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BVI Remarks on the EU Commission's Retail Investment Package of 24 May 2023

BVI[1] gladly takes the opportunity to present its views on the proposed new requirements of the Commission's Package of measures to increase consumer participation in capital markets (Retail Investment Strategy).

I. General remarks

We support the Commission's stated goal of broader participation of retail clients in the capital markets. Especially with regard to private pension planning, it is essential to encourage private investors to benefit from the opportunities of the capital markets. However, we feel that many of the proposals are not helpful for achieving this goal, while some others are probably outright counterproductive.

We believe that many of the targeted improvements have already been triggered by MiFID II and other EU Directives which are the subject of the draft Omnibus Directive. Instead of burdening market participants with new requirements, the existing ones should be better enforced and, if necessary, further specified. Especially MiFID II already contains comprehensive requirements for the goals of the Commission and is increasingly proving its effectiveness, as we will show in our specific comments below.

A proper evaluation of the practical consequences of the proposals is difficult, if not impossible, because far too many material decisions are left to future Delegated Acts or other subordinate pieces of regulation. As a matter of fact, many of the Level 1 proposals on the table, such as the "best interest test" or the new benchmarking process to avoid undue costs under MiFID, are mere "black boxes", while the relevant parameters and thus the overall impact of the legislation (constructive or destructive, sustainable or disruptive, etc.) will be decided on Levels 2 and/or 3.

In order to serve as the basis for Member States to amend their national legislation, EU Directives need to be sufficiently specific and clear. The more serious prospective rules in their application and in their economic impact on the legal addressee are, the more it is necessary for the legislators to fulfil their duty to create legal certainty themselves and not to delegate substantial decisions to downstream institutions. The approach chosen by the Commission raises questions regarding the democratic legitimacy of the whole project.

This is especially the case since proposals for Level 2 and 3 provisions are not subject to mandatory consultation – legislative decisions are thus removed from the democratic process. The fact that Parliament and Council will have to approve any RTS in the end does not change this substantially because of the "all or nothing" principle which does not allow for targeted adjustments by the Parliament or the Council. The inhibition threshold to block a complete legislative act by refusing to approve it is

[1] BVI represents the interests of the German fund industry at national and international level. The association promotes sensible regulation of the fund business as well as fair competition vis-à-vis policy makers and regulators. Asset managers act as trustees in the sole interest of the investor and are subject to strict regulation. Funds match funding investors and the capital demands of companies and governments, thus fulfilling an important macro-economic function. BVI's 116 members manage assets of some EUR 4 trillion for retail investors, insurance companies, pension and retirement schemes, banks, churches and foundations. With a share of 28%, Germany represents the largest fund market in the EU. BVI's ID number in the EU Transparency Register is 96816064173-47. For more information, please visit www.bvi.de/en.

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generally very high, as shown by practical experience. This has happened, for instance, in the process of developing the first RTS[2] on the PRIIPs regulation. It was obvious that the "arrival price" methodology for calculation of transaction costs would lead to arbitrary results, but due to time constraints in combination with the "all or nothing" principle, no adjustments could be made.

This also leads to a follow-on problem: Levels 2 and 3 are often finalised only after Level 1 is already implemented and in force on national level or will come into force shortly afterwards. This has been the case, for instance, with the AIFM Directive which had to be applied on national level from 22 July 2013, while the crucial Delegated Act on "types of AIFM" has been published only in December 2023[3]. One result is that initial implementation in the Member States can vary greatly (no level playing field). On the other hand, it also leads to costly adaption requirements for the stakeholders after Level 2 and 3 have been concretised.

[2] Commission Delegated Regulation (EU) 2017/653 of 8 March 2017
[3] Commission Delegated Regulation (EU) 694/2014 of 17 December 2013

II. **Proposal for a Directive**[4] (Omnibus Directive)

The elements of the draft Omnibus Directive must be seen in their entirety, as they partly interact and the effects are thereby amplified. We are of the opinion that they are not necessary in this totality, even if they appear suitable at first glance to achieve the objective in detail.

1. Draft Articles 14(1a) – (1f) UCITS Directive, 12(1a) – (1f) AIFMD, 16a MiFID, 25 IDD: "Preventing clients from undue costs"

The EU Commission proposes to introduce new requirements to prevent clients from being charged undue costs when acquiring financial instruments. The Commission is seeking to ensure that the legal framework for retail investments sufficiently empowers consumers, encourages improved and fairer market outcomes and ultimately creates the necessary conditions to grow retail investor participation in capital markets.

We support this goal. Undue costs are to be avoided – this is a legitimate objective. Nevertheless, we consider the present proposals to be excessive and ultimately not conducive to achieve the objective. The focus of our comments below relates to Article 14 UCITS Directive and Article 12 AIFMD. They apply *mutatis mutandis* to the proposals on MiFID/IDD.

