FINAL

eusipa EUROPEAN STRUCTURED INVESTMENT PRODUCTS ASSOCIATION

EUSIPA (aisbl-ivzw)
Bastion Tower Level 20
Place du Champ de Mars 5
B-1050 Brussels
Belgium

Phone +32 (0) 2 550 34 15
Mail secretariat@eusipa.org
Web www.eusipa.org

To

Mr. Paul Rosenmöller
Chairman
Autoriteit Financiele Markten (AFM)
The Netherlands

Brussels, 31 March 2017
PER MAIL

Ref.:

Market consultation initiated by the AFM on product intervention measures aimed at certain Financial Products thereby exercising powers entrusted under a planned new article 56a of an amended *Royal Decree* under the Dutch Law on Supervision of Financial Undertakings ("Wet op het financieel toezicht")

Dear Sir,

By way of this letter, the European Structured Investment Products Association (EUSIPA) in their capacity as umbrella association for issuers of structured products seeks to outline the position of the industry with regard to aforementioned consultation. (More details on EUSIPA you find at the back end of the document.)

We are highly concerned about the AFM project of limiting the marketing of certain financial products (hereinafter called "**marketing ban**") based on a specifically created new article 56a in the Dutch law on supervision of financial undertakings ("*Wet op het financieel toezicht*") and executed by amending the Further Regulation on Market Conduct Supervision ("*Nadere regeling gedragstoezicht financiele ondenemingen Wft"*) by inserting into section C 2:8 of aforementioned legal act the following:

" (…)
a) cash warrants;
d) convertible bonds that are converted, subject to predetermined circumstances, into shares or for which, subject to predetermined circumstances, the principal or interest payments are written down in full or in part;
e) derivatives contracts consisting of an underlying value and the financing of the underlying value, unless the financial leverage of the derivatives contract when it is offered is lower than 10 and the ensuing risk for the consumer is not higher than the amount invested by the consumer; (…).".

For the sake of easier readability the products captured under a), d) and e) are in the following referred to as "**certificates, warrants and turbos**".

President
Heike Arbter

Vice-President
Roger Studer

Secretary General
Thomas Wulf

Board of Directors
Jean-Philippe Cavrois
Alain Flas
Jyrki Iisalo
Zak De Mariveles
Erik Mauritz
Dr Hartmut Knüppel
Dario Savoia
Jürg Stähelin
Frank Weingarts

Bank Account
ING Belgium
IBAN: BE 53 310177409753
BIC: BBRUBEBB

International Non-Profit Association
(Association Internationale Sans But Lucratif)
R.L.E. (Brussels): 0806.241.432

As stated, our concerns relate in particular to the application of the marketing ban to structured notes in the form of certificates, warrants and turbos and are rooted mainly in the following:

1. The **absence of any evidence**, empirical or other, supporting the envisaged marketing ban in the area of certificates, warrants and turbos,

2. The **insufficient distinction between the financial instruments** covered by the marketing ban thereby neglecting technical features, relevant markets and, partially linked to the before, transparency towards and risk exposure of retail investors with regard to certificates, warrants and turbos,

3. The **inadequacy of the regulatory impacts** of the marketing ban in relation to its intended purpose on certificates, warrants and turbos, and last not least,

4. Foreseeable **upcoming conflicts with EU law** with regard to banning the marketing of certificates, warrants and turbos.

In more detail:

1. Absence of evidence

The marketing ban is meant to block financial service providers from engaging in product-specific marketing activities with retail investors. Prohibiting marketing activity touches on a core business practice of any free-market economy. It therefore needs substantial justification.

We are of the view that the reasoning outlined by the AFM in the documents consulted upon does not suffice this requirement. What is needed in terms of the wide-ranging impact of the envisaged marketing ban is quantitative evidence in relation to the specific Dutch market situation that covers the various asset classes/product types mentioned. It should have been gathered through advance-defined and transparent processes designed to establish a base of evidence data which can be tested on their correctness by independent external experts.

Such base of evidence however has not been established by the AFM, at least not with regard to certificates, warrants and turbos.

Independent of the AFM's failure to deliver such evidence base for the marketing ban, EUSIPA and its local member NEDSIPA are not aware of any situation in the Dutch market which would deliver such evidence with regard to the Dutch market of certificates, warrants and turbos.

To our knowledge there have throughout the last years neither been mis-selling incidents, small or large-scale, nor investor complaints above average level compared to regular fund or deposit products, nor has there been a market failure, e.g. in terms of certificates, warrants or turbos performing widely against investor expectations.

