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Mr. Olle Schmidt
Member of the European Parliament

Bât. Altiero Spinelli
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Per electronic mail

Brussels, 10 May 2012

Re.: MiFID/MiFIR legislation Package / ECON reading

Dear Mr. Schmidt,

Further to conversations held with your staff in the previous days, EUSIPA, the European association for issuers of structured retail investment products in Austria, Germany, France, Italy, Sweden and Switzerland, takes great pleasure in submitting to you our comments on some amendments tabled by your colleague MEP Markus Ferber on the MiFID/MiFIR package in the ECON committee some weeks ago.

Our comments relate in particular to the amendment 64 on the requirement of issuing products to an identified target market and to the amendments 66 to 72 which deal with product intervention rights before the launch of a product.
We explicitly thank you in advance for considering our proposals in your positioning as ECON liberal fraction's shadow rapporteur for the MiFID/MiFIR package and remain at your full disposal for any additional question or background information.

Sincerely,

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Comments

of the

European Structured Investment Products Association

For discussion in the

Committee on Economic and Monetary Affairs

on

(i) the draft report on the proposal for a directive of the European Parliament and of the Council on markets in financial instruments repealing Directive 2004/39/EC of the European Parliament and of the Council (recast) (COM(2011)0656 – C7 0382/2011 – 2011/0298(COD)) ("**MiFID**") dated 27 March 2012; and

(ii) the draft report on the proposal for a regulation of the European Parliament and of the Council on markets in financial instruments and amending Regulation [EMIR] on OTC derivatives, central counterparties and trade repositories (COM(2011)0652 – C7 0359/2011 – 2011/0296(COD)) ("**MiFIR**") dated 16 March 2012.

1 MiFID II Proposal - Amendment 64

Article 24 – paragraph 1 a (new)

The proposal was to insert the following new paragraph: "Member States shall ensure that where investment firms design investment products or structured deposits for sale to professional or retail clients those products are designed to meet the needs of an identified target market within the relevant category of clients and that the investment firm takes reasonable steps to ensure that the investment product is marketed and distributed to clients within the target group."

In our view, an obligation on investment firms as stated above would, for the reasons set out below, represent both an inappropriate burden on the investment firms and an unnecessary obligation for the administrative bodies concerned with the monitoring and implementation of the intended new concept.

We thus recommend to delete this new paragraph, as:

- In most cases, investment products are not distributed/sold to the end-investors by the product designer (i.e. the investment firm). Hence, it is particularly difficult for an investment firm (as opposed to the distributing entity) to define the target market for a product and thus to ensure that a product will exactly meet the needs of that market. It would also be extremely difficult for third parties – as for example the regulators – to review what the target market for a certain product would be and thus to monitor whether product designers have complied with this obligation.

- Further, the mere design of a product does not per se give rise to, or increase, a threat for any rights of investors. It is only at the time the product is marketed and distributed, and with a view

to how and to whom it is so marketed and distributed, that the needs and rights of investors might be in jeopardy. Thus, it does not seem appropriate to impose an additional obligation on the investment firms in their capacity as product designers.

- In most cases, investment products are in the large majority of cases not marketed and distributed by the issuer (designer) itself but rather by an intermediary. This will in particular be the case in the Italian and in the German market. The needs of the relevant clients and investor groups and their rights are thus already sufficiently protected by the rules of conduct set out by MiFID. At the time the clients get in contact with the product, the MiFID rules of conduct ensure that the clients will obtain sufficient information; further, due to the suitability and adequacy tests, it is also ensured that the product meets the needs of a client to which it is recommended and/or sold. It is thus in our view not necessary to further increase the liability of the investment firms when structuring new products.

- It should also be noted that there is no similar obligation for any other regulated issuer (designer) of investment products, such as insurance companies or investment funds.

- In any case, amendment 66 already provides for an obligation to inform the client of the risks associated with a specific product due to its structure and to also provide the client with appropriate risk warnings. In our view, this obligation should be sufficient to preserve the clients' rights.

2 MiFIR Proposal – Amendment 66 to 72 (also Amendment 5)

Article 31

It was proposed to further extend ESMA's powers of intervention in the market for a single product or for a type of product, by allowing intervention already at a time when the investment product or financial instrument is not yet marketed and distributed. The proposed clause should read as follows:

"In accordance with Article 9(2) of Regulation (EU) No 1095/2010, ESMA shall monitor the investment products, including structured deposits and financial instruments which are marketed, distributed or sold in the Union and may proactively investigate new investment products or financial instruments before they are marketed, distributed or sold in the Union in cooperation with the competent authorities."

