

EU Retail Investment Strategy proposals

-

Regulation amending the PRIIPs Regulation Directive amending investor protection aspects of MiFID

-

ICMA feedback

EXECUTIVE SUMMARY

- (1) The retail investment strategy should avoid disrupting the institutional/wholesale bonds markets.
- (2) Regarding PRIIPs, the limited scope clarification proposal is incrementally welcome even though it seems unlikely to materially impact bond market practices / promote retail bond supply.
- (3) Regarding MiFID product governance, the proposals are not expected to impact current bond market ICMA1/ICMA2 approaches – but the regime remains conceptually flawed regarding commoditised instruments such as bonds, which should be excluded from the regime altogether (at least in a professional investor context).
- (4) Regarding MiFID inducements, the underwriting & placing exemption from the proposed retail execution-only inducement ban is essential and welcome (even if it is questionable to what extent a MiFID ‘service’ is being provided to investors as ‘clients’).
- (5) Regarding MiFID costs & charges, the proposals need correcting to clearly preserve the CMRP alleviations concerning professional investors and eligible counterparties.
- (6) Regarding MiFID marketing communications, there is substantive existing compliance with the proposed new requirements as the Prospectus Regulation already regulates advertisements.
- (7) Regarding MiFID client categorisation, the elective professional criteria widening (rather than creation of an entirely new client category) is welcome.

-
-
1. **Introduction** – ICMA welcomes the opportunity to provide feedback from the perspective of the international bond markets on the proposals of the European Commission (“EC”) for a Regulation amending the PRIIPs Regulation ([COM\(2023\) 278 final](#) / the “RIS/R”) and for a Directive amending inter alia the investor protection aspects of MiFID ([COM\(2023\) 279 final](#) / the “RIS/D”). ICMA also notes the EC’s Impact Assessment Report accompanying its proposals ([SWD\(2023\) 278 final](#) / the “Impact Assessment”).
 2. **Avoid disrupting institutional/wholesale bond markets** – Whilst there are many challenges facing retail investor participation in the bond markets (as further noted below), care needs to be taken

that any attempts to minimise retail bond supply disincentives avoid disrupting the institutional/wholesale bonds markets that have been reliably providing trillions in financing to the global economy over the years.

3. PRIIPs regime application

- (A) **Proposed formal scope clarification limited** – ICMA notes that the proposed RIS/R Art.3(a) sets out just a narrow technical exclusion to the PRIIPs Regulation Art.4(1) definition of a PRIIP for make-whole clauses (as defined in Art.4(1)(44a) of MiFID¹) and does not include any other scope clarification, whether from the non-binding (and limited content²) October 2019 Joint Supervisory Statement ([JC-2019-64](#)) of the European Supervisory Authorities or otherwise (including based on PRIIPs Regulation Recital 6 as suggested by ICMA³).
- (B) **Such clarification welcome though unlikely to materially impact bond market practices / promote retail bond supply** – The above EC proposal is welcome (as an incremental improvement) even if it seems unlikely to materially change existing market practices in the international bond markets, where there have long been (i) conceptual/liability concerns with preparing KIDs and (ii) uncertainty regarding PRIIPs regime scope. The combination of these two factors has materially contributed to disincentivising, and so reducing, corporate bond supply to direct retail investors. All of this is acknowledged at paragraph 4.1 on pp.111-112 of the Impact Assessment – which is reproduced in full in the Annex to this feedback paper. (The convoluted retail summary requirements introduced in the 2010 review of the EU prospectus regime, the MiFID product governance regime and non-regulatory considerations⁴ also contributed.) In this respect, the bond markets are now primarily institutional in nature – with any retail exposure to corporate bonds has been generally indirect: via funds or, for high net worth investors, on a discretionary (professionally managed) portfolio basis.
- (C) **Informal scope clarification welcome, but of unclear impact** – ICMA welcomes the EC’s informal acknowledgment at paragraph 4.1 of the Impact Assessment (footnote 257 notably) explaining why “plain” bonds are out of scope (and which has similarities to ICMA’s prior suggestions³ in being based on PRIIPs Regulation Recital 6). But it is currently unclear whether such an informal reference will materially change existing market practices.

