

"Client protection on European financial markets – from inform your client to know your product and beyond : an assessment of the PRIIPs Regulation, MiFID II/MiFIR and IMD 2"

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Abstract

This article aims at assessing some of the most recent developments in European law which are said to improve clients' protection buying on European financial markets. It focuses on (a) provisions relating to pre-contractual and marketing information obligations, and related liability, supervision and sanction regimes, (b) developments in product governance arrangements which are meant to reduce potential risks of failure to comply with investor protection rules and on (c) "product intervention powers" of supervisory authorities, considered as the last resort measure for investor protection purposes. This article concludes that European regulators move in the right direction where they focus on point-of-sale regulation and product governance arrangements. This article also stresses that appropriate rules should go hand in hand with a change of culture to bring back ethos at manufacturers' and distributors'. Not only the letter of the rules, but more fundamentally, the spiri...

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Client protection on European financial markets – from inform your client to know your product and beyond : an assessment of the PRIIPs Regulation, MiFID II/MiFIR and IMD 2¹

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I. Introduction

Retail investors are encouraged to invest on European financial markets. Their investments contribute to finance the economy.² Their investments should also help them build or simply protect their wealth for health, education and retirement needs at a time where they should expect less from governments.

This political encouragement could not go without regulators dedicating particular attention to their protection. Indeed, compared to the product manufacturer and the financial intermediary, they are the “weak party” on financial markets. Their lack of appropriate competence to understand the risks related to their investments, their limited cognitive capabilities and their behavioral biases could all lead to disastrous investment decisions, with great social and economic impacts. Well-thought rules and regulations contribute to build their confidence to make retail financial markets a success.

The regulations analyzed in this article were inspired in some respects by the works done at international level. After the financial crisis, international regulatory bodies focused primarily on the sale of “structured products” to retail investors. IOSCO suggested a toolkit outlining regulatory options to regulate retail structured products along the value chain of the product, from issuance to distribution to investment.³ ESMA issued good practices to national competent authorities for product governance arrangements for structured retail products, with the belief that “*sound product governance arrangements are fundamental for investor protection purposes, and can reduce the need for product intervention actions by competent authorities*”.⁴ They were inspired in part by the joint position of the European Supervisory Authorities on manufacturer’s product oversight and governance processes

which aim at strengthening manufacturer’s internal controls prior to product launch.⁵

Immediately after the financial crisis, the European Commission focused on stabilizing financial markets and the banking sector.⁶ It then turned to address retail financial markets weaknesses. Stories of mis-sellings of financial products are indeed numerous.⁷ In an effort to reduce or even avoid them, European instances issued what some refer to as a regulatory tsunami. This article aims at assessing some of the most recent developments in European law which are said to improve clients’ protection buying on European financial markets. It focuses on (II) provisions relating to pre-contractual and marketing information obligations,⁸ and related liability, supervision and sanction regimes,⁹ (III) developments in product governance arrangements which are meant to reduce potential risks of failure to comply with investor protection rules and on (IV) “product intervention powers” of supervisory authorities, considered as the last resort measure for investor protection purposes.¹⁰

Given its sectoral approach for financial regulation, the European Union introduced distinct regimes for banking, securities and insurance. This article is concerned with financial products that have an investment element, including investment-based insurance products (“IBI products”).¹¹ It stresses the similarities and differences to assess whether there is a “level playing field” between competing (or substitutable) products in terms of protection of investors’ best interests.

This article concludes that European regulators move in the right direction where they focus on point-of-sale regulation and product governance arrangements. This article also stresses that appropriate rules should go hand in hand with a change of culture to bring back ethos at manufacturers’ and distributors’. Not only the letter of the rules, but more fundamentally, the spirit of the rules should be complied with at

1 Researches for this contribution were made until 1st July 2014.

2 The size of the European market of packaged retail and insurance-based investment products was valued at approximately €10 trillion by the European Commission in the context of researches relating to the PRIIPs Regulation. Outstanding amounts of structured products – a sub-category of PRIIPs – sold to retail investors in the European Union accounted for around € 770 billion at end-2012 according to ESMA, Economic report, Retailisation in the EU, 3 July 2013, at 15 (citing structuredRetailProducts.com).

3 IOSCO, Regulation of retail structured products, Final Report, December 2013.

4 ESMA, Opinion – Structured retail products – Good practices for product governance arrangements, 27 March 2014, at 2. This opinion covers *inter alia* product design, target market, distribution strategy and product testing. See also, ESMA, Investor warning – Risks of investing in complex products, 7 February 2014 (setting out the different risks).

5 Joint position of the European Supervisory Authorities on manufacturer’s product oversight and governance processes, JC-2013-77, 28 November 2013 (senior management to take responsibility for compliance with the product governance processes ; target market ; product testing ; distribution strategy ; periodic monitoring of the product).

6 See, *inter alia*, the new framework for financial supervision and oversight of systemic risk, the regulation on derivatives, the new capital requirements directive, the alternative investment fund managers directive, and the new credit rating agencies regulation.

7 € 2 trillion of losses were sustained between end of 2007 and end of 2008 in the European packaged retail investment products’ market.

8 Specific disclosure obligations relating to conflicts of interests and remunerations are outside the scope of this contribution. So is client reporting.

9 This contribution will have a companion article to be published in 2014 in the *Revue Internationale des Services Financiers*. The latter will look at some of the most recent developments in Belgian law in the topics covered here to assess to what extent they are compatible with (existing or forthcoming) European law.

10 This article thus leaves aside other important investor protection topics, including independent advice and remuneration arrangements.

11 This article therefore does not consider banking products, including the consumer credit directive.

each level of the distribution chain. Only that combination will bring back investors' confidence for the long-term.