We would like to comment on this as follows:

- The proposed Article 31 MiFIR as a whole provides for very extensive intervention rights for ESMA and it is our concern that the threshold for intervention of those rights should be clearly defined in MiFIR.

- In that respect, we further refer to the comments and suggestions for changed wording made by Deutscher Derivate Verband, one of our members, in relation to the proposed Article which we attach herewith as **Annex 1**.

- As set out in that document, the criteria which must be fulfilled under Article 31 paragraph 2 lit. (a) through (b) in order to justify intervention by ESMA are stated very generally and, in our view, are not strict enough. Especially with regard to the very broad range of severe consequences which

such a measure can have for the issuer or supplier of a product, the criteria for an intervention must represent a sufficiently appropriate high hurdle. This would become even more important, if the intervention rights of ESMA would be extended to products which are not even marketed and distributed. This is in particular true with respect to the question of how to identify to which (not yet existing) product an intervention relates and to which it does not.

- Please refer to Annex 1 to this document for our already made arguments on the proposed Article 31 of MiFIR.

- Finally, we take the liberty to consider that extensive rights usually are countered with a heightened responsibility. While of course any action of ESMA (and of the national regulators as set out in Article 32 MiFIR) against a product or product designer could lead to a potential liability of ESMA (or the relevant national regulator) in case of an excessive or inadequate measure, in our view such responsibility and related potential liability for ESMA (and the relevant national regulators) would be increased if the rights for intervention would be even further extended.

We also note that it is considered that the appropriateness of intervening measures that have been taken shall only be re-visited after one full year (instead of three months), if investor protection concerns were the reason for the taking of the relevant measure:

"6. ESMA shall review a prohibition or restriction imposed under paragraph 1 at appropriate intervals and at least every three months. Where the prohibition or restriction is imposed for reasons of investor protection, ESMA shall review the prohibition or restriction annually. If the prohibition or restriction is not renewed after that three-month or annual period it shall expire."

- On the one hand, this further reinforces our concern, that the hurdles for the taking of any such measures must be set sufficiently high in order to justify the potentially extremely harsh consequences of such measures.

- On the other hand, any such long timeframe for the duration of an intervention must per se be regarded as clearly leaving any acceptable timeframe for a product intervention. The legitimate market interest for most investment products relies on the availability of certain investment opportunities in the context of the relevant market environment (interest rates, share prices, volatility etc.) at the relevant time. As a result, the usual offer periods for most investment products only comprise a couple of weeks at most. Accordingly, a period of a fully year for a product intervention is no longer really attributable to a particular product and its appropriateness in the relevant market context.

- In contrast, any such long-lasting measure becomes much more an intervention into the whole related business of the affected investment firm and, hence, changes its character from a "product intervention" to a "market participant suspension". This is clearly beyond what was intended and what can be justified by the purpose of the regulation.

Annex 1

Wording suggestions and comments made by Deutscher Derivate Verband DDV on the Draft Regulation of the European Parliament and of the Council on markets in financial instruments and amending Regulation [EMIR] on OTC derivatives, central counterparties and trade repositories

Based on Document 2011/0296 (COD)

Article 31 MiFIR – ESMA powers to temporarily intervene

a. Article 31 paragraph 2 MiFIR

"Article 31
In accordance with Article 9(5) of Regulation (EU) No 1095/2010, ESMA may where it is satisfied on reasonable grounds that the conditions in paragraphs 2 and 3 are fulfilled, temporarily prohibit or restrict in the Union:
[...]
2. ESMA shall only take a decision under paragraph 1 if all of the following conditions are fulfilled:
(a) the proposed action is required to ~~addresses a threat to the~~ avoid permanent and sustainable damage to investor protection for retail investors, which cannot be avoided in any other way, or to address a serious, sustainable and permanent threat to the orderly functioning and integrity of financial markets or to the stability of the whole or part of the financial system in the Union;
(b) regulatory requirements under Union legislation that are applicable to the relevant financial instrument or activity do not address the threat;
(c) a competent authority or competent authorities have not taken action to address the threat or actions that have been taken do not adequately address the threat, and are generally not suitable to address the threat."

Reasons:

(i) The criteria which must be fulfilled under Article 31 paragraph 2 lit. (a) through (c) in order to justify intervention by ESMA are stated very generally and, in our view, are not strict enough. Especially with regard to the very broad range of potential consequences which such a measure can have for the issuer or supplier of a product, the criteria for an intervention should represent a high hurdle.