Finally we wish underline that the burden of proof for the existence of a situation that requires regulatory intervention clearly needs to lie with the authorities. Non-withstanding this general principle of public law the industry surely would have been supportive of any effort put forward by the regulatory authorities to establish the factual situation/base of evidence so to better judge whether a regulatory intervention is necessary. However, such effort was to our knowledge never undertaken by the AFM with regard to the marketing ban in question here.

2. Insufficient distinction of financial instruments

The envisaged ban would apply its legal consequence, namely the prohibition of marketing activity, without any levelling or further differentiation, to all products it covers by way of numerical listing.

EUSIPA is convinced that, independent of the absence of evidence justifying the intervention (see above point 1), such undifferentiated application in itself is legally flawed. This insufficient distinction relates in particular to the named products' different technical features, different relevant markets and, partially arising from before, their difference in terms of transparency towards and risk exposure of retail investors.

EUSIPA wishes to stress the relevance of the insufficient differentiation with particular regard to certificates, warrants and turbos.

Whilst many European countries (France, Italy and others) have in the recent months and years restricted the marketing/sale of non-securities such as binary options, Contracts for Difference (CFDs) and certain FOREX and virtual currency products, or intend to do so (UK) they have not done so for listed securities, e.g. certificates, warrants and turbos. A reason for this may be that certificates, warrants and turbos are distinctly different from the aforementioned non-securities and illustrated by some facts set out in an exemplary fashion hereunder:

a) The maximum loss an investor can incur with certificates, turbos and warrants is limited to the initial investment, which especially with turbo and warrants generally remains a relatively small amount;
b) Most products sold in Holland are listed on the Euronext Exchange, a regulated market licensed by the Dutch Ministry of Finance ensuring the application of European and Dutch rules and their supervision, including negotiation and liquidity in the secondary market;
c) Certificates, turbos and warrants sold to retail are publicly offered and hence strictly require prospectuses all of which are approved by regulatory authorities within The Netherlands or other EU countries. The distribution of these products is already today regulated by MiFID rules meant to ensure that the product is sold only to appropriate retail customers whose investment needs and strategy it needs to suit;
d) The hedging of positions by the issuer does not conflict with the interests of the client. Contrary to common belief, the economic model of warrants, certificates and turbos is not based on a zero-sum game. The issuer of securities does not intend to benefit from customer anticipation errors. Its economic model relies, as the markets of professionals, on its ability

to hedge the risk initiated by the position of the investor, benefiting from a size effect ("global hedging");

e) This risk hedging policy is opposed to the practice of several players in the universe of CFDs and binary options. The latter have applied risky economic model, positioning themselves as direct counterparty to the client positions, without hedging.

3. Inadequate impacts

Generally, EUSIPA wishes to indicate our surprise that such wide-ranging marketing ban as proposed by the AFM are being considered in the Dutch legislative framework at all with regard to certificates, warrant and turbos. These products have been widely issued, marketed, sold and traded in Holland for about 25 years. Up until now The Netherlands, in line with a few other European countries, have been known within the European Union as market place following a sensible approach to financial sector regulation, also when it comes to retail financial products. In the area of derivatives and structured products regulation the administrative focus seemed rather to have been put on ensuring that issuers and distributors had the necessary internal governance provisions in place which ensured a financial product being sold to the customer it was meant for and wanted by. This continues to be in our eyes the most efficient approach for regulating retail markets.

Issuing a wide-ranging marketing ban without further evidence signifies to our understanding therefore a fundamental change to the before, which we would regret.

However, even when assuming that the marketing ban is being implemented despite the regulatory tradition in Holland it would, in our eyes, abandon the path of good law-making as it inflicts a burden on market participants which would not have been needed given its underlying intention, as there were other, equally effective means available than an outright marketing ban.

EUSIPA would be keen to understand in particular, why instead of seeking to impose a marketing ban, self-governance rules/restrictions have neither been discussed with the industry nor otherwise been considered. This failure is the less understandable especially in the Dutch market context, given that self-governance restrictions in the area of turbos and warrants had been successfully implemented by the industry before[1].