II. The PRIIPs Regulation

1. Background

The final report of the behavioural study commissioned by the European Commission in 2010 suggested that simpler and standardised product information could greatly improve European consumers' investment decisions.¹²

On 3 July 2012, the European Commission published a proposal for a Regulation on "Key Information Documents" for investment products.¹³ On 4 April 2014, the Council of the European Union announced it reached political agreement with the European Parliament, which formally adopted the text at a plenary vote on 15 April 2014, effectively ending the legislative process. The final, marked-up approved compromise text was also published online and is referred to in this contribution.¹⁴

The PRIIPs Regulation forms an important part of the Commission's wider package of proposals on the regulation of PRIIPs. It complements the investor protection measures on investment advice and sales services that are being extended to apply to all products covered by the PRIIPs Regulation under MiFID II¹⁵ and IMD 2.¹⁶

2. Scope

Despite the European Parliament's attempts to extend the scope of the PRIIPs Regulation,¹⁷ the Regulation will apply only to "packaged retail investment products" and to "insurance-based investment products".¹⁸ It will only apply when products are sold to retail investors.¹⁹

To be a "packaged product", investors must be exposed to fluctuations in the market, rather than obtaining a simple interest rate for instance. By way of example, such fluctuations might be due to exposure to reference values or to the performance of one or more assets which are not directly purchased by the investor. In other words, some sort of "wrapping" mechanism, e.g., pooling of capital, use of derivatives, or reference rates, must intervene between them and the market.

The investment component of the product means that the product must offer medium-to-long term capital accumulation that beats the risk-free rate, typically by combining exposures to multiple underlying assets. Individual PRIIPs may offer additional features, e.g., capital guarantees or insurance.

Broadly speaking, PRIIPs can be categorised into four groups: investment funds, IBI products, retail structured securities and structured term deposits.²⁰ The definition of PRIIPs includes UCITs and other investment funds,²¹ all structured products, whatever their form (packaged as insurance policies, funds, securities, structured deposits further to their MiFID II definition, or banking products), insurance products whose surrender values are determined indirectly by returns on the insurance company's own investments or even the profitability of the insurance company itself (including with-profits), as well as derivative investments and some instruments issued by Special Purpose Vehicles. The PRIIPs Regulation also captures those investment products that may not have a packaged element but describe themselves as "guaranteed" where the investment return may vary, or even where all or a portion of the investment return is guaranteed. PRIIPs exclude products with no investment risk (products where the precise rate of return is set in advance for the entire life of the product);²² deposits other than structured deposits; non-life insurance products, or life insurance products where the benefit is payable only on death or in respect of incapacity due to injury, sickness or infirmity, as any surrender value of those products will not be exposed to market fluctuations; pension products which provide an investor with an income in retirement and entitle the investor to certain benefits, and occupational pension schemes covered by the Occupational Pensions Funds Directive or the Solvency II Directive;²³ and pension products for which a financial contribution from the employer is required by national law and where the employee has no choice as to the pension product provider.

12 Decision Technology Ltd, Consumer Decision-Making in Retail Investment Services: A Behavioral Economics Perspective, Final Report, November 2010, at 19.

13 The history of the PRIIPs initiative dates back at least to 2009, where, contrary to the text eventually published and which focuses on disclosure, point-of-sale regulation was contemplated. See for more details, G. Schaecken Willemaers, *Product Intervention: a European perspective*, in Laure Nurit-Pontier and Stéphane Rousseau (dir.), *Risques, crise financière et gouvernance: perspectives transatlantique*, Montréal/ Zurich/Limal, Éditions Thémis/Schulthess/Anthémis, 2013, at 25.

14 See position of the European Parliament adopted at first reading on 15 April 2014 with a view to the adoption of Regulation (EU) No .../2014 of the European Parliament and of the Council on key information documents for packaged retail and insurance based investment products (PRIIPs).

15 See the definition of "financial instruments" in Annex 2 C MiFID II which covers PRIIPs.

16 See below for full references to these directives.

17 During dialogue negotiations, the European Parliament proposed almost 400 pages of amendments, including a massive extension of scope whereby the Regulation would cover all retail investments.

18 Note that the compromise text uses the term "PRIIPs" next to the word "PRIIPs". But "PRIIPs" now means something different to what it used to. "PRIIPs" in the new text now just means "PRIIPs" minus insurance-based investments (which were included in the original definition of "PRIIPs"). This contribution will use "PRIIPs" throughout when referring to all retail investments, insurance or otherwise, covered by the Regulation.

19 See below.

20 See European Commission, Key Information Documents (KIDs) for packaged retail investment and insurance products - Frequently asked questions, 15 April 2014.

21 During a transitional period of 5 years, UCITs will continue to use the KIID provided in the UCITS directive as they do today. After that 5-year period, the relevant KIID provisions shall be repealed from the UCITS directive or maintained but aligned. There is also a possibility to extend the transitional period. This will follow a review of the effectiveness of the Regulation which is set to take place 4 years after its implementation.

22 Any securities exchangeable or convertible into shares or other securities will not fall within this exclusion.

23 Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) (recast), Official Journal, 17 December 2009, L 335/1. It will come into force on 1 January 2016.

3. The KID

3.1. Who to draft ?

Product manufacturers are responsible for drawing up (and keeping up-to-date) a KID, and publishing it on their website before a PRIIP can be made available to retail investors. Preparation of the KID can be delegated to a third party, but the manufacturer will still remain liable for any failings. The European Parliament's suggestion that manufacturer and distributor should both be responsible for drawing up the KID was ultimately abandoned. "Manufacturers" also includes anyone who has made substantive changes to an existing PRIIP including, but not limited to, altering its risk and reward profile or the costs associated with an investment in the PRIIP, for instance by combining products.

3.2. When to provide ?

3.2.1. Ex-ante notification to competent authorities

It is up to Member States to require in national law provisions product manufacturers to provide competent authorities with copies of every KID before commencing any marketing activities (*ex-ante* notification). The European Parliament's suggestion that competent authorities should need to sign-off every KID before a product can be marketed was, however, ultimately abandoned in the final text, as was the proposed requirement that manufacturers should regularly (re)assess the suitability of products for the needs of retail investors *via* a "documented product approval process".²⁴

3.2.2. Provision to retail investors

The KID must be provided before concluding a sale.

The Regulation provides for one limited exception to *ex-ante* provision of the KID, if certain conditions are met.²⁵ The KID will then have to be provided without undue delay, after the conclusion of the transaction. This will apply in case of unsolicited distance sale where the *ex-ante* provision of the KID is not possible and the retail investor consents to the *ex-post* provision of the KID.

Detail on the timing for providing disclosure is intended to be further developed in Level 2 measures.

