European Financial Markets Lawyers Group

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European Commission

Ms Maria Luís Albuquerque

Commissioner in charge of Financial Services and the Savings and Investments Union

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Hungarian Presidency of the Council of the European Union

Mr Mihály Varga

President-in-Office of the Economic and Financial Affairs (ECOFIN) Council

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Re: Retail investment strategy

Dear Ms Albuquerque, dear Mr Varga,

As you may know, the European Financial Markets Lawyers Group (the "**EFMLG**") is a group of senior legal experts from the EU banking sector dedicated to making analysis and undertaking initiatives intended to foster the harmonization of laws and market practices and facilitate the integration of financial markets in Europe. The members of the Group are selected on the basis of their personal experience amongst lawyers of major credit institutions based in the EU active in the European financial markets. The Group is hosted by the European Central Bank.

As already expressed in the EFMLG letter dated 25 September 2023 (the "**Initial EFMLG Letter**" included as an annex to this letter), the EFMLG supports the aims of the Retail Investment Strategy ("**RIS**") as a way to increase retail participation in European capital markets at a fair price.

Over the past few months, we have observed the European Parliament and the Council making progress in their respective positions on the RIS, which we welcome, given the importance of this initiative. Similarly, we have noted how European authorities have emphasized the urgent need to decisively advance in the different initiatives comprising the Capital Markets Union ("**CMU**"), as a key aspect to improve the competitiveness of the European Union and accelerate the growth of our companies and the real economy. The EFMLG welcomes those messages and shares the view about the importance of the CMU for the European Union, its companies and citizens.

Without prejudice to the more specific observations in our Initial EFMLG Letter, in this letter we would like to convey the opinion of the EFMLG regarding the need to align both initiatives, RIS and CMU, and to share our concerns about how some of the RIS proposals could negatively impact the CMU. Our concerns particularly relate to those proposals that could affect the existence of a homogeneous and levelled regulatory framework across the European Union that facilitates a truly unified, integrated and competitive market.

I.- RIS and CMU

As stated on the European Commission's dedicated webpage, the CMU "*is a plan to create a single market for capital. The aim is to get money – investments and savings – flowing across the EU so that it can benefit consumers, investors and companies, regardless of where they are located*." In this context, the interconnection and mutual dependency between the RIS and the CMU is evident. In particular, we would like to stress the importance of the last part of the sentence, "*regardless of where they are located*", as it is linked with the EFMLG's objective of fostering the harmonization of laws and market practices and facilitate the integration of financial markets.

In our opinion, the existence of a single, clear legal framework in the European Union and uniform regulatory criteria across all Member States are key components to ensuring that capital effectively flows throughout the European Union, and that investors and companies have the ability to invest and receive investment services regardless of where they are located. To that end, it is of the utmost importance that the regulatory actions taken to increase participation of investors (including retail) in the capital markets do not undermine the single legal framework nor give rise to regulatory arbitrage. European financial regulation must be aimed at strengthening the competitiveness of the EU single market, avoiding the creation of silos in each of the Member States due to regulatory specificities.

II.- Risk of divergencies

Before the adoption of the final texts that make up the RIS, we want to convey our concerns in this area, specifically regarding some proposed modifications to Directive 2014/65/EU[1] (**"MiFID 2"**):

1.- Suggested changes to Article 24(12) of MIFID 2: Article 24(12) MiFID 2 currently in force outlines a process whereby a Member State who wishes to impose "*additional requirements on investment firms*" on the matter covered by Article 24 'General principles and information to clients', must **i)** notify the European Commission without undue delay and **ii)** include a justification for that requirement.

The requirement must **i)** be proportionate and **ii)** address specific risks to investor protection or to market integrity which are of particular importance to the market structure of that Member State. The European Commission has two months from the notification to provide its opinion on the justification and proportionality of the additional requirements proposed by the Member State. Additionally, the Commission shall make public on its website the additional requirements.