Our key points:

- The proposal ignores the fact that ongoing costs for retail funds have been declining for years. In this respect, the measures introduced with MiFID II, such as cost transparency, are already taking effect. The introduction of new measures will jeopardise this positive trend. In addition, costs and charges are already subject to annual fund audits.

- The proposed obligations for management companies to identify and prevent undue costs interfere significantly with commercial freedom and introduce price regulation. This should be the measure of last resort in a free market economy.

- We fear that the result will be that only the costs will be taken into account while other characteristics of the product will be neglected. The expected return and the quality of a product and of the fund's management play an even more important role for the investor. In addition, it is questionable to what extent management companies will be able to continue to provide additional services such as engagement in the context of sustainability.

- The loss of jobs (relocation to non-European markets) and an increased participation in non-European markets is likely.

- Decisive specifications must be made at Level 1. See also our general remarks.

Should the legislators follow the Commission's proposals, the following considerations should definitely be taken into account.

[4] COM (2023)279

a) Comparison to market standards and launch of a benchmark

According to the proposal, management companies should compare the costs of their funds with those of the market (draft Articles 14(1c) UCITS Directive, 12(1c) AIFMD). In addition, ESMA is mandated to develop a benchmark that should include a "range of costs and performance" (draft Articles 14(1e) UCITS Directive, 12(1e) AIFMD). In individual cases, management companies can justify why their costs are outside the benchmark.

- Effects of a comparison to market standards

  The comparison with the market standards will likely lead to a price spiral that comes with a decline in product quality (e.g. volatility, risk-return ratio etc.) and choice for retail investors.

  If a management company realises that its costs for a fund are (even if only slightly) higher than the costs of a comparable product, it will be effectively forced to reduce its costs. Although it is not forbidden to provide products and services above the market price, in the end it is likely that in the retail mass market only the price of a product will be taken into account. Other features such as rate of return and quality become secondary. In order to continue to be sold, management companies would have no choice but to submit to a possible price war. The resulting margin pressure will have a detrimental impact on the quality of investment products because product providers lack the resources to invest in internal systems innovation. In addition, in order to reduce internal production costs, fund management companies, especially smaller ones, will be tempted to move their business to low-cost third countries outside the European Union, thus cutting jobs within Europe. This again is against the European Union’s goals for sustainable business and also against the goal to keep knowledge on financial services there.

  Hence, the introduction of a benchmark that management companies have to include in their pricing process incurred under the Commission's proposals (draft Article 14(1)(d) MiFID) is to be regarded as a form of price regulation with the consequence of reduced competition and free market economy. Even though management companies may demonstrate in individual cases that the costs and charges are justified and proportionate (draft Article 14(1)(d) UCITS Directive), this is of no use in practice as the distributors will likely not recommend such products because the explanation of the price differences and the administrative effort of such exceptional cases is too high.

  We do not consider such a drastic measure necessary. Recent analyses conducted by ESMA[5] and the US Investment Companies Institute (ICI)[6] found that ongoing costs for European retail funds are already declining. Complete transparency of costs allow the retail investor to compare the available products and make an informed decision. The measures introduced with MiFID II are obviously taking effect. The interference with free competition, on the other hand, would lead to a reduction in the quality and choice of financial products.

[5] ESMA Market Report “Costs and Performance of EU Retail Investment Products 2023”, p. 5 (UCITS) and annexes p. 25 chart ASR-CP-S. 63
[6] www.ici.org/system/files/2022-10/per28-08.pdf

- Lack of clarity

  For the time being, it is absolutely unclear how such benchmarks are to be defined and calculated. Already today, here is a vast universe of performance benchmarks tailored to the needs of the industry and end clients which in translation to cost and performance benchmarks could lead to existence of a at least six digit number of benchmarks.

  The proposed top-down, pan-European benchmarks would disregard differences across national retail markets. In addition, the creation of a benchmark is very difficult for certain asset classes, such as multi-sector and multi-asset products. Also in the field of non-standardised assets such as alternative assets and real estate there are usually no sources available to base a benchmark on with which a meaningful and appropriate comparison could be effected. If there are, their use is very doubtful since particularly such asset classes are designed for longer holding periods. However, the same is true for more standardised assets since the composition of funds with active management can mitigate market movements in another way as ETF.

  The Commission's proposal does not even elaborate on the most basic features of such benchmark. By delegating the development of the benchmark completely to ESMA, significant parts of the regulation are not decided by the legislators themselves and at a later stage.

  This makes a final evaluation of the proposed measures almost impossible for the time being. Only the requirements to be set at Levels 2 or 3 will provide clarity as to whether the Level 1 rules are appropriate, disproportionate, or even counterproductive. Against this background, it is not surprising that several national supervisory authorities have already expressed doubts about an "EU value for money" approach.[7]

  If the benchmarking requirement were to come, it is important to bear in mind the following aspects. ESMA is supposed to determine products groups for benchmarking – although the comparability of products has always been extremely difficult. If this is done, it is imperative to ensure that the differentiation is very granular. Comparing "apples with pears" must be avoided at any cost, also in the interest of investors. This is because a misleading comparison can lead to the investor's disadvantage.

b) Reimbursements of undue costs

Member States shall require management companies to reimburse investors where undue costs have been charged to the UCITS or its unit-holders (draft Article 14(1d)).