3.3. Who to provide and to whom ?

Product distributors/advisers – including the product manufacturer for direct sales – must "provide"²⁶ the KID to retail investors. Product manufacturers will have to set up dedicated KID websites where the library of KIDs will be contained in order for distributors to be able to provide them to retail clients.²⁷ They will also have to ensure it is clear between themselves and their distributors who has the responsibility for providing the KID to retail investors.²⁸

²⁴ But see the product approval process in MiFID II (below).

²⁵ Article 12, 2a of the compromise PRIIPs Regulation.

²⁶ Like under the UCITs directive, it is not sufficient to make the KID "available" to retail clients.

²⁷ And one should make sure the hyperlinks on the website work.

²⁸ Where the distributors/advisers consider they are not responsible for

It is not required to be provided to any investor other than "retail investors"²⁹ or to a person with written authority to make investment decisions on behalf of that investor.³⁰ This means that the product must be meant to retail investors. This is something determined at the point of sale, and not by reference to the manufacturer's intentions – although no-one would need to prepare a KID for a product which is never going to be sold to retail investors.

3.4. What to provide ?

The KID is a stand-alone document, separate from marketing material and any other disclosures required under other regimes which will continue to exist in parallel. The KID constitutes pre-contractual information and must be accurate, fair, clear and not misleading. It must provide key information and be consistent with all other information about the PRIIP.³¹

The Regulation also sets out principles for style and presentation. The KID must be short and non-technical, a maximum of three A4-sized paper, use characters of readable size and be presented in a common format allowing investors to compare details of different PRIIPs. It shall not contain cross-references to marketing material. It may contain cross-references to other documents including a prospectus where applicable, and only where the cross-reference is related to the information required to be included in the KID by the Regulation. The Regulation specifies in detail the content of the KID ; the order in which it should be arranged ; and even some of the required boilerplate text and section headings.³² Regulatory technical standards ("RTS") will be adopted to further detail the content and presentation of the KID, including disclosures of risks and costs for specific types of PRIIPs.

The information in the KID must be kept up-to-date. This requires frequent review of the KID and updated disclosure where there has been a change to the PRIIP.

Details on the frequency of the review and the conditions for updating disclosure are to be further developed in Level 2 measures.

3.5. How to provide ?

The means of providing the KID are also detailed in the Regulation : paper,³³ or, where certain conditions are met,³⁴ other durable medium or website.³⁵

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providing the KID (because they act as agent for the product provider), they should make sure this is reflected in their distribution arrangements.

²⁹ Defined as "retail clients" further to MiFID II and as "customers" further to IMD (to the extent these customers cannot be considered as "professional clients" under MiFID).

³⁰ Where a discretionary manager invests in a PRIIP for a retail client account, the obligation is satisfied by providing the KID to the discretionary manager.

³¹ Article 6 of the compromise PRIIPs Regulation.

³² Article 8 of the compromise PRIIPs Regulation.

³³ Paper is the default medium for a KID where there is a face-to-face communication, unless the investor requests otherwise.

³⁴ Note that these conditions might prove difficult to meet when providing the KID to a retail client.

³⁵ See recent European case law on the accessibility of disclosure documents, European Court of Justice (Timmel), C-359/12, 15 May 2014 (deciding, in a case involving a prospectus, that "[...] the requirement that a prospectus must be easily accessible on the website on which it is made available to the public is not fulfilled where there is an obligation to register on that website,

The detail on the method and conditions for providing disclosure is intended to be further developed in Level 2 measures.

The Regulation provides that PRIIP manufacturers need to publish the KID on their websites.³⁶ Therefore, product providers will need to set up dedicated KID websites to host the library of KIDs for their PRIIPs.

4. Additional interesting provisions

Product manufacturers and distributors must put in place effective procedures which will allow investors to submit complaints to manufacturers.

The Regulation gives national regulators product intervention powers (where they did not have these already) to ban or restrict the marketing, distribution or sale of particular PRIIPs. In practice, this extends the product intervention powers in MiFID II to any PRIIPs that would not otherwise fall under the ambit of MiFID II, i.e., essentially IBI products.

Marketing communications that contain specific information relating to the PRIIP shall not include any statement that contradicts the information contained in the KID or diminishes the significance of the KID. Marketing communications shall indicate that a KID is available and supply information on how and from where to obtain it, including the manufacturer's website.

Further to the Regulation, manufacturers/remanufacturers are liable where a retail investor suffers loss as a result of relying on a KID where the KID is (a) inconsistent with binding pre-contractual or contractual documentation, (b) misleading or inaccurate or (c) does not comply with the required form and content requirements as set out in Article 8 of the Regulation. There is no longer the concept of a "reverse burden of proof," which was included in the Commission's proposal, whereby the product manufacturer would be liable unless it could show that the KID complied with the content requirements of the Regulation. Having in mind the requirement relating to the use of plain language, it is likely to be challenging for product manufacturers/remanufacturers to find a balance which satisfies the intention behind the Regulation while at the same time ensuring they are protected in the event of a retail investor claim. Civil liability of a manufacturer in relation to the KID will remain a matter of national law.

The Regulation provides that administrative sanctions and measures shall be put in place in case of breach of specific provisions, including prohibition/suspension of marketing of a PRIIP, a public warning, minimum administrative pecuniary sanctions, prohibition of provision of a non-compliant KID. Member States shall ensure that, where the competent authorities have imposed one or more administrative penalties and other measures, the competent authorities have the power to issue or require the PRIIP manufacturer or person advising on or selling the PRIIP to issue a direct communication to the retail investor concerned, giving them information about the administrative measure

entailing acceptance of a disclaimer and the obligation to provide an email address, where a charge is made for that electronic access or where consultation of parts of the prospectus free of charge is restricted to two documents per month").

36 Article 5.1 and Article 9 of the compromise PRIIPs Regulation.

or administrative sanction, and informing them where to lodge complaints or submit claims for redress. Member States shall provide whistle blowers' protection and publication of the name of the liable person, subject to exemptions where, for example, such disclosure would not be proportionate or would jeopardize the stability of the financial markets.

5. Interaction with other disclosure requirements

The European Commission intends the KID to serve a specific purpose different to other disclosure requirements. Therefore, the KID will exist in parallel to the disclosure requirements under the other directives, including under the prospectus directive ("PD"), the Solvency II directive, IMD 2,³⁷ and MiFID II.³⁸

6. Next step

At the time of writing, the Council of the European Union still needed to adopt the text of the Regulation. But, as the text has already been agreed with the European Parliament, this step should just be a formality. Shortly after this, the Regulation will be published in the Official Journal, and will come into legal force two years later. The European Commission stated on 14 April 2014 that it expects KIDs to be in place by the end of 2015.³⁹ However, it is more realistic that it will come into force by mid-2016. In the meantime, the European supervisory authorities will prepare draft RTS for approval by the European Commission.

