NORDIC SECURITIES ASSOCIATION

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NSA's comments to the European Commission's Have Your Say consultation on Retail Investment Strategy

The Nordic Securities Association (NSA)[1] welcomes the opportunity to respond to the European Commission's "Have Your Say Consultation" on Retail Investment Strategy (RIS).

Key points

- In order to achieve the overall goal with RIS i.e., to increase retail client's participation on EU capital markets, it is crucial that the outcome of this review is to make the EU-rulebook more proportional, less complex and to tackle the existing problems with information overload to retail clients. However, the effects of Commission 's proposal in several respects steers in quite the opposite direction and we urge the co-legislators as well as ESMA to take this into consideration in their forthcoming work.

- It is important to underline that the level of maturity of retail markets within the EU, for instance when it comes to digitalization and financial literacy, still differs substantially between member states. This has a direct impact on the investment services and products which are requested by retail clients and offered to retail clients. Moreover, it should be noted that "retail clients" is a heterogenous group that includes both mass consumers, sophisticated investors as well as SME companies. Thus, in order for investment firms to be able to meet the needs of all types of retail clients on different local markets, it is important to ensure that the EU-regulatory framework does not unduly restrict different business models (e.g., advisory and execution services) or destroy the open architecture (e.g., access to

[1] NSA is composed by the Danish Securities Dealers Association (Børsmæglerforeningen), the Finance Finland (Finanssiala ry), the Norwegian Securities Dealers Association (Verdipapirforetakenes Forbund) and the Swedish Securities Markets Association (Föreningen Svensk Värdepappersmarknad).

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both internal and external products). A one size fits all approach is not the way forward to achieve a well-functioning capital market in the EU!

- In fact, from a CMU perspective, it is very important to ensure that the EU framework allows for a healthy competition between financial institutions (smaller and larger, universal, and more specialized). Unproportional and complex regulation creates barriers of entry for new investment firms/product manufacturers and can also hamper financial innovation and increase costs, which is not to the benefit of clients. Moreover, it should be noted that if sophisticated retail investors are not able to get the services or products, they need from EU investment firms they might turn to firms outside the EU instead. A competitive legal framework is therefore key if EU capital markets shall stay attractive also in a global context.

- The NSA is concerned with the fact that many of the Commission's proposals focus on providing retail clients with "the most cost-efficient" product, without regard to other preferences and objectives of the clients. At a general level, NSA agrees that investment products should give retail clients "value for money" but we object to the idea that the appropriate price of products and services should be determined by EU benchmarks developed by ESMA and EIOPA. In our view, the Commission's vfm-proposal comes dangerously close to a price regulation at EU level, depending on the level 2 and 3. This would not be acceptable in a market economy. We also question if it is even possible from an operational perspective to implement EU-benchmarks, which are granular enough and take into account local differences, for all types of PRIIPs products which according to the current interpretation of PRIIPs unfortunately also includes many bonds and OTC-derivatives. In fact, the complexity and costs linked to an implementation of the Commission's proposal is tremendous and it is very difficult to see how it will help increasing the engagement of retail clients on EU capital markets.

- We [2] welcome the fact that the Commission has refrained from proposing a total ban on inducements for advisory services since we believe that this would have caused an

[2] The Norwegian Ministry of Finance is in a process evaluating a national ban on inducements. The Norwegian Securities Dealers Association (NSDA) has in the national consultation commented that Norway should not have rules deviating from those in the EU in regard of inducements. Thus, the NSDA has refrained from taking a stand on the NSA's comments on this point.

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"advice gap" that would be to the detriment of mass retail clients who are not willing to pay for advice. However, we do have several questions and concerns linked to the proposal, such as how firms from a technical perspective should be able to separate between advisory and execution services. In our opinion, the new "best interest test" also introduces a very complex regime into MiFID II and it is unclear how this test relates to the existing suitability regime, in particular taking into account that retail clients may have other preferences than simply investing in the "the most cost-efficient product" (cf. above). In the opinion of NSA, a more reasonable solution would have been for the co-legislators to improve the existing quality enhancement rules as well as the disclosure regime and to ensure that there is an effective supervision and enforcement of the rules.

