21st May 2025

Dear Chief Executive Officer,

Dear Compliance Officer,

MFSA Expectations in the Context of MiFID II Sustainability Requirements

You are receiving this letter as the Chief Executive Officer and Compliance Officer of an investment firm supervised by the Malta Financial Services Authority (referred to herein as the 'MFSA' or the 'Authority').

INTRODUCTION

The MFSA endeavours to stimulate compliance with applicable rules governing investment services licensed entities (also hereinafter referred to as "licensed entities", or "investment firm/s") for a fair, honest, and transparent financial market, which in turn strengthens confidence within same market, with the aim of protecting investors. To this end, the Authority's supervisory activities are aimed at attaining high compliance standards within the supervised licensed entities using diversified tools encompassing mystery shopping exercises, thematic reviews, off-site work, supervisory meetings, and on-site inspections.

A thematic review undertakes an in-depth analysis of the risks and issues identified which tend to have wider implications on the financial services market. By investigating specific key issues in detail, a thematic review provides meaningful comparisons which can be drawn and analysed. The scope of this letter is to provide further guidance to licensed entities on how certain issues should be tackled adequately in line with the applicable rules, regulation and guidelines. This letter provides an insight on a thematic review undertaken in 2023 specifically on the element of the consumers' sustainable preferences are integrated into the advisory processes of investment firms as required under MIFID II. Furthermore, this letter contains identified observations, highlighting good and bad practices noted as well as laying out the Authority's expectations in this area.

The concept of sustainability has recently gained significant importance especially due to the introduction of rules, regulations and guidelines within the context of the European Union (EU) Sustainable Finance Action Plan (SFAP). Overall, the scope of SFAP is to ensure that finance is being redirected towards meeting the ambitious goals outlined in the Paris Agreement, which was signed in 2016 with the scope to limit the global warming and shifting towards sustainable economic activities.

Within this context, the following set of sustainability-related EU legislation and guidelines were introduced (or amended to cater for the introduction of the sustainability element) which are applicable to investment firms:

i. The Sustainable Finance Disclosure Regulation (EU) 2019/2088 (SFDR) and the Commission Delegated Regulation (EU) 2022/1288 (SFDR Delegated Regulation).
ii. MiFID amending Delegated Acts related to the Commission Delegated Directive (EU) 2021/1269 and the Commission Delegated Regulation (EU) 2021/1253.
iii. ESMA Guidelines on certain aspects of the MiFID II suitability requirements (2023) and ESMA Guidelines on MiFID II product governance requirements (2023) (hereinafter called the "ESMA Guidelines or ESMA Guidelines 2023").

In view of the results of this thematic review, the MFSA expects that all investment firms undertake an in-depth and thorough assessment of the outcomes included herein. It is imperative that all investment firms should take the necessary actions to ensure that the element of sustainability within the suitability assessment and the respective policies and procedures are in line with the applicable rules, regulations and guidelines, related to sustainable finance. Overall, the Authority strongly believes that all investment firms should ensure that adequate training is provided to all client facing staff, the compliance officer and senior management to keep abreast of any updates in relation to sustainable finance.

BACKGROUND AND METHODOLOGY

During the year 2023, the Authority's high–level supervisory priorities continued to focus heavily on Sustainable Finance.[1] The main scope of this priority is to increase awareness on sustainable finance amongst licensed entities by ensuring compliance with the relative legislative requirements but also to drive ambitious policies for the benefit of all stakeholders and society at large. Overall, the Authority aims to ensure that the consistent implementation and application of the EU sustainability – related requirements, assist to enhance transparency of the market, tackle the issue of greenwashing in an effective and efficient manner, leading to sustainable economies. Besides, the Authority strongly believes that having a consistent and coherent cross-sectoral supervisory approach is deemed to be beneficial for this structural shift in the financial landscape. Furthermore, by exploring also their clients' sustainability preferences during the suitability assessment, investment firms will ensure that they offer the products which best meet their client's financial and sustainability-related objectives.

On the 23 September 2022, ESMA has published its Final Report on Guidelines on Certain Aspects of the MiFID Suitability Requirements (2022) which also included guidelines on how investment advisors were expected to assess the sustainability preferences of their clients.

[1] MFSA Supervision Priorities 2023

These Guidelines have been transposed also in the Conduct of Business Rulebook respectively as per the MFSA's Circular dated 19th October 2023 outlining the main revisions to the Conduct of Business Rulebook. The Circular outlines the requirements applicable to the investment services sector. In fact, various provisions in the main body of Chapter 2 and Chapter 4 of the Conduct of Business Rulebook have been amended and/or shifted to three new appendices which primarily implement both the Guidelines on certain aspects of the MiFID II suitability requirements and Guidelines on MiFID II product governance requirements. The key amendments have been made in relation to Rule R.2.19 of the Conduct of Business Rulebook, which mainly led to the implementation of the ESMA Guidelines on MiFID II product governance requirements, which now form part of Appendix 1 of Chapter 2 of the Conduct of Business Rulebook. On the other hand, key amendments have been made to Rule R.4.4.16 of the Conduct of Business Rulebook, which mainly led to the implementation of the ESMA Guidelines on certain aspects of the MiFID II suitability requirements, which now form part of Appendix 7 of Chapter 4 of the Conduct of Business Rulebook.

Further to the publication of the abovementioned ESMA Guidelines, the MFSA has carried out a Thematic Review with the purposes of assessing how investment firms have updated their policies and procedures to come in line with the requirements of these Guidelines and the respective MIFID II requirements. Therefore, by means of an official letter dated 5th October 2022, the Authority requested investment firms to submit of the following documentation, for its assessment, by 30th March 2023:

i. An explanation of the changes which were implemented in the Company's suitability policies and procedures (including the Client Fact Find template);
ii. The relevant section of the firm's policies and procedures relating to the suitability assessment, with specific reference to the sustainability preferences in the context of advisory processes, as well an explanation of the changes which were implemented to the Client Fact Find; and
iii. A copy of the template questionnaire constituting the Client Fact Find detailing the collection of information on the client's suitability preferences in so far as sustainability factors are concerned. Any updates to such documentation relating to the identification of the client's sustainable preferences were required to be clearly indicated.

Furthermore, the official letter reminded all investment firms to:

i. Incorporate the collection and analysis of the necessary information about the client's or potential client's sustainability preferences within their sustainability policies and procedures, as part of the client's suitability assessment.
ii. Update and/or review the process relating to the ESG data sourcing, including those related to obtaining reliable ESG information from products manufacturers.
iii. To provide appropriate training to relevant staff, including with respect to assessing client's sustainability preferences.

As part of its supervisory workstream, during the months of July and August 2023, the Authority, via its Conduct Supervision Function, carried out a detailed desktop review of all the documentation submitted by the licensed investment firms which offered investment advice and/or discretionary portfolio management services - in total fifty – one (51) investment firms. The scope of this supervisory workstream was to assess the extent to which the submitted responses and the documentation are in line with the applicable EU regulation and guidelines, particularly the amendments to MiFID II Regulation relating to suitability assessment (incorporating sustainable element).

Following the finalisation of this desktop review, the Authority subsequently conducted a total of ten (10) supervisory meetings in 2023, which represent around 20% of the investment firms providing investment advice and/or discretionary portfolio management services at the time of the thematic review. The sample of the investment firms selected for a supervisory interaction meeting was based on several criteria including the level of adherence of the submitted documentation to the requirements emanating from the salient aspects outlined in the Authority's letter dated 5th October 2022. Nevertheless, the Authority ensured that in selecting the sample of firms for supervisory meetings, it also considered the investment firm's size, complexity of business model, range and type of products being offered, and the respective services being provided. The Authority informed the selected licensed entities of the upcoming supervisory meetings by means of an official letter. Supervisory meetings were held during the months of September, October, and November 2023, whereby the Authority outlined the main findings and shortcomings of the submitted documentation and additional guidance was provided during same meetings, to rectify such deficiencies.

For this reason, the Authority is issuing this *"Dear CEO letter"* to outline the common shortcomings identified during this supervisory workstream.

The findings emanating from the desktop review are structured as follows:

A) Information to clients about the purpose of the suitability assessment, including the sustainability preferences.
B) Collection of information from clients on sustainability preferences:
   B.I. Policies and Procedures;
   B.II. Arrangements necessary to understand Investment Products;
   B.III. Organisational Requirements; and
   B. IV. Client Fact Find.
C) Other Findings.

Throughout this letter, the Authority will be outlining the regulatory requirements and guidelines and will provide further guidance on how investment firms will be expected to comply to the applicable rules and regulations. In terms of guidance, the Authority shall refer to the ESMA Guidelines on certain aspects of the MiFID II suitability requirements issued in 2023 and such indication will be included in the respective section accordingly.

The Authority would like to remind all investment firms to undertake a deep thorough assessment of the outcomes included herein and encourages all investment firms to keep abreast with the regulatory developments, by also referring to the various circulars issued by the Conduct Supervision Function on Sustainable Finance, from time to time.[2]

KEY FINDINGS

A. *Information to clients about the purpose of the suitability assessment, including the sustainability preferences*

Investment firms providing investment advice or portfolio management services are amongst others, obliged to assist their clients to understand the concept of sustainability, the environmental, social and governance (ESG) aspect, the sustainability preferences and the choices to be made in this context. Furthermore, investment firms are expected to define and explain these in a clear way without making use of any technical language to ensure that clients can better understand such concepts.