In short, although this article opens the door to local divergences, it introduces a proportionality criterion by which a third party (the European Commission) assesses the specific proposal and determines whether it is balanced with the risks it is intending to address.

The **General Approach** agreed on by the Council of the EU on 12 June 2024:

[1] Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU.

i. **expands** the scope of Article 24(12) MiFID 2 to allow Member States to **impose "additional requirements" in relation to two new clauses and related matters: 1) Article 24b (costs and charges) and 2) Article 24c (marketing communications and practices**[2]**)**,

ii. **introduces** a **new provision** i.e. **paragraph 9** in the **newly introduced article dedicated to inducements (i.e. Article 24a)** which explicitly entrusts Member States with the power **1) to prohibit or restrict inducements and 2) to impose stricter requirements in respect of the inducement test**

iii. **removes the European Commission's review from the process** and, therefore, its ability 1) **to assess** the **justification** and the **proportionality** of these additional requirements and 2**) to adopt** an **opinion** about these requirements

iv. **removes any transparency requirement.**

These suggested amendments raise concerns regarding the risk for market fragmentation, unlevelled playing field and the weakening of the principle of harmonized regulation across the EU.

Please find below our detailed arguments about these changes.

i. We believe these amendments directly 1) contradict the spirit of the conclusions of the Special European Council held on 17 and 18 April 2024 as well as of Recommendation #15 issued by ESMA in the position paper on "Building more effective and attractive capital markets in the EU" issued on 22 May 2024 and 2) are at odds with the Letta Report. The Special European Council, ESMA and Mr. Letta call for ensuring the harmonization of EU legislation and improving consistency of implementation and interpretation.

ii. We also call out Recommendation #16 in the ESMA report above that '[t]he European Commission and ESMA should take the opportunity of the next legislative cycle to focus on streamlining and tidying up the single rulebook. During legislative reviews, the focus should be on identifying and addressing inconsistencies and complexities across sectoral rules.'

iii. These amendments seem to be directly transposed from IDD[3] into MiFID 2 per *analogiam legis*. From a legal and technical perspective, their consistency with the overall MiFID 2 architecture is questionable:

   - Unlike MiFID 2, IDD is a "minimum harmonization" Directive, (i.e. Member States are not prevented from maintaining or introducing tighter rules). This peculiar nature of the IDD was explicitly acknowledged by the co-legislators.[4]

   - With specific reference to the treatment of the inducements, IDD adopts a different (lighter) approach to the inducements: IDD allows for the payment or receipt of inducements to the extent they do not have a detrimental impact on the quality of the

[2] The European Commission text already introduced the possibility for Member States to impose the use of risk warnings by investment firms in information materials related to particularly risky financial instruments where those instruments could pose a serious threat to investor protection. As stated in the Initial EFMLG Letter, the obligation itself seems to be reasonable, but the possibility that some local authorities trigger it whilst others do not goes against the spirit of the European single market and also against one of its main purposes of encouraging cross-border investment.

[3] Article 29(3) of Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution. No material change to this clause is being discussed during the RIS legislative proceeding currently under way.

[4] For example, Recital 3 of the IDD states: "(..)this Directive is aimed at minimum harmonisation and should therefore not preclude Member States from maintaining or introducing more stringent provisions in order to protect customers, provided that such provisions are consistent with Union law, including this Directive".

service ("no detriment test") while inducements under MiFID 2 must enhance the quality of the service in order to be allowed ("quality enhancement test")[5].

In short, the changes proposed in the Council General Approach diverge from the CMU objective of getting *investments and savings flowing across the EU so that it can benefit consumers, investors and companies,* ***regardless of where they are located.***

While we understand the challenge that reaching an agreement that reflects the different interests and realities of the various Member States poses, it is of vital importance that such agreements are reached. If it is not possible to achieve a consensus that results in market unity, the co-legislators should assess the merits of the proposed changes while taking into account the potential scope for market fragmentation under those proposed changes.

