competition at EU and international level and on the development of capital market-based financing in the Union;
AMAFI hereby respectfully but strongly suggests that ESMA harmonises the inducement-related disclosure requirements in this context and do so in furtherance of the CMU objectives by confirming that Article 24(9) does not impose on placing agents the obligation to disclose to potential investors the exact remuneration they receive from issuers.

- **Costs and charges**

AMAFI fully supports the principle of transparency on costs and charges. **Disclosure of costs is indeed essential for investor protection purposes**. However, current requirements are difficult to implement given the complexity caused by the number of parameters to be considered and **certainly does not take enough into account of the principle of proportionality nor client wishes or needs**. It does not suit the very heterogeneous degrees of knowledge between eligible counterparties, professional and retail clients and degrees of sophistication between a complex structured product and an ordinary share.

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Most issues encountered concern application of MiFID II *ex-ante* costs disclosure requirements to professional clients and eligible counterparties. **AMAFI believes requirements in that context lack of proportionality and that the so-called limited application does not operate like it should.**

Rather than provide again more detailed rules, **AMAFI would like to propose amendments to the current regime in order to make it simpler, more proportionate and respectful of client wishes.**

Indeed, AMAFI proposes to set up 2 **regimes**:

- "***Full regime***": disclosure on **both** product costs and service costs always on a trade-by-trade basis;
- "***Proportionate regime***": disclosure of only service costs through tariff grids that is an essential tool.

These regimes would be applicable according to the types of customers and products involved:

- Eligible counterparties: possibility to **switch off** completely the cost and charges disclosure requirement unless the eligible counterparty so requests (and if so, to be provided under the "proportionate regime");

- Professional clients: application of the "**Proportionate regime**" unless they requested more detailed information.

- Retail clients: application of the "**Full regime**" where the product is a **packaged product** within the meaning of the PRIIPs Regulation; if not, the "Proportionate regime" unless they requested more detailed information.

In that context, PRIIPs Regulation should also be amended to shift the current product cost indicator – the Reduction in Yield – towards a Total Expense Ratio possible to add to other MiFID II costs. That would bring more synergy where it should, meaning the 2 regimes – PRIIPs and MiFID II – do apply. As far as the illustration of the impact of costs on return is concerned, AMAFI believes that the cost-benefit analysis of such requirements in MiFID II is quite bad and consider that since it may be relevant only within a PRIIPs context, the KID should be enough.

All suggested amendments are detailed in our answer to Question R and propositions of text amendments accordingly in Annex.

AMAFI welcomes ESMA initiative to collect issues encountering by market participants when applying MiFID II. AMAFI would like to point out that financial institutions face issues on other topics than costs and charges relating to investor protection (such as product governance requirements) that should be taking into account for the revision of MiFID II.

RESPONSES TO ESMA QUESTIONS

- **Disclosure requirements for inducements permitted under Article 24(9) of MiFID II**

Question A: What are the issues (if any) that you are encountering when applying the MiFID II disclosure requirements in relation to inducements? What would you change and why?

AMAFI's aim is to alert ESMA on the damaging effect on fair competition within the EU and on the attractivity of EU capital markets international level, of the reading made by certain Member states of article 24(9) of MiFID II to placing activities.

It appears that diverging approaches have been taken by EU regulators on the treatment of the remuneration received by placing agents from issuers (or sellers as far as the secondary market is concerned) for the purpose of applying the inducement-related disclosure requirements:

- Certain Member States either consider that article 24(9) of MiFID II does not apply because no investment service is provided to investors, or that, if one is, there is either no requirement to disclose the exact fee received or no disclosure imposed at all.
- Others have however argued that the activity of finding investors for the issuer also constitutes a service provided to the investor. Following this line of reasoning and adding that there is a connecting between the two services, the remuneration received by the placing agent from the issuer becomes an inducement subject to disclosure to the investors in accordance with Article 24(9) of MiFID II.

As a consequence of the above, placing agents across the EU, in theory subject to the same set of rules, end up being treated differently, one more harshly than its neighbour, depending on the Member State it is based in.

In order to foster a level playing field across the Union and in furtherance of its strategic priority for 2016-2020[1], ESMA could play a key role in the harmonisation effort needed in this regard.

It is crucial however, that ESMA refrain from adopting an excessively conservative position which would severely damage the competitivity of the Union in the context of the withdrawal of the United Kingdom. In addition, a careful examination of the provisions of MiFID II does beg the following question: would such a conservative position have any legal basis or, in other words, be based on a correct reading of European law?

A. The economic perspective

The Commission launched the CMU initiative because of concerns that, compared to other jurisdictions, capital market-based financing in the EU is relatively underdeveloped and businesses in the EU remain heavily reliant on banks as a source of funding. The purpose of each of the intended measures is to remove barriers between investors' money and investment opportunities and to overcome the obstacles that prevent businesses from reaching investors.

For the CMU to bear fruits, it is crucial that a level playing field be ensured within the EU and that EU capital markets be attractive compared to the rest of the world.

[1] ESMA has identified Supervisory Convergence as a strategic priority for 2016-2020.

Imposing an obligation on placing agents to disclose to investors the exact remuneration they receive from issuers does not, in our view, further these objectives:

- Issuers are generally against such a disclosure, which thus, when imposed, constitutes an additional reason for them to prefer other sources of funding;

- The lack of a consistent approach across the EU compounds inequalities between Member States and creates an environment conducive to regulatory arbitrage.

  The United Kingdom has taken the view that investors are not to be treated as clients but rather as Corporate Finance Contacts[2]. It is further considered that, even in a situation where an investor is indeed a client of the placing agent[3], there would be no connection between the service provided to the investor and the one provided to the issuer, again resulting in the disapplication of article 24(9) of MiFID II.

  More recently, the FCA confirmed that in its view, provided the fees received by the placing agent from an issuer client and investor client respectively directly relate to the provision of a MIFID investment service then these would not be considered as a third party payment or benefit under the inducements rules in Article 24(7), (8) or (9) of MiFID II. Instead, they would constitute a client fee or payment. This approach, which does make sense, in turns means that the placing agent is only required to disclose to investors the fact that it receives a remuneration from the issuer (or the seller) and its structure under the general conflict of interest rules, but not the exact fee.

  It seems that the German regulator, albeit not officially, has too adopted a commercially minded position.