4. Upcoming conflict with European Union law

Going forward the envisaged marketing ban finally runs the danger to conflict with European law. As your services are certainly aware the European Markets in Financial Infrastructure Regulation (MiFIR) will come into force in January 2018. The provisions of this regulation set out in article 42 the intervention powers of national authorities. We do not share in that context the view brought

[1] We refer here in particular to the self-governance of issuers represented by our Dutch member association NEDSIPA to commit to respect a minimum distance between the underlying price and the stop-loss of Turbo leverage products (so-called "issuance buffer") resulting effectively in a leverage lower than 50.

forward by the Dutch ministry of Finance in their consultation on the insertion of a new article 56a, that marketing activities ("reclame-uitingen"/advertising) are not covered by MiFIR. Advertising is an essential business practice inherently linked to offering services in a market economy. Consequently, the marketing ban will fall into an area which is going to be covered as of January 2018 by MiFIR as new legal framework. Enforcing a national provision shortly before applicable legal rules change fundamentally does need to be justified on reasons of urgency. As stated before, reasons that require intervention are not discernible to us as in the Dutch market of certificates, turbos and warrants.

Adding to this, the hastened enforcement of the planned marketing ban would for all stakeholders create a high level of legal uncertainty already by the fact that, should it be passed as foreseen still in 2017, it needs to be reviewed on its legal validity under MiFIR as of January 2018.

Most importantly though we assume the planned marketing ban would fail to comply with the future MiFIR rules on market intervention, at least insofar as it applies to certificates, warrants and turbos.

> Article 42 MiFIR foresees in section 2 (a), (i) that any intervention will need to be justified "*on grounds that give rise to significant investor protection concerns or pose a threat to the orderly functioning and integrity of financial markets or commodity markets or to the stability of whole or part of the financial system within at least one Member State.*"

As mentioned before above we do not see any such grounds in the area of certificates, turbos and warrants. Given the severity of conditions mentioned in the quoted article 42 section a), their consideration as reasoning in a regulatory intervention would in our eyes need to be outlined by the AFM in the format of quantitative evidence, which as mentioned before is lacking here completely.

> Any action taken under the future article 42 MiFIR further according to section 2 (c) would need to be "*proportionate taking into account the nature of the risks identified, the level of sophistication of investors or market participants concerned and the likely effect of the action on investors and market participants who may hold, use or benefit from the financial instrument (…)*".

EUSIPA is convinced that the marketing ban would not fulfil this condition either given that, as outlined before, certificates, warrants and turbos have certain features which are distinctly different from other, especially non-security instruments. In context with their decade-long market presence and inclusion in retail-directed marketing activities they form an established part of the retail product landscape available to Dutch and other European retail investors. (For more details on the features of the relevant products and markets please see above point 2.)

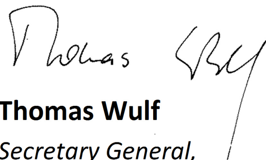
The planned marketing ban would thus be very likely incompatible with the future MiFIR intervention rules set out in article 42.

Summing up we think that the marketing ban envisaged by the AFM should fundamentally be re-considered at least insofar as certificates, turbos and warrants are concerned.

We hope that you find above arguments a useful contribution to the discussion and thank you for their consideration in advance.

Please do not hesitate to get back to us should you have any questions,

Sincerely,



Heike Arbter
President,
EUSIPA

Thomas Wulf
Secretary General,
EUSIPA

EUROPEAN STRUCTURED INVESTMENT PRODUCTS ASSOCIATION

Background on EUSIPA

EUSIPA, the European Structured Investment Products Association was set up in 2009 and is the European umbrella organisation for the issuers of structured products, which includes investment and leverage products alike. Currently, EUSIPA has nine member associations, which are the relevant national trade bodies from Austria (ZFA), Belgium (BELSIPA), France (AFPDB), Germany (DDV), Italy (ACEPI), Sweden (SETIPA), Switzerland (SVSP) The Netherlands (NEDSIPA) and the United Kingdom (UK SPA).

EUSIPA seeks to promote initiatives that enhance the proliferation of market standards and support the transparency of the structured products marketplace. A key tool offered and managed by EUSIPA in that context is the EUSIPA Derivative Map©, the world-wide only mapping of the most prevalent structured products types. It is aimed at professionals and widely used by issuers, distributors and many regulators. The current version can be found here:
http://www.eusipa.org/images/Presse/European_map_20160530_2016.pdf

The European retail markets in structured products are very diverse and differ in terms of listed/unlisted OTC and in terms of wrapper structures used (bonds, funds, insurance-linked products). For the retail markets in structured notes EUSIPA regularly publishes a market report whose latest version is available here:
http://www.eusipa.org/research-and-statistics/market-reports

The volume currently invested by retail clients in structured products within the EU-28 and Switzerland is estimated at Euro 450 billion.

Please also visit our website under www.eusipa.org for more information.