ABI remarks on the ESMA Consultation Paper on the Draft Guidelines on MiFID II product governance requirements

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POSITION PAPER

Foreword

ABI welcomes the opportunity to provide its own contribution to this consultation on the Draft Guidelines on MiFID product governance with the hope of ensuring that the totality of the product governance rules are properly integrated with all other investor protection rules.

Therefore, before responding to the specific questions raised by the consultation paper, we think it would be useful to comment on some general aspects in order to achieve a better understanding of the product governance rules as a whole.

General remarks

1. Concept of distributor

The Draft Guidelines specify that "distributors", when defining their product assortment and the target market of the products they recommend or offer, shall assess:

- the type of investment services they are going to perform in relation to those products;
- their knowledge of the personal characteristics and needs of their clients;
- their ability to assess the size of the target market of each product, as defined by both manufacturer and distributor, with perspective clients.

The output of such an evaluation, according to the Draft Guidelines, should be the definition of a product assortment which, in light of the specific type of investment service provided by the distributor, ensures general compatibility between each of the products recommended or offered to clients and their respective target market.

This obligation, according to the Draft Guidelines, should apply in relation to products recommended or offered by distributors within both the primary market and the secondary market.

In our opinion, the Guidelines should better clarify that the above mentioned rules do not apply to any firm performing an investment service in relation to a financial product subject to product governance rules, irrespective of the specific context in which the service is provided, but "only" to those investment firms which can be actually classified as a "distributor" of the relevant financial product.

Pursuant to the definition provided within the Draft Guidelines, "distributor" means «*in accordance with Recital 15 ….of the MiFID II Delegated Directive, a firm that offers, recommends or sells an investment product and a service to a client*».

Such a definition must be read in accordance with provisions contained in article 10, paragraph 1, of the Delegated Directive, which specify that "*product governance obligations*" shall be complied with by investment firms «*when deciding on the range of financial instruments issued by themselves or other firms and the services they intend to offer or recommend to clients*» and «*when offering or recommending financial instruments manufactured by entities that are not subject to Directive 2014/65/EU*».

These definitions, from our point of view, make clear that **investment firms** providing a service to their clients in relation to the purchase of a financial product cannot be **qualified as "distributors"** in any case, irrespective of the activity performed, but "**only" when they are actually "*offering or recommending*" such a product to the client.**

This means that an investment firm, in order to be classified as a "distributor" in relation to a financial product, shall be somehow connected to the manufacturer of the product and integrated within the "distribution chain" it has set up for that product **a situation which occurs only when there is a distribution agreement between the manufacturer and the investment firm.**

This is consistent also with other rules on product governance provided by the Delegated Directive. **As a matter of fact, if in the absence of a distribution agreement an investment firm was qualified as a "distributor" under the MiFID II framework, many of the obligations provided by the MiFID II Delegated Directive in relation to product governance could not be effectively applied.**

We point out that, in such cases:

- the investment firm/distributor, in order to establish the target market of all the financial products that can be purchased by its clients, as required by article 10 of the Delegated Directive (as well as by the Draft Guidelines), shall take into consideration, for example, all the financial instruments listed in the trading venues potentially accessible to its clients (which could be, for example, all financial instruments listed in Europe);
- the investment firm/distributor would have no instruments or channels for providing the manufacturer with information on product sales and, in particular, sales outside the identified target market, as it would be required to do by article 10, paragraph 9, of the Delegated Directive;
- the manufacturer would not be in a position, with respect to the distributor, to fulfil requirements provided by article 9, paragraph 15, letters f) and g), of the Delegated Directive, regarding the obligation, upon the occurrence of certain events affecting the product, to (*i*)

contact the distributor in order to discuss changes to the distribution process or (*ii*) terminate the relationship with the distributor[1].