  The French regulator, on the other hand, does consider that an investment service is generally provided by placing agents to end investors and that the remuneration received as regard the Placing service is connected therewith, as a result of which the disclosure requirement under the inducement regime is triggered[4][5]. Any investment bank based in France directly suffers from such an approach in that it is placed in a much less comfortable position than a competitor based in a more lenient Member State, and issuers, which are generally (as stated above) against disclosing the fees they have agreed to pay, will necessarily prefer the latter over the former.

- If adopting the conservative option would certainly ensure a level playing field within the EU, it would however reinforce the imbalance between the EU and the rest of the world, thereby penalising even further EU capital markets. This unwanted but unavoidable effect would constitute a major blow to the CMU initiative which ESMA should not and cannot ignore, all the more so in the context of the United Kingdom leaving the Union tomorrow.

B. The legal standpoint

In addition to seriously damaging the attractivity of EU capital markets, imposing the disclosure requirement stemming from article 24(9) of MiFID II on placing agents raises the question of the legal foundation of such an approach.

- This line of argument is based on the assumption that a placing agent provides two separate investment services: one to the issuer, the other one to investors. The corollary of that assumption is that, in order to perform Placing services, an investment firm would necessarily need to obtain

[2] FCA Handbook, COBS 3.2.2
[3] In relation to other services.
[4] AMF DOC-2013-10
[5] Save in relation to primary market activities where (i) no prospectus is required, (ii) the investors are professional clients and (iii) the service provided to them is reception and transmission of orders or execution of orders on behalf of clients: the AMF considers that the disclosure may be performed by way of disclosing a fee range.

not only a regulatory permission for "Placing of financial instruments" (either with or without a firm commitment basis) **but also a separate one** for "reception and transmission of orders" or "execution of orders on behalf of clients".

- As a matter of fact, however, a close reading of MiFID reveals that there is no provision, not even a recital, to that effect.

  This is somewhat logical in that:
  - The service of Placing is provided by the investment firm to the issuer, not to the investors;
  - Its essential feature is the obligation on the investment firm to find investors willing to buy the issuer's financial instruments

- It has been argued that, even though the conservative approach may not, as demonstrated above, be supported by any MiFID provision, it is nonetheless necessary to ensure that the client remains well informed. However, once again arises the question of the legal basis of such a statement given that MiFID is again silent in that regard. Moreover, not only investors are largely not interested in knowing the exact fee that placing agents receive from issuers, but it is also unclear as to what benefit or additional protection the disclosure of precise information would provide, even more so where the wholesale market is concerned.

Costs and charges disclosure requirements under Article 24(4) of MiFID II

AMAFI fully supports this obligation to inform investors, and in particular retail ones, of the costs and charges incurred. Disclosure of costs is indeed absolutely essential for investor protection purposes. However, this obligation is difficult to implement given the complexity caused by the number of parameters to be taken into account in identifying the obligation applicable to each situation and does not take sufficient account of the principle of proportionality and the very heterogeneous degrees of knowledge between eligible counterparties, professional clients and retail investors.

This obligation, which has been complicated to implement for investment firms and which has not yet been stabilised, as evidenced by numerous ESMA question-and-answer publications, is, in AMAFI view, one of the priority topics for review MiFID II investor protection rules.

Question I: What are the issues that you are encountering when applying the MiFID II costs disclosure requirements to professional clients and eligible counterparties, if any? Please explain why. Please describe and explain any one-off or ongoing costs or benefits.

Summary of AMAFI Answer to Question I

Main issues encountering when applying MiFID II costs disclosure requirements to professional clients and eligible counterparties concern the *ex-ante* disclosure. AMAFI believes requirements in that context lack of proportionality and that the so-called limited application does not operate like it should (like explained in our detailed answer here below). AMAFI would like to propose amendments to the current regime in order to make it simpler, more proportionate and respectful of client wishes.

Indeed, AMAFI proposes to distinguish only **two regimes**:
- "***Full regime***": communication of information on **both** product costs and service costs on a trade-by-trade basis;
- "***Proportionate regime***": communication of information only on service costs through tariff grids.

These regimes would be applicable according to the types of customers and products involved:

- Eligible counterparties: possibility to **switch off** completely the costs and charges disclosure requirement unless the eligible counterparty so requests (and if so, to be provided under the "proportionate regime");
- Professional clients: application of the "**Proportionate regime**" unless they requested more detailed information.
- Retail clients: application of the "**Full regime**" where the product is a **packaged product** within the meaning of the PRIIPs Regulation; if not, the "Proportionate regime" unless they requested more detailed information.

In the meantime, and to suggest a quicker "quick win" solutions, a new Q&A on the limited application would be welcomed like suggested in our detailed answer to Question I, here below.

Detailed AMAFI answer to Question I

A. Lack of proportionality

Concerning the *ex-ante* disclosure, AMAFI's members are facing two main difficulties when disclosing costs and charges information to professional clients and eligible counterparties:

- Firstly, in many cases, those clients refuse or at the very least do not value this information. They often ask to stop receiving that information but at present investment firms cannot acquiesce to those requests and must continue to produce and provide information that their clients neither use nor want. Unfortunately, MiFID II does not permit for investment firms not to provide such information even if the client request to do so. Thus, investment firms are facing a dilemma of risking a commercial incident if they do not respond to their clients demand or risking a sanction from their competent authority if they do not provide the information requested by MiFID II.

- Secondly, the Article 50 does not take sufficiently into account the proportionality principle when requiring disclosing costs and charges without taking into account the category of clients' type.

  - Eligible counterparties do not need to receive (and many complain about receiving) such information as they already put several investment firms into competition when placing an order in order to obtain the best price.
  - Some professional clients may value more the disclosure of costs and charges than eligible counterparties. However, it appears that the **requirement lacks proportionality** in many situations.
  - Notably for relatively simple financial instruments and execution services, it is far more **relevant and efficient to provide them the information on costs and charges through tariff grids** (*see B (i) below*). In that context, AMAFI welcomes the recent ESMA Q&A (Q&A 23) even if we regret that some conditions or restrictions provided by ESMA in that answer should have been waived for professional clients and/or in the context of the so-called "limited application" (*see B. below*).