It should be borne in mind that management companies usually have no information on who the investors in their retail funds are. This knowledge is residing only with the entity that keeps the custody account. Many retail funds are held by hundreds of thousands of different investors. Determining the respective investors in the case of undue costs retroactively is therefore, practically impossible. Especially as investors may have already sold their shares in a fund, this may end up as another "bureaucratic monster" which may in turn not allow management companies to reduce management fees. In any case, thresholds should be set at which an

[7] See ESMA opinion; 2023, Q 16 (p. 79f)

obligation to pay a reimbursement arises (e.g. x percent of the NAV). The requirements must be proportionate.

2. Draft Article 24a(2) MiFID: "Partial ban on inducements"

We welcome that the EU Commission has decided against proposing a complete ban of inducements. We fully agree with the majority of Member States, as quoted in the Explanatory Statement, that in particular in the context of advice, a ban on inducements would likely have a "disruptive effect" on existing retail distribution systems at banks, insurance companies, MiFID firms, insurance intermediaries, and IFAs of all sorts. Also, recent research shows that the introduction of a ban on inducements in the UK and the Netherlands has not led to higher returns for retail investors or better participation in capital markets.[8]

But also the "partial" ban on inducements, as proposed by the Commission, would be disruptive and runs counter the Commission's stated objectives.

Our key points:

- The ban on inducements for non-advised distribution services will increase costs for retail clients and deter them from participating in the capital markets. This is exactly the opposite of the results the Commission wants to achieve.
- As a result of declining retail business, service providers and distributors will likely withdraw from the market or focus on institutional clients or high-net-worth individuals only.
- The proposed new wording of the ban on inducements for portfolio management services will narrow down the investment opportunities for retail clients without any improvement of investor protection.
- We therefore strongly suggest addressing perceived or factual shortcomings in investor protection by reinforcing existing MiFID II safeguards on Level 1 and striving for harmonised implementation among Member States rather than by calling for new rules which are untested and likely to produce detrimental results.

a) Ban on inducements for non-advised distribution services

According to draft Article 24a(2) MiFID, no inducements shall be paid or received in connection with the investment services of "execution of orders" (execution only) as well as "reception and transmission of orders". We are concerned that also this "partial" ban on inducements is not fully thought through since it would have effects which are detrimental to the interests of retail investors and the goals of the Retail Investment Strategy to strengthen the access of retail investors to the capital markets.

[8] BVI: Effects on Bans on Inducements Revisited, August 2023

- Lack of conflicts of interest

  Advice-free financial services are, by definition, not prone to conflicts of interests. The MiFID firm provides as the core function the execution or reception and transmission, respectively, of the order. In contrast to investment advice, no individual recommendation for the purchase of specific investment products is given by the firm. Therefore, due to the very nature of this service, there is no risk that the financial service provider can influence the decision-making process for the purchase of a specific financial product by the customer which gives the highest inducement for the service provider. Even the Commission is obviously struggling to find even one example for a conflict of interest in the context of advice-free sales. The one example stated – the risk of giving "more prominence to certain products in their product offerings"[9] – can hardly serve as a justification for such drastic measures as the proposed "partial" inducement ban. Self-advised retail clients are certainly beyond the influence of "prominence" of presentation of investment products. This circumstance is particularly evident in the nature of these transactions. The self-advised retail clients have already identified the product before contacting the firm and intentionally forego the advice as well as the suitability test.

- Inducements are essential also for the provision of non-advised services

  It goes without saying that also non-advised services and sales are complex services that cause many, in particular regulatory duties and expenses on behalf of the service provider. These start with the effort necessary for the financial service itself (i.e. the execution as such and/or the reception and transmission of orders) and do not end with various ancillary activities such as compliance with information and reporting obligations (e.g. cost information and product governance obligations), performance of appropriateness tests (if necessary), and other services that may or may not be legally required which now would have to be provided, agreed with the investor and invoiced individually.

  For example, nowadays a large part of transmission of orders services for funds are provided by fund platforms. These platforms receive from the fund managers compensation for their services. Depending on their nature, such payments might be considered (partially) as inducements. In this case fund platforms might not be entitled to receive these payments any longer. In this case, the firms will move out of the European Economic Area and order flows will then be routed over third country platforms only, thus driving jobs out of Europe.

  The same applies to neo-brokers. Buying ETFs or ETF saving plans via digital neo-brokers can count as non-advised transactions because clients act as self-directed investors. Also here, the proposed ban would have negative consequences for retail investors because inducements are regularly paid as reimbursements for transaction costs from asset managers to neo-brokers, which would otherwise have to be borne by the investors themselves. These reimbursements enable millions of retail investors to access cost-efficient ETFs (and ETF saving plans). With the ban preventing these reimbursements in the interest of retail investors, saving digitally would become more costly, especially for the younger generation of "digital natives" with lower saving rates.