2. Relationship between target market assessment by the distributor and suitability / appropriateness

The process of determining the target market for financial products by the distributor is undoubtedly a requirement prior to and distinct from the process for the assessment of the suitability/appropriateness of the individual client's investments based on these financial products. Indeed, the Draft Guidelines lay down in points:

- 23 "*the target market identification should occur at an early stage, when the firm's business policies and distribution strategies are defined by the management body, on an ex-ante basis and before beginning daily business*";
- 33 **"***distributors should conduct a thorough analysis of the characteristics of their* ***client base****, i.e. current/existing clients, as well as potential clients who have a high likelihood of becoming clients";*
- *29 "The obligation of the distributor to identify the actual target market and to ensure that a product is distributed in accordance with the actual target market shall not be replaced by an assessment of suitability or appropriateness and shall be conducted in addition to, and before such an assessment. In particular, the identification, for a given product, of its target market and related distribution strategy should ensure that the product ends up with the type of customers for whose needs and objectives it had been designed, rather than another group of clients with whom the product may not be compatible".*

While sharing this approach, we do however believe it is important to stress that the process of determining the target market conducted by the distributor must necessarily take place **in a coordinated manner** with its own suitability and/or appropriateness assessment procedures. **The two concepts cannot be considered apart.**

In fact, as required by the Delegated Directive:

- the manufacturer defines a potential target market;
- the distributor defines the concrete target market on the basis of both information obtained by the manufacturer (potential target market) and available information on its customers (using the customer profiling questionnaire and any internal information used for the purpose of the suitability/appropriateness assessment).

[1] As a matter of fact, any possibility that the manufacturer may (*i*) contact the distributor in order to discuss changes to the distribution process and/or (*ii*) terminate the relationship with the distributor, preliminarily requires that a relationship between the manufacturer and the distributor effectively exists.

In addition, in line with the Draft Guideline, the distributor:

1. defines the target market at an early stage, on an ex-ante basis and before going into daily business (when they define their product assortment) and does so at a general level; all this in order to reduce from the outset any potential risks of failure to comply with investor protection rules (such as the suitability test);
2. subsequently applies at the "point of sale" the rules for suitability and appropriateness at single operation level and single client level.

Therefore the *target market assessment* carried out previously by the distributor at an early stage is then by the same declined to device level (that is, when the orders relating to individual transactions on financial instruments are given) by the measures and rules relating to the suitability/ appropriateness assessment. Consequently, at the "point of sale" the current measures in terms of rules of conduct are deemed valid, even for the purposes of product governance, and it is not justified the introduction of additional disclosure requirements towards investors such as those set out in points 42 and 61 of the Draft Guidelines to justify the difficulty of thorough assessment of the target market or deviations from the positive target market defined by the manufacturer. For more details on this, refer to what is stated in the answers to Q1, Q3, Q4 and Q5.

Answers to Specific Questions

Q1: Do you agree on the list of categories that manufacturers should use as a basis for defining the target market for their products? If not, please explain what changes should be made to the list and why

From the point of view of both the manufacturer and the distributor, there is a requirement to:

- match the "Clients' Objectives" category only to the time horizon envisaged for the investment and not to features such as *liquidity supply* or *retirement provision,* because the time horizon is the main component - together with the risk profile - in identifying the financial features of the investment, a component that is not necessarily covered by different attributes such as those mentioned above;
- delete the "Clients' Needs" category because:
  - the set required by other envisaged categories in itself allows a clear and complete identification of the target market in terms of end clients' "needs", particularly the categories effectively underlying needs relating to the financial situation, risk tolerance and time horizon of the investment;
  - unlike other criteria for identifying the features of the product that make it unequivocally marketable/unmarketable to target

clients, client needs instead refer only to the preferences of a particular target customers, which do not necessarily involve the product not being marketable to other target clients. In addition, the consultation document seems to suggest that client needs cannot be standardised, therefore making it impossible to cross-reference this criterion for determining the target market with the client information collected by the distributor;
- the further structuring of client needs with attributes such as, for example, *green investments or ethical investment* is disproportionate with respect to the provisions of article 9, paragraph 11, of the Delegated Directive of the Commission, which requires, in particular, the consideration of the product's risk/return profile and not the features of the type mentioned above.