[i] Definitions/ Terminologies related to Sustainable Finance

Regulatory Requirement and Guidelines

Article 2(7) of the MiFID Delegated Regulation 2017/565 defines the concept of *"sustainability preferences"*. According to this Article, investment firms are obliged to explain the terms and distinctions between the different elements of sustainability to their clients for these to be able to make informed investment decisions in terms of sustainability. Although, there is no definition of the term 'explanation' and whether such can be provided orally or in written format, it is the Authority's expectation that. as a measure of good practice, investment firms are to ensure that they explain, in both verbal and written format, in a clear manner and without the use of technical jargon the nature and characteristics of the following types of financial instruments, when providing investment advice:

i) Financial instruments that pursue (in full or in part):
   a. sustainable investments in economic activities that qualify as environmentally sustainable under the Taxonomy Regulation (Regulation EU 2020/852);
   b. sustainable investments as defined in Article 2, point (17) of the SFDR (Regulation (EU) 2019/2088;
   c. Financial Instruments that consider Principal Adverse Impact (PAI) that might be eligible for recommendation as meeting individual sustainability preferences of Client.

ii) Other Financial Instruments without specific features referred to in (i) above that should not be eligible for recommendation to Clients that have individual sustainability preferences.

[2] Circulars on Sustainable Finance

Investment firms are also expected to explain what the environmental, social and governance (ESF) framework is. The Environmental aspect considers the factors related to climate change mitigation and adaptation. However, other environmental aspects also take into consideration such as: biodiversity, pollution prevention mechanisms and circular economy. On the other hand, the social aspect considers the matters related to inequality, labour relations, human rights issues, inclusiveness and social matters which impact society at large. Whilst the governance aspect considers management structures and employee relationship which would reinforce both the environmental and social aspects of the organisation which issues or manufactures the financial instrument in question.

Also, Rule R.4.1.14 of the Conduct of Business Rulebook requires that a Regulated Person shall explain to the Client words and expressions of a technical nature which are used in a document in either the Maltese or the English language depending on which language the client understands better.

Findings

Following a review of the client fact finds, policies, and procedures provided (hereinafter referred collectively as the "submitted documentation"), the Authority noted various discrepancies in the definition of the term *"sustainability preferences"*, *"the types of preferences"* and "*the ESG framework"*. The Authority noted that most of the investment firms did not granularly define the ESG framework and respective terminologies in the documentation submitted.

In another instance, the Authority noted that the investment firms have referred solely to applicable European Union (hereinafter referred to as 'EU') Regulation definitions. Whilst such definitions emanate from the regulations and are correct, the Authority expects that investment firms explain such definitions/terminologies in layman's terms, for retail investors to better understand these concepts, in line with R.4.1.14 of the Conduct of Business Rulebook. As a measure of best practice, it is investment firms should be able to provide various examples to support such definitions/terminologies, especially with respect to the "ESG framework".

To further explain the above affirmations, reference is being made to the lack of inclusion of definitions/terminologies in the documentation used to collect client information (client fact find) and policies and procedures of certain investment firms. The Authority noted that in certain instances such terminology and definitions related to Article 2(7) of the MiFID Delegated Regulation would be either included in the client fact find but omitted in the policies and procedures, or vice versa. It is deemed to be a good practice that such definitions/terminologies reflected in all the relevant documentation used by the investment firm (the client fact find and the relevant policies and procedures of the company). The Authority noted that only few investment firms have outlined, in the submitted documentation, the main difference between instruments having sustainability features as per the with the definitions and explanations provided in their documentation relating to sustainable preferences (e.g. definition of terms such as "Taxonomy Aligned", "SFDR Aligned", "PAI Integration") vis-à-vis instruments without such features.

Identified Good Practices

Some investment firms have either added explanatory information to explain the definitions/terminologies relating to sustainable finance within the existing client fact find document itself, whilst other companies have included a separate explanatory note on sustainable finance in both Maltese and English annexed to the client fact find document. The Authority noted that several companies have also established a separate policy on ESG in context of the investment advisory process.

One investment firm drafted a question-and-answer (Q&A) paper which includes various questions relating to the sustainable finance definitions/terminologies. Such approach is deemed to be a good practice, since such an approach will allow the firm to explain these complex concepts in a simpler manner.

An investment firm highlighted within its policy that the explanation of sustainability preference is critical to enable the client to understand the different degrees of sustainability. This investment firm outlined in its policy, that such explanation should provide accurate and sufficient information to enable the clients to make informed decisions and advocate effectively in relation to their own sustainability preferences and wider sustainability motivations. The firm's guidance document also outlined that investment advisors should take steps to avoid introducing any unconscious bias in the way that the explanation of sustainability preference is articulated. Examples of articulated biases were also provided whereby such bias was indicated as being possibly driven by various factors including the existence of an inducement to recommend certain financial instruments or for instance the advisor's level of knowledge and own preconceptions about the different instrument. Furthermore, this investment firm further outlined that the advisor's level of knowledge on the subject matter is extremely important. Other unconscious bias considered relate to the cost, financial return and level of risk of the financial instrument having sustainable features.

This same investment firm has also considered that the explanation of sustainability preferences would need to accommodate differing levels of financial literacy and knowledge of sustainability issues by the client. Since many of the definitions/terminologies are unlikely to be familiar to the average client, the policy of this firm requires investment advisors to enquire on the client's level of financial literacy and knowledge of sustainability issues to ensure that the explanation of sustainability preferences is effective. An annex was also prepared by the company for its investment advisors to ensure that the key considerations and content would guide them to explain the key considerations accordingly. The annex also includes reference to the fact that the client has an opportunity to ask further questions for clarification and the advisor is obliged to assist with the client's own understanding of the explanation of sustainability preferences. The Authority notes and considers that this type of guidance for investment advisors is crucial to explain the concept of sustainability and the related definitions/ terminologies adequately whilst considering the level of knowledge of the client respectively. The Authority therefore encourages investment firms to adopt such a practice and incorporate this within their policies accordingly.

Identified Bad Practice

A particular investment firm included a glossary on its website to explain the respective sustainable finance definitions. Nevertheless, the list related to sustainable finance was included with the list of financial definitions in alphabetical order. The Authority is of the view, that a consumer who is not familiar with the terminology related to sustainable finance would not find this glossary very user friendly.

The Authority noted that while in client fact finds and policies and procedures of certain investment firms the definitions relating to Taxonomy Aligned, SFDR Aligned and PAI considerations were explained in detail, in others these were either not so clearly defined or not mentioned at all.

MFSA Expectations

Client facing personnels are expected to have a clear understanding of the terminology used in the context of sustainability preferences and sustainable finance in general such that they are able to clearly explain these to their clients.

All investment firms are expected to include specific of definitions/terminologies in the policies, procedures and the client fact find. In this way, client facing individuals would have clear direction on how to present the information to clients and the client eventually would benefit from the information being provided. Therefore, such terms should also be defined in the investment firm's respective policies, procedures and as well as in client fact find. Defintions of certain terminology related to sustainable finance which are found on the investment firms' websites should ideally feature under a separate section on sustainable finance to ensure easy access.

If these concepts are not clearly explained to clients, it would possibly lead to a situation whereby the retail client would avoid selecting any products having sustainability characteristics, just because they do not understand such products. The Authority considers this situation as highly undesirable since it would detract from the common objective of promoting sustainable finance in general.

The Authority therefore expects that investment firms' client fact find and the policies and procedures include definitions, in a simple and non-technical language, on sustainability preferences, the ESG concept, as well as a clear explanation on instruments having sustainable features vis-à-vis instruments not having sustainable features.

It is imperative that all investment firms provide ongoing training related to sustainable finance and ensure that any regulatory developments are circulated to the relevant staff accordingly.

Also, any information included in the investment firm's website must be easily accessible and drafted in terms which are easy to understand by the reader.

Overall, the Authority expects all investment firms to keep in mind the challenges faced by the retail clients in terms of the terminology used in the context of sustainable finance when designing/amending and providing the necessary information about the financial products having sustainability features to client. Any supporting documentation such as a Question-and-Answer (Q&A) document or explanatory notes are all viewed positively by the Authority since these serve as an aid to clients or potential clients in understanding concepts linked to sustainability.

B. Collection of information from clients on sustainability preferences

In view of the amendments of the Commission Delegated Regulation (EU) 2021/1253, investment firms are required to update their client fact find and collect information from their clients on their sustainability preferences. Such information would ensure that the investment advisor can adequately assess, amongst others, their client's sustainability preferences to offer products that match the respective client's sustainability preferences. Throughout this process, firms need to adopt a neutral and unbiased approach which would not influence client's investment decisions. As part of this supervisory exercise, the Authority assessed how the respective client fact find document was updated, specifically the section related to sustainable preferences.

Regulatory Requirement and Guidelines

The Commission Delegated Regulation (EU) 2021/1253 modifies the Commission Delegated Regulation (EU) 2017/565 and aims to integrate sustainability factors in the suitability assessment carried out by investment firms providing investment advice and/or portfolio management. It aims to clarify, amongst other matters, that investment firms providing such services shall carry out a mandatory assessment of the sustainability preferences of their clients. The said amendments also require investment firms to appropriately take their clients' sustainability preferences into account when recommending products. Such requirements became applicable as from 2nd August 2022.

The sustainability-related amendments to the said MiFID II Delegated Regulation were also supplemented by the ESMA Guidelines on certain aspects of the MiFID II suitability requirements (2023) which reflect, inter alia, the integration of sustainability preferences in the suitability assessment under MiFID. The said ESMA Guidelines have been included in the Conduct of Business Rulebook and became applicable as from 3rd October 2023.