- We do not support the proposals to extend the partial ban for inducements in respect of execution services to retail clients. We fail to see the benefits with this proposal, in particular taking into account that there is no conflict of interest in respect of these services since transactions are done on the client's initiative and there is no risk that the firm is influenced by the inducements (as sometimes can be the in the case in respect of advisory services). We also consider that a partial ban for execution services would create significant risks of market distortion, including an un-level competition between different types of service providers. In particular, it should be noted that the existence of self-serving channels (both in universal banks and specialized internet banks) is one important reason why the Nordic capital market today has such active retail participation. And many clients benefit from being able to both receive advice and trade independently – with access to the same products. In our members experience there has been no problems with inducements in respect of execution services that could possibly justify a ban, e.g., in the form of sanctions or scandals of mis-selling. We fail to see that the Commission has provided any clear proof of this to justify the proposal. We therefore find it most worrying that the Commission has presented a proposal of a ban for inducement for one segment of the market, especially since they do so without conducting a proper impact assessment of the potential effects of this, neither in general within the EU, nor on local markets where execution services are an important part of retail participation.

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- Finally, the NSA wants to stress that the RIS proposals are very extensive, and that implementation will require a lot of IT development, changes to internal procedures and policies as well as staff training. It is therefore important not to repeat the mistake of MiFID II but to ensure that the implementation time (which should be at least 24 months) is counted from the publication of level 2. Otherwise, there is a risk of a "time gap" between level 1 and level 2 which is costly and creates unnecessary legal uncertainty for investment firms and their clients.

Comments on specific proposals.

Cost & charges

- The NSA is generally in favor of increased standardization regarding cost & charges disclosures provided that this leads to the information becoming easier to understand and more accessible to retail clients. However, we are however concerned that the Commission's proposal on disclosure will in fact increase the information overload, not the opposite, and potentially also make it more complex. (cf. Kantar report). For instance, we note that the new rules on annual statements are much more detailed that the existing rules and question whether this is really in the retail client's interest. We also want to underline how important it is to ensure that the new disclosure requirement work in a digital environment and that co-legislators should ensure that the format of the disclosures is flexible so that it can be adjusted to clients accessing services though smartphones and other online services.
- There is uncertainty regarding the alignment between the Commission's proposals on cost & charges and the MiFID Quick Fix exemptions for professional clients and eligible counterparties, in particular as regards provisions enabling agreement with clients on a limited application of the rules. This matter should be looked into by co-legislators in the forthcoming work.
- The NSA questions whether it is reasonable to include expected performance into the cumulative effects on expected returns. It seems that the proposed rules on cost disclosure in this regard further complicates rather than simplifies disclosures for retail clients.

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Warnings for particularly risky products

- Since the fundamental criteria for which products are particularly risky etc. will be set on level 2 and 3, the NSA finds it difficult to provide comments to the proposal at this stage. From a general perspective we are however surprised that the Commission proposes a new warning for particularly risky products in MIFID when the current requirement for "comprehension alert" in PRIIPs is removed because it did not achieve the intended policy objectives. We are uncertain how risk warnings are perceived to have a better effect in a MiFID II context. It should also be noted that many warnings can actually contribute to the existing problem of information overload and discourage retail participation.

Marketing communications and practices

- The NSA notes that the key policy objective is to regulate investment firms' responsibilities when marketing though digital channels and through third parties. However, we note that the Commission's proposal is much more far reaching than this, due to the very wide definition of "marketing communications" and "marketing strategy" in article 4. These wide definitions could have unintended consequences, e.g., by leading to an unproportional burden in terms of e.g., record keeping, and we therefore propose that the co-legislators review the scope of these provisions, including the relationship between the new MiFID II rules on marketing communications and other legislation such as distance marketing rules and prospectus regulation.

Inducements[3]

- As mentioned under general comments, the NSA does not support the introduction of a new partial ban for execution services which we consider would be very disruptive to the well-functioning markets in the Nordics where retail investors invest through these services to a large extent. If such a ban were introduced, it would in fact lead to a decrease of retail participation on the Nordic market, which would disrupt our market and be counterproductive from a RIS perspective.

[3] The Norwegian Ministry of Finance is in a process evaluating a national ban on inducements. The Norwegian Securities Dealers Association (NSDA) has in the national consultation commented that Norway should not have rules deviating from those in the EU in regard of inducements. Thus, the NSDA has refrained from taking a stand on the NSA's comments on this point.

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- The NSA notes that the proposal for a ban on inducements for execution services has not been subject to a thorough impact assessment by the Commission, which we find worrying (see General Comments). In our view, the proposal would create an unlevel playing field between different types of investment service providers in EU, which is not in line with the objectives of a well-functioning capital market where firms of different sizes and level of specialization should be able to provide a variety of investment services to their clients. Retail clients benefit from competitive markets and execution-only services provide an added value by pressing costs and increasing investment choices. It should be noted that also other quality enhancement services are often provided in connection with execution only (e.g., access to educational material, analysis, profiling-tools etc.) which are beneficial to retail clients from a financial literacy perspective.