- **Those difficulties explain why AMAFI recommends such solutions, in compliance with proportionally principle, in its Guidance AMAFI 19-73- MiFID 2 Implementation Costs and charges Guidance**

Extract from "*MiFID II/MiFIR/PRIIPs Regulation Impact Study: Effectiveness and Efficiency of New Regulations in the Context of Investor and Consumer Protection - A qualitative/empirical analysis*" (Prof. Dr Stephan Paul, Nicola Schröder, M.Sc., Simon Schumacher, M.Sc.; on behalf of the German Banking Industry Committee), February 2019

The **ex-ante cost disclosure** is a mandatory document which informs clients about all (ancillary) costs associated with the securities transaction and the financial product concerned. This must be provided to the client, prior to their concluding a trade, in durable form (meaning in hardcopy or by e-mail, fax, in an electronic mailbox, or via a website).

The objective is to increase transparency of the investment in terms of its cost structure, and to facilitate comparison, also with rival products or services.

Yet this objective – which is also built on the concept of informed decision-making, is largely not reflected in clients' perceptions: in fact, only 42.7% of clients (μ=1.6; s=1.03) assign benefits to ex ante cost disclosure.

This might be driven once again by information overload, as well as a wish to largely leave decisions to the advisor. 54.2% (μ=1.3; s=1.03) of clients even perceive this additional information as a (serious) nuisance. Like with the suitability report, retail clients (49.2%; μ=1.4; s=1.01) assign the strongest benefits to the ex-ante cost disclosure. Again, this is likely due mainly to their having less experience in securities transactions than corporate or private banking clients. **The more experienced the client, the more they felt bothered or annoyed: the most active investors** (>48 transactions per year) **felt the most bothered** (78.1%; μ=0.7; s=0.84). **This corresponds to a very pronounced wish for a waiver, at 86.2%** (μ=0.4; s=0.76), compared to 62.7% (μ=1.0; s=1.1) of all clients who would like to waive the ex-ante cost disclosure.

B. Limits and ambiguity of the so-called "limited application" of article 50.1

When dealing with a professional client or eligible counterparty, firms can potentially implement limited application of the obligations for costs disclosure in the following situations (*MiFID II DR, art. 50.1*):

- For professional clients, except when (non-cumulative conditions):
  - an investment advice or portfolio management service is provided; and/or
  - the financial instrument in question embeds a derivative.
- For eligible counterparties, except when (cumulative conditions):
  - the financial instrument in question embeds a derivative; and
  - the eligible counterparty intends to offer it to their clients.

ESMA already provides precisions (*ESMA Q&A, 9.19*) on which specific limitations may professional clients and eligible counterparties agree on. In particular, ESMA clarified that this regime cannot lead to disapplying the minimum obligations imposed pursuant to Article 24.4 – namely:

- disclosure of all costs and charges;
- the information has to be aggregated;
- it has to be provided in good time before the service.

Also, ESMA recall examples of detailed requirements that firms may not provide in accordance with limited application regime: illustration on the cumulative effect of costs on return and indication of the currency.

Considering other details requirements prescribed by article 50 of Delegated regulation but also by answers provided by ESMA in its numerous Q&A, question remain on what other arrangements are possible in accordance with the limited application regime.

As per limited application regime, and considering that *ex-ante* costs disclosure should be tailored to fit investor's information needs and should be proportionate and tailored to the nature of the client or the counterparty, specific features of the type of investment service or ancillary service that is provided and the type of financial instrument, some arrangements should be possible concerning the timing and the format for *ex-ante* disclosure.

(i) Possibility of using a tariff grid for *ex-ante* disclosure

In many cases, *ex-ante* disclosure should be compatible with the immediacy and instantaneousness of transactions. Typically, in wholesale markets, where sales and traders are trading flow financial instruments, it is not possible to give, just before trading, a comprehensive disclosure of costs. It could be against best execution duty (and speed criteria for execution).

It would not be proportionate especially for eligible counterparties and professional clients that, on one hand, are sufficiently informed about costs and market practices and, on the other hand, often use competition between market actors to choose the best price.

In some situations, when the limited application is justified, it should be possible that *ex-ante* costs disclosure could take the form of a tariff grid of the firm costs, about both services provided by the firm (*i.e.*, orders execution services, etc.) and financial instruments traded by the firm, presented by standard categories (shares, bonds, vanilla flow derivatives, etc.); considered that the grid would have to be regularly reviewed (at least annually); and "*provided in good time*" to clients, for instance delivered to them when they are on-boarded by firms and kept always available to them.

This is partially already possible as per new Q&A 23 but not entirely since the answer excluded product costs even for relatively simple products such as vanilla derivatives.

Therefore, **it could be clarified that within limited application regime (and/or for professional clients and eligible counterparties), tariff grids should be possible for displaying not only service costs but as well as product costs.**

(ii) Format of the figures displayed in the grid ("fixed figures or ranges/max?")

There are two possibilities for disclosing service costs:

(1) The service cost amount is fixed: for example, a fixed percentage of the amount of the client's order[6]. In this case, the fixed amount is added to the cost table;
(2) The service cost amount is not fixed and cannot be precisely determined *ex-ante*. In this case, a "*reasonable estimation*" must be provided (*MiFID Delegated regulation 50.8*).

For providing this reasonable estimation, one may wonder if that implies necessary a fixed figure or if the estimation could be provided in the form of a range or a maximum.

ESMA answered (*ESMA Q&A, Question-Answer 9.30*) that it should not be possible to provide such information in a form of a range or a maximum considering that "*Disclosures made in the form of a range or maximum amount of fees that the client may incur would not give the client a sufficiently good idea of the fees such client may incur*". Surely this assumption should be inaccurate for professional clients and *a fortiori* for eligible counterparties[7]. **Therefore, one may consider that in the context of limited application, such detailed requirement does not apply on condition that ranges and maximum used are as close as possible to real ones.**

(iii) Absolute figure

Considering that the exact amount of transactions cannot be known prior to their execution, a generic amount (for example, €1,000 or €10,000) can be used to communicate the aggregate costs in absolute value and percentage to the client.

In the case of professional clients and eligible counterparties, they should be considered to have the knowledge and expertise required to determine the absolute value of the costs from information provided in percentage form only. **Therefore, one may consider that in the context of limited application, such detailed requirement does not apply.**

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[6] For example, this is the case of a significant number of order transmission and share execution services which may have floor and/or maximum prices and a sliding scale based on the order amount.
[7] See AMAFI Guidance 19-73, § 5.2.2

Question J: What would you change to the cost disclosure requirements applicable to professional clients and eligible counterparties? For instance, would you allow more flexibility to disapply certain of the costs and charges requirements to such categories of clients? Would you give investment firms' clients the option to switch off the cost disclosure requirements completely or apply a different regime? Would you distinguish between per se professional clients and those treated as professional clients under Section II of Annex II of MiFID II? Would you rather align the costs and charges disclosure regime for professional clients and eligible counterparties to the one for retails? Please give detailed answers.

