esma European Securities and Markets Authority

Date: 06 May 2020
ESMA35-43-2391

PUBLIC STATEMENT

COVID-19: Reminder of firms' MiFID II conduct of business obligations in the context of increasing retail investor activity

1. The spread of COVID-19 across the world and the measures taken by countries to prevent its spread have been a major shock to the global economy and financial markets. Heightened uncertainty has led to high market volatility and an increase in market, credit and liquidity risks.

2. Amidst these exceptional financial market circumstances, several National Competent Authorities (NCAs) have noticed a significant increase in the number of investment accounts opened by retail clients and a surge in trading by retail clients.

3. The European Securities and Markets Authority (ESMA) highlights the risks for retail clients when trading under these highly uncertain and unprecedented market circumstances. ESMA is therefore issuing this Statement to draw firms' and clients' attention on these risks and to remind investment firms[1] of their conduct of business obligations under MiFID II.[2] ESMA believes that firms have even greater duties when providing investment or ancillary services to investors, especially when they are new or have limited investment knowledge or experience, who decide to invest during these times of intensified market volatility.

4. In this context, ESMA reminds firms of their obligation to act honestly, fairly and professionally in accordance with the best interests of their clients when providing investment or ancillary services and to comply with all relevant MiFID II conduct of business and related organisational requirements.[3] In particular, ESMA points to the product governance, information disclosure, suitability and appropriateness requirements.

5. Firms must have adequate product governance arrangements in place to ensure that financial instruments will only be offered when in the interest of the client or potential client.[4] Amongst others, firms must determine the target market and associated distribution strategy for the financial instruments that they manufacture or intend to offer.

[1] The term investment firm also refers to credit institutions when providing investment services and activities and UCITS and AIF management companies when providing investment services.
[2] Directive 2014/65/EU of the European Parliament and of the Council.
[3] See Article 24(1) of MiFID II.
[4] See Articles 16(3) and 24(2) of MiFID II, Articles 9 and 10 of Commission Delegated Directive (EU) 2017/593 (MiFID II Delegated Directive) and the ESMA Guidelines on MiFID II product governance requirements (Ref: ESMA35-43-620).

6. This target market assessment should be done in an appropriate and proportionate manner, taking into account the nature of the financial instrument and the investment service provided. ESMA stresses that, especially for more complicated financial instruments, the target market should be identified with more detail. In determining the distribution strategy for such instruments, firms should be mindful of the more limited level of investor protection afforded by the appropriateness test than by the suitability test required when providing investment advice and portfolio management to clients.

7. Firms shall provide appropriate information in good time to clients or potential clients with regard, inter alia, to the investment firm and its services and the financial instruments offered. All information provided to clients shall be fair, clear and not misleading.[5]

8. Amongst others, firms must provide information on the financial instruments in which their clients or potential clients can invest. This information must include an appropriate description of the nature and risks of financial instruments to enable the client to take investment decisions on an informed basis. The description shall also explain whether the financial instrument is intended for retail or professional clients, taking account of the identified target market.

9. Finally, ESMA reminds firms of the suitability and appropriateness requirements.[6] When providing investment advice or portfolio management, firms shall obtain the necessary information regarding the client's or potential client's knowledge and experience, his financial situation including his ability to bear losses, and his investment objectives including his risk tolerance to assess whether the financial instrument or service is suitable for the client. ESMA emphasises that firms should pay particular attention to the possible ramifications of the COVID-19 crisis for the client's personal situation and the risk profile of his financial instruments to ensure that these financial instruments are suitable for him.

10. When providing services other than investment advice or portfolio management, firms must obtain information regarding the client's or potential client's knowledge and experience to assess whether the financial instrument or service is appropriate for the client. ESMA stresses that this appropriateness assessment is particularly important for new clients wishing to invest in complex financial instruments during these times of intensified market volatility. Firms should also be sure they correctly categorise financial instruments for the purpose of the appropriateness assessment.

11. Under certain conditions, when providing the investment services of execution or reception and transmission of client orders with respect to the financial instruments specified in Article 25(4)(a) MiFID II ('non-complex financial instruments'), firms are allowed to provide those investment services without the need to undertake an

[5] See Article 24(3) and (4) of MiFID II.
[6] For the suitability assessment, see Article 25(2) of MiFID II and Article 54 of Commission Delegated Regulation (EU) 2017/565 (MiFID II Delegated Regulation), and the ESMA Guidelines on certain aspects of the MiFID II suitability requirements (Ref: ESMA35-43-869). For the appropriateness assessment, see Article 25(3) of MiFID II and Articles 55 and 56 of the MiFID II Delegated Regulation.

appropriateness assessment.[7] ESMA stresses that firms, when providing investment services that fall under this execution-only exemption, still need to comply with the other requirements outlined in this Statement, especially those relating to product governance and information to clients.

12. NCAs, which are in charge of supervision of firms, and ESMA, will continue to monitor retail clients' involvement in the financial markets and firms' compliance with their conduct of business obligations and related organisational requirements under MiFID II.

[7] See Art. 25(4) of MiFID II and Article 57 of MiFID II Delegated Regulation detailing all other conditions for the provision of "execution-only" services.