  NSA notes that the implementation of the partial ban for execution services would be extremely challenging from an operational perspective which would be to the detriment for both firms and clients. The proposal fails to recognize the "client journey" and the fact that clients often move between different services over time. For full-service banks especially, many consumers benefit from both receiving advice and then being able to trade on their own later – with the same pool of products available to them. Thus, we perceive a risk that the product offering available to investors trading execution only will become limited due to the required separation of products. This will harm the investors' experience and freedom in the investment process. If the proposals means that firms would be required to develop separate classes of products and/or client accounts i.e., with or without inducements, it will increase both complexity and costs for clients. If kept, it is also of utmost importance that some sort of grandfathering clause is introduced in the regime.

- We welcome the fact that the Commission recognizes that fees that are paid by clients in return for investment services on the primary market (such as underwriting fees and placing fees) should not be subject to a ban on inducements, since the opposite interpretation would clearly have a detrimental effect on the ability for corporates to seek financing on EU capital market. However, in our opinion the exemption for PRIIPs products must either be rephrased or deleted in its entirety. The reason for this is that the existing interpretation of PRIIPs scope is that it includes certain bonds which means that MiFID II inducement rules could have the unreasonable result of not allowing investment firms that assist corporate clients to

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issue bonds to get paid for these services in case they also offer retail clients the possibility to subscribe for such bonds. Besides, for other PRIIPs products such as investment funds, insurance products and derivatives the exemptions serve no purpose as issuer fees do not exist for these products.

- The NSA notes that the Commission has changed the wording of the existing ban for portfolio management in a way that it will no longer be possible to forward inducements to clients ("accept and retain" is replaced by "pay or receive"). We are uncertain whether this is an intentional change since the proposal does not seem to have been subject to an impact assessment. We also have difficulties to see the benefits from the client's perspective with such a change. Forwarding inducements to clients actually removes the conflict of interest which the ban is intended to handle. In our opinion, the ban should therefore be re-phrased as "accept and retain" inducements i.e., it should be possible to pass inducement on to clients. Otherwise, the products available for portfolio management will be restricted without any reason which is detrimental to clients and markets. From a competition perspective it is important that the same principle applies to all services which are subject to a partial ban e.g., independent advice, portfolio management and, if introduced though RIS, execution services.

- The new "best interest of client test" in our view raises questions as it assumes that the most cost-efficient products are always the most suitable for clients and fails to recognize that the client may have other objectives and preferences. The NSA is concerned that instead of simplifying the existing rulebook, the Commission introduces additional complexity in MiFID II through new undefined concepts in article 24.1 a ("cost efficient", "additional features") and we also have difficulties to understand how this new regime is supposed to be aligned with the existing rules on suitability, sustainability preferences as well as the new concept value for money. Furthermore, we note that the scope of the best interest test is much wider than the existing quality enhancement rules as it applies to all types of investment advice and regardless of inducements, which leads to additional questions such as what impact the proposals might have on non-MiFID firms. Lastly, we are concerned that this test will also contribute to limiting the product offering – or at least which products that are consistently presented to investors – depending on the interpretation and operationalization of the terms "cost-efficient" and "additional features."

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- The NSA proposes that the 3-year review clause is changed into 5 years because 3 years is much too short time period to see all the effects of the proposals. Especially considering that it is unclear exactly which expectations the sector must live up to in order for the Commission not to impose a full ban at the time of the review. In this sense the review clause seems biased towards introducing a full ban in a short timeframe.

Product Governance; Value for money

- The NSA agrees that investment services and products should deliver "value for money" (vfm) to retail clients and we can support that this is clarified through the introduction of a new high-level principle in the product governance regime in MiFID II. However, we strongly object to the proposal that vfm shall be determined by comparing products with EU benchmarks calculated by ESMA and EIOPA. First of all, we consider that this proposal depending on level 2 and 3 measures resembles price regulation at EU level which is very serious and not in line with fundamental principles of a market economy. Secondly, it should be noted that from a competition law perspective, price information is very sensitive to share with external actors which makes the proposals of data sharing very concerning. Thirdly, the proposal fails to recognize that it is not always most suitable for retail client to invest in the "cheapest ETF," which we perceive as a possible outcome of the benchmarks since they could severely limit the product offering. In fact, which product is suitable for a retail client to invest in depends on a range of factors such as investment objectives, sustainability preferences and existing portfolio. We also fail to see how such benchmarks could be constructed granular enough and taking into account local differences and the vast variety of PRIIPs products (asset classes, sector exposures, investment styles, leverage level, currency exposures, liquidity profiles, etc.). Fourthly, to apply this regime to all PRIIPs products is not possible considering that the PRIIPs scope (unfortunately) also includes many bonds and OTC derivatives, including derivatives only used for hedging. What constitutes "value for money" varies between different products and the regulatory framework must allow firms flexibility to adjust its methodology, also taking qualitative aspects into consideration. Finally, the proposal is very complex and will be very administratively burdensome and costly to implement which is unproportionate considering the little value it will bring to clients.

