European Forum of
Securities Associations

EFSA members:

Asociation de Mercados Financieros (AMF)

Association française des marchés financiers (AMAFI)

Associazione Intermediari Mercati Finanziari (AMF Italia)

Belgian Association of Stock Exchange Members (ABMB-BVBL)

Bundesverband der Wertpapierfirmen (bwf)

Capital Market Denmark (CMD)

Polish Chamber of Securities Brokers (IDM)

Swedish Securities Markets Association (SSMA)

FOR REGULAR USE

24 October 2024

Key messages regarding the Retail Investment Strategy – for the Trilogue negotiations

EFSA is a collaboration between trade associations representing the interests of investment firms in Europe.

EFSA strongly believes in the policy objective of building a Savings and Investment Union to strengthen retail investors' engagement and trust in the capital markets. However, it is important to keep in mind that retail markets in Europe today have different levels of maturity. In order for investment firms to be able to serve retail clients' needs in *all* of the EU, it is therefore important that the regulatory framework does not unduly restrict retail clients' access to different types of investment services (e.g. advisory and execution) and different types of investment products. It should also be ensured that disclosures to retail clients, while including the necessary information, are simple and easy to understand and that the level of information to be collected from such clients in the advisory process is proportionate. Information overload as well as cumbersome on-boarding procedures create barriers of entry for retail clients and must therefore be avoided.

During the past months, several reports have been published with an aim to provide input to the strategy of the new European Commission, including on how to improve the competitiveness of EU capital markets. In EFSA's view, it is crucial that this ambition is not only reflected in future measures but that it is also incorporated into ongoing legislative procedures, such as the Retail Investment Strategy. In fact, one of EFSA's key concerns is that the cumulative and combined effect of the RIS-proposals (e.g. value for money, inducement rules, best interest test as well as more detailed reporting and disclosure requirements) will create additional layers of complexity into the EU-rulebook. It will lead to significant operational challenges for firms, putting especially smaller firms in a difficult situation due to the increasing administrative costs they

Internet: www.efsa-securities.eu
Mail: contact@efsa-securities.eu
EU Transparency Register: 038014348035-13

will have to bear. For retail clients, the new rules will have a negative impact on competition and thereby restrict their investment choices. Considering the policy aims of a future Savings and Investment Union, such development would be very counterproductive.

This position paper presents the key points on the Retail Investment Strategy as identified by EFSA members, which are important for the co-legislators to consider in the forthcoming trialogues.

Partial ban on inducements for execution services
EFSA opposes the Commission's proposal for a partial ban on inducements for execution services. We strongly believe that this would limit product offerings to retail clients and increase costs. It would also negatively affect the competitiveness of independent and smaller asset managers/investment firms, benefiting larger institutions with in-house products. It is important to note that not all retail clients are willing or able to pay directly for value-added services. Against this background, EFSA welcomes the fact that the proposal for an extended ban for execution services has been deleted in both the Parliament and Council texts.

We are however very concerned with the proposal by the Council that Member States could introduce a total or partial ban on inducements at a national level without ensuring that it is proportional and objectively justified by market structure- or investor protection concerns on that local market. In our view, a key objective of EU-rules should be to remove barriers to cross-border investment services, including the distribution of investment products. It is also essential that the rules ensure a level playing field across the Union.

The rules on inducements should exempt clients' payments for investment services e.g. underwriting and placing fees
The Council has proposed that a definition of inducements is introduced into Article 4 MiFID II. In this regard, EFSA would like to remind the co-legislators that there still is a need to clarify that a corporate client's payment for an investment service relating to an issuance (e.g. underwriting or placing) should not be considered as an inducement in relation to an end client that buys another investment service relating to that same issuance (e.g. advice or execution services). Without such a clarification, there is a risk that the inducement rules (i.e. ban on accepting and retaining, quality enhancement/inducement test, disclosures etc.) could in practice prevent firms from charging issuer clients for the investment services provided and/or from offering end-clients the option to subscribe for financial instruments where the firm has assisted with the issuance. Such an interpretation would have very problematic effects on the primary market in the EU with negative effects

on the real economy as a result[1]. Thus, in EFSA's view it must be clarified (either through an exemption or a recital) that payments received by the investment firm for providing services to different clients should be addressed through the conflict of interest rules in MiFID II, rather than the inducement rules.

New inducement test

EFSA acknowledges the need for further clarification of the existing "quality enhancement- test" in MiFID II. To our understanding, several of the requirements in the Councils so-called inducement test are a codification of existing level 2 and 3 which could contribute to increasing supervisory convergence. However, more work needs to be done to ensure that this new test is not drafted in an overly complex manner which would add legal uncertainty, and that the requirements work for the different types of financial instruments and investment services that are in scope of the inducement rules. From an operational standpoint, it is crucial to retain the Council's proposal to include "where applicable" in the text and to ensure that the proportionality regime is workable in practice (e.g. no client-by-client assessment). Otherwise, there is a risk that this new inducement test will effectively result in a total ban "through the back door", which could have adverse effects on the well-functioning of the distribution of investment products in EU.