7. Assessment

The Regulation will have a substantial impact on the documentation used in offerings of structured products to retail investors in the European Union.

It is difficult to see how the complex structures that can sit behind packaged/structured products and their opacity can be broken down and explained in order to show their true likely return and risks. It is being left to the Level 2 measures to determine how risks and costs and returns can be disclosed in a consistent manner. As in many other cases, the burden to draft appropriate detailed rules relies on the European supervisory authorities.

Besides, given the vast array of products that are caught by the Regulation, it is questionable whether standardization of disclosure can be achieved in any meaningful way and, if so, whether the KID will be helpful or whether it will further confuse retail investors.

Moreover, imposing a KID in addition to the summary prospectus or any other similar disclosure requirement under another financial market directive seems to run counter to the objective of providing a more level playing field between

37 As PRIIPs include IBI products which are covered by IMD 2.

38 As PRIIPs include structured deposits and other financial products that are covered by MiFID II.

39 See European Commission, Key Information Documents (KIDs) for packaged retail investment and insurance products - Frequently asked questions, 15 April 2014. Be reminded that as a European Regulation, it will be directly and uniformly applicable in all Member States, without the need for national implementing measures.

different types of products. It also seems unnecessarily confusing that in some instances investors will receive two different types of summaries, which are both intended to set out key features and risks of the product.⁴⁰ The European Commission seems conscious of the problem and has indicated that it is open to addressing the case for removing duplication across disclosure requirements in the future. In the meantime however, manufacturers will need to review all disclosures for each investment product, to ensure consistency.

It is intended that the Regulation will be reviewed within four years to assess its impact. The European Commission is open to widen the scope to other products, if necessary. We hope that a costs-benefits assessment will be done at that stage and that the European Commission will have the courage to withdraw the KID if it is established that it did not meet its objectives, i.e., that this prescriptive approach increases administrative costs to the detriment of investors, without necessarily aiding comparability across different sectors.

III. MiFID II/MiFIR

1. Background

The European Commission adopted on 20 October 2011 two proposals for the review of the first directive on markets in financial instruments (“MiFID” I). The new measures have recently been published in the Official Journal and are known as MiFID II⁴¹ and MiFIR.⁴²

MiFID II/MiFIR contain over 100 requirements for ESMA to draft RTS and Implementing Technical Standards (“ITS”), and to provide Technical Advice to the European Commission to allow it to adopt delegated acts. ESMA published a consultation paper on technical advice (the “CP”)⁴³ which was open to consultation until 1st August 2014. ESMA will finalize the draft technical advice for submission to the Commission by December 2014. The investor protection section is the longest part of the CP comprising some 150 odd pages.

2. Scope

The European Commission recognised in a November 2010 Consultation that it would be preferable to amend MiFID I and the first Insurance Mediation Directive (“IMD” I) to address the PRIPs issues on sales rules.⁴⁴ Consequently, it suggested in its proposal of the MiFID review making more

uniform regulatory treatment concerning the distribution of different packaged retail investment products in order to ensure an adequate level of investor protection across the European Union, and notably included structured deposits in the scope of MiFID II.

Even if investments that involve contracts of insurance are often made available to customers as potential alternatives or substitutes to financial instruments subject to MiFID, and therefore require investor protection provisions equal to those provided in MiFID, it was decided that the different market structures and product characteristics of IBI products make it more appropriate that detailed requirements are set out in the ongoing review of the Insurance Mediation Directive (“IMD I”) rather than setting them in MiFID II.⁴⁵

3. Disclosure requirements

Investment firms must provide fair, clear and not misleading information to (potential) clients and the conditions set out in the MiFID implementing directive only apply to (potential) retail clients. One of the objectives of the MiFID review was to improve, where appropriate, the treatment of non-retail clients, i.e., professional clients and eligible counterparties. Consequently, ESMA suggested extending some of the principles to professional clients for information addressed to or likely to be received by them.⁴⁶

In addition, ESMA noted that there were some deficiencies in the information provided to retail clients.⁴⁷ Consequently, ESMA suggested the strengthening for retail clients of the conditions for the information to be fair, clear and not misleading.⁴⁸

Among the new disclosure requirements, we can note the following pre-contractual information obligations. Appropriate information shall be provided in good time⁴⁹ to clients or potential clients with regard to the investment firm and its services, the financial instruments and proposed investment strategies, execution venues and all costs and related charges. That information shall include, when investment advice is provided, (a) whether or not the advice is provided on an independent basis ; (b) whether the advice is based on a broad or on a more restricted analysis of different types of financial instruments and, in particular, whether the range is limited to financial instruments issued or provided by entities having close links with the investment firm or any other legal or economic relationships, such as contractual relationships, so close as to pose a risk of impairing the independent basis of the advice provided ; (c) whether the investment firm will provide the client with a periodic assessment of the suitability

40 For instance, issuers of structured securities issued to retail investors under a PD-compliant prospectus will have to ensure that both a KID and an issuance-specific summary – required by the PD – are produced.

41 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 (recast), OJ, 12 June 2014, L 173/349.

42 Regulation N° 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending regulation n° 648/2012, OJ, 12 June 2014, L 173/84.

43 See ESMA, Consultation paper MiFID II/MiFIR, 22 May 2014, 2014/549. ESMA also published a discussion paper on the draft RTS/ITS (ESMA, Discussion paper MiFID/MiFIR, 22 May 2014, 2014/548) which was also open to consultation until 1st August 2014.

44 See Consultation by Commission Services on legislative steps for the Packaged Retail Investment Products initiative, 26 November 2010 (closed on 31 January 2011).

45 Recitals (87) MiFID II.

46 ESMA, CP, at 92-93 (information, including marketing communications, should be accurate and not reference any potential benefit without giving a fair and prominent indication of any relevant risks ; it shall not disguise, diminish or obscure important items, statements or warnings ; and it should be up-to-date, relevant to the method of communication used).