[9] P. 16 of the draft Directive

If remuneration from third parties, particularly from issuers or providers of financial instruments, were no longer a legitimate source of compensation for investment firms to cover own costs, services that were hitherto available for retail clients free of charge or at a very moderate price would have to be charged in full to the investor in the future. Given the manifest aversity of retail clients to pay even moderate fees for financial services[10], the result is obvious: even more retail clients would turn away from the financial markets. This will lead to a self-fulfilling prophecy: If the current service providers and distributors are confronted with dwindling retail business, they will withdraw from the market or focus on institutional clients and high-net-worth-individuals only, thus further reducing the choice and attractiveness for the average retail clients. In other words: the proposal would do three of the key objectives of the Retail Investment Strategy a disservice – to reduce costs, to attract more retail clients to financial markets and to ensure a high level of investor protection.

The variety of products and product distributors for (especially self-deciding and self-informing) retail clients will be reduced in future and services for customers will be significantly minimised as a consequence of the proposed inducement regulation.

- The MiFID II regime takes care of any remaining conflicts of interest

  The current MiFID II regime for inducements is an effective and beneficial tool to address conflicts of interest for the benefit of retail clients. It works equally for distribution with or without advice. The less complex a given service is, the more difficult it is to justify any inducements.

  If there are indeed deficits in the application and enforcement of the current safeguards of retail clients' interests among EU Member States, the first step should be to seriously strive for harmonisation in this regard, i.e. via more specific rules on Level 1 and/or stricter enforcement by the ESAs through peer reviews, rather than dumping the current framework altogether in favour of new rules without any track record and with questionable benefit. This is all the more the case since a new regulatory framework will always cause considerable additional costs (one-off as well as ongoing) along the whole distribution chain which will ultimately have to be borne again by the retail investors.

b) Ban on inducements for portfolio management services

Draft Article 24a(1) MiFID is supposed to replace Article 24(8) of MiFID II, banning inducements in connection with portfolio management. The proposed rephrasing is seemingly editorial, given that there is no justification in the Explanatory Statement or draft recitals. It will, however, have a massive impact on existing business models to the detriment of retail investors.

- While asset managers are allowed under the current wording to grant inducements to third parties, they would not be able to do so in the future. We see no benefit in this change. If for any reason the portfolio manager is able to enhance the quality of his service by granting inducements, why should he be forbidden to do so? Legitimate cases for such inducement are, for instance, well-established cooperation models between banks and asset managers for retail portfolio management services. In such models, asset managers enter into

[10] KPMG, The Future of Advice, November 2021, p. 23

portfolio management agreements with (retail) clients and focus on the management of the asset, while the banks take on the client servicing (e.g. suitability assessment of the different portfolios for (potential) clients).

- While an asset manager is not allowed to accept any inducements granted by third parties in order to keep them for himself, he is perfectly allowed under MiFID II to accept inducements in order to pass them on to his clients. This option is extremely important in practice since many retail investment funds distribute a part of their management fees to the sales channels. Under the Commission's proposal, the asset manager would either be forced to refuse the payment rather than passing it on to the client, thus reducing the returns for the investor, or be restricted to a very limited choice of investment product which do not grant such inducements. Neither option is in the interest of the retail clients.

Since there is no risk for a conflict of interest in these situations, we strongly recommend sticking to the current wording of Article 24(8) MiFID II.

3. Draft Articles 24(1a) MiFID/29b(1) IDD: "Best Interest Test"

Our key points:

- The Commission's proposals are extremely ambiguous. Level 1 remains imprecise in many contexts and does neither allow for an exhaustive impact assessment nor serves the firms as basis for implementation. Level 1 rules must be sufficiently clear – it is not permissible to transfer essential political decisions to Levels 2 or 3. Moreover, this leads to diverging implementation standards in the different Member States.

- The combination and interaction of effects caused by the various new proposals remain unclear.

- The proposals are not suitable for achieving the stated goal, namely, to encourage improved and fairer market outcomes and ultimately to create the necessary conditions to raise retail investor participation in capital markets. To the contrary, they may even pose an obstacle for this goal.

- **Instead of burdening distributors with new requirements, the focus should be on the existing ones which may have to be better enforced in certain aspects and, if necessary, tightened up.** MiFID II already contains comprehensive requirements for the goals of the Commission.

The EU Commission proposes to introduce new criteria for investment advice in order to ensure that a firm acts in the best interest of the client, i.e. an "appropriate range" of investment products as the basis for advice, recommending the most "cost efficient" one and, additionally, one without "extra features … that give rise to extra costs". Contrary to the Commission's intention, we consider the present proposals neither suitable nor necessary to achieve this goal.

