



OP FINANCIAL GROUP RESPONSE - DRAFT GUIDELINES ON MIFID II PRODUCT GOVERNANCE REQUIREMENTS

OP Financial Group is Finland's largest financial services group. It provides its customers with the best loyalty benefits and the most extensive and diversified range of banking, investment and insurance services. The Group has three business segments: Banking, Non-Life Insurance, and Wealth Management.

The Group consists of some 180 independent member cooperative banks and OP Cooperative which they own, including its subsidiaries and closely related companies. Group's operations are based on the cooperative principle - cooperation and sharing the fruits of success with everyone. OP's mission is to promote the sustainable prosperity, safety and wellbeing of their owner-members, customers and operating regions. Our long-term customer-centred approach also enables continuous renewal. We develop our services and products to meet our customers' needs.

1 GENERAL COMMENTS AND KEY MESSAGES

The OP Financial Group welcomes the opportunity to comment ESMA Draft guidelines on MiFID II product governance requirements. Further to our specific comments below, we endorse the response drafted by the European Association of Co-operative Banks ([EACB](#)). Our key messages are:

Harmonised approach on target market. – MiFID II aims at harmonised investor protection rules across the EU. Further guidance on a completely new item concerning target market of financial instruments is therefore necessary and welcomed. The level III should aim at simple, robust and harmonised set of guidelines that facilitate smooth cross-border distribution of financial products and services. No domestic gold-plating should be allowed.

Hedging and portfolio diversification. – Portfolio diversification and hedging are very important elements when considering impact of target market rules. We generally agree with ESMA's analysis but encourage to incorporate this text into final guidelines.

Secondary markets and manufacturers falling outside the scope of MiFID II. – Large number of simple financial instruments, such as shares and bonds listed on regulated markets, are issued ("manufactured") by firms that are not authorised MiFID investment firms. According to Level II Directive investment firms distributing these instruments shall have in place effective arrangements to ensure that they obtain sufficient information about these financial instruments. New guidelines should clarify, that proportionality principle should apply. It should be sufficient to refer publicly available initial and on-going disclosure based on Transparency Directive and forthcoming Prospectus Regulation.

Digital distribution of financial instruments. – Distribution of financial instruments under MiFID II can be based on execution only, appropriateness- or suitability test regimes. We take note of the regulatory debate that aims at reducing the scope of sales under execution only or appropriateness regime and channelling it to advices sales under suitability regime. However, digital distribution of financial instruments is channelling the demand to the opposite direction, either execution only or appropriateness test based sales. The EU Commission has ambitious goals to accelerate digitalisation, financial technology and digital distribution of financial services. The new guidance should not, directly or indirectly, question the scope of distribution channels.

Analysis of distributors client base. – Distributors should base their own target market on information and knowledge of their own client base. We agree with this general provision but question the level of detail on the "thorough analysis".



DETAILED COMMENTS

Q1: Do you agree on the list of categories that manufactures 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.

Yes, we broadly agree on the list of categories with following more detailed comments.

On point (e) Clients' Objectives we question, whether "expected investment horizon" is client objective *per se*. In case it is deemed necessary we would prefer to have it as an independent category.

On point (f) Clients' Needs we note that demand for special features such as "green investment" and "ethical investment" is growing. However, it should be noted that measuring these parameters might prove challenging in practice. Therefore, we suggest to remove the point from the list of categories.

We note that the question on "green and sustainable investment" is not mature and standardised enough. For example, the PRIIPs Regulation [No 1286/2014](#) does not cover this question. Pursuant Article 33 "costs and possible benefits of introducing a label for social and environmental investments" are subject to further review by the end of 2018.

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

Yes. We agree that the target market assessment should be done in an appropriate and proportionate manner. It is important to consider the nature of investment product. The guidance should not complicate digital distribution of simple "mass retail products". The main focus should be on more complex products.

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

We agree that distributors should base their target market on their information and knowledge of their client base and the information received from the manufacturer (where relevant). We also agree that the distributor has a general duty to specify the target market in more concrete terms.

However, we question the level of detail in paragraph 33, according to which distributors should "conduct a thorough analysis of the characteristics of their client base" based on various databases. In our view, introduction of such an extensive requirement is not in line with Level I and II directives. Information gathering requirements could potentially complicate digital distribution of financial instruments.