It is also noted that the provision of the *Clients' Objectives* and *Risk Tolerance* categories does not appear consistent with the approach adopted under article 54 of the Delegated Regulation of 25/04/2016, which, for the purposes of suitability assessment, considers risk tolerance as a sub-category of the client's investment objectives, and not a category in itself.

Furthermore, in particular, from the distributor's point of view:

- it is believed that the requirement for the *financial situation with a focus on the ability to bear losses* should not be structured to the point of also identifying the specific cases of *additional payment obligations that might exceed the amount invested,* as there is an arguably sufficient distinction between, for example, limited, moderate, significant and high losses, considering that the concept of high losses in itself also incorporates cases of *obligations that might exceed the amount invested*;
- it is not considered acceptable to use risk classes identified for PRIIPs purposes, but on the distributor side it seems more appropriate to make use of risk attributes assigned to individual products relevant to the purposes of assessing the suitability of client investments, in order to avoid the duplication of risk indicators used internally by the intermediary (also taking into account that not all products are PRIIP);
- for target market identification purposes it should be sufficient to adopt the same criteria used in client profiling for assessing the suitability of investments because, although they satisfy different aims, there should be convergence between the two areas (suitability and product governance) in terms of identification of the financial features of the clientele. Refer to to what is stated in the answer to Q3 with regard to cases of intermediaries operating in an inappropriateness-only regime

with clients classified as professionals or in an execution-only regime.

Q2: Do you agree with the approach proposed in paragraphs 18-20 of the draft guidelines on how to take into account the nature of the products? If not, please explain what changes should be made and why.

We think that the approach outlined in para 18-20 of the Draft Guidelines focuses excessively on the individual product manufactured and does not take sufficiently into account the overall situation of clients' personal investment portfolios. Therefore, the Guidelines should require that the identification of the target market shall be done in an appropriate and proportionate manner, considering the nature of the investment product as well as the clients' need and objectives on the basis of his/her portfolio.

Q3: Do you agree with the proposed method for the distributor's identification of the target market?

In general we agree with the approach adopted by the Draft Guidelines on the need that the potential target market defined by the manufacturer be concretely structured by the distributor considering the features of its own clientele, taking into account also the nature of the financial instruments (e.g. comparable products vs. products with specific features) and investment services provided (para. 11 states "*these guidelines should …. be applied in a way that is appropriate and proportionate, taking into account the nature of the financial instrument, the investment service and the target market of the product*".)

In order to ensure the concrete structuring of the target market assessment by the intermediary, it is however necessary to state, **as stated in the introduction ("General Remarks"), that the existence of a relationship between the manufacturer and the distributor is an essential prerequisite for the proper and full application of product governance.** We need only remember that the distributors "*should use the manufacturer's more general target market assessment together with existing information on their clients to identify their own target market for a product*"; *"distributors should base their target market on …. information received from the manufacturers"* (Annex 3, 32); any decision to depart from the target market identified by the manufacturer *"should be reported to the manufacturer as part of the distributor's obligation to provide the manufacturer with sales information"* (Annex 3, 46); without counting the distributor's obligations to the manufacturers at the annual review.

It is quite clear that this ongoing dialogue between manufacturer and distributor can be arranged only if the investment firm already has a distribution agreement with the manufacturer.

We believe, therefore, that the Guidelines should better develop the application of the proportionality principle, distinguishing between governable and non-governable products, and taking into account the definition of the distributor as mentioned before, meaning:

- for "**governable products**" those offered by the investment firm on the basis of a pre-selection made in advance and distribution agreements with manufacturers, in which the latter's rights and obligations are also formalised;
- for "**non-governable products**" all financial products for which the intermediary does have an existing distribution agreement with the manufacturer. These cases include: i) the types of operations on a particular financial instrument, made on the "initiative of the client", who autonomously decides on the investments to be implemented (e.g. receiving and transmitting orders and negotiation); ii) investment advice models (independent or non-independent), characterised by the client's freedom to have access to a wide and diversified range of products, which necessarily includes a significant number of instruments traded on the secondary market (e.g. ETFS, bonds listed on regulated markets) that are selected in the customer's interest and for which it is not possible to establish a distribution agreement with the issuer.