The example of Germany shows that the existing requirements for advisory services alone can ensure an adequate level of investor protection. The criterion of quality enhancement as a precondition of inducements under MiFID II is implemented by the distributors and must be proven

by the so-called list of inducements and uses. The German supervisory authority BaFin checks this comprehensively. The requirements for the recommendation of equivalent, but less expensive products are also sufficiently observed in Germany.

We therefore advocate that existing regulations should be better implemented and uniformly enforced instead of issuing new time-consuming and costly regulations for all Member States with limited benefit or even detriment for the retail investor.

If, however, legislators should intend to fundamentally overhaul the existing rules, it is crucial to consider our remarks on the Commission's proposals below.

a) Unclear requirements

In its Explanatory Memorandum, the Commission states that "*these amendments further substantiate the obligation for investment firms, insurance undertakings and insurance intermediaries to act in accordance with the best interest of their clients and customers, by introducing a new test with clear criteria which will be applied both in MiFID and IDD (a test which replaces the existing 'quality enhancement' test of MiFID, and the 'no detriment' test of IDD).*"[11]

In contrast to this claim, the proposals on draft Articles 24(1a) MiFID and 29b(1) IDD are so imprecise that their practical impact will nearly exclusively be determined by the future provisions of Delegated Acts according to draft Articles 24(13)(d) MiFID and 29b(2) IDD, respectively. Hence, an evaluation of these proposals is virtually impossible at the current state since we have to work with vague assumptions regarding the content of future RTS which have not been drafted yet.

The following examples illustrate the problem. We focus our remarks on the proposals regarding draft Article 24 MiFID. They apply *mutatis mutandis* also to draft Article 29b IDD.

i. Draft Article 24(1a)(a) MiFID: "appropriate range" of financial instruments

Investment advice to retail clients shall be provided on the basis of an assessment of an "appropriate range" of financial instruments. There is no guidance whatsoever on what makes a range of financial instruments appropriate or not. Instead, specification will be left to future delegated acts according to draft Article 24(13)(d) MiFID.

For the time being, an "appropriate range" of financial instruments could be anything – from a mere number (e.g. "more than three") to a variety of qualitive/quantitative criteria such as a minimum number of product providers (e.g. inhouse and third party), asset classes (e.g. bonds, equity and/or real estate), or product types (e.g. funds and structured notes).

The impact of this lack of clarity is staggering. As a matter of fact, a meaningful appraisal of this "appropriateness" requirement is impossible as long as there is no clarity in this regard. This is why the legislators must not let the reins out of their hands and leave it to future delegated acts to decide on the scope – and thus the ultimate range – of this

[11] COM (2023) 279, p. 16.

provision. Given the immense practical relevance of this definition, it is obvious that the legislators themselves must provide clarity and detail on what they have in mind on Level 1.

In any case, it is crucial that distributors remain free to decide which products and how many products they include in their product and consulting portfolio and want to and can advise on. This is also largely dependent on the size of a distributor. Distributors cannot be forced to offer advice for specific kinds of financial instruments on the market. This is already legally impossible. For example, licences for advice or other services regarding distribution of investment products are usually limited to certain types of products.

Annex I Section C MiFID II defines the different types of financial instruments. This should be the starting point for the "appropriate range of financial instruments". It would not be acceptable for the legislator to make further sub-categories in the different financial instruments. For example, a distributor must not be forced to offer certain types of funds.

If a distributor decides in favour of a certain type of fund (e.g. equity, bond, or real estate), however, several funds of this type should then be offered.

This means that distributors themselves must remain able to decide which products and variety of products they want to include in their advisory services. Within the framework of these selected products, a certain range of products must then be available.

According to legal requirements the client must be informed about the range of product types which is the base of investment advice and whether that the range of products offered is limited (Article 24(4)(a) MiFID II, Article 52(2) Delegated Regulation MiFID II). This approach provides for the necessary flexibility for service providers and ensures sufficient transparency for retail clients with respect to the range of products that is covered by the advice of a certain service provider. This obligation should of course be maintained.

Distributors do not only need to ensure a certain size of variety within their product range, but also that all of these can be advised in an appropriate manner. Therefore, most of the distributors are interested in limiting their product range where they are offering advice.

If these principles would not be incorporated in the future rules, it is to be feared that distributors will discontinue their advisory services due to excessive complexity or too comprehensive requirements for the advisory process. This is likely to apply in particular to small distributors. However, since there are many retail clients who want advice and feel too insecure to act as self-deciders on the capital market, this would be extremely unfortunate. Here, too, the Commission’s declared goal – broader participation of retail clients in the capital market and an increasing number of retail investors will be excluded from the capital market – will not be achieved.

ii. Draft Article 24(1a)(b) MiFID: most “cost-efficient” financial instrument

Distributors should recommend the most “cost-efficient” financial instruments among financial instruments identified as suitable to the client and offering similar features. We note that the Commission used this term rather than simply requiring the “cheapest” instrument. Still, the effect of this semantic difference and the requirements for the advisor

to identify the most cost-efficient product remains unclear. Again, clarification will be left to Level 2, thus leaving the actual impact of the proposal in the dark.