Summary of AMAFI Answer to Question J

AMAFI would like propose amendments to the current regime in order to make it simpler, more proportionate and respectful of client wishes.

Indeed, AMAFI proposes to distinguish only **two regimes**:
- "***Full regime***": communication of information on **both** product costs and service costs on a trade-by-trade basis;
- "***Proportionate regime***": communication of information only on service costs through tariff grids.

These regimes would be applicable according to the types of customers and products involved:
- Eligible counterparties: possibility to **switch off** completely the cost and charges disclosure requirement unless the eligible counterparty so requests (and if so, to be provided under the "proportionate regime");
- Professional clients: application of the "**Proportionate regime**" unless they requested more detailed information.

In the meantime, and to suggest a quicker "quick win" solutions, a new Q&A on the limited application would be welcomed like suggested in our detailed answer, here below.

Detailed AMAFI answer to Question I

We would indeed make changes to the cost disclosure requirements applicable to professional clients and eligible counterparties in order to simplify the regime and make it more proportionate.

Typically, **yes, we would allow more flexibility to disapply certain of the costs and charges requirements to such categories of clients, including the option to switch off the cost disclosure requirements completely** for eligible counterparties and apply a different regime for professional clients.

A. Ex-ante

In order to provide solution for more appropriate and proportionate requirement for eligible counterparties and professional clients, AMAFI wishes to propose the following solutions: one, for the long run, within the context of a "MiFID II refit" that would amend accordingly the Level 1 and Level 2 texts.
Second, for a shorter term, a more immediate solution compatible with in the current set of texts with a new Level 3 Q&A dedicated to the "limited" application.

(a) MiFID II Refit

For a more comprehensive MiFID II Refit exercise, on costs and charges issue, AMAFI would like to propose a solution that would both drastically simplify the current regime as well as providing more proportionality and respectful of clients wishes, more notably for eligible counterparties and professional clients.

As detailed in answer to question R, AMAFI would amend the Levels 1 and 2 texts in order to set up 2 regimes applicable according to the types of customers, products and services involved:

- Eligible counterparties: **possibility to switch off completely** the cost and charges disclosure requirement (meaning no requirement to provide information on costs and charges - neither in *ex-ante* nor in *ex-post*) **unless the eligible counterparty so requests.** In this latest case information would be provided to through tariff grids;
- Professional clients: **application of a different regime**; e.g. communication of costs and charges in *ex-ante* using tariff grids. **When requested** by the professional client, **more detailed** information will be communicated to this client.

(b) New Q&A

In a shorter term, AMAFI believes an amendment to current Q&A 19 could help solving some of the issues we have with eligible counterparties and professional clients, like proposed below:

Question 19 [Last update: 3 October 2017] ***[new] xxx***
Which specific limitations to the cost transparency regime may professional clients and eligible counterparties agree on?

Answer 19

Article 50(1) of the MiFID II Delegated Regulation allows - in certain situations described in paragraphs 2 and 3 thereof - for a limited application of some of the detailed requirements set out in Article 50. The more limited application which needs to be agreed by the two parties should however never lead to disapplying the obligations imposed on investment firms pursuant to Article 24(4) MiFID II.

ESMA emphasizes that Article 24(4) MiFID II requires that the information provided to clients, amongst others, includes information on all costs and charges, including information relating to both investment and ancillary services, the financial instrument recommended or marketed to the client and any third-party payments. In addition, the information shall be aggregated and where the client so requests, an itemised breakdown shall be provided. The information about costs and charges shall be provided to the client in good time before the investment service is provided and, where applicable, on a regular basis, at least annually.

Recital 74 provides examples of detailed requirements which could be the object of such limited applications under article 50 of the Delegated Regulation. For instance, the investment firm could agree, at the request of the client, to not provide the illustration showing the cumulative effect of costs on return, not provide an indication of the currency involved and not provide the applicable conversion rates and costs where any part of the total costs and charges is expressed in foreign currency.

[new]

[**Such limited application could allow the firm not to provide costs disclosure information with absolute figures, *i.e.* provided only with percentage.**

Firm could as well agree on providing a grid or table displaying the relevant costs and charges as per answer Q&A 23 even where there are product costs on the condition that it remains clear and understandable by those professional clients or eligible counterparties.

Also, professional clients and eligible counterparties can agree with the firm that relevant costs and charges will be displayed by way of a range (between X% and Y%) or as a maximum amount, provided that such range or maximum are reflecting as closely as possible the possible exact amount of costs.]

B. Ex-post disclosure

As regards the *ex-post* disclosure:

- Such requirement does not seem relevant for eligible counterparties who have knowledge to estimate themselves the costs and charges charged to them by their various investment firms;
- For professional clients, it only seems relevant to provide this *ex-post* report if the client has an "ongoing relationship" with the investment firm. AMAFI proposes to precisely define the "ongoing relationship" into the Level 2 of MiFID 2 by using investment services listed in the Annex I of MiFID 2.

Please see MiFID II Refit AMAFI solution to those issues in answer R. Please see proposal of text amendments accordingly in Annex.

As far as the question as we would distinguish per se professional clients and elective professional clients, AMAFI considers that it is a very relevant one. However, we consider that it goes beyond the questions of costs and charges disclosure and should be dealt in a more in depth and separately in a different consultation.

Question K: Do you rely on PRIIPS KIDs and/or UCITS KIIDs for your MiFID II costs disclosures? If not, why? Do you see more possible synergies between the MiFID II regime and the PRIIPS KID and UCITS KIID regimes? Please provide any qualitative and/or quantitative information you may have

For the *ex-ante* disclosure, in AMAFI's view, there are several limits for relying on PRIIPs KID for our MiFID II costs disclosures.

First, PRIIPs KID exits only where PRIIPs applies. MiFID II has a far wider scope and covers many situations where PRIIPs does not apply: all financial instruments that are not packaged products (such as ordinary shares and bonds) and wherever the product (packaged or not) is not available to retail investors. Such situations correspond to most global markets activities and should not be forgotten nor be underestimated.