47 ESMA, CP, at 91 ((a) the language of different documents sent to retail clients is not always consistent ; (b) information provided by investment firms is not always updated, even when provided online ; (c) the presentation of risks/warnings to clients does not always reflect the particular relevance of these pieces of information ; and (d) information about the future performance does not illustrate sufficiently the potential functioning of the financial instruments or services).

48 ESMA, CP, at 93 (answering the concerns raised in the previous footnote).

49 See for more details recital (83) and recital (84) MiFID II.

of the financial instruments recommended to that client. The information on financial instruments and proposed investment strategies must include appropriate guidance on and warnings of the risks associated with investments in those instruments or in respect of particular investment strategies and whether the financial instrument is intended for retail or professional clients, taking account of the identified target market. The information on all costs and associated charges must include information relating to both investment and ancillary services, including the cost of advice, where relevant, the cost of the financial instrument recommended or marketed to the client and how the client may pay for it, also encompassing any third-party payments. The information about all costs and charges, including costs and charges in connection with the investment service and the financial instrument, which are not caused by the occurrence of underlying market risk, shall be aggregated to allow the client to understand the overall cost as well as the cumulative effect on return of the investment, and where the client so requests, an itemised breakdown shall be provided. Where applicable, such information shall be provided to the client on a regular basis, at least annually, during the life of the investment.⁵⁰ ESMA is advocating that the aggregated amount in costs should be stated both as a total amount and as a percentage. That pre-contractual information can be presented on a standardized format to clients, should that possibility be provided by national law.⁵¹

Member States may impose, in exceptional cases, additional requirements provided that they are objectively justified and proportionate so as to address specific risks to investor protection or to market integrity which are of particular importance in the circumstances of the market structure of that Member State. A specific procedure of notification to the Commission must be followed. Such additional requirements shall not restrict or otherwise affect the provision of services on the basis of the free movement of services or the establishment of a branch.⁵²

4. Product governance arrangements/organizational requirements – Know your product

Investment firms must act in accordance with the best interests of their clients and avoid conflicts of interests.

In that context, manufacturers shall have and periodically review a process for the approval of each financial instrument and for significant adaptations of existing financial instruments before marketing or distributing to clients.⁵³ The product approval process shall (a) specify an identified target market of end clients ;⁵⁴ (b) ensure that the financial instruments are designed to meet the needs of the identified target market⁵⁵ and therefore assess all relevant risks to such market and make sure that the target market is able to bear those

risks ; (c) ensure that the distribution strategy is compatible with the target market⁵⁶ and take reasonable steps to ensure that the financial instrument is distributed to the target market.⁵⁷ Manufacturers shall regularly review the financial instruments it offers or markets, including whether the financial instrument remains consistent with the needs of the identified target market and whether the distribution strategy remains appropriate.⁵⁸

Product governance arrangements will apply to firms that manufacture products as well as firms that sell financial products. An investment firm shall assess the compatibility of the financial instruments with the needs of the clients to whom it provides investment services, also taking account of the identified target market, to ensure that the financial instruments are offered or recommended only when this is in the interest of the client.⁵⁹ To that end, the manufacturer shall make available to its distributors all information on the product and the product approval process, including the identified target market.⁶⁰ An investment firm that does not manufacture the products it markets shall have the adequate arrangements to get the information and to understand the characteristics of the product.⁶¹

In its CP,⁶² ESMA suggested ways to detail the product governance obligations of manufacturers and distributors. In particular, at the manufacturer's level, ESMA suggested that the design of the product be compliant with the requirements relating to the management of conflicts of interest (including remuneration) ; staff have the necessary expertise or appropriate training to understand the characteristics and risks of the products they want to manufacture ;⁶³ the management body have effective control over the firm's product governance process ; the group of investors for whose needs, objectives, characteristics the product is not compatible be identified ; and the products be submitted to stress-test.⁶⁴ At the distributor's level, the product governance obligations apply when deciding the range of products distributors intend to provide to clients. Distributors should have product governance arrangements in place (regularly reviewed) to ensure that the products or services they intend to offer are compatible with the characteristics, objectives and needs of the identified target market ; should regularly review the pro-

duct review, FG12/09, March 2012. See as well, ESMA/2014/332, Opinion, 27 March 2014, at 6 (structured products should meet the financial needs, investment objectives, knowledge and experience of the target market ; compliance function should be involved in the design process ; avoidance of conflicts of interest ; an external party to challenge the pricing, valuation, and risk/reward trade-off relative to the target market).

56 Article 24.2 MiFID II. See as well, IOSCO, Regulation of retail structured products, Final Report, December 2013, at 28 (regulatory tool 14 (distribution channel considerations)).

57 Article 24.2 MiFID II.

58 Article 16.3 and Article 24.2 MiFID II. See as well ESMA CP, at 44 (product review and the discussion of its frequency).

59 Article 24.2 MiFID II.

60 Article 16.3 MiFID II.

61 Article 16.3 and Article 24.2 MiFID II. See also ESMA CP, at 45.

62 See as well in that respect the consultation paper of the European Commission prior to adopting MiFID II (European Commission, Public Consultation - Review of the Markets in Financial Instruments Directive, 8 December 2010, at 68).

63 See as well ESMA/2014/332, Opinion, 27 March 2014, at 5.

64 See as well IOSCO, Regulation of retail structured products, Final Report, December 2013, at 18 (regulatory tool 4 (use of financial modeling)). See for more details on stress-testing, ESMA, Trends, Risks, Vulnerabilities, 12 March 2014, 2014/0188, at 63 *et seq.*

50 Article 24.4 MiFID II.

51 Article 24.5 MiFID II.

52 Article 24.12 MiFID II.

53 Article 16.3 MiFID II. See as well, IOSCO, Regulation of retail structured products, Final Report, December 2013, at 19-20 (regulatory tool 5 (product approval process)).

54 See as well regulatory tool 3 (intended investor identification and assessment) of IOSCO report, at 16-17.

55 See FSA, Retail product development and governance – structured pro-

ducts they market ; should have trained staff that understand the products ; should provide manufacturers with sales information to support product reviews by manufacturers ; should involve the compliance function in the development and review of product governance arrangements and the management body in the endorsement of the products and services offered. Where there are multiple intermediaries in the chain, the final distributor has ultimate responsibility to meet the product governance obligations. The intermediate distributor must ensure that the relevant information is passed from the manufacturer to the final distributor and that the manufacturer is provided with all information he needs on product sales, and he must apply the product governance arrangements for manufacturers in relation to the service it provides.