In any case, if an assessment of cost-efficiency is supposed to also include a future-oriented perspective (e.g. target return) to determine “cost-efficiency”, this may seduce product manufacturers to include high target returns to compensate for high costs.

It is important to note that the requirement can only refer to the range of products that the distributor has previously defined for itself for the advice process. The provisions of Article 24(1a)(b) and (c) MiFID are therefore, in a graduated relationship to the provision of Article 24(1a)(a) MiFID.

A comparable requirement already exists under MiFID II. Article 54(9) of Delegated Regulation MiFID II states: *“Investment firms shall have, and be able to demonstrate, adequate policies and procedures in place to ensure that they understand the nature, features, including costs and risks of investment services and financial instruments selected for their clients and that they assess, while taking into account cost and complexity, whether equivalent investment services or financial instruments can meet their client's profile.”*

We assume that the Commission does not want to introduce significantly new requirements with this proposal and we cannot see any additional benefit arising from the new proposed requirement, which was not already achieved by Article 54(9) of Delegated Regulation. Therefore, the wording needs to be clarified. Instead of “equivalent products” as before, the wording refers to products with “similar features”. This creates legal uncertainty because the term "similar features" is unclear.

Distributors might feel obliged to compare products that have different characteristics – the comparison of "apples with pears” is to be feared. This could lead to a situation where, in the end, not the most suitable product for the client but any product is recommended just because it is (minimally) cheaper. It is decisive that the most suitable product for the customer is chosen first. In a second step, the product is selected that has the same features, i.e. is equivalent, and is more cost-efficient.

iii. Draft Article 24(1a)(c) MiFID: Recommendation of products without additional features

Investment firms should be obliged to recommend among the range of financial instruments identified as suitable to the client, a product or products without additional features that are not necessary to the achievement of the client’s investment objectives and that give rise to extra costs.

As we said before, it is important to note that the requirement can only refer to the range of products that the distributor has previously defined for itself for the advice process. The provisions of draft Article 24(1a)(b) and (c) MiFID are therefore, in a graduated relationship to the provision of draft Article 24(1a)(a) MiFID.

It is not clear what is meant by "additional features". Recital 6, which gives some examples, is also of limited help. Sentences 5 and 6 of Recital 6 should be deleted. Given

the immense practical relevance of this definition, it is obvious that the legislators themselves must provide clarity on what they have in mind on Level 1.

In our view, it must be clear that the higher costs must result from the additional features. For example, one could say that a share class of a fund with fx hedging has an additional feature – but this does not automatically result in higher costs. The link between feature and costs is therefore, essential.

We fear that this additional requirement will lead to the cost factor becoming the sole feature when recommending products. Ultimately, however, it is a matter of determining which product is suitable for the client, and the potential returns must not be disregarded. Focusing solely on costs is not in the interest of the investor.

The more detailed the customer's wishes are asked in the suitability test, the less likely it is that there will be equally suitable products without additional feature in the end.

Therefore, Article 24(1a)(c) could in our understanding have only relevance in situations when the range of as suitable identified financial instruments includes also products with additional features that are not necessary to the achievement of the client’s investment objectives.

Finally, it is not clear why under Article 24(1a)(b) "financial instruments" (plural only) are to be recommended whereas under Article 24(1a)(c) "product or products" (singular and plural) should be recommended.

III. Proposal for a Regulation[12] (PRIIPs Regulation)

Our key points:

- Delete the proposal to introduce a "product at a glance" dashboard.
- Extend the proposed section on environmental sustainability to all core sustainability characteristics to be presented in line with the standardised disclosures under SFDR.
- Adjust the provision of the PRIIPs KID for savings plans and information on performance and costs.

Concerning the present proposals

1. Amendments to Article 8

a) New point (aa) in Article 8(3)

Under an additional section titled “Product at a glance” a “dashboard” is to be added to the PRIIPs KID with some summarised information. We reject this for the following reasons:

- The PRIIPs KID is already a short information document which is intended to provide investors with the most important information in a condensed form. It is astonishing that the Commission sees room for presenting this short information once again in a further abridged form. We do not think this makes sense.
- It is already a challenge for manufacturers to present all the required information in the permitted three pages. The addition of further sections is at the expense of the comprehensibility of other sections – because cuts have to be made somewhere.
- It is doubtful that it is in the interest of investors. Further information, e.g. what is meant by the risk indicator at all, is located further down in the PRIIPs KID. Thus, repetitions happen – this is not in the interest of transparency and, in case of doubt, rather leads to confusion of the investor.

We are therefore, clearly in favour of not including the proposed dashboard.

b) Deletion of Article 8(3)(b)

We welcome the deletion of the comprehension alert "You are about to purchase a product that is not simple and may be difficult to understand". The alert has no added value for the investor as it is not specific. PRIIPs are products that are developed especially for retail investors. Such a "warning" alert, which only refers to a certain type of product without considering it individually, only deters the retail investor. This contradicts the declared aim of the Commission to strengthen the participation of retail investors in the capital market.

