Brussels, 16.12.2022

To:
Mr Valdis Dombrovskis – Executive Vice-President of the European Commission
Ms Mairead McGuinness – Commissioner for Financial Services, Financial Stability and CMU
Mr John Berrigan – Director-General for Financial Stability, Financial Services and CMU

Cc:
Ms Tatyana Panova – Head of Unit, DG FISMA B.1
Mr Eric Ducoulombier – Head of Unit, DG FISMA B.3
Mr Tilman Lueder – Head of Unit, DG FISMA C.3
Mr Alain Deckers – Head of Unit, DG FISMA C.4
Mr Didier Millerot – Head of Unit, DG FISMA D.4

Subject: EC's Retail Investment Strategy: the importance of financial advice

Dear Vice-President Dombrovskis, Commissioner McGuinness, Director-General Berrigan,

As representatives of the European financial services industry, we believe that the Retail Investment Strategy (RIS) provides a golden opportunity to preserve and improve consumer protection, as well as making investing more understandable, accessible and appealing to European retail investors.

We understand that the European Commission is assessing different policy options to improve retail investor participation in capital markets, including intervening on the current coexistence of fee-based and commission-based advice. We strongly believe it will be crucial to avoid radical approaches in the RIS that would restrict European consumers' access to financial advice. In this context, we would like to recall the fundamental objectives the Commission has committed itself to pursuing via the RIS, i.e. guaranteeing that retail investors can reap the full benefits of capital markets, and thus we take this opportunity to clarify some misconceptions around the topic of advice.

The value of advice for consumers

There is strong evidence that qualified advice is highly valued by European retail investors[1], with the most important source of information for European consumers' financial decisions being recommendation by financial advisors[2]. Access to advice is even more critical in the current context of high inflation[3] and low financial literacy. If unable to ask questions and receive personalised guidance, investors are more likely to turn to unsuitable or unregulated products, or simply continue to keep their savings in bank accounts as is currently the trend in most of Europe. Access to advice can also strongly contribute to one of the Commission's key CMU objectives: financial inclusion.

Furthermore, advice will become more critical in helping retail investors understand how to meet their sustainability preferences as interest in sustainable finance increases[4]. Indeed, ban on commissions in countries where a commission model is prevalent creates a clear risk of excluding investors from critical

[1] See: European Commission (2022), "Disclosure, inducements, and suitability rules for retail investors"; Eurobarometer Survey on Retail Financial Services (2022).
[2] 45% of respondents to the Retail Financial Services and Products Eurobarometer relied on the professional advice of their advisors
[3] For instance, with current inflation levels soaring, qualified advice helps manage retail investors' expectations, for instance, by not making false promises of fast or high returns — as rightly warned against by ESMA in the context of crypto-assets
[4] For example, 62% of respondents to the Retail Financial Services and Products Eurobarometer find it important that their savings and investments do not fund economic activities that have a negative impact on the planet

guidance as they navigate their way through various products in a complex environment. This will either damage the uptake of sustainable products, or lead retail investors to take the higher risk of buying without qualified advice; either outcome would strongly harm the CMU and sustainable finance objectives.

The risk of an "advice gap" thus stands out as the primary concern triggered by ban on commissions in countries where a commission model prevails. This is the risk that the very groups of retail clients who would most benefit from advice — whose provision has been made possible up to now by the commission-based model — are prevented from accessing it.[5] This group of clients are less affluent, less digitally and financially literate and, ultimately, more financially vulnerable. As a result, an EU-wide ban on commissions would preclude major groups of EU citizens from financial advice, which we cannot envision as being in line with the aims of the European Commission's CMU.

Financial inclusion, financial literacy and the social value of commission-based advice

Commission-based advice involves no upfront costs for retail investors, as the advisor is at least partially remunerated by commissions from the product manufacturer. In this way, commissions socialise the cost of financial advice across all retail investors to the benefit of the less affluent ones, whether they are online or not, financially literate or not, and regardless of their geographical location. Here, there is also a close link to the European Commission's commitment to the fight against old age poverty, as the most vulnerable group are older people, living in remote areas and/or small municipalities, with lower digital skills and income.

An EU-wide ban on commissions could disrupt the market at the expense of consumers

As any professional service, advice comes at a price. However, the cost of not being able to access advice when needed could be extremely high for consumers: some could turn to other sources of unregulated information such as social media and be more exposed to scams or high-risk investments (eg, bitcoin/ GameStop), while others would be less likely to invest[6], and then less equipped to face financial challenges, as well as less prepared for retirement.

In any case, a commission is only charged when purchasing a financial product. This enables consumers to shop around and seek advice multiple times without being charged until a product is purchased. In some markets, there are national rules on mandatory advice, and if the payment of commissions is banned, consumers might not be willing or able to pay a fee to get advice and may thus resort to unregulated markets.

Consumers' ability to access finance varies by country

According to multiple pieces of research, many European investors consider financial advice essential, but are unwilling to directly pay a fee for it.[7] Hence, if commission were to be banned, many European consumers would be left with the option of taking less advice or none at all.