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Appropriateness assessment

- The NSA objects to the introduction of new criteria (risk tolerance and ability to bear loss) for the appropriateness test. This proposal will in our view create a significant boundary-drawing problem between today's well-established concepts of "suitability assessment" and "appropriateness assessment," as it seems to "mix" advice (suitability test) into the process for clients wishing to trade complex products independently (appropriateness). This unclarity would be very unfortunate as it would make the EU rulebook even more complex and difficult for clients to understand and we fail to see the benefits of the proposal.

Suitability light for independent advisors

- The NSA generally welcomes the introduction of alleviations regarding the rules on suitability assessment but questions from a competition perspective whether it is appropriate for the Commission to use the regulatory framework to favor one business model (independent advice) over another (not independent advice). One alternative solution could be to introduce a lighter suitability regime for all types of advice when retail client invest only a smaller amount in safeguarded and well diversified products e.g., investments in UCITS below a certain monthly or yearly limit. This could foster digital and less costly advisory services to the mass retail market.

New standardized report on collected client information

- The NSA finds it difficult to evaluate the consequences of this proposal because it depends on the design of level 2 and whether new requirements are introduced that have an impact on the scope and level of detail in the information to be collected from the client. If kept, the requirements should be limited to retail clients, excluding potential clients as well as professional clients and eligible counterparties. It is important that firms have flexibility in terms of the design of questions to their customers, so that these can be adapted to the type of service and the type of instrument and distribution channel. One-size-fits-all should be avoided.

- We foresee a link between the reporting obligation on collected client information and the Open Finance proposal. We are worried that the level 2 requirements on the content of these reports and data sharing might limit the flexibility in terms of the design of questions towards retail investors.

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- As regards, the new explicit requirement to consider diversification aspects and the customers entire portfolio when providing investment advice, this must be a requirement "where relevant." Firms can never be required to collect information on a client's portfolio held by another firm and must be allowed to provide advice to a client who refuses to provide this information on a voluntary basis. Moreover, recital 34 indicates that advisors should also consider client's non-financial assets. This proposal could have unintended negative consequences for retail clients, e.g., the fact that the client's house has a high market value does not mean that is suitable to invest in more risky products… Also from the advisor's perspective, we believe that this requirement would be difficult to fulfil considering both the possibly very large scope of "non-financial assets" and the added time and resources it would take for the advisor to assess such assets in conjunction with the client's finances. This would also make the process more complicated and lengthier for the client, perhaps again to the detriment of their experience. Also, clients must be able to request advice on a limited part of their entire portfolio of investments.

Client categorization; opt-up

- The NSA find it positive that the Commission has proposed rules to make it easier for sophisticated non-professional clients to request to be treated as professional clients (opt-up) under certain conditions. This is an important issue for Nordic markets which are characterized by many sophisticated retail investors.

- In addition to the proposals by the Commission, we also consider that the criteria linked to the number of transactions should be subject to review. At present, this criterion (10/quarter) is difficult to apply for less liquid instruments such as corporate bonds and OTC-derivatives. Preferably a mandate should be given to ESMA to properly calibrate per asset class on level 2. Thus, we welcome that the Commission has proposed to lower the wealth criterion, but we believe that reviewing the transaction requirement would have an even more beneficial impact for the engagement of more sophisticated retail investors on EU capital markets.

Cross border reporting

- It is important to ensure that the reporting requirements regarding cross border activities are proportionate and result in comparable data. In this connection, the NSA

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wants to underline that the question of when an investment firm cross borders and conducts business in another Member State without establishing a branch is complicated and must be subject to proper discussion and legal analysis, not least considering the digital environment firms and clients operate in.

PRIIPs scope

- The NSA welcomes the ambition to clarify the scope of PRIIPs, which for many years has proven difficult to apply for both investment firms and retail clients. We note that this issue has become even more important in the context of RIS, as the Commission proposes to introduce new references to PRIIPs in MiFID II (see above re. inducements and vfm) which means that the legal implications for an investment to be in scope of PRIIPs may become even greater in the future.

- According to NSA, PRIIPs scope should only cover packaged investment products that are used for investments. Derivatives that are only used for hedging and all non-structured bonds should be excluded. We also see a need for the co-legislators to review the references to the prospectus regulation which in some parts appear to be obsolete and also with the proposal would include more types of investment products than before.

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