Paragraph 81 of Section I.III entitled 'Matching Clients with Suitable Products' of the ESMA Guidelines on certain aspects of the MiFID II suitability requirements (2023) requires that sustainability preferences should only be addressed by the investment advisor once the suitability in terms of the criteria of knowledge and experience, financial situation and other investment objectives has been assessed. Once the range of suitable products has been identified following this assessment, in a second step a product or, in cases where portfolio management or investment advice with a portfolio approach is being provided, an investment strategy that fulfils the client's sustainability preferences should be identified.

B. I Policies and Procedures

[i] Particular Situations related to the Clients' Sustainability Preferences

Regulation & Guidelines

Article 54(9) of MiFID II Delegated Regulation highlights that investment firms shall have to demonstrate that they have in place adequate policies and procedures to ensure that they understand the nature, features, including costs and risks of investment services and financial instruments selected for their clients and that they assess, while considering cost and complexity, whether equivalent investment services or financial instruments can meet their client's profile.

Section V.I – *Know Your Client and Know Your Product*, paragraph 28 of the ESMA Guidelines on certain aspects of the MiFID II suitability requirements highlights that investment firms should have policies and instructions in place for their client–facing staff to address situations where clients answer that they do have sustainability preferences but do not state a preference with regard to any of the specific aspects mentioned under points (a) to (c) of Article 2(7) of the MiFID Delegated Regulation or with regard to a minimum proportion of sustainable investments in their portfolio.

Findings

The Authority is concerned to note that most of the investment firms did not include a dedicated section in their policies and procedures to address the situation when their clients have sustainable preference but do not state a particular preference for financial instruments outlined under Article 2(7) of the MIFID II Delegated Regulation.

MFSA Expectations

Investment firms are expected to update their policies and procedures and ensure that a dedicated section is included to outline how clients having non sustainable preferences will be treated. Moreover, it is expected that investment firms provide further information about this situation either in the client fact find, or any question and answer issued or any other informative document which is provided to their clients as deemed necessary.

[ii] Subsequent Updates to the Clients' Sustainability Preferences

Regulatory Requirements

As from 2nd August 2022, investment firms have been obliged to ensure that their clients update their sustainability preferences. Paragraph 57 of the ESMA Guidelines 2023 highlights that regarding the sustainability preferences of a client, this information should be updated, especially for ongoing relationships, at the latest through the next regular update of client information following the entry into application of the Commission Delegated Regulation

2021/1253. Therefore, clients should be provided the opportunity to have their investment profile updated immediately if they wish so. However, where the client does not request the immediate update of their profile, and during the period preceding the acquisition by the firm of the information on the client's sustainability preferences, the client will be considered as "sustainability-neutral" and therefore, in line with paragraph 85 of the ESMA Guidelines 2023, the client could be recommended products both with and without sustainability-related features.

Findings

Whilst most of the investment firms have included a dedicated section in the respective policies and procedures outlining how subsequent updates to the sustainability preferences will occur, some of the firms did not address this matter within their policies and procedures The Authority would like to remind all investment firms to ensure that all clients have their sustainability preferences updated and recorded accordingly.

MFSA Expectations

The Authority understands that obtaining such information from clients is quite a laborious task, however, the Authority encourages all investment firms to ensure that they have the necessary policies and procedures in place to obtain the necessary information such that all clients have their profiles updated with their sustainability preferences, at the earliest opportunity. Such approach would ensure that all investment firms are in line with the regulatory requirements.

[iii] Where Clients' Sustainability Preferences do not match Financial Instruments Available Through An Investment Firm

Recital 8 of Commission Delegated Regulation (EU) 2021/1253, clarifies 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. In order to allow for further recommendations to clients or potential clients, where financial instruments do not meet a client's sustainability preferences, the client should have the possibility to adapt information on his or her sustainability preferences. Furthermore, in order to prevent mis selling and greenwashing, investment firms are to keep records of the client's decision along with the client's explanation supporting the adaptation.

Guidelines

Section I.III, – *Matching clients with suitable products*, Paragraph 83 of the ESMA Guidelines on certain aspects of the MiFID II suitability requirements outlines that where a client adapts his original sustainability preferences, this adaption should only refer to the investment advice in question and not to the client's profile in general. In case of an investment advice, the adaptation should also be documented in the suitability report and to be subject to the regular monitoring procedure. Once, clients express the intention to adapt their preferences, and not before, the investment firm could disclose to the client, the necessary information on the financial products with sustainability features.

Paragraph 84 of the aforementioned ESMA Guidelines 2023 outlines that in the case of portfolio management, the client's sustainability preferences, including the minimum proportion that shall be invested in investments with sustainability features needs to be collected and assessed when agreeing on the mandate and the investment strategy. However, if the firm cannot meet those preferences, it should discuss this with the client, when agreeing on the mandate in which the investment strategy is defined and ask the client if he/she would like to adapt his/her preferences. Eventually, such decision should be recorded in the respective mandate.

Findings

From the assessment carried out, the Authority concluded that most of the investment firms did not consider the above requirements in their policies and procedures.

Identified Good Practice

As part of its procedures, an investment firm has introduced a sustainability assessment adaptation form to reflect the client's adaptations respectively. This comprehensive form included exhaustive lists related to the following areas:

i. The main reasons for request by the investment firm to the client to adapt his/her sustainability preferences.
ii. The changes in client's sustainability preferences and outlines the main elements being updated.

A dedicated section related to the consequences of a failure to adapt the sustainability preferences by a client was included in the form which also contained the necessary disclaimers concerning the inability of the firm to provide financial products having sustainability features matching the client's latest sustainability preferences, in such cases.

MFSA Expectations

The Authority expects that all investment firms ensure that their respective policies and procedures have detailed sections relating to updates of their clients' sustainability preferences and their adaptation thereof, in a comprehensive manner. The concept of adaptation must be clearly defined within the policies of the Company and clear guidance must be provided to all client facing personnel in order to have a clear picture of the process to be followed when clients need to adapt their sustainability preferences. The policies and procedures must include the process to be followed, the persons that are involved in the adaptation process, the documentation to be completed as well as the proper notification to the client concerned.

[iv] Product Oversight Governance Policies identifying a Range of Suitable Products in line with the identified Client's Sustainable Preferences

Regulatory Requirements and Guidelines

Section I.II – *Arrangements necessary to understand investment products*, Paragraph 72 of the ESMA Guidelines on certain aspects of the MiFID II suitability requirements highlights that firms should adopt robust and objective procedures, methodologies and tools that allow them to appropriately consider the different characteristics, including sustainability factors, and relevant risk factors (such as credit risk, market risk, liquidity risk) of each investment product they may recommend or invest in on behalf of clients. This should include taking into consideration the firm's analysis conducted for the purpose of product governance obligations.

Rule R.4.4.26 of the Conduct of Business Rulebook requires Regulated Persons to determine the extent of information to be collected in view of the services being offered such as for instance: investment advice and portfolio management. Such information is necessary for the investment firm to understand the essential facts about the client and to have a reasonable basis for determining and considering the nature and extent of the service provided satisfies the following criteria:

i) It meets the investment objectives of the client in question, including the client's risk tolerance and any sustainability preferences;
ii) It is such that the client is able financially to bear any related investment risks consistent with his investment objectives;
iii) Is such that the client has the necessary experience and knowledge in order to understand the risks involved in the transaction or in the management of his portfolio.

Paragraph 81 of the abovementioned ESMA Guidelines which highlights that sustainability preferences should be only addressed once all the other elements (criteria of knowledge and experience, financial situation and other investment objectives) have been addressed in the client fact find. This is further transposed in Guideline G.4.4.19 of the Conduct of Business Rulebook recommends that investment firms should account for the sustainability preferences and the type of products and services available.

Regulated Persons should be able to recommend suitable financial instruments to their clients and should therefore be able to ask questions to identify a client's individual sustainability preferences.

In addition, Regulated Persons shall ensure, in line with the obligation to provide products and services which are in the best interest of clients, that recommendations to the client reflect both the financial objectives and any sustainability preferences expressed by that client.

Therefore, Regulated Persons are required to ensure that the inclusion of sustainability factors in the advisory process must not lead to mis-selling practices or to the misrepresentation of financial instruments or strategies as fulfilling sustainability preferences where in fact they do not. To avoid such practices or misrepresentations, the Regulated Person shall first assess the client's other investment objectives, time horizon and individual circumstances, before asking for his or her potential sustainability preferences.

Findings

In view of the regulatory requirements, the Authority is concerned to note that only few investment firms have updated their policies and procedures outlining how they intend to identify a range of suitable products in line with the identified client's sustainable preferences.

It has been explained to the Authority by several investment firms that they did not identify such a range of suitable products, because the ESG framework is not part of their investment strategy or else because the services being provided focussed more on other areas rather than investment advice. However, such investment firms are obliged to adhere to the requirements emanating from the MiFID II Delegated Regulation. Therefore, all investment firms are required to include a dedicated section in their respective policies and procedures to outline how they intend to identify products which could meet their client's sustainability preferences.

Identified Good Practice

One investment firm has in place a sustainability risk policy outlining the philosophy and the comprehensive approach undertaken to ensure that ESG considerations are embedded throughout the investment process and strategies being employed. In fact, the investment firm referred to the principles related to sustainable finance, especially the United Nations' seventeen (17) Sustainable Development Goals and the ten (10) principles of the United Nations Global Compact. The policy also outlines the entity's commitment to responsible investing when it comes to investment decisions. The ESG factors were split in different thematic areas for the firm to assess the material impact on the value of the companies and securities. For instance: the Environment factor included different thematic areas related to climate change, natural resources, environmental opportunities, pollution and waste. These thematic areas would then have other factors being considered. The policy also focuses on the strategy being considered and the respective sustainability indicators used to measure the attainment of these characteristics. The investment firm also considers the ESG performance of the underlying investments, apart from considering the financial performance accordingly.

