EFSA

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Retail Investment Strategy – EFSA priorities

General comments

EFSA is a strong supporter of the policy objective of the CMU Action Plan on Retail Investment Strategy (RIS), i.e., to build retail investors' engagement and trust in EU capital markets.

However, it is important to underline that retail markets in EU differ; some are more sophisticated with a high degree of retail participation, whereas others are less mature. Therefore, when developing RIS, it is important to include proposals which are both targeted at facilitating and improving existing retail clients' **participation** on EU capital markets, and proposals which aim at encouraging participation of those who currently do **not yet participate** in the market, and for whom it is important to ensure continued access to advice and to increase financial literacy.

EFSA wants to emphasize the importance of ensuring that all amendments are subject to a **thorough analysis, consultation, impact assessment and consumer testing**. Focus should be on proposals which are evidence-based and bring a clear positive impact for retail clients, whilst avoiding proposals that could have unintended negative consequences for clients, investment firms or the EU capital market as a whole.

To ensure the attractiveness of EU capital markets it is furthermore important to consider the regulatory developments in UK and other third country jurisdictions. For instance, EFSA notes that it is under discussion to repeal PRIIPs and replace it with more flexible retail disclosure requirements.

Importance of different business models

According to EFSA, it is of utmost importance that the regulatory framework **allows for different business models to co-exist.** This means that retail clients should be able to have access to different types of services to serve their needs - both advisory and execution services – and that firms should be able to structure their fees according to how the local distribution network is organized in member states. **A regulatory framework that is based on a "one size fits all approach" will not create a competitive and efficient EU capital market, especially given the existing diversity of business models.** Moreover, the profile of retail clients differs among Member States with regards to wealth, financial and digital literacy as well as level of participation on capital markets.

Ban on inducements

EFSA **does not consider that a total ban on inducement would be beneficial** for the EU or consistent with the CMU objectives. In fact, we see clear risks that a ban would lead **to advice gaps and limit product offerings to retail clients.** Also, it would **negatively affect the competitiveness** of independent asset managers/investment firms to the benefit of larger institutions with in-house products. In addition, since there is no common interpretation across Member States about which payments are to be included in the concept of "inducement" or "third party payment," imposing a total ban could also have a number of **serious unexpected consequences,** e.g. for primary market transactions, with a negative effect on the real economy as a result.[1]

[1] See article 41 delegated regulation to MiFID II which suggests that a placing fee/underwriting fee is an inducement in relation to end-client which receives investment services and ESMA technical advice: https://www.esma.europa.eu/sites/default/files/library/esma35-43-2126_technical_advice_on_inducements_and_costs_and_charges_disclosures.pdf

We also strongly question using the UK and the Netherlands as case studies to justify a total ban in the EU. These two markets have specific characteristics that differ from most EU member states and their experience so far from a total ban is not convincing from an investor protection point of view. [2]

In the opinion of EFSA, it is important to keep in mind that the payment of an advice through inducement constitutes an affordable way for less wealthy clients to get access to advisory service that would otherwise not be available for them. Access to such services have become increasingly important during recent years, considering the complexity of disclosures required under EU-law, e.g. in the area of ESG-investments.

EFSA also wants to encourage EU policymakers to learn from the negative experience from the introduction of the MiFID II-rules on research unbundling. The financial research reform was imposed in MiFID II without clear evidence of a substantial market failure and despite the fact that the industry repeatedly expressed strong concerns that SME research coverage would decrease as a result of the new rules. Today, EU policymakers have realised that the desired outcome with unbundling rules was not achieved and are trying to fix the problem via Listing Act. However, since business models have already changed in EU it will be very difficult to get back to the starting point. In our view, this shows how important it is to take a cautious approach. In fact, instead of proposing a total ban on inducements, which could have very negative effects on the EU capital market, EFSA considers that focus should be to **improve the inducement regime within the current framework.** This could be done by clarifying and making the rules more coherent and by increasing the supervisory convergence (e.g., as regards "quality enhancement" and proportionate criteria), thus ensuring that fee disclosures become easier for retail clients to understand.

Appropriateness and suitability

In EFSA members experience, the MiFID II rules on **appropriateness and suitability** generally work well and we note that ESMA is doing a lot of work to increase the level of supervisory convergence. We were therefore very concerned by the Commission's targeted consultation in February 2022[3] which suggested substantial changes to the current regime, without presenting any evidence of a market failure. In our view, it is very important that the MiFID II framework **maintains the distinction between execution and advisory services**, considering that these services serve different needs for clients. A requirement to provide retail clients who receive execution services with a list of suitable financial instruments and a personal asset allocation strategy could in fact give them the impression of having received advice. This could be confusing as well as give rise to liability concerns etc. In EFSAs view, what is needed in this area is not more detailed rules but rather to continue the work on convergence which should be combined with more effective supervision from the NCAs.

Additional aspects of importance for retail investors in EU

EFSA notes that **action 8 in the CMU Action Plan** contains several topics which are important to include in the forthcoming RIS. In particular, we support:

- A review of the rules on **cost & charges** in MiFID II with the aim of reducing the complexity of the framework. Evidence show that retail clients are interested in price and total costs, not detailed breakdowns, or methods of calculation.[4] It would also be welcome with closer alignment between PRIIPs/MiFID II, as suggested by ESMA[5].

[2] https://www.fca.org.uk/publications/consultation-papers/cp22-24-broadening-access-financial-advice-mainstream-investments
[3] https://commission.europa.eu/system/files/2022-02/2022-suitability-appropriateness-assessments-consultation-document_en.pdf
[4] https://op.europa.eu/en/publication-detail/-/publication/5d189b3c-120a-11ed-8fa0-01aa75ed71a1/language-en
[5] https://www.esma.europa.eu/press-news/esma-news/esma-makes-recommendations-improve-investor-protection

- A horizontal approach regarding **electronic communications per default**, i.e., that the current MiFID II approach should be adopted in other regulatory frameworks as well. (If needed, this could be combined with a phase-in period to accommodate the needs of those member states which today have a very low level of digitalization).
- A review of Annex II to MiFID II as regards the conditions that increase the ability for **sophisticated retail investors to** be treated as professional clients for certain products or services.
- A clear mandate for **ESAs to work with financial literacy** e.g., develop educational material for retail clients and/or standard information as regards different types of financial instruments, meaning of sustainability preferences etc.
- Developing more fit-for-purpose product governance (PoG) rules, with nonpackaged/simple/plain vanilla instruments (bonds and shares) not being subject to this regime to encourage retail investments.
- Clarifying **the scope of EU frameworks for products used for investment purposes**. For example, PRIIPs requirements are currently applicable to **hedging derivatives** used to mitigate risk for SME corporates, which is not consistent with the intended objective to cover information for investment products only.

About EFSA

EFSA is a forum of European Securities Associations gathering, the French Association of Financial Markets (AMAFI), the Spanish Asociación de Mercados Financieros (AMF), the Italian Association of Financial Markets Intermediaries (ASSOSIM), the Danish Securities Dealers Association (DSDA), The German Federal Association of Investment Firms (bwf), The Belgian Association of Stock Exchange Members (ABMB-BVBL), The Polish Securities Dealers Association (IDM) and the Swedish Securities Markets Association (SSMA).