Where PRIIPs does apply, it should be very clear that costs information provided within the **KID PRIIPs are highly limited useful for MIFID II purposes for several reasons**[8].

(1) KID PRIIPs **only covers the product costs**. MiFID II requires to add service costs and any inducement both separately and additionally.
(2) **KID PRIIPs does not display a total of costs *per se.*** It provides an impact of the costs but on the return of the product, based on the assumption that such return would be the one as provided in the moderate performance scenario (via Reduction In Yield – **RiY** – methodology).

RiY indicator of costs is therefore not a pure factual information on total of costs that MiFID II requires to disclose. Worst, it is not an addition and therefore **cannot itself be added to another figure for service costs**, hence again that MiFID II requires a single total addition.

As allowed by ESMA Q&A 9.7 though and despite the above points, **PRIIPs KIDs can be used to extract product costs requested by MiFID under conditions**. One may therefore understand that according to ESMA, RiY is an enough close estimate of the total costs of the product despite the above considerations.

[8] On this topic, regarding PRIIPs Revision, AMAFI proposes to replace the RiY by the disclosure of a "total expense ratio" (TER) (*AMAFI Position on KID PRIIPs Revision / 19-54*).

Still, in any cases, MiFID II would still require distributors, on the top of the KID, to provide additional information for service costs and inducement even if those are inexistent (in that case, the firm shall disclose product costs = costs from KID / service costs = 0 / inducement =0) as requested by combined ESMA Q&As 13 and 20.

In order to bring closely PRIIPs and MiFID II **wherever it is relevant to do so (meaning both texts apply**), and have more possible synergies, AMAFI considers that the following amendments should be made:

(1) **The best solution should be to change within PRIIPs, the cost indicator of KID PRIIPs towards Total Expense Ratio (TER) that is the best consistent choice with MiFID II**
(2) In any case, in MiFID II, allowing the possibility to provide only the KID PRIIPs where there are only product costs

We may add that for *ex-post* disclosure as required by MiFID II, KID PRIIPs is not relevant. KID PRIIPs and MiFID II *ex-post* report do not have the same purpose:

- the KID aims at showing an aggregated annualized number of one product cost over its Recommended Holding Period, with the objective to be comparable to other products
- MiFID II *ex-post* report aims at providing end clients a yearly report of the total of all the costs he/she actually incurred from one firm, including all service costs.

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Question L: If you have experience of the MiFID II costs disclosure requirements across several jurisdictions, (e.g. a firm operating in different jurisdictions), do you see a difference in how the costs disclosure requirements are applied in different jurisdictions? In such case, do you see such differences as an obstacle to comparability between products and firms? Please explain your reasons.

Yes, AMAFI's members have been experiencing differences in the way requirements are implemented across jurisdictions. It seems that there are different expectations as how to comply with costs and charges disclosure. In some countries, costs disclosure seems quite flexible and allows narrative/generic disclosure, especially for wholesale clients. In others, it may be less flexible but pragmatic and using tariff grids wherever it is relevant to do so. Finally, other countries may be more demanding and for instance do not use tariff grids despite ESMA's Q&A 23.

Question M: Do you think that MiFID II should provide more detailed rules governing the timing, format and presentation of the ex-ante and ex-post disclosures (including the illustration showing the cumulative impact of costs on return)? Please explain why. What would you change?

AMAFI considers that such elements would have been relevant before the entry into force of MiFID II. Investment firms already take positions and made costly IT developments to meet their obligations of disclosing costs and charges as exposed in Level 1 and Level 2 of MiFID 2 (in France they could rely on the AMAFI's Implementation Guide on costs and charges requirements).
Bringing today new details would imply expensive modifications of their systems and regulatory instability in general which is detrimental to everyone.

Instead of providing more detailed rules through more level 3 Q&A on the basis of the current texts, AMAFI would rather propose to amend those level 1 and level 2 texts (and Q&As accordingly) so to find a more appropriate, satisfactory and viable solution to the many issues encountered. Our propositions are mentioned in our answers to Questions I, J and R.

Regarding ESMA's Q&As already published in those topics, AMAFI believe that the use of the tariff grid must not be restricted to the conditions imposed by ESMA Q&A 23 and, contrary to the developments made in ESMA Q&A 30, that those tariff grid must be completed by range or maximum – which are the best estimate that can be disclose to the client in many situations (*see AMAFI proposals on answer "R"*).

As far as the question on **cumulative impact of costs on return is concerned, AMAFI tends to consider that this requirement is overwhelming and burdensome for a limited added value for investors at the end**. It makes little or no sense for some financial instruments like ordinary shares and bonds. For structured products, one may argue that information provided in KID PRIIPs, with both performance scenarios for the return and the presentation of costs should be enough. We would recommend removing the requirement in the MiFID II refit context.

Question N: For ex-ante illustrations of the impact of costs on return, which methodology are you using to simulate returns? Or are you using assumptions (if so, how are you choosing the return figures displayed in the disclosures)? Do you provide an illustration without any return figure?

Practice shows that this notion of impact of costs on return is difficult for investors to understand, especially for retail investors who understand more easily costs expressed in absolute value or in percentage as required by Article 50.2.

In addition, AMAFI's members face issues to compute the impact of costs on return required by Article 50.10.

Generally, they provide the client an explanation on the fact that costs impacted the future performance of their investment and provide a generic example to illustrate this statement.

In line with the current European-wide discussions on removing this cumulative effect on the yield of PRIIP KIDs, **it seems appropriate to remove this MiFID II requirement** as well, as it provides more confusion than transparency for retail investors.

Please see proposal of text amendments in Annex.

Question O: For ex-post illustrations of the impact of costs on return, which methodology are you using to calculate returns on an ex-post basis (if you are making any calculations)? Do you use assumptions, or do you provide an illustration without any return figure?

As developed in answer N, AMAFI proposes to delete the requirement expressed in Article 50.10 to provide the client the impact of costs on return.

Question P: Do you think that the application of the MiFID II rules governing the timing of the ex-ante costs disclosure requirements should be further clarified in relation to telephone trading? What would you change?

