

Vienna, October 6th 2022

CONSULTATION PAPER ON REVIEW OF THE GUIDELINES ON MIFID II PRODUCT GOVERNANCE REQUIREMENTS (ESMA35-43-3114)

Zertifikate Forum Austria ("ZFA") is the representative of the issuers of structured investment products to retail consumers in Austria.

ZFAs response:

Q2. Do you agree with the suggested approach on the identification of any sustainability-related objectives the product is compatible with? Do you believe that a different approach in the implementation of the new legislative requirements in the area of product governance should be taken?

ZFA agrees with ESMA's approach to align the definition of sustainability-related objectives with the definition of "sustainability preferences" according to Article 2(7) of the MiFID II Delegated Regulation. We also see no need for further clarifications or a different approach for structured products as the specification of sustainability-related objectives for structured products according to 7a-7c MIFID is in our view well feasible.

As to the question whether a manufacturer should specify sustainability-related objectives of a product by referring to the sustainability data of either the issuer of the product, or the product itself (para. 27), there is no one size fits all-approach. In certain cases, it should even be possible to combine both concepts. For example, the manufacturer of a structured product that is issued as a bond and has a basket of shares as underlying (derivative component) could specify the sustainability-related objectives of that product by making reference to both the bond and the derivative component. The sustainable characteristic of the bond component could e.g. derive from the issuer's use-of-proceeds whereas the sustainable characteristic of the derivative component is stemming from the demand impact which is caused by the issuer's risk reducing hedging practice. Insofar a sustainable structured product should be treated as an indirect investment having a similar effect to any secondary market acquisition, including those exercised by investment funds such as UCITS and AIFs.

Against this background, we strongly encourage ESMA to go further down the road and allow for different concepts of specifying sustainability-related objectives along the broad product range.

Q4: Do you agree with the suggested guidance on complexity in relation to the target market assessment and the clustering approach?

In general we wish to point out that the assumption that due to complexity stricter rules shall per se apply is not reasonable as i.e also ESG features add complexity to a financial product. In this regard we want to refer to the findings of the “Study on disclosure, inducements and suitability rules for retail investors” (hereinafter “Study”) published by the European Commission in 2022 whose findings clearly indicate that the existing (disclosure) rules, such as the EU PRIIPs Regulation, lead to structured products having shown no misleading potential while performance and cost information as rather easily understandable (see Study, page 188). This finding of the study is clearly evidencing that complexity alone does not justify a tighter regulatory corset may it be through the target market rules or other provisions.

We explicitly welcome the recognition of the clustering approach for the definition of a target market for types of financial instruments which bear sufficiently comparable product features (paragraph 27 of the consultation).

However, the broad and undifferentiated exclusion of OTC derivatives or structured products from the clustering approach is not justified (see last sentence of paragraph 27 of the consultation).

In both asset classes the overwhelming number of products on the market are by practical necessity highly standardized and only certain product features such as term or underlying of the instrument may differ while the main product characteristics and risk factors remain unchanged. As manufacturers typically issue a large number of such products a high degree of operational automation of the issuance process is required which, in turn, leads to the standardization of product features enabling a uniform assessment approach for the target market.

From a technical point of view the implementation of a clustering approach does not restrict the manufacturer to define specific target market criteria on a product level, if necessary. For example, manufacturers of structured products regularly derive the risk level or risk/reward profile of an instrument from the respective SRI of the PRIIPs KID of such instrument and, thereby, tailor these important target market criteria to the level of the individual product. Therefore, a clustering approach can also be suitable for OTC derivatives or structured products as a clustering approach does not mean that all product features are assessed for target market purposes on a generic product type level only.

Furthermore, the proportionality approach also justifies that the clustering approach for products which are not marketed to retail clients can be applied with less granularity. This particularly applies to OTC derivatives distributed to professional clients and eligible counterparties.

We, therefore, request that the exclusion of OTC derivatives or structured products shall not be reflected in the final guidelines. The requirements set out in the consultation (paragraph 27) that “homogenous clusters” must be identified and that “the more complex the underlying products of a cluster become, the more granular the clustering should be” are prudent standards for the target market definition which can be applied to all asset classes. A per se exclusion of certain asset classes on general terms without a material assessment of the specific product governance process of a specific manufacturer by the competent authority is neither necessary nor justified.

With regard to the newly introduced number 28 we suggests clarifying that the mentioned factors might need to be considered, but not necessarily all reflected in separate clusters. More generally these factors should be understood as non-exhaustive and non-binding examples. From a more general perspective, we would like to stress how important it is that the key factors are not cumulative in order to allow for a certain degree of flexibility in the clustering approach.

Q10: Do you agree with the suggested approach on the negative target market assessment in relation to a product with sustainability factors? Please also state the reasons for your answer.

We agree with ESMA's approach that manufacturers should not be obliged to consider the sustainability-related objectives of the product when performing a negative target market assessment. This would jeopardize the overarching goal of the European Sustainable Finance regulation to make products with sustainability factors easily available for all kinds of clients, including those that do not have explicit sustainability preferences.