2.- Value for money ("VFM") and national benchmarks: without prejudice to the comments we already conveyed in our Initial EFMLG Letter regarding our concerns about the price control mechanism included in the value for money proposal, the creation of national indices (as suggested by the European Parliament) exacerbates the risk of creating national barriers rather than single European markets. In our opinion, national regulations and criteria should be avoided or, ultimately, limited to the minimum necessary, which includes the definition of national benchmarks for VFM purposes.

We are also concerned about the Council position which expressly allows Member States to provide for the possibility for investment firms to opt, for the purpose of the market comparison in their value-for-money assessment processes, from comparing a financial instrument with the relevant EU benchmark, instead of a peer group. Since such opt-out might result in different approaches across Member States, this proposal risks i) further market fragmentation in contrast with the Capital Markets Union and ii) weakening the principle of harmonized regulation across the EU.

III.- Risk of legal uncertainty

As we indicated in our Initial EFMLG Letter regarding the European Commission's text, some of the proposals included in the co-legislators' texts introduce vague legal concepts[6] and obligations without clear consequences or action criteria[7]. This may lead to legal uncertainty and, due to their complexity, may result in different interpretations by various stakeholders[8].

In addition, notwithstanding the potential developments that will be implemented through level 2 regulation and ESMA guidance, such uncertainty may lead to more national Q&A and other interpretative documents from national competent authorities, with the risk of exacerbating market fragmentation and an unlevelled playing field.

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[5] For the sake of completeness, both MiFID 2 and IDD both currently prescribe that the inducement must not impair compliance with the duty of the investment firms (in the case of MiFID 2) or with the duty of the insurance intermediary or the insurance undertaking (in case of IDD) to act honestly, fairly and professionally in accordance with the best interest of its clients.

[6] Terms such as "an appropriate range of instruments", "most cost-efficient", "additional features" or "extra cost" included in the so called low cost driven advice are open-ended and, together with the complexity of the assessment, may lead to legal uncertainty and different interpretations by stakeholders.

[7] For instance, in connection with VFM, the idea of the benchmarks to be used only for supervisory purposes, without further guidance about the consequences.

[8] Harmonising the definition of key concepts in the EU regulatory frameworks stands out as one of the policy priorities set out by the ECB in the document "Financial Integration and Structure in the Euro Area" (June 2024).

A clear and more simplified regulatory framework would definitively help market participants to provide investment services and, thus, increase investment by consumers and companies. We have seen in the recent past how some regulations (ie: BMR or MiFIR) need to be amended to introduce a proportionality approach, foster competitiveness of the European Union and reduce administrative burdens[9]. The RIS should also take that approach and avoid introducing more complexity and administrative burdens to a commercial process which is already burdensome even for the simpler financial instruments (i.e.: shares or bonds)[10].

IV.- Conclusions:

We are convinced that the European Union harmonization of financial markets legislation and practice (harmonization of laws, market practices and regulatory criteria) will increase the provision of cross-border investment services in the European Union and thereby bring us closer to the achievement of the objectives sought through the CMU and the RIS. We encourage the co-legislators to continue working strongly towards such harmonization and suggest that harmonization is in principle always preferred to the inclusion of additional restrictions to the provision of cross-border services or to the possibility for Member States including their regulatory bodies to deviate from the common regulatory framework.

The EFMLG remains at your disposal for any assistance or support you may need on this matter. Please kindly keep the EFMLG informed on the progress on the matters covered in this letter. We thank you sincerely for your attention.

Yours faithfully,

Fernando Conlledo

Vice Chairman of the EFMLG

Encl. Annex: Initial EMFLG Letter dated 25 September 2023

[9] A recommendation to account for the EU's global competitiveness in policy making stands out as one of the recommendations delivered by ESMA (#20) in the position paper mentioned above in the body of the text.
[10] We refer here to our comments in the Initial EFMLG Letter where we stated the need to reassess the proposed changes in the appropriateness and suitability test and the removal of the changes introduced in MiFID Quick Fix for the cost and charges regime.