Without prejudice to the changes that AMAFI would recommend of the current regime of costs disclosure, we think that **an exception to the obligation to provide information on a durable medium prior to the transaction should be granted, in all cases, for orders placed by telephone** when the investment firm cannot communicate a tariff grid to fulfil is *ex-ante* disclosure obligation. This could consist in providing information by telephone at the time of the transaction, followed by sending the information on a durable medium to the client.

For AMAFI, the answer provided by ESMA in its latest Q&A 28 is **not satisfactory** because it requires to provide to the client the durable medium **simultaneously** (and not "immediately after") to the communication over the phone which is very **difficult to implement and to comply with**. Moreover, legally speaking, it seems essential to have this exemption in Level 1 or Level 2 rather than in a Q&A.

This exception has already been granted:

- for the submission of the MiFID II suitability statement when the order " *is concluded using a means of distance communication which prevents the prior delivery of the suitability statement*" (*MiFID II, art. 25.6*);
- for the delivery of PRIIPs KIDs when the investment service is provided by telephone and the KID cannot be communicated to the client before the service is provided (*PRIIPs, art. 13*).

Please see proposal of text amendments in Annex.

> **Question Q:** Do you think that the application of Article 50(10) of the MiFID II Delegated Regulation (illustration showing the cumulative impact of costs on return) helps clients further understand the overall costs and their effect on the **return** of their investment? Which format/presentation do you think the most appropriate to foster clients' understanding in this respect (graph/table, period covered by the illustration, assumed return (on an ex-ante basis), others)?

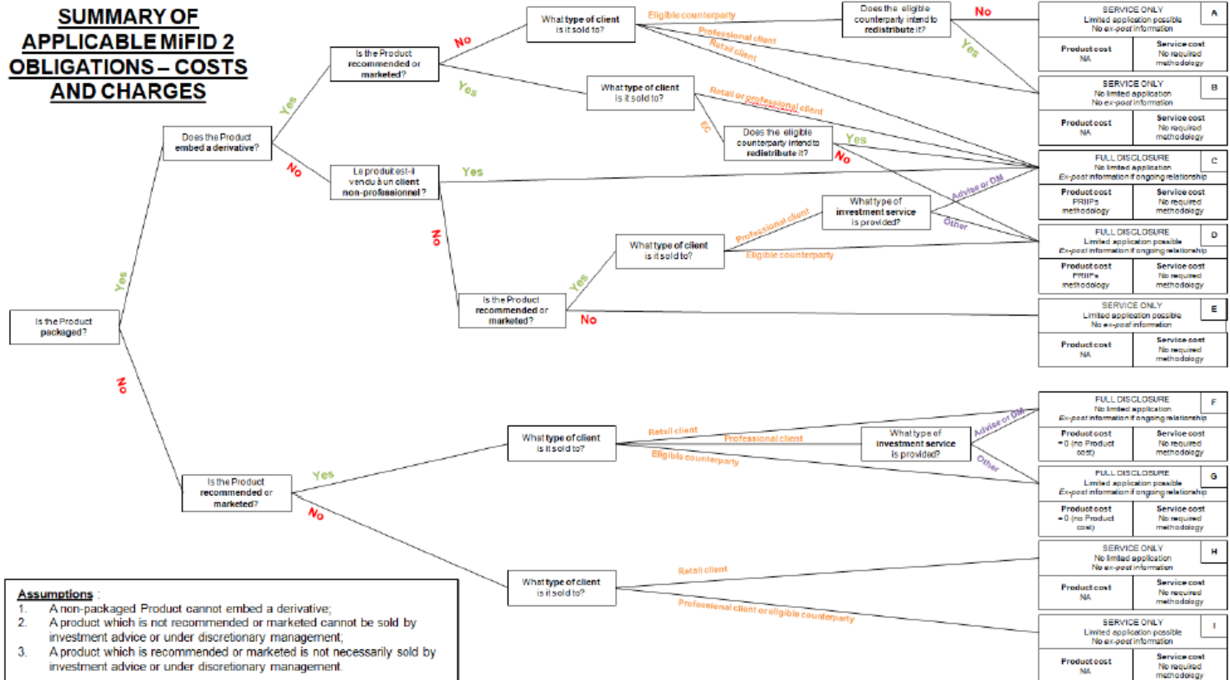
No. In AMAFI's view and as evidence by practise (especially with the PRIIPs KID) showing an impact on return in addition to (or instead of for PRIIPs KID) absolute figure **gives confusion to retail investor rather than more transparency. That is why, again, AMAFI is supportive to remove this requirement.**

> **Question R:** Are there any other aspects of the MiFID II costs disclosure requirements that you believe would need to be amended or **further** clarified? How? Please explain why.

Yes. AMAFI would like to propose amendments to current Article 50 of MiFID II Delegated regulation in order to both drastically **simplify the regime as well as re introduce more proportionality** into the requirements to take more into account the category of clients and the complexity of financial instruments.

Simplify the regime as a whole

As it is currently drafted, Article 50 is difficult to understand because it requires the articulation of several regimes that do not easily combine: (1) *ex-ante* information: total or only service costs, (2) *ex-post* information and (3) limited application. As illustrated in the diagram below, this means having to differentiate between 9 situations, which seems difficult to implement and disproportionate given the objectives pursued.



Therefore, it seems appropriate to simplify this system for both *ex-ante* and *ex-post* information.

<u>More proportionality and respect of client wishes</u>

<u>For ex-ante information</u>, AMAFI proposes to distinguish only **two regimes**:

- "**Full regime**": communication of information on both product costs <u>and</u> service costs <u>on a trade-by-trade basis</u>;

- "**Proportionate regime**": communication of information <u>only</u> on service costs through <u>tariff grid</u>. This tariff grid should be declined by asset class, the amounts indicated in may be fixed amounts or, where applicable, ranges or maximum amounts (provided that the latter reflect as closely as possible the economic reality of the costs). This grid, which is sufficiently granular according to the activities of the investment firm, must be communicated at the time of entering a relationship or at the first operation. It is updated at least annually and made available all times to clients.