[12] COM 2023(278)

c) New point (ga) in Article 8(3)

We disagree with the Commission's proposal for a dedicated new section on environmental sustainability for the following reasons:

- Focus on selected KPIs for environmental sustainability is entirely inappropriate to inform investors about the key sustainability characteristics of PRIIPs that can relate to environmental or social factors and in many cases follow a holistic ESG approach.

- Investors who are asked about their sustainability preferences at the point of sale will not be able to relate the criteria for sustainability preferences presented in the suitability questionnaires by advisers to the relevant product characteristics displayed in the PRIIPs KID. This will only add to the current confusion and uncertainty about sustainable investing.

- Contrary to the Commission's assumption in Recital 4, last sentence, of the proposed amending Regulation, disclosure of "expected greenhouse gas emission intensity" associated with the PRIIP is required so far neither by SFDR nor by any other piece of EU legislation. Products disclosing under Articles 8 or 9 SFDR are not even required to report such KPI as part of their periodic disclosures. In contrast to the Commission's claims, the proposed amendment would thus introduce an additional reporting burden on PRIIPs manufacturers.

Given that the Commission's approach is to introduce a sustainability-dedicated section specifically for products subject to pre-contractual disclosure obligations under SFDR, we strongly suggest creating a clear reference to the content and presentation of ESG-related information in the pre-contractual annexes for Article 8 and Article 9 products. Specifically, the section should be renamed in "*Does this product have environmental or social characteristics or a sustainable investment objective?*" For products disclosing under Articles 8 or 9 SFDR, two options for providing the relevant information should be considered:

- Option 1: Including a direct link to the pre-contractual ESG annex under SFDR that would provide investors with the full overview of the sustainability features and commitments (this option is preferable in case the 3-pages-limitation of length will be maintained);

- Option 2: Display the core sustainability characteristics directly in the PRIIPs KID by including the standardised product dashboard that is presented at the top of the pre-contractual SFDR annex. We recommend referring to the dashboard version as proposed by the ESAs in the recent joint consultation on the review of the SFDR DR[13]. The ESAs' suggestion in this regard is to limit the dashboard to the core features and commitments that are relevant in terms of sustainability preferences at the point of sale. The final recommendations for respective changes shall be presented by the ESAs by October 2023.

[13] Cf. Joint Consultation Paper on Review of SFDR Delegated Regulation regarding PAI and financial product disclosures, revised templates for pre-contractual templates to Annexes II and III.

2. Amendment to Article 10(2)

The ESAs shall submit draft regulatory technical standards to determine the conditions under which the key information document must be revised, distinguishing between PRIIPs that are still made available to retail investors and PRIIPs that are no longer made available.

We are not aware of any problems with the implementation of the existing requirements (Article 10 PRIIPs Regulation in connection with Articles 15 and 16 Delegated Regulation to the PRIIPs Regulation) that would require further concretisation by the Commission.

In particular, the cases in which a PRIIP is no longer made available are sufficiently clear. Closed-ended funds whose number of investors is limited from the outset can be mentioned here, for example. Or also all kinds of funds if no new units are issued.

3. Amendment to Article 14

a) Article 14(1)

We very much welcome the fact that the electronic provision of the PRIIPs KID is to represent the standard case in future. This corresponds to the requirements that already apply today under MiFID II. Digital formats are becoming increasingly important for investors – but the option of continuing to receive the PRIIPs KID in paper form if desired takes into account the needs of all investors. The conversion from paper format to digital formats is also important, particularly from a sustainability point of view.

b) Article 14(2)

The introduction of an interactive tool is also understandable under the aspect of advancing digitalisation and does justice to the various digital access options. We welcome the fact that this should be introduced as a voluntary option to the standard PRIIPs KID.

In the existing legal framework, the PRIIP-manufacturer “produces” the KID (Article 5 PRIIPs Regulation) and this KID is then “provided" by the distributor. Article 14(2) introduces the option to provide the KID electronically via “an interactive tool”.

The responsibilities for the provision of the tool are not entirely clear at this point. It should be borne in mind that some information can only be provided by the manufacturer, other only by the distributors. If such an interactive tool is introduced, it should be exactly specified which information is actually suitable for customisation.

c) Article 14(5)

The requirement to inform the retail client "electronically or in written form of the address of the website and the place in the website where the key information document can be accessed" has apparently been transferred from the current wording of Article 14(5)(c). However, this requirement has been rendered irrelevant by the decision that the standard provision should now be in an electronic format. Up to now, special requirements have applied to the provision of the KID on a website (as a possibility of an electronic format), the

one-time information where the KID can be accessed on the website was part of this and also made sense in this context.

The proposed paragraph 5 is completely unclear: On the one hand, it is not clear whether the reference should be made regularly for each acquisition (which in turn could lead to a break in the system) and what is meant by written form (paper-based information?).