We suggest that investor protection is best promoted via forward looking suitability and appropriateness tests when investment services are offered. Detailed analysis of previously executed trades is burdensome and could potentially produce redundant information.

Furthermore, transferring information based on anti-money laundering questionnaires etc. would potentially breach anti-money laundering rules. According to the fourth AML Article 41(2) "Personal data shall be processed by obliged entities on the basis of this Directive only for the purposes of the prevention of money laundering and terrorist financing as referred to in Article 1 and shall not be further processed in a way



that is incompatible with those purposes. The processing of personal data on the basis of this Directive for any other purposes, such as commercial purposes, shall be prohibited.”

Data protection issues could potentially arise as well in case the client information is used without client consent.

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.

Portfolio diversification and hedging are very important elements when considering impact of target market rules. We generally agree with ESMA’s approach on p. 9–10. Indeed, it is very important to consider the client portfolio as a whole with regard to riskiness and ability to bear losses. If the focus is too much on flatly matching individual products to clients overall preferences, instead of matching the products to their portfolios, there is a risk that some abilities to build diversification and effectiveness into the portfolio are lost. As a result the client portfolio might turn out sub-optimal. I.e. too rigid target market rules might hinder the ability to diversify client portfolio.

Furthermore, too much focus on individual products could incentivise manufacturing of purpose-built packaged investment products.

We take note that hedging and portfolio diversification issues explained only in "Background of the draft guidelines". However, these considerations are not expressed in "Draft guidelines". In our view this approach is unclear and should be clarified. We suggest to "up-grade" relevant text on page 9-10 (at least paras. 29 and 30) to official guidelines.

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?

The new guidance should not complicate investments in non-complex instruments, notably ordinary shares listed on regulated markets. Further red-tape would be clearly against the goals of the EU Capital Markets Union project.

For listed shares and similar non-complex instruments the "distributor" (such as bank or investment firm providing on-line trading on listed shares) should be able to rely on publicly available information without additional "information gathering process". It should be sufficient to refer on public information based on general regulatory obligations of listed companies. For example, pursuant to Prospectus Directive and forthcoming Regulation prospectuses are available on webpages of supervisors. Furthermore, the investor should follow the on-going disclosure of the issuer based on the EU Transparency Directive. Similar issues could potentially arise with other listed instruments, such as ETFs, warrants etc.

We also highlight, that the guidance should not complicate the professional bond and other non-equity trading that is mainly conducted on the OTC / SI –basis.

We agree with the reference to proportionality on paragraph 53. Duty to gather information should be in line with the complexity of the product.

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



The concept of negative target market is in our view mainly the tool of product manufacturer. In case the concept is introduced, we highlight our comments on Question 4 and portfolio diversification aspects.

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

We agree with the distinction of professional clients as intermediaries and professional clients as end clients. It is our understanding that, although the product governance requirements apply also to professional clients and eligible counterparties, the focus of the guidelines is in the retail business. Considering the knowledge and experience of professional clients, it is important that a high level and proportionate approach is allowed with regard to the product governance requirements for professional counterparties. There are slightly lighter disclosure requirements for wholesale securities under the Prospectus Directive and the forthcoming Regulation. Therefore, we consider that the product governance requirements should take a similar approach to wholesale business.

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

Yes. We have a very important comment on paragraph 22 under heading “Articulation between distribution strategy of the manufacturer and its definition of the target market”.

Distribution of financial instruments under MiFID II can be based on execution only, appropriateness- or suitability test regimes. We take note of the regulatory debate that aims at reducing the scope of sales under execution only or appropriateness regime and channelling it to advised sales under suitability regime. The EU Commission has ambitious goals to accelerate digitalisation, financial technology and digital distribution of financial services. The new guidance should not, directly or indirectly, question the scope of distribution channels.

We have serious concerns that paragraph 22 and references to “preferred acquisition channels (face-to-face, via telephone, online)” would undermine the scope of legitimate distribution channels based on MiFID II Level I Directive. Therefore, we suggest to delete the paragraph 22.

OP Financial Group

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