These regimes would be applicable according to the types of customers and products involved:

- <u>Eligible counterparties</u>: **possibility to switch off completely** the costs and charges disclosure requirement (meaning no requirement to provide information on costs and charges (neither in *ex-ante* nor in *ex-post*) **unless the eligible counterparty so requests**. In this latest case information would be provided under the "Proportionate regime" (through tariff grids);

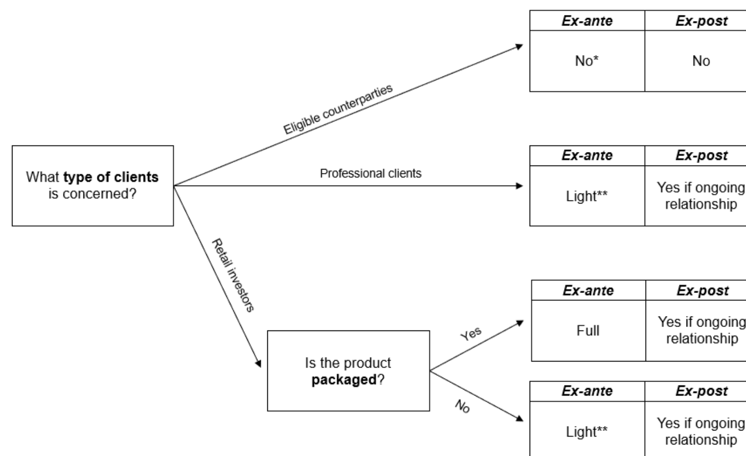
- <u>Professional clients</u>: **application of the "Proportionate" regime**; e.g. communication of costs and charges in *ex-ante* using tariff grids. **When requested** by the professional client, **more detailed** information will be communicated to this client.

- <u>Retail clients</u>: application of either the

    - "**Full regime**": when the product is a **packaged product** within the meaning of the PRIIPs Regulation, whatever the service provided;
    - "**Proportionate regime**": when the product is **<u>not</u> a packaged product** within the meaning of the PRIIPs Regulation, regardless of the service provided unless the client requested more detailed information.

<u>Ex-post information</u> would be provided to professional and retail clients who have been in an "ongoing relationship" with the investment firm over the past year.

This simplification proposal, which would make a distinction between 4 situations, is illustrated in the diagram below.



Clarify the scope the "ongoing relationship"

ESMA, in its Q&A 15.1 tries to **clarify the scope of the "ongoing relationship"**. For the AMAFI, the answer provided is not satisfactory for two reasons: first, it does not precisely use the investment services (or ancillary services) defined in MiFID 2 and, second, it seems to consider that execution services which are by nature one-off services, enter into the scope of the "ongoing relationship". **For that reasons, AMAFI proposes to precisely define the "ongoing relationship" into the Level 2 of MiFID II and to remove, or at least amend accordingly, ESMA's Q&A 15.1.**

Regarding the definition of the ongoing relationship, AMAFI considers that an investment firm has an "ongoing relationship" with a professional or retail client when it provides to this client the safekeeping service (Section B(1) of Annex I of MiFID II), the portfolio management service (Section A(4) of Annex I of MiFID II) or a service that involves providing a periodic assessment of the suitability within the meaning of Article 24(4) of MiFID II and Article 52 of the DR.

ANNEX: TEXT AMENDMENTS PROPOSAL

- **Level 1**

Article 30 of MiFID II

1. Member States shall ensure that investment firms authorised to execute orders on behalf of clients and/or to deal on own account and/or to receive and transmit orders, may bring about or enter into transactions with eligible counterparties without being obliged to comply with the obligations under Article 24, ~~with the exception of paragraphs 4 and 5~~, Article 25, with the exception of paragraph 6, Article 27 and Article 28(1) in respect of those transactions or in respect of any ancillary service directly relating to those transactions.

   Investment firms shall comply with the obligations under paragraphs 4 and 5 of Article 24 when the eligible counterparty so request.

   […]

- **Level 2**

Article 50 of MiFID 2 Delegated Regulation

1. For the purposes of providing information to **retail and professional** clients on all costs and charges pursuant to Article 24(4) of Directive 2014/65/EU, investment firms shall comply with the detailed requirements in paragraphs 2 to 10.

   ~~Without prejudice to the obligations set out in Article 24(4) of Directive 2014/65/EU, investment firms providing investment services to professional clients shall have the right to agree to a limited application of the detailed requirements set out in this Article with these clients. Investment firms shall not be allowed to agree such limitations when the services of investment advice or portfolio management are provided or when, irrespective of the investment service provided, the financial instruments concerned embed a derivative.~~

   ~~Without prejudice to the obligations set out in Article 24(4) of Directive 2014/65/EU, investment firms providing investment services to eligible counterparties shall have the right to agree to a limited application of the detailed requirements set out in this Article, except when, irrespective of the investment service provided, the financial instruments concerned embed a derivative and the eligible counterparty intends to offer them to its clients.~~

   When providing investment services to retail clients, investment firms shall comply with the requirements of paragraph 2, unless the financial instruments concerned are not packaged financial instruments. In the latter situation, investment firms shall comply with the requirements of paragraph 3 unless the retail client requests more detailed information.

   When providing investment services to professional clients, investment firms shall comply with the requirements of paragraph 3, unless the professional client requests more detailed information.

   Pursuant to Article 30.1 of Directive 2014/65/EU, when an eligible counterparty wishes to receive information on costs and charges, investment firms shall comply with the requirements of paragraph 3.

2. For ex-ante ~~and ex-post~~ disclosure of information on costs and charges to clients, investment firms shall aggregate the following:

   (a) all costs and associated charges charged by the investment firm or other parties where the client has been directed to such other parties, for the investment services(s) and/or ancillary services provided to the client; and

   (b) all costs and associated charges associated with the manufacturing and managing of the financial instruments.

   Costs referred to in points (a) and (b) are listed in Annex II to this Regulation. For the purposes of point (a), third party payments received by investment firms in connection with the investment service provided to a client shall be itemised separately and the aggregated costs and charges shall be totalled and expressed both as a cash amount and as a percentage.

   Where any part of the total costs and charges is to be paid in or represents an amount of foreign currency, investment firms shall provide an indication of the currency involved and the applicable currency conversion rates and costs. Investments firms shall also inform about the arrangements for payment or other performance.

3. **In conditions developed in paragraph 1, i**~~I~~nvestment firms ~~that do not recommend or market a financial instrument to the client or are not obliged to provide the client with a KID/KIID in accordance with relevant Union legislation~~ shall inform their clients about all costs and charges **only** relating to the investment and/or ancillary service provided.

   This information may be communicated to clients, at the time of entering into the relationship or concluding the first transaction, through tariff grids by asset classes, sufficiently granular according to the investment firm's activities.