(ii) A product intervention can have a great harm in the form of harm to the reputation as the result of publishing the measure by ESMA pursuant to Article 31 paragraph 5 MiFIR. Of course, we welcome the possibility for the supervisory authorities to effectively combat excesses in the capital market. Shady offers and market participants must be sanctioned and hindered in order to protect the capital market and the investors and, thus, the entire industry. However, we wish to point out that a product intervention does not always affect only black sheep in the capital market and that instead also proper participants can be affected. For example, this could be the case if a market participant is permissibly active in a market which is used in an improper manner by others. A prohibition of (or because of) certain activities or products in such market could affect all participants in such market, even if they are acting within the limits of what is permitted and fair. If the affected

market is a relatively small market, it is quite possible that all participants who are active in this market are known and would suffer harm to their reputations as a result of the prohibition. Finally, product interventions under the proposed rules are most likely to be applied, where the affected participants in the market are by no means in conflict with applicable national law (because otherwise measures of the relevant national authorities for breach of national laws could and probably would have been taken).

(iii) Therefore, we consider the soft criteria of "a threat to investor protection or to the orderly functioning and integrity of financial markets or to the stability of the whole or part of the financial system in the Union" to be too low a hurdle for imposing such far reaching measures. The criteria should be specified and tightened as we have proposed above. In particular with respect to investor protection, it should be ensured that only in case of dramatic situations where damage cannot be avoided by any other means a product intervention should be allowed. With respect to the protection of the orderly functioning and integrity of the financial markets, the term "serious, sustainable and permanent threat" makes it clear that not every threat is sufficient for a product intervention and that instead an intervention by ESMA only occurs in special situations. At the same time, this term, in our view, still gives ESMA an adequate leeway for discretion in order to permit measures in all situations where it is necessary. The term "serious threat" is also used in Article 32 paragraph 2 lit. (a) MiFIR in the context of product intervention by national supervisory authorities. The change we are proposing would, thus, also establish consistency in the applicable provisions.

(v) Furthermore, it is our understanding that a measure of ESMA is only supposed to be taken in special situations which require actions that go beyond action by the individual national authorities. This is already clear under lit. (b) of Article 31 paragraph 2 MiFIR, according to which a measure of ESMA is only permitted if the existing European legal framework cannot prevent the threat. To the extent that this is the intent of the European legislative body, however, the third criterion in lit. (c) of the same paragraph does not fit, in our view. If general action falling under the jurisdiction of ESMA is required due to the nature of the damage or threat, the question about whether a national supervisory authority has become active or not is not decisive. In order to make sure that a damage or threat is actually involved which requires general action, however, it is important to determine whether the measures taken by the national competent authorities are capable of countering the damage or threat. In our view, lit. (c) of Article 31 paragraph 2 MiFIR should accordingly be modified as proposed.

b. Article 31 paragraph 1 MiFIR together with Article 31 paragraph 5 MiFIR

"Article 31 – ESMA powers to temporarily intervene

1. In accordance with Article 9(5) of Regulation (EU) No 1095/2010, ESMA may where it is satisfied on reasonable grounds that the conditions in paragraphs 2 and 3 are fulfilled, temporarily prohibit or restrict in the Union:
(a) the marketing, distribution or sale of certain financial instruments or financial instruments with certain features; or
(b) a type of financial activity or practice.
A prohibition or restriction may apply in circumstances, or be subject to exceptions, specified by ESMA.
[...]

5. ESMA shall publish on its website notice of any decision to take any action under this Article. The notice shall specify details of the prohibition or restriction and specify a time after the publication of the notice from which the measures will take effect. . The notice shall contain a detailed description of the relevant financial instruments or financial activity or practice. A prohibition or restriction shall only apply to action taken after the measures take effect."

Reasons:

This provision in its current draft version is very broad and not very tangible. There is no clarity about how the terms "certain financial instruments" or "financial instruments with certain features" and "type of financial activity or practice" should be delineated. We appreciate the fact that, due to the many conceivable factual situations, the national competent authorities must have a broad leeway in order to make sure that action is possible in every conceivable situation which poses a threat. However, this involves great uncertainties for the participants in the market. A prohibition or restriction must be drafted in such a manner that it is possible to clearly determine which financial instruments are affected. Therefore, we suggest imposing on the national authorities the additional obligation to specify as exactly as possible the financial instruments and financial activities which are affected by a prohibition or a restriction in order to provide legal certainty both to the providers of financial services as well as to customers and other participants in the market. With respect to financial instruments, either the specific product (e.g. by its ISIN) or, where not possible, the determining features of the financial instrument must be clearly specified.

End of Annex 1