4. MiFID product governance

- (A) **Bond market background** – ICMA has historically focused on proportionate application of the MiFID product governance (“PG”) regime in a way that is compatible with preserving European companies’ ability to raise capital funding in the international bond (Eurobond) markets (which are primarily institutional in nature as noted in #3(B) above). A company borrowing in these markets can, within hours intra-day, both hire a temporary syndicate of underwriter banks and have them place a bond issue on its behalf with investors – raising funds worth up to several billion euros. This ability to secure large sums quickly becomes particularly important for companies in challenging macro-economic conditions when markets are volatile, with access opportunities opening and closing unpredictably within days.

¹ “(44a) ‘make-whole clause’ means a clause that aims to protect the investor by ensuring that, in the event of early redemption of a bond, the issuer is required to pay to the investor holding the bond an amount equal to the sum of the net present value of the remaining coupon payments expected until maturity and the principal amount of the bond to be redeemed”.

² ICMA noted (at Q24 on pp.11-12 of ICMA’s [December 2021 response to ESMA](#)) three specific examples of product features falling outside the Supervisory Statement despite involving no ‘intercession’ (as contemplated under Recital 6 of the PRIIPs Regulation): bonds with make-whole provisions, sustainability-linked bonds and bonds with coupon caps / non-zero floors.

³ ICMA has at various times flagged its suggestions relating to scope clarification – see further #7 on pp.4-5 of ICMA’s [September 2018 response to FCA](#) (in terms of potential regulatory guidance) and at Q22 on pp.10-11 of ICMA’s [December 2021 response to ESMA](#) (in terms of potential legislative amendment).

⁴ These include heightened reputational and logistical considerations from the issuer perspective and over a decade of low rates from the investor perspective. (#4.1 of the Impact Assessment, footnote 260 suggests some further aspects also.)

- (B) **Current ICMA1 & ICMA2 approaches in the bond markets** – In this respect, ICMA published in December 2017 (and notified to staff at ESMA and at various NCAs) two papers setting out distinct potential PG compliance approaches that MiFID-regulated underwriters (together with any MiFID-regulated bond issuers) could choose to adopt to enable them to continue operating, as PG co-‘manufacturers’, within the international bond market dynamics set out above:
- (i) the [‘ICMA1’ approach](#) relating to all syndicated bonds sold to professional investors (this was followed by a [revision of its Schedule 1](#) in October 2022 to reflect technical changes regarding the integration of sustainability factors into the PG regime⁵) and
 - (ii) the [‘ICMA2’ approach](#) relating to simple, listed bonds sold to all investors including retail (this was similarly followed by a [revision of its Schedule 1](#) in October 2022).
- (C) **Proposed PG amendments noted** – ICMA notes that the proposed RIS/D sets out various amendments to the MiFID PG provisions, namely: (i) RIS/D Art.1(8)(b) deleting MiFID Art.16(3)#2-7; (ii) RIS/D Art.1(9) inserting new MiFID Art.16-a; (iii) RIS/D Art.1(10) amending MiFID Art.16a; and (iv) RIS/D Art.1(12)(c) amending MiFID Art.24(2).
- (D) **Proposed PG amendments not expected to impact bond markets** – Though the above proposed amendments involve significant textual changes, the substantive impact (notably further to new MiFID Art.16-a) appears relatively specific. Whilst the Impact Assessment (at pp.15-16) explains that the amendment proposals follow from target market definitions being sometimes “formalistic” with “insufficient granularity”, it however explicitly states this is in the context of “cost structure” / “high costs” / poor “value for money” (which is echoed also in the EC’s Explanatory Memorandum at pp.16-17 of the RIS/D proposal) – and consequently away from the mainstream bond space (where there are no costs relating to the bond and bonds are priced in line with prevailing interest rates to market demand). In this respect, ICMA welcomes that certain new requirements in proposed new MiFID Art.16-a are specifically limited to not apply beyond the context of PRIIPs.⁶ It is consequently expected that the bond market ICMA1/ICMA2 compliance approaches set out in #4(B) above will not be impacted by the proposed PG amendments.
- (E) **PG regime conceptually flawed for (and should not apply to) commoditised instruments such as bonds** – Regardless of the practical compliance approaches above, ICMA has previously warned and remains of the view that the PG regime is conceptually flawed regarding commoditised funding products such as **Eurobonds**, which **should be outside the scope of the PG regime altogether**. In the context of the existing regime ICMA (i) acknowledges the potential legislative drafting expediency/convenience of an exclusion just for ‘non-complex’ bonds⁷ and (ii) notes that, at a minimum, there is no practical rationale for the regime to apply in a professional investor context (with ICMA referencing several technical exemptions in this respect).⁸
- (F) **Capital Markets Recovery Package (CMRP) insufficient in this respect** – ICMA’s [August 2021 response](#) to the Commission’s retail investment strategy consultation (under Q6.9 on p.7)