Value for Money (VfM)

As a general principle, EFSA opposes all forms of obligatory benchmarks in VfM which we consider to be a form of price regulation. We find the current drafting of the value for money proposals to be complex and are unsure how these requirements are going to work from an operational perspective, taking different types of PRIIP-products into account (e.g., investment funds, bonds, structured products and derivatives). EFSA would be in favour of an internal model that is based on the existing product governance regime, combined with robust internal governance requirements. A supervisory benchmark could in our view have the same effects as price regulation and must therefore be carefully considered by the co-legislators. We also take the view that the reporting requirements regarding costs and performance to the supervisory authority are unproportionate, in particular in the context of the Commission's goal of reducing reporting burden by 25 %[2].

---

[1] See article 41 delegated regulation to MiFID II which provides that a placing fee/underwriting fee is an inducement in relation to end-clients that receive 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

[2] https://commission.europa.eu/system/files/2023-10/Factsheet_CWP_Burdens_10.pdf

Best interest test
Considering that the intention by the Commission with the best interest test was to replace the existing quality enhancement-test and that the quality enhancement test now has been retained in both the Parliament's and Council's texts, EFSA considers that the rules on best interest test should be deleted. In fact, in our view the best interest test will only add yet another layer of rules to an already complex, while providing minimal additional protection for clients.

If the best interest test is kept, EFSA believes that more calibration is needed to make the rules workable from an operational perspective. Firstly, we consider that it is important to keep the proposal by Parliament that allows consideration of the business model of the investment firm. We also agree that other factors than costs must be taken into consideration by investment firms and note that the wording of this requirement needs to be carefully drafted considering the interaction with other parts of the rules e.g. VfM and the suitability regime. Finally, we support the proposal by Parliament to delete the criteria "additional features" and find the proposal by Council to introduce a similar requirement in the suitability regime is misguided as it limits client's choice (see below).

Appropriateness and suitability
EFSA opposes the new proposals to introduce the criteria on ability to bear losses and on risk tolerance to the appropriateness assessment. Adding such criteria would make the distinction between suitability and appropriateness more difficult and we therefore strongly support the Parliament's proposals for deletion.

Furthermore, EFSA believes that the scope of the "suitability light – regime "should apply regardless of whether the investment firm claims to be independent or not and include portfolio management. This amendment is important for competition reasons and to ensure that the protection of the retail client is consistent regardless of the type of advice/investment service provided, i.e. portfolio management.

From an operational perspective, we also find the proposal by Council that a financial instrument should not be considered as suitable if it has additional features which lead to extra costs, to be very challenging. According to EFSA members, to verify that the level of product charges is reasonable in relation to their characteristics, performance and qualitative features duplicates the VFM's requirements. Moreover, recommending a more expensive product with features that go beyond a client's profile can be perfectly legitimate, for example when that product offers better performance prospects, a better guarantee, particular ESG characteristics or opportunities to diversify the client's asset. A one-size fits all approach to the suitability rules must therefore be avoided.

Cost & Charges

EFSA is genuinely concerned with the complexity of the disclosure regime and finds it unfortunate that this part of the Commission's proposal does not seem to have been subject to in-depth discussions in neither the Parliament nor the Council. We would like to emphasize that one of the key objectives of the Retail Investment Strategy at the outset was to address the problems with information overload faced by retail clients. Evidence shows that retail clients are interested in price and total costs, not detailed breakdowns, or methods of calculation.[3] Against this backdrop, the new requirement regarding an annual report on both portfolio and instrument level should be reassessed in trialogues with the aim of simplifying and reducing the information- and reporting requirements. Furthermore, closer alignment between PRIIPs/MiFID II would be beneficial, as previously suggested by ESMA.[4]

Client categorization (opt-up)

Retail client is a wide concept which, in addition to consumers, also includes sophisticated retail investors and SME-companies. In order for investment firms to be able to serve the latter sub-categories of retail clients, we believe a review of the opt-up criteria is necessary. In some markets, in particularly the "transaction" criteria is difficult to apply e.g., for corporate bonds which do not trade very often.

PRIIPs scope and KID

EFSA supports a review of the PRIIPs scope to ensure that it is only applicable to packaged products. The application of PRIIPs to simple bonds unduly restricts retail client's access to these products which is detrimental to clients' need for diversification and to the capital market as a whole. Moreover, considering the new requirements regarding "product at a glance" and sustainability information, keeping the three-page limit of the KID will be challenging.

*****

[3] https://op.europa.eu/en/publication-detail/-/publication/5d189b3c-120a-11ed-8fa0-01aa75ed71a1/language-en

[4] https://www.esma.europa.eu/press-news/esma-news/esma-makes-recommendations-improve-investor-protection