For governable products the target market assessment can be carried out comprehensively for all categories that include the potential target market determined by the manufacturer (obviously where the manufacturer is subject to product governance obligations[2]), except for cases in which the intermediary operates in an appropriateness-only regime or operates with clients classified as professionals; in these cases, the Guidelines should clarify that the distributor product governance obligations should refer only to the level of knowledge and experience of the client, without any additional requirement, given that the absence of any further information concerning, for example, the client's investment goals, does not allow the distributor's concrete structuring of the target market.

In contrast, for **non-governable products** the target market assessment can be carried out only in a partly simplified way, because, in the absence of a direct dialogue with the manufacturer, the distributor may not find ex-ante all the necessary information for the prompt and precise execution of the product governance obligations provided by the ESMA Guidelines in relation to all six categories provided for in paragraph 16, nor can it choose in advance, from a tremendously broad universe of financial products, which specific products to analyse (because it does not know which ones will be

[2] There should also be clarification of the exclusion from product governance obligations of own-account negotiation activities carried out by the ***market maker***, this availability of this negotiator figure being directed towards the market as a whole and its role being typically connected to the functioning of the markets.

requested by clients). In particular, we believe that the simplifications necessary for this reason hinge on two aspects:

- defining the target market **not by individual product, but by product type**, taking into consideration the essential features common to the products themselves (knowledge/experience needed to assess that kind of product, degree of risk, likelihood of creating losses, etc.). The prospect of identifying in this case a target market by product "type" is even more appropriate considering that, however deeply granular the target market is, it would still not allow the maintenance of a truly differentiated target market by each individual product from a particular category;

- relying on information and assessments, also of risk, **made directly by the intermediary** applying as much as possible (and not being obligatory) and on the basis of various service models, the 6 categories provided for in paragraph 16 of the Draft Guidelines. The speed with which it is necessary to execute the orders received by the investor does not, in fact, allow to collect/review the information made available by the manufacturer. In addition the information made public by the manufacturer in the documentation relating to the individual product (eg. KIID or prospectus) and related to the target market are descriptive and thus cannot be managed through information flow made available in a standardized way by the information providers.

In this case, where the intermediary operates in an appropriateness-only regime or with professional clients or in an execution-only regime, the Guidelines should specify that the definition of the target market of the intermediary should refer exclusively to the identification of the level of knowledge/experience of the client without any additional obligation.

In any case - given the absence of a distribution agreement – non-governable products cannot be subject to "reporting" obligations to the manufacturer.

It should be emphasised that the imposition of Guideline-dictated rules on "non-governable" products would have important consequences because:

- it would make it extremely difficult for distributors to accept client orders for a large number of non-standardised financial products, issued and placed by third parties, due to the objective difficulty of acquiring the necessary information in time for determining the target market of each product;
- there would then be a "forced" and unmotivated restriction of the offer of executive services in the secondary market: many financial products (especially when the issuer is less known, or when the amount issued is not very substantial) would end up being processed only by the distributors who had placed them;
- it would also be difficult to explain to the client such a refusal to provide the service, without being able to precisely verify its inclusion or not in the target market;

- there would be a real possibility of legal disputes;
- the restriction of the services offer would impact on the market liquidity of many financial instruments, which would be traded on the secondary only by the distributors who had placed them;
- it would limit the development of forms of independent investment advice and/or open architecture, which the distributors might consider appropriate in order to achieve more effective management of conflicts of interest.

On the other hand, the proposed solution does not rule out that distributors can decide that some categories of products are not marketable to its clients and then choose to never offer them, not even through the executive services. This would however be a voluntary choice (i.e. not dependent on the lack of information).

In this way the distributors would still be required to determine ex-ante the target market (even if negative) for all categories of distributed products through a decision-making process involving top management

Q4: Do you agree with the suggested approach on hedging and portfolio diversification aspects? If not, please explain what changes should be made and why.