5. Product intervention powers⁶⁵

MiFIR introduces a framework for product intervention in order to enable national competent authorities and ESMA,⁶⁶ provided that certain conditions are met and in the circumstances specified by ESMA, to “temporarily” prohibit or restrict the marketing, distribution or sale of certain financial instruments or structured deposits or financial instruments or structured deposits with certain specified features or a type of financial activity or practice.⁶⁷

ESMA shall only take a decision to prohibit or restrict if all of the following conditions are fulfilled : (a) the proposed action addresses a significant investor protection concern or a threat to the orderly functioning and integrity of financial markets or to the stability of the whole or part of the financial system in the Union ; (b) regulatory requirements under European legislation that are applicable to the relevant financial instrument or activity do not address the threat ; (c) a competent authority or competent authorities have not taken action to address the threat or actions that have been taken do not adequately address the threat.

ESMA may impose the prohibition or restriction on a precautionary basis before a financial instrument has been marketed, distributed or sold to clients.

When taking action, ESMA shall take into account the extent to which the action (a) does not have a detrimental effect on the efficiency of financial markets or on investors that is disproportionate to the benefits of the action ; and (b) does not create a risk of regulatory arbitrage. Before deciding to take any action, ESMA shall notify competent authorities of the action it proposes. ESMA shall publish on its website notice of any decision to take any action. The notice shall specify details of the prohibition or restriction and specify a time after the publication of the notice from which the measures will take effect. As provided under ESMA Regulation,⁶⁸ ESMA shall review a prohibition or restriction imposed at appropriate intervals and at least every three months. Potentially,

the prohibition or restriction could last indefinitely if properly renewed. If the prohibition or restriction is not renewed after that three month period it shall expire. Action adopted by ESMA shall prevail over any previous action taken by a competent authority. The European Commission shall adopt by means of delegated acts measures specifying criteria and factors to be taken into account by ESMA in determining when the threats to investor protection or to the orderly functioning and integrity of financial markets and to the stability of the whole or part of the financial system of the Union arise. Those criteria and factors shall include (a) the degree of complexity of a financial instrument and the relation to the type of client to whom it is marketed and sold ; (b) the size or the notional value of an issuance of financial instruments ; (c) the degree of innovation of a financial instrument, an activity or a practice ; (d) the leverage a financial instrument or practice provides.

ESMA suggested details of the criteria in its CP, stressing that flexibility is key in this new area and the list of criteria should be a non-exhaustive one. ESMA also made it clear that frequency of intervention should be limited, given the many conditions attached ; and expects the product governance principles to limit the need for product intervention as well.

6. Sanctions

MiFID II strengthens the existing regime to ensure effective and harmonized administrative sanctions.⁶⁹ The use of criminal sanctions is framed so as to ensure the cooperation between authorities and the transparency of sanctions. Lastly, a harmonized system of strengthened cooperation will improve the effective detection of breaches of MiFID.⁷⁰

7. Next step

MiFID II and MiFIR came into force on 2 July 2014. At the time of writing, it is said that ESMA is expected to finalize its technical advice for the delegated acts in December 2014. It should submit its final RTS to the European Commission in June 2015 and the final ITS in December 2015. Member States will need to adopt and publish the domestic legislation necessary to transpose MiFID II by 2 July 2016. Such legislation and MiFIR will then apply from 2 January 2017.

8. Assessment

Details on the disclosure requirements will be set out in Commission’s delegated acts. In that respect, MiFID II explicitly states that account shall be taken of “*any relevant standardized information required under Union law*” when formulating the requirements for information on financial instruments, including information on the structure of the product.⁷¹ This is of course welcome to avoid duplication in pre-contractual standard disclosure documents.

As the PRIIPs Regulation and MiFID II contain disclosure requirements, ideally, the disclosures required by both would

65 In a narrow acceptance, product intervention refers to the rules dealing with the design and the structure of investment products. It comes next to the set of regulations concerning disclosure and distribution of investment products. In a broader sense, it refers to any regulatory intervention with respect to financial products (e.g., restricting in any way their marketing). This section deals with the latter.

66 This applies as well to the European Banking Authority (“EBA”) under Article 41 MiFIR.

67 Articles 40 and 42 MiFIR.

68 Regulation (EU) No 1095/2010 of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC, Official Journal, 15 December 2010, L 331/84.

69 See Article 70.6 MiFID II and also Article 71 MiFID II (publication of decisions and measures as a general rule).

70 Article 79 *et seq.* MiFID II.

71 Article 24.13, *in fine* MiFID II.

have overlapped. But in many respects, they do not. There will be implementation challenges for firms in reconciling the different rules. For example :

where structured deposits are sold, MiFID II disclosure requirements are set to apply, as structured deposits are not caught by the PRIIPs Regulation, whereas where personal pensions are sold, the PRIIPs Regulation requirements will apply, as these are not encompassed by MiFID II ;

the MiFID II disclosures are likely to apply where any "financial instruments" are sold to any type of clients.⁷² The PRIIPs Regulation disclosures however are only required where investment products are sold to retail clients ;

where products within scope of both national legislation (such as the UK Retail Distribution Review) and MiFID II (e.g., structured products) are sold to retail clients, the national supervisory authority could apply the national requirements. This is because MiFID II does not prohibit Member States from imposing stricter rules.

Most financial institutions already have some sort of product approval process in place. They will have now to see if additional measures need to be taken to adapt their existing processes and policies to the new European requirements in that respect. This being said, even if everything has been done to implement each formal requirement of applicable regulations, it will be worth nothing if there is not a strong will inside each manufacturer and each distributor to adopt ethos, and to convey it to each of their employees, to really work in the best interests of clients. It seems that what is still lacking today is a change of culture to make finance really work for the benefit of society.

IV. IMD 2

1. Background

Even though the insurance sector came out of the financial crisis reasonably well – with the notable exception of AIG – it however had its own raft of regulatory and political attention at national, European and global level. The major regulatory change for insurers in the European Union is the implementation of the Solvency II directive which will determine how much capital an insurer will need. In addition, the Solvency II directive calls upon the European Commission to revise IMD I, taking into account the consequences of Solvency II for policyholders.