   These tariff grids must be updated regularly and, at least, annually. The figures in this grid correspond to the best possible cost estimates and may, in some situations, correspond to the maximum costs and charges incurred by the investor, provided that they are as close as possible to the actual costs to be incurred by the investor.

4. In relation to the disclosure of product costs and charges that are not included in the UCITS KIID, the investment firms shall calculate and disclose these costs, for example, by liaising with UCITS management companies to obtain the relevant information.

~~5. The obligation to provide in good time a full ex-ante disclosure of information about the aggregated costs and charges related to the financial instrument and to the investment or ancillary service provided shall apply to investment firms in the following situations:~~

   ~~(a) where the investment firm recommends or markets financial instruments to clients; or~~

   ~~(b) where the investment firm providing any investment services is required to provide clients with a UCITS KIID or PRIIPs KID in relation to the relevant financial instruments, in accordance with relevant Union legislation.~~

6. Investment firms that do not recommend or market a financial instrument to the client or are not obliged to provide the client with a KID/KIID in accordance with relevant Union legislation shall inform their clients about all costs and charges relating to the investment and/or ancillary service provided.

7. Where more than one investment firm provides investment or ancillary services to the client, each investment firm shall provide information about the costs of the investment or ancillary services it provides. An investment firm that recommends or markets to its clients the services provided by another firm, shall aggregate the cost and charges of its services together with the cost and charges of the services provided by the other firm. An investment firm shall take into account the costs and charges associated to the provision of other investment or ancillary services by other firms where it has directed the client to these other firms.

8. Where calculating costs and charges on an ex-ante basis, investment firms shall use actually incurred costs as a proxy for the expected costs and charges. Where actual costs are not available, the investment firm shall make reasonable estimations of these costs. Investment firms shall review ex-ante assumptions based on the ex-post experience and shall make adjustment to these assumptions, where necessary.

9. Investment firms shall provide **to retail and professional clients** annual ex-post information about all costs and charges related to both the financial instrument(s) and investment and ancillary service(s) where ~~they have recommended or marketed the financial instrument(s) or where they have provided the client with the KID/KIID in relation to the financial instrument(s) and~~ they have or have had an ongoing relationship with the client during the year. Such information shall be based on costs incurred and shall be provided on a personalised basis.

   Investment firms may choose to provide such aggregated information on costs and charges of the investment services and the financial instruments together with any existing periodic reporting to clients.

   An investment firm shall be considered to be in an ongoing relationship with its client when it provides the client with the safekeeping service referred to in Section B(1) of Annex I of Directive 2014/65/EU, the portfolio management service referred to in Section A(4) of Annex I of Directive 2014/65/EU or a service that involves providing a periodic assessment of the suitability within the meaning of Article 24(4) of Directive 2014/65/EU and Article 52 of this Regulation.

~~10. Investment firms shall provide their clients with an illustration showing the cumulative effect of costs on return when providing investment services. Such an illustration shall be provided both on an ex-ante and ex-post basis. Investment firms shall ensure that the illustration meets the following requirements:~~
~~(a) the illustration shows the effect of the overall costs and charges on the return of the investment;~~
~~(b) the illustration shows any anticipated spikes or fluctuations in the costs; and~~
~~(c) the illustration is accompanied by a description of the illustration.~~

11. By way of derogation from paragraph 2, and subject to Articles 3(1), 3(3)(a) and 6 of Directive 2002/65/EC, an investment firm may provide information on costs and charges to the retail investor after the provision of the service, without undue delay, where all the following conditions are met:

(a) the retail investor chooses, on his own initiative, to contact the investment firm and conclude the transaction using a means of distance communication;

(b) the investment firm has informed the retail investor that it is not possible to provide ex-ante information on costs and charges and has clearly stated that the retail investor may delay the provision of the service in order to receive and read this information before providing the service;

(c) the retail investor consents to receiving ex-ante information on costs and charges without undue delay after the provision of the service rather than delaying the provision of the service to receive such information in advance.

- **Level 3**

ESMA's Q&As on costs and charges

Q&A	Amendments to be achieved ?	Comments
1	NA	
2	To be deleted	Suppression of the requirement to communicate an illustration of the cumulative effect of costs on performance.
3	To be deleted	Suppression of the requirement to communicate an illustration of the cumulative effect of costs on performance.
4	To be kept	
5	To be kept	
6	To be deleted	No more PRIIPs costs methodology in MiFID II for products that do not fall within the PRIIPs field.
7	To be deleted	No more PRIIPs costs methodology in MiFID II for products that do not fall within the PRIIPs field.
8	To be deleted	No more PRIIPs costs methodology in MiFID II for products that do not fall within the PRIIPs field.
9	To be deleted	No more PRIIPs costs methodology in MiFID II for products that do not fall within the PRIIPs field.
10	NA	
11	To be amended	Keeping of the answer except for the part importing the PRIIPs costs methodology in MiFID II for products that do not fall within the PRIIPs field.
12	To be deleted	No more PRIIPs costs methodology in MiFID II for products that do not fall within the PRIIPs field.
13	To be amended	The scope of this question should be restricted to situations for which trade-by-trade information should be communicated to the client
14	To be kept	
15	To be deleted	No more PRIIPs costs methodology in MiFID II for products that do not fall within the PRIIPs field.
16	To be kept	
17	To be deleted	No more PRIIPs costs methodology in MiFID II for products that do not fall within the PRIIPs field.
18	To be deleted	This question-answer will no longer be relevant if the two new regimes proposed by AMAFI are retained
19	To be deleted	This question-answer will no longer be relevant if the two regimes proposed by AMAFI are retained

20	A modifier	The scope of this question should be restricted to situations for which trade-by-trade information should be communicated to the client
21	To be kept	
22	To be deleted	This question-answer will no longer be relevant if the two regimes proposed by AMAFI are retained
23	To be deleted	This question-answer will no longer be relevant if the two regimes proposed by AMAFI are retained
24	To be kept	
25	To be kept	
26	To be kept	
27	A conserver	
28	To be deleted	This question-answer will no longer be relevant if AMAFI's proposal on orders placed by telephone is retained
29	NA	
30	To be deleted	This question-answer will no longer be relevant if the two regimes proposed by AMAFI are retained

ESMA'Q&A Other issues

1	To be deleted	The term "ongoing relationship" would be clarified by an exact reference to the relevant investment services so this question-answer would be no longer relevant