The answer, as a consequence of what is described above, must refer only to “governable products”. In the case of the provision of personal recommendations, at the request of the client, concerning "non-governable products" and with portfolio suitability assessment in order to provide a service with higher added value to the client, even in the absence of specific distribution agreements, deviations from the potential target market may occur for the same reasons as for any deviation from the target market in the case of the provision of investment advice for governable products; however, in the case of non-governable products, the absence of a distribution agreement does not enable the performance of activities that imply a direct relationship with the manufacturer.

Paragraph 30 of the background to the Draft Guidelines makes clear that the target market assessment, as provided by the manufacturer, is essentially focused on the individual product manufactured and, therefore, cannot take into account the personal features of each potential client and, in particular, the general situation of his personal investment portfolio.

Subsequently, the same paragraph explains that the personal features of each client can in any case be properly considered and assessed by the distributor providing its investment services to the client, for example in the context of the suitability (or appropriateness) test.

This, according to the proposed text, could in some cases lead to permissible deviations between the general target market of a product (as identified by

the manufacturer) and the eligibility of that product for a certain client, provided that the recommendation by the distributor complies with all other applicable legal requirements, especially in terms of suitability as an instrument for the management of conflict of interests.

According to the view proposed by the document under consultation, however, such deviations from the target market identified by the manufacturer:

- shall not occur on a regular basis;
- shall be properly documented to the client in the context of the suitability report;
- shall never occur in those cases where there are significant conflicts of interest at the point of sale (due, for example, to self-placement or inducements).

The situation described above, from our point of view, does not properly take into account more recent and sophisticated developments in the operating model implemented by investment firms for the provision of investment services to clients, in particular investment advice.

Many firms, in fact, are currently offering their clients (non-independent) investment advice according to a portfolio approach, in which any recommendation issued takes into account not only the personal characteristics of the client (in terms of knowledge and experience in investments, financial situation, investment objectives and risk profile) but also the general situation of its investment portfolio, in terms of underlying financial risks, degree of diversification and financial efficiency.

This type of investment advice aims in fact to ensure that the client's portfolio, regarded as whole, is the most consistent with the financial profile of the client.

Under the operating model described above, it could happen that financial instruments recommended to clients have some specific features (e.g. liquidity degree or risk profile) that:

- considered individually, would not be fully aligned with each of the personal characteristics of the client;
- considered in the context of the client's portfolio, would render the portfolio itself, considered as a whole, consistent with the financial profile of the client.

The operating model described above, even if designed to further enhance both the quality of the service provided to clients and the degree of protection granted to investors by MiFID rules, could not always fit in with the general obligation for distributors not to deviate from the target market identified by the manufacturer in relation to each product if not exceptionally and in limited cases.

Investment advice taking into account the overall situation of the client portfolio may not only exceptionally consider as suitable for that client financial products whose target market – being based on the individual product – would not fully fit with the characteristics of the client.

The explanatory text of the Guidelines, and the Guidelines themselves, therefore, should consider the above, granting more flexibility, with respect to the target market identified by the manufacturer, to those investment firms providing investment advice according to a portfolio approach, provided, of course, that all other applicable legal requirements are fulfilled, and that the distributor:

- taking into due consideration the suggested distribution strategy of the manufacturer, provides the manufacturer with ex ante information about the portfolio approach provided by its investment services model. This resolves the need to provide the manufacturer with information on actual deviations from the potential target market just because no such deviations would occur;
    - adopts appropriate blocking mechanism within the suitability assessment (i.e. checking: the product's saleability according to the client's level of knowledge and experience; the portfolio according to the other categories described in the Guidelines in order to protect the best interests of the client but also to diversify and protect investments while continuing to respect objective and predetermined parameters that must have been plotted (such as: concentration control by the issuer, concentration in complex products control, diversification control);
- provides adequate ex-ante disclosure on the service model described above in the contract signed by the client. On the contrary, no additional information is required on this regard within the suitability report.