⁵ A related explanation is set out in a contemporaneous paper [ICMA proposed approach to sustainability-related amendments to product governance and MiFID II Delegated Directive](#).

⁶ ICMA does not comment on whether such requirements are appropriate even within the context of PRIIPs (other trade associations will presumably provide feedback in this respect) – but ICMA reminds (as noted in #3(B)) that uncertainty regarding PRIIPs regime scope (combined with KID preparation concerns) has materially contributed to disincentivising, and so reducing, corporate bond supply to direct retail investors.

⁷ Such instruments can in any case be sold on an execution-only basis, with PG target market definitions thus being arguably inconsequential.

⁸ See further ICMA [May 2020 response](#) to European Commission MiFID II/R review consultation, as summarised in a [related July 2020 ICMA Quarterly Report article](#).

noted that the CMRP (i.e. current MiFID Art.16a) was not expected to have any useful impact.⁹ Regarding the make-whole clause alleviation, it is not worth bond underwriters (as ‘manufacturers’) expending resources implementing ‘lighter’ internal compliance policies and procedures for just a narrow ‘slice’ of bonds (those with a make-whole clause but no other embedded derivatives), which is sandwiched between the wider universe (of bonds with other embedded derivatives and of bonds with no embedded derivatives at all) that remains subject to the PG regime. Regarding the eligible counterparties (“ECPs”) alleviation, it is worth noting that bonds are not routinely distributed to ECPs exclusively – as the typical professional investor base has been wider than ECPs.

5. MiFID inducements and costs & charges

(A) **Retail execution-only inducement ban / Exemption for underwriting & placing essential and welcome** – ICMA notes the proposed RIS/D sets out various amendments to the MiFID inducements provisions, namely: (i) RIS/D Art.1(12)(i) deleting MiFID Art.24(9); and (ii) RIS/D Art.1(13) inserting new MiFID Art.24a. New MiFID Art.24a(2) bans any fee, commission or non-monetary benefit in the context of providing, to retail ‘clients’, the MiFID services of ‘reception and transmission of orders’ or of ‘execution of orders’. New MiFID Art.24a(4) however exempts remuneration from a (non-PRIPs) issuer client receiving the MiFID services of underwriting and placing. This (non-PRIPs)¹⁰ exemption is essential and welcome in the context of a new bond issue – to the extent a MiFID ‘service’ is also being provided to investors as ‘clients’ (which is questionable).⁸

(B) **Costs & charges / Need for clear preservation of CMRP alleviations concerning professionals and ECPs** – ICMA notes the proposed RIS/D sets out various amendments to the MiFID cost & charges provisions, namely: (i) RIS/D Art.1(12)(e) amending MiFID Art.24(4); and (ii) RIS/D Art.1(13) inserting new MiFID Art.24b. The EU’s Capital Markets Recovery Package introduced an alleviation from the costs & charges disclosure requirements in the contexts of (i) professional clients (by introducing the MiFID Art.29a(1) exception from MiFID Art.24(4)(c)) as well as (ii) ECPs (by widening the MiFID Art.30 exception to include MiFID Art.24(4)). There is no indication in the RIS/D or the Impact Assessment of any intention to reverse this alleviation – unsurprisingly since the policy focus is about retail clients and not professional clients or ECPs. Regarding professional clients, MiFID Art.29a(1) continues to reference MiFID Art.24(4)(c) directly and so in turn also new MiFID Art.24b but only indirectly. It would thus be helpful, in terms of ease of understanding, for **MiFID Art.29a(1) to also reference new MiFID Art.24b directly**. Regarding ECPs, MiFID Art.30 continues to reference MiFID Art.24(4) directly and so in turn also new MiFID Art.24b indirectly – but MiFID Art.30 is then proposed to effectively contradict itself in simultaneously narrowing its scope by excluding new MiFID Art.24b(1). This seems to be a manifest technical error (it would be absurd for the alleviation to apply regarding less sophisticated professional clients but not regarding more sophisticated ECPs) and so the **MiFID Art.30 exclusion of new MiFID Art.24b(1) should be corrected**.