Article 14(5) should therefore, be deleted without replacement.

Topics that are not covered

We strongly advocate that further important topics be incorporated in Level 1:

1. Saving Plans

Under Article 13(4) PRIIPs Regulation distributors would be obliged to provide a KID when conducting the savings plan and afterwards, every time the KID has been modified according to the requirements of Article 10 PRIIPs Regulation.

Savings plans on funds are very popular in Germany. For instance, one large German fund manager alone has a total of some 4.5 million savings plans under administration. Most of these contracts have been concluded years ago.

Due to the fact that funds will fall into the scope of the PRIIPs Regulation and therefore, Article 13(4) PRIIPs Regulation will apply, many banks and savings banks currently only enter into a savings plan if the client opens an electronic mailbox allowing to provide the KID electronically.

In the past, there has been no reason to open an electronic mailbox when conducting a savings plan (since the KID under the current regime only needs to be provided once). That is why many clients do not have an electronic mailbox. In the case of the fund manager with 4.5 million savings plans electronic communication via an electronic mailbox has been agreed with only 21% of the clients.

This would mean that the KIDs for more than 3.5 million savings plans need to be sent by post (whenever there is a change in the KID) if a more flexible approach is not allowed. Given the current postage rate in Germany of 85 ct. per standard letter, one information round via letter amounts to the sum of nearly 3 million Euro! The procedure is also very burdensome and would also enervate the average retail investor by a frequent inflow of mail.

Also the ESAs have recognised this problem in their "Final Report following consultation on draft regulatory technical standards to amend the PRIIPs KID"[14] and propose the following solution:

Where successive transactions regarding the same PRIIP are carried out on behalf of a retail investor in accordance with instructions given by that retail investor to the person selling the PRIIP prior to the first transaction, the obligation to provide a key information document under

[14] Draft Final Report following consultation on draft regulatory technical standards to amend the PRIIPs KID.

paragraph 1 shall apply only to the first transaction, and to provide a detailed description where the revised key information document in accordance with Article 10 can be found. Additionally, prior to an additional subscription, the latest revised version of the key information document shall be provided to the retail investor upon request. (p. 44)

This solution is both practical and in the interest of investors. We strongly recommend taking it on board when re-opening the PRIIPs Regulation.

2. Limits of standardisation: Performance information/Presentation of costs

We believe that the current degree of standardisation of the PRIIPs KID that enforces comparability of information for all PRIIPs is not suitable to ensure adequate product information in every case.

For investment funds, the following two subjects are critical:

- Performance information: The discussion about appropriate performance scenarios for investment funds continues since the inception of the PRIIPs idea. After many rounds of debates involving different possible approaches, we must come to the conclusion that performance scenarios are not the right way forward for informing investors about the performance prospects of linearly performing funds that are dependent on the performance of their portfolio assets. Therefore, we insist on our long-standing demand (which is shared by investor representatives)[15] that past performance should be the only performance indicator for linear products in line with the current UCITS KIID framework.

- Presentation of costs as monetary amounts: The PRIIPs Regulation requires presentation of total aggregated costs based on several assumptions in particular with regard to the investment amount and the annual performance. Especially the latter causes significant problems for illustration of cost components that are triggered by the annual yield like performance-related fees. Under the Delegated Regulation 2021/2268 for instance, it is foreseen to present fund cost components in the table “composition of costs” based on 0% annual return. For performance fees, this should then mean that in most cases, no cost amount will be shown (because no performance fee is generally being charged in such circumstances), even if a product has actually charged performance fees in the preceding years (and is likely to charge them in future). This example shows that a standardised approach to cost disclosures in any circumstances is not appropriate for the purpose of meaningful investors information. Given their dependence on the actual performance level, performance-related fees should not be accumulated with other cost elements, but shown separately on the basis of the recently generated fees from the past in accordance with the current UCITS KIID standard.

- Another area of concern is the problem of implicit transaction costs computed under the arrival price methodology. The methodology itself that is enshrined in Annex VI of the PRIIPs RTS generates positive and negative transaction costs since it compares actual execution prices to mid-market prices (arrival prices) prior to the execution of the order. Because the existence and disclosure of negative costs is not easily understood by retail

[15] See Better Finance, betterfinance.eu/wp-content/uploads/PRIIPs-Position-Paper-BETTER-FINANCE.pdf

investors this disclosure of negative costs has been prohibited in the latest revision of the PRIIPs-RTS. In our view a method the results of which are not comprehensible for the consumer should not be considered valid in general because it then renders the whole formula useless. Therefore, rather than prohibiting disclosure of the result, the formula itself should be removed. In this matter we point to Article 12 of the PEPP-Regulation (EU 2021/473) where the disclosure of transaction costs is limited to explicit costs only.

These examples illustrate that comparability of PRIIPs disclosures must be always considered secondary to the primary purpose of the PRIIPs KID which should be ensuring meaningful key investor information and enabling (self)-informed investment decisions.