On the other hand, another investment firm considered different sustainability related elements vis-à-vis the type of financial instruments being considered. For instance, the following factors were being considered: the non-financial disclosures, the KPIs aligned with environmentally sustainable activities for environmentally sustainable investments; the sector/country exclusions, controversies in relation to violations when it comes to PAI considerations). If the client selects multiple sustainable investments (unless a clear preference is chosen), the investment firm interprets the remaining options as alternatives and may recommend the investments that fall within the respective category, whilst acting in the best interest of the client.

An interesting, good practice noted by the Authority relates to the approach adopted by another investment firm which has in place a comprehensive guide on how the clients' sustainability preferences are assessed. Indeed, this comprehensive guidance assists the respective investment advisor when carrying out the suitability assessment for the client. Firstly, the guide delves into the differences of the client sustainability preferences in line with Article 2(7) of the MiFID Delegated Regulation but also considers the wider client sustainability motivations both in terms of sustainability goals, values and priorities. Such approach signifies that the investment firm has gone beyond the selection of the compulsory features and has considered the impact-oriented financial instruments, whereby such financial instruments would not fall under the respective categories outlined in Article 2(7) (a) to (c) of the MiFID II Delegated Regulation. For instance, the firm may consider a set of value and priorities which relate to the seventeen (17) United Nations Sustainable Development Goals (SDGs) segregated in terms of both environmental and social sustainability objectives. Besides, a firm may also consider the exclusion strategies related to the Environmental (E), Social (S) and Governance (G) put in place when selecting the type of sustainable investment products. The firm's guidance could also highlight the different investment strategies which may be pursued in view of the different types of sustainable finance instruments, whether the strategy would be related to either of the following: the ESG integration, negative screening, impact and thematic investing.

[v] Matching the Client's Sustainability Preferences with the Clients' Quantitative Indications

Regulatory Requirements and Guidelines

Section I.II *Know your client and know your product,* Paragraph 72 of the ESMA Guidelines on certain aspects of the MiFID II suitability requirements highlights that investment firms should adopt robust and objective procedures, methodologies and tools that allow them to appropriately consider different characteristics including sustainability factors and the relevant factors of each investment product that they may recommend or invest in on behalf of clients.

Moreover, paragraph 73 of the aforementioned ESMA Guidelines (2023) provides that when considering the sustainability factors of products in view of the subsequent matching with the client's sustainability preference, firms could, for example, rank and group the financial instruments included in the range of products they offer in terms of:

i. the proportion invested in economic activities that qualify as environmentally sustainable (as defined in Article 2, point (1) of the Taxonomy Regulation 2020/852);
ii. the proportion of sustainable investments (as defined in Article 2, point (17), of the SFDR 2019/2088; and

iii. the consideration of principal adverse impacts and other environmental, social and governance sustainability features.

Such grouping should also be consistent with the firm's analysis conducted for the purposes of product governance obligations. Firms are reminded that grouping of financial instruments for the purpose of the suitability assessment cannot replace the collection of information from clients as described in paragraph 27 of the ESMA Guidelines 2023.

Findings

Most of the investment firms did not outline the methodology applied on how clients' sustainability preferences will be matched minimum proportions established by clients in the context of sustainable preferences and which would be obtained during the client fact find. This can lead to a potential risk where investment firms will not be effectively able to match the sustainability preferences of the clients with the respective sustainability features of the product.

MFSA Expectations

Since various investment firms have a substantial number of investment advisors, it is imperative that investment firms ensure harmonisation across the board especially with respect to the methodology used to meet the clients' minimum proportions as indicated in the respective client fact finds. The Authority expects that the investment firms should agree and approve their sustainable finance related methodology at senior management level such as for instance during the investment committee meetings.

[vii] Adequate Record Keeping on Suitability Assessment Including Sustainability Preferences.

Regulatory Requirement and Guidelines

In order to ensure adequate record keeping for both the clients and the competent authority, investment firms are obliged to adhere to various obligations emanating from: Article 16(6), Article 25 (5) and Article 25 (6) of the MiFID II Regulation (EU) 2014/65. On the other hand, Articles 72 to 75 of the MiFID II Delegated Regulation (EU) 2017/565 highlight the obligations that investment firms need to adhere in relation to record keeping related to transactions and order processing.

Paragraph 109, General Guideline 12 of the ESMA Guidelines on certain aspects of the MiFID II suitability requirements on certain aspects of the MiFID II suitability requirements highlight that investment firms should maintain adequate recording and retention arrangements to ensure, orderly transparent record keeping regarding the suitability assessment. Adequate record keeping arrangements are crucial to enable the detection of failures regarding the suitability assessment especially in case of mis-selling.

Paragraph 111 of the ESMA Guidelines on certain aspects of the MiFID II suitability requirements further outlines that investment firms are obliged to record all relevant information about the suitability assessment (both information about the client and the instrument). Records should include reference to any changes made to the suitability assessment, especially in relation to the client's investment risk profile, the types of financial instruments that fit in that profile and instances whereby the client's sustainability preferences are adapted in line with Article 54(10) of the MiFID II Delegated Regulation, including a clear explanation of the reasons for such adaption.

Rule R.4.4.29 of the Conduct of Business Rulebook and the supporting Guideline G. 4.4.20 provides that investment firms are to ensure adequate record keeping on suitability assessment.

Guideline G.4.4.8 of the Conduct of Business Rulebook provides guidance to investment firms on the importance of regular updates related to suitability assessment. This guideline recommends to investment firms to identify the Client's individual sustainability preferences at the next regular update of the existing suitability assessment.

Key Findings

Although the policies and procedures reviewed by the Authority as part of this exercise generally included a record keeping section, it was noted such section does not consider the record keeping obligations related to the sustainable preferences of clients (such as, for example, the records to be kept when clients adapt their sustainable preferences).

MFSA Expectations

The Authority expects investment firms outline in their policies and procedures how they will effectively ensure proper record keeping of their clients' sustainability preferences and any updates or adaptation thereof.

B.III. Arrangements necessary to understand Investment Products

In view of the previously outlined obligations, investment firms should adopt robust and objective procedures, methodologies and tools that allow them to appropriately consider the different characteristics of each investment product. Ultimately, these arrangements would ensure that investment firms may recommend or invest in products that have sustainability features on behalf of clients, to match their client's sustainability preferences accordingly.

Regulatory Requirement and Guidelines

The Commission Delegated Directive (EU) 2021/1269 modifies Commission Delegated Directive (EU) 2017/593 and aims to clarify, amongst other matters, that sustainability preferences need to be taken into account in the Product Oversight and Governance process. Thus, sustainability preferences are to be duly considered when specifying the type or types of clients for whose needs, characteristics and objectives the financial instrument is compatible with.

The relevant amendments to Delegated Directive (EU) 2017/593 to integrate sustainability factors into product governance obligations became applicable as from 22 November 2022 and are transposed in the Authority's Conduct of Business Rulebook.

The sustainability-related amendments to the said MiFID II Delegated Directive triggered also amendments to the ESMA Guidelines on MiFID II Product Governance Requirements, which include as part of the product governance process the specification of any sustainability-related objectives a product is compatible with. The said ESMA Guidelines have been implemented in the Conduct of Business Rulebook and became applicable as from 3 October 2023.

Section I.II of the ESMA Guidelines 2023 paragraph 76 highlights that to match clients with suitable investments, firms should establish policies and procedures to ensure that they consistently consider:

- All available information about the client necessary to assess whether an investment is suitable, including the client's current portfolio of investments (and asset allocation within that portfolio).
- All material characteristics of the investments considered in the suitability assessment, including all relevant risks and any direct or indirect costs to the client.

Also, Rule R.4.4.23 of the Conduct of Business Rulebook highlights that Regulated Persons shall have in place and be able to demonstrate that they have adequate policies and procedures in place to understand the nature, features (costs and risks) of services and financial instruments selected for their clients including sustainability factors to meet the client's profile.

[i] Product Due Diligence Procedures

Findings

From the assessment undertaken by the Authority, it can be concluded that almost none of the investment firms had in place a detailed description of the procedures/methodologies and tools used in the process of identifying the main characteristics of each investment product having sustainability features. As a result, investment firms are not able to effectively consider the different characteristics of each investment product having sustainability features, in a comprehensive manner.

On the other hand, the Authority noted that few investment firms are making use of a particular tool which collects data and information related to the ESG factors. In various instances, it was noted that such assessment/process was only described briefly in the respective policies and procedures.

Some investment firms outlined specifically that they will adopt robust and objective procedures, methodologies and tools that will allow them to appropriately consider the different characteristics of each investment product they may recommend or invest in on behalf of client, whilst also considering the sustainability factors of products in view of the subsequent matching with the client's sustainability preferences. Nevertheless, these investment firms did not provide a comprehensive overview of how such analysis will be carried out.

MFSA Expectations

The Authority stresses on the importance of outlining how third-party tools are being utilised to identify the investment products having sustainability features, whilst having detailed policies and procedures which are relevant with the investment firm's size, nature of business, products and services being offered. Firms are also expected to ensure that they assess the sustainability features of the products they offer so that they could be in a position to offer clients products which match the latter's sustainability preferences.