On 3 July 2012, the European Commission adopted a proposal of IMD 2, which is today at the stage of Presidency compromise.⁷³

The goal of the Commission's proposal is to upgrade consumer protection in the insurance sector by creating common standards across insurance sales and ensuring proper advice. Compared to IMD I, IMD 2 provides for, *inter alia*, more

detailed professional requirements⁷⁴ as well as new conduct of business rules.⁷⁵ In addition, further to MiFID II, additional customer protection provisions are introduced in connection with IBI products as these products are considered potential alternatives or substitutes to products subject to MiFID.⁷⁶ These provisions are further detailed in IMD 2.⁷⁷

An IBI product is defined as “an insurance product which offers a maturity or surrender value and where that maturity or surrender value is wholly or partially exposed, directly or indirectly, to market fluctuations”. This indicates that an IBI product would need to include an investment component that is expected to provide a variable rate of return. This would be likely to cover unit-linked and index linked contracts, fixed index annuities and variable annuities. In addition to the non-life insurance products listed in Annex I to Solvency II, the following are excluded from the definition of an IBI product : life insurance contracts where the benefits under the contract are payable only on death or in respect of incapacity due to injury, sickness or infirmity ; pension products which, under national law, are recognised as having the primary purpose of providing the investor with an income in retirement, and which entitles the investor to certain benefits ; officially recognised occupational pension schemes falling under the scope of the Occupational Pension Funds Directive or the Solvency II directive ; individual pension products for which a financial contribution from the employer is required by national law and where the employer or the employee has no choice as to the pension product or provider.⁷⁸

2. Disclosure requirements

As all other customer protection provisions of IMD 2, the pre-contractual information requirements apply to “insurance distribution” activity carried out by insurance intermediaries or insurance and re-insurance undertakings that sell directly to customers. Just a few exceptions are provided.⁷⁹

Following the IMD definition of insurance distribution, this includes the following : (a) introducing, proposing or carrying out other work preparatory to the conclusion of a contract, (b) concluding a contract or (c) assisting in the administration and performance of a contract, in particular in the event of a claim.

All information, including marketing communications, addressed by the distributor to (potential) customers must be fair, clear and not misleading. Marketing communications must be clearly identifiable as such. The conditions with which information must comply to be fair, clear and not misleading will be detailed in Level 2 measures, as well as the content and format of pre-contractual information.⁸⁰

Prior to the conclusion of a contract, whether or not advice is given, a retail customer shall be given free of charge the

⁷² See however the possibility to make distinctions in the level 2 measures.

⁷³ The presidency compromise on which this article relies is the one dated 20 June 2014, available on the Internet website of the documents from the Council of the European Union.

⁷⁴ Chapter V IMD 2.

⁷⁵ Chapter VI IMD 2.

⁷⁶ Article 91 MiFID II amending IMD I. In autumn 2013, EIOPA requested that provisions on the sale of insurance PRIIPs be included in the MiFID II as negotiations on IMD 2 were not progressing very rapidly.

⁷⁷ Chapter VII IMD 2.

⁷⁸ Article 2 (4) IMD 2.

⁷⁹ See Article 19 IMD 2 (exceptions include mediation in the insurance of large risks, mediation by re-insurance undertakings/intermediaries ; or in relation to professional customers).

⁸⁰ Article 15 IMD 2.

relevant information about the insurance product in a comprehensible form to allow the customer to make an informed decision, while taking into account the complexity of the insurance product and the type of customer.⁸¹ IMD 2 also provides for specific pieces of pre-contractual information to be provided to retail customers by the insurance intermediary, the ancillary insurance distributor or the insurance undertaking, as the case may be.⁸² The form of the disclosure,⁸³ the means of communication⁸⁴ and the language are also detailed.⁸⁵

The information requirements of IMD 2 provide for minimum harmonization. Member States could provide stricter rules provided that such rules comply with Union law.⁸⁶

Breach of the information requirements provisions must be sanctioned by administrative sanctions and measures.

3. Product governance arrangements/organizational requirements – Know your product

Insurance manufacturers shall maintain, operate and review a process for the approval of each insurance product or significant adaptations of an existing insurance product before it is marketed or distributed to customers.

The product approval process shall specify an identified target market of customers for each product and ensure that all relevant risks to such identified target market are assessed, the intended distribution strategy is consistent with the identified target market and take reasonable steps to ensure that the insurance product is distributed to the identified target market.

The insurance undertaking shall understand and regularly review the insurance products it offers or markets, taking into account any event that could materially affect the potential risk to the identified target market, to assess at least whether the product remains consistent with the needs of the identified target market and whether the intended distribution strategy remains appropriate.

Insurance manufacturers shall make available to any distributor all appropriate information on the insurance product and the product approval process, including the identified target market of the insurance product. Where an insurance distributor advises on or proposes insurance products which it does not manufacture, it shall have in place adequate arrange-

81 Article 15a.4 IMD 2 (for insurance intermediaries), Article 15b (for ancillary insurance distributors), Article 15c.5 (for insurance undertakings) and Article 24.8 (with respect to IBI). See also Article 19.1 for the limited exceptions (professional customers, reinsurance intermediaries and reinsurance undertakings, large risks).

82 Including, for instance, whether advice is given, the complaint procedure, whether it acts independently or not, the nature and the method of calculation of the remuneration.

83 Clear and accurate manner, comprehensible to the customer.

84 Paper is the default medium.

85 Article 20 IMD 2.

86 Article 19.2 IMD 2. It seems that individual national regulators want to retain the right to play a significant role in the regulation of insurance products and be able to respond to local market (and political) pressures.

ments to obtain the information and to understand the characteristics and identified target market of each insurance product.⁸⁷

4. Professional requirements

IMD 2 provides for professional knowledge and competence requirements for natural persons carrying out insurance or re-insurance distribution. Specific ones are provided for IBI products in Annex II to the directive. These requirements should be met on a permanent basis and update of professional knowledge and competence should take place regularly.⁸⁸

Breach of the professional requirements provisions must be sanctioned by administrative sanctions and measures.