6. **MiFID marketing communications / Substantive existing compliance with Prospectus Regulation already regulating advertisements** – ICMA notes the proposed RIS/D sets out new MiFID provisions relating to marketing communications, namely: (i) RIS/D Art.1(8)(c) inserting a new

⁹ ICMA’s response referenced, in the context of make-whole clauses specifically, p.25 of the [2021Q3 ICMA Quarterly Report](#), which cited ICMA’s then informal understanding of EU co-legislator intention. This was subsequently formally established in ESMA’s November 2021 *MiFID II and MiFIR investor protection and intermediaries topics* Q&A ([ESMA35-43-349](#)), at PG Q5 on pp.130-131.

¹⁰ ICMA does not comment on whether this inducements ban is appropriate even in the context of PRIIPs (other trade associations will presumably provide feedback in this respect) – but ICMA reminds (as noted in #3(B)) that uncertainty regarding PRIIPs regime scope (combined with KID preparation concerns) has materially contributed to disincentivising, and so reducing, corporate bond supply to direct retail investors.

MiFID Art.16(3a); and (ii) RIS/D Art.1(13) inserting new MiFID Art24c. Regarding new bond issues, it is worth noting that the [Prospectus Regulation \(EU/2017/1129\)](#) currently requires *inter alia*:

- (a) advertisements (i) to be clearly recognisable as such, (ii) to not to be inaccurate or misleading and (iii) to indicate where investors are or will be able to obtain the prospectus; and
- (b) prospectuses to (i) to be approved by a regulator, (ii) to contain the necessary information which is material to an investor for making an informed assessment, (iii) to contain (in a retail context) a summary providing key information that investors need to understand the nature and the risks of the issuer, the guarantor and the securities and (iv) to be in an easily analysable, concise and comprehensible form.

Compliance with such Prospectus Regulation requirements also seems likely to substantively satisfy the proposed new MiFID Art.24c(1)/(2) provisions applicable to individual marketing communications.

7. **MiFID client categorisation / Elective professional criteria widening (rather than entirely new client category) welcome** – ICMA notes the proposed RIS/D widens the MiFID criteria relating to elective professional status namely: (i) RIS/D Art.1(24); and related Annex I amending MiFID Annex II, part II.1. This is preferable than creating an entirely new category of ‘semi-professional’ investors⁸ and so is welcome.

ICMA contact

Ruari Ewing: Ruari.Ewing@icmagroup.org

International Capital Market Association

ICMA Brussels | Avenue des Arts 56, 1000 Brussels | T: +32 2 801 13 88

ICMA London | 110 Cannon Street, London EC4N 6EU | T: +44 20 7213 0310

ICMA Hong Kong | Unit 3603, Tower 2, Lippo Centre, 89 Queensway, Hong Kong | T: +852 2531 6592

ICMA Paris | 62 rue la Boétie, 75008 Paris | T: +33 1 70 17 64 72

ICMA Zurich | Dreikönigstrasse 8, 8002 Zurich | T: +41 44 363 4222

www.icmagroup.org

ANNEX

Extract from Impact Assessment Report

4. Clarification of the scope of PRIIPs regarding corporate bonds and immediate annuities

4.1 Problem description – corporate bonds

Another technical issue that is covered in this annex is the lack of legal clarity over the exclusion of certain types of corporate bond from the scope of PRIIPs, which according to some stakeholders is one of the factors limiting the offer of these instruments towards retail investors.

Plain corporate bonds (i.e. which are not particularly complex) have a number of advantages that would seem to justify their purchase by retail investors. For example, they are relatively easy for investors to understand and, compared to equities, corporate bonds issued by the same issuer are considered a less risky form of investment. From the point of view of the issuer, more retail investor participation in corporate bond markets would benefit companies by giving them a more diversified investor base for their funding needs.