[ii] Grouping and Ranking of Sustainable Investment Products

Regulatory Requirement

Section I.II – *Know Your Client and Know Your Product*, paragraph 73 of the ESMA Guidelines on certain aspects of the MiFID II suitability requirements states that:

"When considering the sustainability factors of products in view of the subsequent matching with the client's sustainability preferences, investment firms could, for example, rank and group the financial instruments included in the range of the products they offer in terms of:

i. The proportion invested in economic activities that qualify as environmentally sustainable (as defined in Article 2, point (1), of the Taxonomy Regulation).
ii. The proportion of sustainable investments (as defined in Article 2, point (17) of the SFDR).
iii. The consideration of principal adverse impacts and other environmental, social and governance sustainability features.

Such grouping should also be consistent with the firm's analysis conducted for the purposes of product governance obligations. Grouping of financial instruments for the purpose of the suitability assessment cannot replace the collection of information from clients as described in paragraphs 26 and 27 of the same ESMA Guidelines (2023).[3] *"*

Findings

The Authority is concerned to note that most of the investment firms did not include a detailed section of how the grouping/ranking of sustainable investment products will be carried out taking into account the following:

i. the proportion invested in economic activities that qualify as environmentally sustainable in line with Article 2, point 1 of the Taxonomy Regulation.
ii. the proportion of sustainable investments in line with Article 2, point 17 of SFDR, which relates to *"an economic activity that contributes to an environmental or social objectives, or an investment in human capital or economically or socially disadvantaged*

[3] Reference should be made to Section B (vii) – Neutral & unbiased approach in the suitability assessment, as outlined in this letter.

communities, provided that such investments do not significantly harm any of those objectives and that the investee companies follow good governance practices."

iii. the PAI considerations and other environmental, social, and governance sustainability features.

In another instance, the Authority noted that a selected number of investment firms have outlined how the grouping/ranking will be assigned in the respective policies and procedures. For instance, an investment firm has undertaken a comprehensive overview of what main factors will be considered to effectively group/rank the sustainable related products. In this case, for the proportion invested in the economic activities in line with the Taxonomy Regulation 2019/2088, the investment firm considers the non-financial disclosures and a number of performance indicators which are aligned with the environmentally sustainable activities. Whilst for sustainable investments in line with Article 2 (17) of the SFDR, the investment firm considers the objectives of the Article 8 and/ or Article 9, as deemed necessary whilst identifying the respective minimum proportion. Lastly, with respect to the PAI considerations, the investment firm would analyse the PAIs disclosures, and the screening carried out by the respective Financial Market Participant (FMP), in order to identify the suitable sustainable related products.

It was noted that certain investment firms have introduced the ranking of sustainability goals within the client fact find with respect to the clients' sustainability preferences (for example: *"positive impact on the society and/or the environment within the investment"* and *"the alignment of investments with personal values*." Nevertheless, the ranking of sustainability goals from a product perspective has not been explained in the policies and procedures relating to the product governance obligations.

Identified Bad Practices

In certain instances, it was noted that the grouping/ranking of products was indirectly outlined through the allocation of the minimum proportions of sustainable investments as identified by clients rather than direct ranking a priori by the investment firm. On the other hand, in the respective client fact finds, the client is requested to rank their sustainability preferences accordingly, however, such dedicated section either did not include the respective minimum proportions to be invested ("minimum 20%'', ''minimum 25%'') or included the minimum proportions for one particular sustainable related product, for instance: PAI considerations whilst omitting other types of products (SFDR Aligned & Taxonomy Aligned). Such approach is considered as a bad practice, given that the investment firms did not take into consideration the grouping and ranking as outlined in paragraph 73 and its interplay with paragraphs 26 and 27 of the ESMA Guidelines on certain aspects of the MiFID II suitability requirements.

MFSA Expectations

The Authority expects investment firms to adopt robust and objective procedures to assess the different characteristics of each investment product they may recommend to, or invest in on behalf of clients, accordingly. If, such procedures also consider the process of grouping/ranking based on the sustainability characteristics of the financial instruments, this process should be incorporated as part of the product oversight and governance procedures. Having a comprehensive process in place makes it easier for the advisors to match the client's preferences with the financial instruments having sustainability features. Thus, this process will also assist in the formulation of the matching process, mentioned earlier on.

B. IV. Organisational Requirements

Investment firms should always ensure that their organisational requirements are robust, adequate, and up to date with the ongoing regulatory developments related to sustainable finance. This ensures that investments firms effectively mitigate instances of regulatory risks, which would have significant implications if the risk materialised.

[i] Training and Competence

Regulatory Requirement and Guidelines

Article 25(1) of MiFID II (EU) 2014/65 which relates to assessment of suitability and appropriateness and reporting to clients outlines that investment firms are to ensure and demonstrate to competent authorities, that natural persons giving investment advice or information about financial instruments, investment services or ancillary services to clients, on behalf of the investment firm, possess the necessary knowledge and competence to fulfil their obligations under Article 24 of MiFID II.

Guideline 6 of the ESMA Guidelines on certain aspects of the MiFID II Compliance Function requirements stipulates that the compliance officer must have the necessary skills, knowledge and expertise to discharge their obligation pursuant to Article 21(1)(d) of the MiFID II Delegated Regulation. It is imperative that the Compliance Officer should be knowledgeable on MiFID II and all related delegated and implementing acts, laws, regulations as well as ESMA Guidelines. Furthermore, guideline 11, paragraph 104 of the ESMA Guidelines 2023 outlines that firms are required to ensure that staff involved in material aspects of the suitability process have and experience. Also, paragraph 106 of the ESMA Guidelines 2023, outlines the obligation that the relevant staff should have the necessary knowledge and competence regarding the criteria of the sustainability preferences as specified in Article 2(7) of the MiFID II Delegated Regulation and be able to explain to clients the different aspects in non-technical terms. Hence, to that effect, firms should give staff appropriate training on sustainability topics.

Key Findings

Following a review of the policies and procedures provided, it was noted that only few investment firms have included a dedicated section on training related to sustainable finance. The Authority is concerned to note that the client facing employees may not be kept sufficiently updated of the abreast of

The Authority noted that Compliance Officers of a selected number of investment firms did not attend any training and conferences on sustainable finance to further their knowledge on this subject matter. Through the interactions during supervisory meetings held by the Authority with a number of the sampled licensed entities, the Authority observed that certain Compliance Officers did not have an in-depth knowledge on sustainable finance, which is quite concerning.

Identified Good Practice

As part of the submitted documentation, few investment firms have also provided copies of the training material being provided to their employees. In some cases, the Authority noted that the training delved into various aspects of the regulation related to the SFDR (EU) 2019/2088 and the Taxonomy Regulation (EU) 2020/852 and the investment firm's obligations vis-à-vis this regulation.

One investment firm has provided training related to the changes of the suitability assessment and suitability report, which includes specific reference to the sustainability preferences. The training also included two different scenarios which delve into differences between financial instruments having sustainable features and those which do not. This type of training equips investment advisors to better match products had instruments having sustainable features with the sustainability preferences of their clients.

Another investment firm drafted a detailed guidance document whereby it explains how advisors should go about the client's sustainability preferences and the sustainable financial product selection process. Following an analysis of these documentation, the Authority noted that throughout different sections, the investment advisors were constantly guided on how the processes should be undertaken and the necessary examples were also provided.

MFSA Expectation

The Authority expects that the compliance officer, all client facing staff and board members attend training related to sustainable finance. It is expected that such training also includes the assessment of the client's sustainability preferences. It is important to ensure that adequate training records are kept on file. In fact, such expectation has already been outlined in the official letter dated 5th October 2022 which was sent by the Authority to the respective investment firms. As highlighted earlier, training of client facing staff is critical to ensure that the investment firm is always acting in the best interest of the client.

B. V. Client Fact Find Questionnaire

[i] Updates to the client fact find document

Following the introduction of several regulations related to the concept of sustainability, as explained above, in their information gathering exercise, firms were required to include a specific section to assess the sustainability preference of the clients.

Findings

From the assessment undertaken, it was noted that nearly all investment firms have updated their client fact find document. However, in certain instances, the Authority also noted that certain investment firms have outlined, in their covering letter to the Authority, that at this point in time, they are not offering financial products having sustainable features, given that their strategy is not focused on sustainable finance related products. On this basis the investment firms in question did not update the client fact find and respective policies and procedures. The Authority would like to highlight that even though investment firms are authorised to provide these aforementioned services but currently to do not offer such services, such investment firms are still obliged to ensure that the client fact find and respective policies and procedures are updated and in line with the obligations emanating from the amendments of the MiFID II Delegated Acts (Commission Delegated Regulation (EU) 2021/1253 and Commission Delegated Directive (EU) 2021/1269).

Furthermore, it was noted however that whilst two investment firms have updated their suitability assessment policy, the updates per se were not reflected in the respective client fact find document. The extent of granular updates to the client fact find document varies across all investment firms.

Overall, the Authority noted that many of the investment firms, as already outlined in Section A of this letter, definitions of terms relating to sustainable finance and products were not included in the client fact find document.

Identified Good Practices

An investment firm has updated its client fact find document to include a dedicated section which needs to be completed by the investment advisor whereby the advisor must tick relevant boxes related to the following elements:

a) The client's level of financial literacy and knowledge of sustainability factors.
b) The explanation provided to the client concerning the sustainability preferences to enable the client to understand the terms and distinctions between the different elements of sustainability preferences as indicated MIFID. In particular section includes reference to whether the advisor has communicated the following elements to the client, namely:
    i. Introductory explanation on the links between financial investment, the environment and society.
    ii. Explanation on what environmental, social and governance aspects mean.
    iii. Explanation on the different types of sustainable financial instruments available on the market.
    iv. Explanation of the different categories of sustainability preferences.
    v. Articulation of sustainability preferences and other investment objectives.