In addition to the above, it shall be noted that, in cases described above, there would be no reasons to prevent firms from deviating from the target market identified by the manufacturer in those cases where significant conflicts of interest exist (due, for example, to self-placement or inducements).

As a matter of fact, the provision of investment advice pursuant to the operating model described above – jointly with all other applicable legal requirements – would represent an effective instrument for investment firms to manage their possible conflicts of interest as distributors, also enhancing the degree of protection granted to clients through the implementation of systems for suitability assessment, thus preventing clients from carrying out any transactions that have been considered as unsuitable for them (so called "blocking suitability").

This is confirmed also by the circumstance that, under the MiFID II framework, the provision of non-independent investment advice to clients (jointly with the conditions specified by article 11, paragraph 2, letter *a*), numbers *i*) and *ii*) of the Delegated Directive), may justify inducements by granting clients with an additional or higher level service.

The explanatory text of the Guidelines, and the Guidelines themselves, therefore, should take the above into account, by deleting or clarifying the ban imposed on distributors with regard to deviations from the target market in situations where a conflict of interests exists.

Having said that, considering that the proper portfolio diversification is key to any client, regulatory changes should promote it instead of inhibiting it and deviations from the potential target market that result from proper portfolio diversification should not be taken as exceptional but fundamental for investor protection. We propose, therefore, to delete the idea that the perspective of the target market assessment is the individual product.

Q5: Do you believe further guidance is needed on how distributors should apply product governance requirements for products manufactured by entities falling outside the scope of MiFID II?

As already anticipated in our answer to Q3, the implementation of product governance rules by distributors must take into account the need to allow certain adaptations/adjustments due to the fact that manufacturers are not always subject to MiFID requirements (such as, for example, companies managing common investment funds and corporate bond issuers). In this case it becomes necessary to admit that the application of product governance rules by distributors must be less rigid and precise compared to the "standard" regime (products issued by MiFID entities), in order to guarantee operational continuity to distribution and negotiation models and to avoid impasse situations, particularly in the case of simple products. Obviously in this case it is necessary to take into account the difference between governable products – where the existence of a distribution agreement with the manufacturer may facilitate the collection of information for defining the distributor target market – and non-governable products, since in the latter case, the absence of a direct relationship with the manufacturer may make it impossible to get information directly from the manufacturer.

In order to take account of such cases, the Guidelines should:

- clarify explicitly (in the first bullet point of paragraph 52, "*target market definition*") that the distributor must determine the target market according to the categories listed in paragraph 16, as far as it is possible. It should therefore be admissible, in the absence of all the specific information related to the categories provided for in the Guidelines (because it is not public or not formalised through specific

bilateral agreements by the non-MiFID manufacturer in terms of product governance), to define a target market:
    - based not on all the required categories, but only on some of them, or;
    - based on information and assessments, also of risk, made directly by the distributor;
- specify (in the second bullet point of paragraph 52, "*information gathering process*") that the reasonable step of "*entering into an agreement*" does not apply in relation to all those products that are negotiated by the distributor in the secondary market stage, without a distribution agreement (e.g. bonds listed on the stock exchange and requests from clients in the area of executive services);
- delete paragraph 54 because the measure is deemed to be excessive and disproportionate compared to the end purpose of product governance, and, given also that the absence of information does not depend on the distributor;
- specify that in such situations there is no return flow from the distributor to the manufacturer, since the latter has no formal obligation to review the product.

Q6: Do you agree with the proposed approach for the identification of the 'negative' target market?

According to the ESMA consultation document, the identification of the "negative" target market by manufacturers and distributors entails the identification of that client segment for whom the created and/or distributed investment products are not compatible. There could indeed be situations where the product, depending on certain circumstances and where all legal provisions are fulfilled, is sold outside of its target market. However, the supervisory authority requires that these situations be justified in relation to the individual case and properly documented.

Because the negative target market constitutes a specific indication of those clients for whose needs, features and goals this product is not compatible and for whom the product should consequently not be distributed, the sale to investors within this group should be, according to ESMA "a rare event" and the justification for deviating from these principles should therefore be meaningful and widely supported compared to the justification of a sale outside of the positive target market.