This is confirmed by the European Commission's recently published study on "Disclosures, inducements and suitability rules for retail investors", which states that it is debatable whether a ban on commissions would lead to better consumer protection, and that there are significant country differences with respect to consumers' willingness to pay for financial advice and the likelihood of doing so, thus leading to an advice gap should there be a ban on commissions. The study highlights that this is particularly a danger in eastern European countries.

An overview of the different national jurisdictions in the EU shows that differences exist not only in terms of (i) features of the prevailing distribution models, but also (ii) composition of households' portfolios, as well as (iii) level and structure of financial assets held by retail investors. These differences imply that

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[5] The receipt of commission is subject to high regulatory standards. Therefore, in the event of a ban, not only will fee-based advice not be available to everyone, but it might also not be subject to quality requirements or quality controls, with a double detriment for consumers.
[6] FCA (2022), "Consumer Investments: Strategy and Feedback Statement"
[7] For instance, see: (i) Investment Trends (2021) Europe Advice Accessibility Report; (ii) KPMG (2021), "The future of advice: A comparison of fee-based and commission-based advice from the perspective of retail clients"; (iii) KPMG (2021), "Commission-based remuneration vs. Fee-based remuneration: is there a better model for retail investors?"

(i) the impact of an EU-wide ban on commissions would vary greatly from one EU member state to another and (ii) a ban would not necessarily achieve the same desired effects in each state.

Indeed, all markets have different economic, social and public environments which impact the effects of a ban, including the Netherlands and the UK. For example, the UK has a unique investment landscape — which is not present in the EU — that made conditions for a ban on commission substantially more favourable, such as pension auto-enrolment that has been markedly successful in driving up the share of the UK workforce investing in their pensions.[8]

Nevertheless, in November 2022, the UK Financial Conduct Authority (FCA) stated in a public consultation[9] that "less wealthy consumers do not tend to access professional support with their finances as often as wealthy customers", and that only 8% of the UK population seeks regulated advice because they have been priced out of the independent financial advisor market. Furthermore, the FCA consultation notes that robo-advice has failed to take off, because consumers value face-to-face interactions.

We also remark that ESMA has specifically warned against a commission ban in its 2020 Report, commissioned by the European Commission, at least until in-depth assessments are carried out into the impact of such a ban on the different distribution models that exist in the EU, as well as what potential additional actions could be taken to counterbalance the risks of undesired consequences linked to a ban[10].

All of the above leads us to raise a fundamental objection to the "one-size-fits-all" approach that underpins an EU-wide commission ban. EU retail investors are not homogeneous in terms of their needs or expectations and they operate in diverse economic, social and public environments that cannot be disregarded.

The quality of advice is not dependent on the form of remuneration

MiFID and the Insurance Distribution Directive (IDD) introduced strong and extensive safeguards at all stages of a product's life cycle, from development to distribution. The non-exhaustive list includes:

- product oversight and governance (POG) requirements
- rules on professional advice
- suitability or appropriateness test
- transparency over the services provided and costs charged to the customer
- robust measures to prevent, mitigate or disclose conflicts of interest
- distributors' continuous training, inter alia.

The current rules also allow tailored sectoral approaches where appropriate, for example to take into account the specific features of products and distribution channels. Looking ahead, it is important to recognise the combined effects of the robust and balanced rules set in MiFID and the IDD, and to keep monitoring the enforcement of such extensive rules at national level.

Importantly, financial advisors, firms and insurers strive to meet the needs and high expectations of their clients in a highly competitive market. This means that (i) remunerations received by the adviser are the counterpart of the provision of a good service[11]; and (ii) any short-term monetary gain for the adviser is clearly and entirely offset by the need to provide advice that results in long-term economic gains for the client. To retain a customer's loyalty and avoid reputational harm, an advisor's first priority is to recommend products that match the client's unique situation, goals and preferences and to provide them with long-term financial returns. This lies at the core of the financial services industry's business model.

Therefore, the coexistence of the fee- and commission-based advice models is one of the pillars of a successful RIS. Other recommendations are improvements to make disclosures more consumer-

[8] OECD (2021) Pensions at Glance – Table 4.2.
[9] FCA (2022), "Broadening access to financial advice for mainstream investments" (CP22/24)
[10] ESMA (2020), "Technical Advice to the Commission on the impact of the inducements and costs and charges disclosure requirements under MiFID II"
[11] The receipt of commission is subject to exceptionally high regulatory standards, including stringent quality requirements or quality control.

friendly, as well as the increased promotion of financial education which would help to ensure a simple and smooth consumer experience.

In conclusion, the EU has one of the highest saving rates in the world, but a low level of retail investor participation. If properly designed, the RIS can help unlock this potential and channel the investments that we need to build a greener and more resilient society. However, this goal can only be achieved if the necessary market infrastructure can be provided by the market participants. Commissions thus plays a significant role because they enable the industry to finance such market infrastructure.

We remain available to further discuss the contents of our letter and to set out — as an alternative to an outright ban on commissions — specific, potential improvements to the current regulatory framework (which is broadly satisfactory), as well as to share with the European Commission the industry's experience.

Yours sincerely,

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