This approach would encourage the advisor to explain the different elements related to the sustainable finance framework in a coherent manner.

In another instance, another investment firm explained the terms related to sustainable finance in a question and answer (Q&A) document and introduced a new sub-section in the pre-contractual disclosures to explain the concept of sustainable preferences which considers the following:

i. The concept of sustainability preferences and the ways in which the client can express them.
ii. The difference between products having sustainable features versus the non-sustainability features.
iii. The ESG concept and the meaning of Environmental (E), Social (S) and Governance (G) factors.

In addition to the above, the investment firm also explained the concept of sustainability neutral and the process of matching suitable financial instruments in line with client's sustainability preferences. When providing investment advice on a portfolio approach, the client is then also given an explanation on how the investment firm will be meeting the sustainability preferences expressed by that same client, in whole and/or in respect of specific part/s thereof of the investment portfolio.

[ii] Assessing Sustainability Preferences through Close-Ended and Open-Ended Questions

Guidelines

Paragraph 26, Section V (I.II) of the ESMA Guidelines (2023) requires that the information on the sustainability preferences of the client should include all aspects mentioned in the definition of "sustainability preferences" according to Article 2 (7) of the MiFID II Delegated Regulation, as outlined under Section A of this letter. In this section, the Authority would like to clearly establish the link between the sustainable finance terminology used in MIFID with that under the SFDR - and provide examples such as PAIs and the definition of sustainable investments under the SFDR. This will underscore the importance of other issues raised in the letter such as the need of clear explanation of such terms and the assessment of such criteria by advisors when they come to recommend products.

In this case, the definition of "sustainability preferences" is taken into the context of the client fact find and thus such information is to be included within the client fact find document. It is imperative to note that the definition of "sustainability preferences" should be sufficiently granular to allow for a matching of the client's sustainability preferences with the sustainability-related features of financial instruments. Firms should collect the following information from clients:

- Whether the client has any sustainability preferences (yes/no).
- If the client answer "yes" to the previous question, whether the client has sustainability preferences regarding to one or more points (a), (b) or (c) of the definition according to Article 2 (7) MiFID II Delegated Regulation. [4]

[4] Points (a), (b) or (c) of the definition according to Article 2 (7) MiFID II Delegated Regulation refer to the following:

a) Sustainable investments in economic activities that qualify as environmentally sustainable under the Taxonomy Regulation (Regulation EU 2020/852);

- For aspects (a) and (b), the minimum proportion.
- For aspect (c), which principal adverse impacts (PAI) should be considered including quantitative or qualitative criteria demonstrating that consideration.

Moreover, paragraph 27 of the ESMA Guidelines 2023 on certain aspects of the MiFID II suitability requirements outlines that to achieve this, firms could choose the following approach:

- Firms could collect information on the sustainability preferences of the client which would refer to one or more of the aspects expressed through points (a) to (c) of Article 2(7) of the MiFID II Delegated Regulation. This aspect could be assessed through closed ended 'yes/no' questions.
- Firms could also collect information on whether the client's sustainability preferences regarding points (b) and (c), if any, have a focus on either environmental, social or governance sustainability factors or a combination of them or whether the client does not have such a focus.
- Where the client expresses preferences in terms of the "minimum proportion" as mentioned in points (a) and (b), firms could collect this information not in terms of an exact percentage but by minimum percentages. These percentages should be presented in a neutral way to the client and should be sufficiently granular. Firms could, for example, assist the customer to identify the minimum proportions, such as *"minimum 20%, minimum 25%, minimum 30%, etc"*.
- In case the client wishes to include a financial instrument that considers PAI, the information collected should cover the qualitative or quantitative elements of PAI mentioned under (c). Firms could test the client's preferences and appetite for PAI integration regarding the families of PAI indicators as whole, based on a possible focus of the client on environmental, social or governance aspects, using the categories presented in the SFDR RTS (instead of an approach based on each PAI indicator) such as emissions, energy performance, water and waste. An evaluation could then be initiated for each category whether is important/key for the client or not. This qualitative evaluation could be based on the approaches in which products consider PAI (for instance: the exclusion strategies/ controversial policies/voting and engagement policies).

  In case the client wishes to include a financial instrument that considers PAI, firms could also ask the client if there are specific economic activities that, on the basis of relevant PAIs, it wishes to exclude from its investments (for example, specific economic activities that are considered as significantly harmful under the EU

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b) Sustainable investments as defined in Article 2, point (17) of the SFDR (Regulation (EU) 2019/2088);

c) Financial Instruments that consider PAI that might be eligible for recommendation as meeting individual sustainability preferences of Client.

Taxonomy framework and/or that are opposed to the environmental and ethical views held by the client and that are linked to certain principal adverse impacts on sustainability factors).

Overall, these ESMA Guidelines (paragraphs 26 & 27) provide a detailed overview of how the suitability assessment should be structured in a simpler manner to ensure that the client express his/her sustainability preferences adequately.

Findings

In this section, the Authority provides an overview of the issues noted whilst assessing the client fact find provided by the investment firms subject to the thematic review. Besides, the Authority shall provide an in-depth overview of the different sections (in paragraphs (a) - (e)hereunder) of the client fact find to indicate its expectations as to how investment firms should ensure that the client's sustainable preferences are adequately collected and recorded.

From the assessment carried out, the Authority noted various discrepancies in the sustainability section within the client fact find document, as most of the investment firms did not include enough questions to gather sufficient information on the clients' sustainability preferences. For instance, the suitability question related to the PAI consideration and ESG related options in the context of sustainability preferences were very often omitted in the documentation provided. The scope and the inclusion of such questions are deemed crucial to assess the clients' sustainability preferences in accordance with the requirements emanating from MIFID and to subsequently offer suitable financial instruments.

a. *Close-Ended Questions concerning Financial Instruments having Sustainable Features*

The questions revolving around sustainability should be made up of open and closed ended questions. Most investment firms have included closed-ended questions to assess their clients' sustainability preferences. The scope of including closed-ended questions in the sustainable preferences section within the client fact find is to ensure that the respective answers (which would be either in the form of *"yes"* or *"no"* answers or ticking of a specific selection) can be sorted in different segments which can be easily comparable and easily understood. Hence, such type of questions would assist the investment firm to match the clients' sustainability preferences to the sustainability features of the financial instrument on offer.

Identified Good Practice

Paragraph 85 of ESMA Guidelines 2023, states that "*where a client does not answer the question whether it has sustainability preferences, or answers "no", the investment firm may consider this client as "sustainability-neutral" and recommend products both with and without sustainability-related features.*" An investment firm has considered the obligations emanating from this paragraph and has explained in detail within its Q&A document such situation and the concept of "sustainability neutral" and how the advisor would proceed to make a recommendation in such circumstances. Such explanation has also been included in the client fact find document and in the respective policy and procedures.

b. <u>ESG Related Questions</u>

Several investment firms did not include closed-ended questions related to points (a) – (Taxonomy Aligned products) and (c) – (PAI Considerations products) of Article 2(7) of the MiFID II Delegated Regulation.

The Authority also noted that although the questions relating to general ESG preferences (point (b) of Article 2(7) of the MiFID Delegated Regulation) were addressed within the client fact find document provided, the investment firm did not explicitly state that they refer to the ESG preferences, in line with paragraph 27 of the ESMA Guidelines.

<u>Identified Good Practice</u>

Certain investment firms have included closed-ended questions related to questions on the ESG (point (b) of Article 2(7) of the MiFID Delegated Regulation) and have also delved into the ESG parameters, by also including different ESG indicators such as the following:

a) the environment;
b) social and employee matters;
c) human rights;
d) anti-corruption; and
e) anti- bribery matters.

In this case, both the 'S' and 'G' element have catered for two **sub-parameters**. Such ESG indicators would be easier to link to the client's sustainability preferences at a later stage of the process.

c. <u>Minimum Proportion Questions</u>

Similarly, the Authority also noted certain discrepancies when it comes to the minimum proportions assigned for the sustainable financial instruments as outlined under Article 2(7) of the MiFID II Delegated Regulation (a) and (b). A significant number of investment firms have included questions related to the minimum proportion. One common finding noted was that the minimum proportion allocations allowed clients to indicate a preferred range for their sustainability preferences (for example: 20% -30%) rather than indicating exactly the minimum proportion preferred (for example: minimum 20%), as further outlined point 2.8 (c) of Appendix 7 of Chapter 4 of the Conduct of Business Rulebook.

On the other hand, the Authority also noted that certain investment firms have also included an option for *"no minimum allocation required"* or else the investment firm did not disclose any range and included a comment box whereby the client would state the preferred percentage. In another instance, it was noted that the concept of minimum proportion is not applied. Rather this investment firm asks the clients, to indicate on a scale (from 0 to 100), the ESG portion of the investment should represent as maximum percentage of the total portfolio. Such approach is not deemed to be in line with paragraph 27 of the ESMA Guidelines 2023, as the scale outlined in the client fact find indicated the maximum amount allocated rather than the minimum proportion to be allocated accordingly.

d. *Questions related to the PAI Considerations – for the purposes of establishing sustainability preference in terms of paragraph (c) of Article 2(7) of MIFID.*

The Authority is concerned to note that questions related to PAI considerations were minimal and to a certain extent inexistent within suitability assessments provided. In fact, a significant number of investment firms did not account for the PAI considerations in the client fact find. However, some investment firms have included PAI considerations, and it seems that such entities have struggled to determine and assign the classification of PAI indicators within the context of the ESG framework. Moreover, reference to the qualitative and quantitative PAI elements were minimal. In certain instances, questions related to adverse economic activities were clearly indicated by few investment firms. On the other hand, no parameters have been provided, with respect to the information of the specific economic activities which should excluded (also referred as the economic activities which are harmful). It is imperative, that considerations should be given to the economic activities which are harmful to the environment. In another instance, the Authority noted that PAI related questions were included, however there was no detailed explanation on what constitutes PAI considerations. This implies that no clear explanation of this concept was provided to clients in order for these to assess whether they would want to base their sustainability preferences on this criterion.