The approach adopted by ESMA to identify the negative target market is in our opinion acceptable if ESMA grants the application to include the assessment of the overall composition of the client portfolio among the criteria for the definition of the positive target market by the distributor. When the overall portfolio assessment was taken into account for the purposes of inclusion of clients in a given target market, it would, in contrast, have been beneficial to have criteria for excluding certain clients from this

target market on the grounds of specific subjective features (such as, for example, complete lack of knowledge and/or experience of a particular type of product), thus balancing the definition of the positive target market under an approach based on the assessment of the total investment made by the customer.

Q7: Do you agree with this treatment of professional clients and eligible counterparties in the wholesale market?

With reference to eligible counterparties, for whom it is suggested that the identification of target market criteria be less stringent (such as knowledge of the markets and the commercial viability of individual investment decisions), there is a need to specify how such criteria could then be subject to control. Otherwise, a workable solution may be the assumption of principle on the existence of the target market criteria in relation to eligible counterparties.

We stress the importance of the provision that in the definition of the target market the end client must be taken into account; for this reason, we think it appropriate that ESMA should further clarify that the reporting requirements regarding the target market apply to the manufacturer and the intermediary in charge of distribution to end clients, while the other parties who buy to resell ("resellers") should not be considered for targeting purposes.

Q8: Do you have any further comment or input on the draft guidelines?

In relation to product governance rules and the target market required by investment firms we would like ESMA Guidelines to take in to account the peculiarities of the portfolio management investment service.

In our view this investment service cannot be merely considered as a form of distribution of financial instruments. Portfolio management aims to invest client assets in accordance with the contractual mandate given by the client relating to the specific portfolio management objectives and its investment rules. Consequently, the portfolio manager does not market or offer financial instruments, but rather fulfils a complex investment service by purchasing and selling financial instruments in the name of and behalf of the client through its mandate.

It is therefore consistent with the specific nature of this investment service to conceive the product governance obligation at the portfolio level rather than as financial instruments to be purchased through the portfolio manager.

In relation to the above, we believe that it would be necessary to reconsider the ESMA proposal in paragraph 43 of the Draft Guidelines where it is said that "*if distributors intend to approach clients or potential clients in any way, to recommended or actively market a product or consider that product for the provision of portfolio management, it is expected that a thorough assessment of the target market is always conducted*".

Moreover, it is important to establish the requirement that, in the case of investment portfolio management, the firm providing the service should apply the manufacturer product governance provisions to the portfolio management. The application of the rules as a manufacturer seems to be borne out also by Final Report – ESMA's Technical Advice to the Commission on MiFID II (ESMA 2014/1569, p. 52).

So, when the investment portfolio is distributed by a firm other than the investment firm that provides the investment portfolio service, the distributor should take into account the "potential" target market defined by the investment manager and identify the effective target market based also on the characteristics of its own clients.

Q9: What level of resources (financial and other) would be required to implement and comply with the Guidelines (market researches, organisational, IT costs, training costs, staff costs, etc., differentiated between one-off and ongoing costs)? If possible please specify the respective costs / resources separately for the assessment of suitability and related policies and procedures, the implementation of a diversity policy and the guidelines regarding induction and training. When answering this question, please also provide information about the size, internal organisation, nature, scale and complexity of the activities of your institution, where relevant.

The scope, approach and parameters of the requirements have significant implications for implementation costs, as no infrastructure currently exists to deliver this. The increase in costs (initial and recurrent) would be particularly marked if the governance product rules were fully applied to all intermediate products by investment firms on secondary markets when providing executive services to the client. In particular, we believe that product testing and monitoring will be the more expensive process.

Moreover we point that the following implementations will be necessary to comply with the rules:

- to strengthen information collection mechanisms, especially in the case of manufacturers not subject to MiFID requirements;
- to modify existing distribution agreements;

- to implement an infrastructure to mark all the steps followed in all the processes designed to be compliant with product governance requirements.