It is therefore unfortunate that there has been a decline in the number of corporate bonds sold to retail investors in the recent years. In a study conducted in 2021 by BaFin, the German national competent supervisor notes an overall decline in the total value of annual corporate bond purchases by retail investors from 4.5 billion Euros in 2016 (which was before the entry into force of PRIIPs on 1 January 2018) to around 2.5 billion Euros in 2019. Other asset classes, such as government bonds or DAX stocks, which are excluded from the application of the PRIIPs Regulation, have not seen such declines.

It would appear that there is a link with the requirements of the PRIIPs Regulation, even as plain corporate bonds do not satisfy requirements to be included in the PRIIPs scope²⁵⁷. In 2019 the ESAs observed that: *“Uncertainty over the application of the PRIIPs Regulation to bonds, has led to negative consequences for the functioning of bond markets, and access to these markets by retail investors.”*²⁵⁸

The uncertainty was especially linked to bonds with so-called “make-whole clauses”, which is defined in the supervisory statement as *“a clause that allows the issuer to pay off the remaining debt early using a reference rate to determine the net present value of future coupon payments that will not be paid”*. Because the investor is exposed to a reference rate should the issuer call back the bond, some issuers had interpreted the make-whole clause as meaning that the bond was a PRIIPs, according to criteria 1 in recital (6). However, the Supervisory Statement did not settle the matter of whether bonds with make-whole clauses should be categorised as PRIIPs²⁵⁹. Although NCAs were recommended to apply the guidance when supervising these requirements, this still resulted in significant uncertainty remaining on the market. And as illustrated above, the limited offer of plain corporate bonds to retail investors may be partially explained by this legal clarity issue²⁶⁰.

In the Call for Evidence, the ESAs asked for views and experiences regarding the Supervisory Statement. The vast majority of respondents expressed support for the Statement while also stating that there remains legal uncertainty on the application of the PRIIPs Regulation to bonds, given that the Statement is a non-binding measure. Some respondents also argued that a number of additional features of bonds, in particular “make-whole” clauses, should not result in a bond being deemed a PRIIP. As a result, plain vanilla corporate bonds are still hard to access for retail investors since it has not been fully clarified that these financial products are not considered as “packaged” retail

investment products (PRIIPs). Consequently, these bonds cannot be purchased by retail investors unless the issuer of the bond publishes a KID.

Apart from retail investors, stakeholders particularly affected are:

1. Non-European firms which do not explicitly market their bonds to European retail investors and therefore do not publish a KID in Europe, or
2. European firms that do not want to take the risk associated with the publication of a KID. The industry standard is that issuers sell their bonds to their bank consortium and have no further interest in the reselling of these bonds by the banks, in particular to retail investors. It would therefore seem that the entities most disadvantaged by this situation are the banks that resell the corporate bonds.

²⁵⁷ In the PRIIPs Regulation, recital (6) explains that the scope should include *“all products, regardless of their form or construction, (...) where: i) the amount repayable to the retail investor is subject to fluctuation because of exposure to reference values, ii) or subject to the performance of one or more assets which are not directly purchased by the retail investor.”* Plain corporate bonds do not satisfy either of these requirements, as the repayable amount is fixed (= the coupon and the principal) and the asset (the bond) is held directly by the retail investor.

²⁵⁸ ESAs: Supervisory Statement on the application of the scope of the PRIIPs Regulation to bonds (JC 2019 6497).

²⁵⁹ It concluded that: *“The inclusion of a clause that allows the issuer to pay off the remaining debt early using a reference rate to determine the net present value of future coupon payments that will not be paid (i.e. make whole) is expected to mean that the amount repayable to the retail investor is subject to fluctuations because of exposure to reference values. However, where the mechanism to calculate the discount rate is known in advance to the retail investor, this could be considered as a separate case, which does not satisfy the criteria in Article 4(1). Therefore, not all callable bonds are considered to be in scope, but some are expected to be on the basis of the specific “callable” feature, as well as depending on the other contractual features of the bond.”*

²⁶⁰ Other factors are likely involved as well, such as typical higher amounts needed for an investment or low liquidity of such bonds in secondary markets, but these are outside the remit of PRIIPs and the Retail investment strategy more broadly.