Reference is also made to Section B II titled 'Assessing Sustainability Preferences through Close-Ended and Open-Ended Questions' of this letter, whereby the MFSA's expectations on how the investment firm should request further information from clients concerning their preferences towards PAI considerations are indicated.[5] An investment firm has implemented all the requirements emanating from this guideline in its policies. However, the Authority noted that this investment firm did not provide in detail any explanation of how it intends to achieve its best practice.

[5] In case the client wishes to include a financial instrument that considers PAI, the information collected should cover the qualitative or quantitative elements of PAI mentioned under (c) of Article 2(7) of MIFID II Delegated Regulation. Firms could test the client's preferences and appetite for PAI integration regarding the families of PAI indicators as whole, based on a possible focus of the client on environmental, social or governance aspects, using the categories presented in the SFDR RTS (instead of an approach based on each PAI indicator) such as emissions, energy performance, water and waste. An evaluation could then be initiated for each category whether is important/key for the client or not. This qualitative evaluation could be based on the approaches in which products consider PAI (for instance: the exclusion strategies/ controversial policies/voting and engagement policies).

e. *Provision of Portfolio Management Services and Provision of Investment Advice based on a Portfolio Approach*

Guidelines

Section I.II – *Know your client and know your product*, of the ESMA Guidelines on MiFID II Suitability Requirements (2023), paragraph 29 outlines that when providing portfolio management or investment advice with a portfolio approach firms should collect information on the client's sustainability preferences with the same granularity as set out in paragraphs 26 and 27 of the ESMA Guidelines 2023. Investment firms should also ask the client which part/percentage of the portfolio (if any) the client wants to be invested in products meeting the client's sustainability preferences. Where investment firms work with model portfolios that combine some or all the criteria listed under paragraph 26,[6] these model portfolios should allow for a granular assessment of the client's preferences and should not be translated into a questionnaire that pushes the client into a certain combination of criteria that would not meet the client's original sustainability preferences.

In view of the above, reference is also being made to paragraph 88 of the ESMA Guidelines 2023 whereby further guidance is being provided to ensure the sustainability preferences are considered within the context of a portfolio approach, as follows:

"When a firm conducts a suitability assessment based on the consideration of the client's portfolio as a whole it could assess suitability as regards the sustainability preferences, for example, by applying those preferences (including the minimum proportion that shall be invested in investments with sustainability features) on average at the level of the portfolio as whole or at the level of the part/percentage of the portfolio the client wants to be invested in products with sustainability features".

This implies that the investment firms should ensure that their client fact find captures all the elements outlined in paragraph 26 and 27 of the ESMA Guidelines 2023 to effectively apply the portfolio approach for their clients.

In addition to this, paragraph 84 of the ESMA Guidelines 2023 highlights the interplay between the portfolio approach and the minimum proportion of sustainable investments identified by clients. Also, this paragraph outlines the main obligations which emanate from the different services being provided by the investment firm, as follows:

"When providing investment advice with a portfolio approach, firms should assess the client's sustainability preferences including the minimum proportion when conducting the initial suitability assessment. Then the firm should monitor whether those preferences are still met or not at portfolio level and issue appropriate recommendations as the case may be.

[6] Paragraph 26 of the ESMA Guidelines outline that investment firms should collect the information from the clients: whether the client has any sustainability preferences (yes/no). If the client answers "yes" to the previous question, whether the client has sustainability preferences with regard to one or more points (a), (b) or (c) of the definition according to Article 2 (7) of MiFID II Delegated Regulation. Also, for aspects (a) and (b) outlining the minimum proportion. For aspects (c), which principal adverse impacts (PAI) should be considered including quantitative or qualitative criteria demonstrating that consideration. Overall, investment firms should adopt a neutral and unbiased approach as to not to influence the clients' answers.

In case of portfolio management or investment advice with portfolio approach, if the client adapts the sustainability preferences after the initial suitability assessment, firms should evaluate the impact of this change and whether this triggers a rebalancing of the portfolio."

Therefore, investment firms are obliged to implement processes for monitoring the client's portfolio depending on the type of investment services being provided, for example: whether they are providing investment advice on a portfolio approach or portfolio management services.

Besides, ESMA has also provided a detailed explanation of how the portfolio approach should be undertaken by investment firms. Reference should be made to the Call for Evidence on the integration of sustainability preferences in the suitability assessment and product governance arrangements, whereby ESMA highlights that the assessment of suitability as regards to sustainability preferences can be performed at four different levels, namely:

i. at the level of every single financial instrument recommended to/invested on behalf of the client.
ii. at the level of every single financial instrument of the part of the portfolio the client wants to be invested in financial instruments with sustainability features; or
iii. at the level of the client portfolio as a whole; or
iv. at the level of the part of the portfolio the client wants to be invested in financial instruments with sustainability features.

When it comes to the sustainability preferences that are expressed as a minimum proportion in accordance with Article 2(7) (a) and (b) of the MiFID II Delegated Regulation, it follows that these minimum proportions could be assessed:

i. at the level of every single financial instrument recommended to the client or invested on behalf of the client;
ii. on average at the level of the client portfolio as a whole;
iii. or at the level of the part of the portfolio the client wants to have invested in financial instruments with sustainability features;
iv. or at the level of every single financial instrument of the part of the portfolio the client wants to be invested in financial instruments with sustainability features.

In fact, practical examples were also provided which focus on the importance of the portfolio approach. Although, such examples are neither exhaustive nor prescriptive; however, these can be considered and adapted by the investment firms accordingly and taken into consideration for the purposes of their respective POG policies and procedures.

Findings

The Authority is concerned to note that many investment firms did not effectively outline how the portfolio approach (concerning the clients' sustainability preference/s) is being tackled within the client fact find.

Identified Good Practices

One particular investment firm has included a question requesting the client to indicate which type of investment (such as for example: equities and bonds) should be considered for the purposes of establishing the client's sustainability preferences. Such question would assist the investment firm to clearly determine which part/percentage of the client's portfolio, the client wants to be invested in sustainable related investments.

Another investment firm has updated its client fact find to include a dedicated section which effectively accounts for the interplay between the portfolio approach and the minimum proportion. In this section, the investment firm specifically asks the client whether s/he would like to include as part of the investment portfolio, certain securities (such as: Collective investment schemes and/or Exchange Traded Funds relating to either local or foreign securities) which have sustainability features. Once the client ticks the respective selections, these are then matched to the client's sustainability preferences.

Given that this investment firm provides the investment advice and discretionary portfolio management services, updates were also made to its policies and procedures and the suitability report accordingly. Furthermore, the investment firm obliges its investment advisor/s and/or the portfolio manager/s to undertake such an assessment and record in the suitability report whether the client's sustainability preferences have been met. With respect to the discretionary portfolio management services provided, the investment firm has also created an adaptation form to cater for those circumstances where the client would need to adapt his/her preferences due to unavailability of sustainable related products, so that a record is kept accordingly.

An investment firm outlined in a comprehensive manner how the portfolio approach is implemented by the firm for the respective investment services, in the Q&A which is provided to its clients. Hence, this disclosure ensures that the client is informed in a transparent manner of how the sustainability preferences will be accounted and assessed on an ongoing basis.

MFSA Expectations

Investment firms are expected to have in place a process to address how sustainability features of an investment product are matched with the client's sustainability preferences Overall, such process needs to be harmonised in the respective policies and procedures which should be made available to all relevant employees so that they would be in a position to collect all the necessary information and data in place to enable such a process. It is thus the Authority's expectation that the investment firm's product oversight and governance policies encompass the work relating to sustainable financial instruments, whilst also having in place adequate, tools and processes to maintain oversight of such instruments during the investment firm's operations to ensure that these continue to meet the clients' sustainability preferences.

[iii] Neutral and Unbiased Approach in the Suitability Assessment

ESMA Guidelines

Reference is made to the regulatory requirements section, under point [ii] of Section B titled *Assessing Sustainability Preferences through Close-Ended & Open-Ended Questions* of this letter which outlines how investment firms should adopt a neutral and unbiased approach as to not influence clients' sustainability preferences accordingly. Indeed, the inclusion of biases would impact the client's replies and as well hinder the selection of products which are truly in line with the client's original sustainable preferences.

Findings

The biased/unbiased approach is another important element which was considered by the Authority to assess whether the client fact find questionnaire provided by the respective investment firm illustrates any biases, in some form or another. The Authority is of the view that such biased approach would lead to a potential risk that the whole process, including the suitability assessment is designed in a way that would impact the client's sustainability preference. In view of this situation, the Authority strongly believes there is a potential risk of conflict of interest which would be evident because the investment advisor could possibly influence the client to state preferences that can be matched to the products the advisor already has to offer when these would not really be in line with the client's original preferences.

Although determining the biased elements can be very subjective, the Authority identified certain biases which are deemed to be a common in the documentation it has reviewed as part of this exercise. The following are some examples: Pre-ticked section related to the question '*'Do you have any sustainability preference?''*. In this case, it was noted that the 'no' sustainability preference was pre- ticked. The Authority deems that this approach is not acceptable since in this way, the investment firm is practically replying to the question on behalf of its client thus denying the latter the possibility to even express whether s/he has sustainability preferences.

In one case, a statement was included in the introductory section of the client fact find questionnaire outlining that the investment firm does not integrate the sustainability risk criteria and nor does it consider the principal adverse impacts on sustainability factors, as part of the investment firm's strategy. Such statement within the introductory section of the client fact find is deemed to be biased since it would lead to client to avoid opting for any financial instrument having sustainable features. Hence, investment firms should consider such statements should not be placed in the introductory section but rather once the assessment has been carried out, also keeping in mind the obligations emanating from MiFID II. With reference to paragraph 27 of the ESMA Guidelines 2023 and the findings outlined in sections B [i] and [ii] of this letter, clearly indicate that omissions by the majority of the investment firms related to the following elements are deemed to be classified as a biased approach undertaken. In fact, the following list provides an overview of the various omissions noted by the Authority such as: the types of products (SFDR Aligned, Taxonomy Aligned and

PAI considerations), the ESG framework and subsequently questions thereof, the lack of minimum proportion and in certain instances the use of exact percentages rather than by minimum proportions. Other omissions noted by the Authority specifically relate to the PAI considerations, such as follows: the omission of the qualitative and/or quantitative elements of the respective PAI families, the non-inclusion of the following elements namely: adverse sustainability indicators[7], the qualitative evaluations to the PAI consideration[8] and the specific economic activities which are considered to be significantly harmful in line with the Taxonomy Regulation (EU) 2020/852 and/or opposing to the environmental and ethical views held by the respective client.

Identified Bad Practice

One investment firm included a statement in the client fact find to the effect that the client is not obliged to indicate his/her sustainability considerations. The investment firm also explained that should the client state his/her sustainability preferences, the financial product selection would be restricted. A warning was also included outlining that sustainable investments would negatively affect the performance of a portfolio, and the client might suffer a loss from time to time. In this case, the Authority is concerned to note that the investment firm did not outline the basis on which it determines that the sustainable investments would negatively impact the client's portfolio. Moreover, the Authority deems that such approach is a bad practice since such a statement would discourage clients from investing in sustainable finance related products, especially since such a widespread statement was not backed up by any evidence.

MFSA Expectations

The Authority expects that all investment firms carry out a detailed documented assessment to identify whether their client fact find documentation and subsequent assessments have any form of bias, as outlined in the findings section above. If such biases have been noted, these should be rectified with immediate effect by means of an update to the client fact find and respective policies and procedures.

C. Other Findings

Findings

In view of this thematic review, the Authority also noted other findings which are worth highlighting, even though such findings go beyond the context of MiFID II sustainability requirements.

In their covering letter to the Authority, certain investment firms outlined that at this point in point time, such firms do not consider, assess the integration of the Environmental (E), Social (S) and Governance (G) factors and the risks emanating from the ESG dimension. Also, such investments firms remarked that PAI considerations are not being considered for the purpose

[7] In terms of the environmental and social aspects as per Annex 1 of Table 1 of the SFDR (EU) 2022/1288 (SFDR Level II).
[8] Investment firms should consider the following: exclusion strategies/ controversies policies, voting and engagement policies.

of the investment firm's investment decisions, with no further information when (timeframe) such PAIs will be considered. Overall, the Authority is concerned that a number of investment firms consider such an integral process to be irrelevant.

MFSA Expectations

In view of such findings, the Authority would like to highlight that in addition to the obligations emanating from MiFID II Regulation and the amendments to the MiFID Delegated Acts, investment firms acting as FMPs and FA are obliged to adhere to the compliance obligations emanating from the SFDR (EU) 2019/2088 (Level I) and, where deemed applicable, to the SFDR (EU) 2022/1288 (Level II). Besides, the Authority expects that the Compliance Officer carries out a detailed compliance gap analysis of the Nature and Art of Financial Supervision-Initial Study on Sustainability Related Website Disclosures in Terms of the Sustainable Finance Disclosure Regulation publication issued in this respect and remediate any shortcomings accordingly.

Going forward, whenever new guidelines, rules, and regulations would be introduced, the Authority expects that all investment firms to carry out a comprehensive gap analysis on their respective policies, procedures and/or disclosures, as deemed necessary.

The Authority expects that effective disclosures, explained in a comprehensive manner are included to outline how sustainability risks are integrated in the decision-making process and the remuneration policy of the investment firm.[9] Moreover, it is expected that the respective disclosures include the policies by means of a hyperlink, for the sake of clarity and transparency.

Whenever, an investment firm is not considering PAIs, such entity should illustrate in the SFDR disclosures concrete commitments in a comprehensive manner as to when the entity will consider PAI. On the other hand, with respect to those investment firms that account for PAI, the Authority expects that these entities include detailed information in their policies and procedures outlining how the investment firm identifies and prioritises such PAIs. Information related to how the respective PAIs impact the investment firm should be included. Reference to the engagement policies should include specific information of how the investment firm is monitoring the investee companies on the relevant matters in line with Article 3(g) of Directive 2007/36/EC on the exercise of certain rights of shareholders in listed companies. Besides, the Authority expects that the investment firm outlines how the monitoring of the investee company/companies should be undertaken and how the engagement policy is being implemented by publishing the respective public disclosures on an annual basis.[10] Besides, the Authority expects that the respective engagement policies outline the alignment with the

[9] Article 3 relates to the transparency of sustainability risk policies, whilst Article 5 relates to the transparency of remuneration policies in relation to the integration of sustainability risks.

[10] The main obligations emanating from Article 3(g) of Directive 2007/36/EC outline that the monitoring of the investment companies should be in relation to the following factors: strategy, financial and non – financial performance and risk, capital structure, social and environmental impact, corporate governance, conduct dialogues with investee companies, exercise voting rights and other rights attached to shares, cooperate with other shareholders, stakeholder communications and the effective management of both potential and actual conflict of interest. The yearly disclosures should outline how the entity has casted the votes in the general meeting of investee companies respectively.

objectives of the United Nations (UN) Climate Change Conference (COP 21), also known as the Paris Agreement. Another expectation is that such engagement policies include reference to any other relevant responsible business conduct codes and internationally recognised standards for due diligence and reporting were included in the respective engagement policies, in with Article 4 (2)(d) of the SFDR.

As a way forward, the Authority will be closely monitoring the SFDR website disclosures of all investment firms to ensure that such disclosure adhere to the applicable regulation (Level I and Level II as deemed applicable) and are in line with the expectations outlined in the Nature and Arts publication.

CONCLUDING REMARKS

The Authority notes the affirmation made by majority of the investment firms forming part of this thematic review, that they do not offer any investment products having sustainable features due to the lack of demand/appetite from the retail clients. Hence, most investment firms have adopted a 'wait-and-see approach' whereby such situation may change in the foreseeable future depending on the subsequent changes in the regulatory and/or legal framework, and certain business strategy/decisions which will be taken at that point in time.

Moreover, the Authority also noted that certain investment firms outlined that the information on sustainability factors does not form part of the investment decision making or the investment recommendation process. These findings are similar to the initial findings emanating from the MFSA Report on Operational and Compliance Readiness by Financial Market Participants and Financial Advisers, which was published by the Authority on 12th April 2022.

The Authority is cognisant of the fact that within a sustainable finance context, the lack of awareness by clients is one of the hurdles in the way of the promotion of sustainable finance in general. Therefore, investment firms have a fundamental role to play to bridge the gap between the investors' fundamental values and their actual behavioural choices. Although, there is a lack of product and data availability in the market, it is extremely important that investment firms work to raise awareness on sustainable products, such as for instance by providing comprehensive information on the concept of sustainable finance and ESG.

Overall, the findings as explained through this letter outline that although investment firms have begun to effectively implement the obligations emanating from the regulation per se; such implementation varies considerably between one investment firm and another. The Authority would have expected that investment firms would have come farther in their application of the rules and regulations related to sustainable finance. Therefore, the Authority expects investment firms to dedicate the necessary resources to implement the requirement emanating from such rules and regulation with immediate effect.

The Authority expects all investment firms to:

i. Incorporate the collection and analysis of the necessary information about a client's or potential client's sustainability preferences within their sustainability policies and procedures, as part of the client's suitability assessment.
ii. Update and/or review the process relating to the ESG data sourcing, including those related to obtaining reliable ESG information from products manufacturers.
iii. To provide appropriate training to relevant staff, including with respect to assessing client's sustainability preferences.

OUR EXPECTATIONS ON FIRMS

The observations and findings arising from this exercise are being highlighted in this letter with a view to sharing experiences, learning valuable lessons, and identifying good practices for the benefit of the financial market and the end consumer.

The Board or Executive Committee is therefore urged to consider which of the observations indicated in this letter are applicable to its business. To this end, firms are expected to carry out a gap analysis with respect to the practices and processes of the firm and then to take prompt action to address any identified shortcomings accordingly.

Kindly note that the Authority will be continuously monitoring compliance by investment services licence holders with the applicable regulatory requirements and may engage with particular investment firms on the matters forming the subject of this letter.

Should you require any clarification on the above, please do not hesitate to contact the Authority's Conduct Supervision Function on csuinvestments@mfsa.mt

Yours faithfully,

Malta Financial Services Authority

Christopher Peter BUTTIGIEG (Signature)

Digitally signed by Christopher Peter BUTTIGIEG (Signature)
Date: 2025.05.21 16:58:58 +02'00'

Sarah PULIS (Signature)

Digitally signed by Sarah PULIS (Signature)
Date: 2025.05.21 17:05:15 +02'00'

Christopher P. Buttigieg
Chief Supervision Officer

Sarah Pulis
Head Conduct Supervision