5. Sanctions and measures

Further to IMD 2, effective, proportionate and dissuasive administrative sanctions and measures must be put in place; sanctions must be applied to members of the management body; all necessary investigatory powers must be made available to competent authorities. Publication of a sanction must become the rule and anonymous publication is provided for in certain circumstances. IMD 2 provides a list of administrative sanctions and measures and a list of the breaches to which they apply. It also introduces provisions on whistle blowing.⁸⁹

6. Interaction with MiFID II and the PRIIPs Regulation

The European Commission recognised that competing products can originate from various providers where sectors can be blurred. It noted that IBI products compete with products from other sectors covered by securities regulation, i.e., MiFID. This links the negotiations over IMD 2 to both MiFID II⁹⁰ and the PRIIPs Regulation.⁹¹

7. Next step

IMD 2 is currently expected to be implemented in 2014 and to come into force in 2016.

8. Assessment

One might regret that instead of having one code to regulate the European markets for financial products and services, we still have sectoral regulations. In particular, MiFID II/MiFIR on the one hand and IMD 2 on the other hand regulate the same topics, each with its specific scope (non-insurance v insurance). The PRIIPs Regulation stands out as a regulation which regulates pre-contractual information for all packaged

87 Article 21a IMD 2. See also recital (37) IMD 2 stating that “*The insurance intermediary should be able to explain to the customer the key features of the insurance products it sells*”.

88 At least 50 hours in 5 consecutive years.

89 Articles 26 *et seq.* IMD 2.

90 MiFID does not cover insurance products.

91 The PRIIPs Regulation governs the disclosure requirements for, *inter alia*, IBI products.

investment products, whatever their form, be they insurance-related or not. This situation of having different regulations regulating the same topics each for different types of products or different contexts⁹² leads to additional costs for firms subject to these regulations. For sure the compliance function within those firms has a bright future ahead. Inconsistencies or small differences between different regulations will require legal advice to ensure full compliance. This leads to an uneven playing field across sectors which runs contrary to the objective of promoting competition to avoid regulatory arbitrage, where market participants structure products so as to minimise their regulatory obligations, and to motivate financial institutions to improve their products to suit clients' demands. One might have hoped to have the same conduct-of-business and organizational rules to apply to all distributors of investment products available at retail level.

V. Conclusions

We note that, today, most regulators and regulations assimilate clients of financial products or users of financial services to “financial consumers”.⁹³ This is definitely an evolution that reflects a change of mind. But is this just window dressing in the urge of restoring investors' trust in financial markets after the 2007-2008 crisis?⁹⁴ Or are the European regulations examined in this contribution really likely to meet their objective of increased clients' protection on financial markets? This is a question worth asking.

For long, and definitely before MiFID I, disclosure to provide investors the information that they need to understand their financial products and make informed decisions was believed to be the panacea to cure the variety of investors' pain and suffering in the financial market. As the effectiveness of disclosure became highly dubious,⁹⁵ the insistence on the part of European policy makers to continue its extensive use⁹⁶ is peculiar, particularly in the retail financial product market. To be sure, one cannot totally dismiss disclosure as a financial user's protection tool. Disclosure is useful where it meets its objectives and this can only be assessed through real costs-benefits analyses taking target markets' opinions into account. We note in that respect that much remains to be done in terms of involvement of target markets' representatives at the discussions and drafting table to ensure that the objectives are met in practice.⁹⁷

92 Refer to the example given above of the summary under the prospectus directive and the KID under the PRIIPs Regulation.

93 See OECD, G20 high-level principles on financial consumer protection, October 2011; ESMA, annual report 2013; Belgian Financial Services and Markets Authority, mission statement (“*The Financial Services and Markets Authority strives to ensure the honest and equitable treatment of financial consumers and the integrity of the financial markets*”).

94 Note that the level of trust vis-à-vis investment services providers and relating to compliance with investors protection rules is rather low in the European Union (33 % in 2012 according to ESMA, Trends, Risks, Vulnerabilities, 12 March 2014, 2014/0188, at 28).

95 See Gaëtane Schaecken Willemaers, *The EU Issuer-Disclosure Regime: Objectives and Proposals for Reform*, Alphen aan den Rijn, Netherlands, Wolters Kluwer Law & Business, 2011. See also, Omri Ben-Shahar & Carl E. Schneider, The Failure of Mandated Disclosure, 159 U. PA. L. REV. 647, 735-42 (2011).

96 See for instance the PRIIPs Regulation.

97 See Better Finance, “London, 4 June 2014: the European financial consumer exclusion day?”, press release, June 2014 (criticizing the European Supervisory Authorities (“ESAs”) for the very limited involvement of financial services users at the “financial consumer protection day” they

Disclosure obligations will certainly not meet their objectives if the people they are meant to protect do not understand the information provided to them. In that respect, it is worth noting the many initiatives in connection with financial literacy.⁹⁸ Unfortunately, it is true only to a certain extent that one can educate investors to understand the risks of their investments. Studies show that, like disclosure, the impact of financial education programmes on investors' understanding of financial products is controversial.⁹⁹

If bad decisions could reflect lack of information or lack of knowledge, they could also reflect behavioural biases. This is an avenue of research which should be more investigated than it is now and which conclusions should be more often used to design correct policies to protect investors.¹⁰⁰

Recently, and even more so under MiFID II and IMD 2, given the failures of disclosure, more focus has been allocated to point-of-sale regulation. Regulatory emphasis seems now to be set at the level of the distribution chain – manufacturer's responsibilities in the product design process, market testing, stress testing, staff training, choice of distribution channel. We certainly believe this is the right approach.

For the reasons explaining disclosure's failures, investors tend to rely heavily and passively on advice.¹⁰¹ This is a fact. In that context, intermediaries' competence and ability to understand the products and to give proper, appropriate and unbiased advice taking only the interests of their specific client into account becomes paramount. This will in turn strengthen investors' trust in professional and trustworthy financial institutions.

Even if product governance arrangements are said to limit the need for it, MiFIR and the PRIIPs Regulation provide for product intervention by supervisory authorities as a response to innovation risks. We believe that intervention in product design or banning of financial products should remain a last resort solution given the costs. While all innovation and choice is not beneficial to investors, regulators should be careful before they act as product intervention could stifle innovation and slow down product development. Investments

organized and the absence from the agenda of such day of the main regulatory issues currently on the table of the ESAs regarding investor and financial user protection).

98 See at international level (OECD 2005), European level (European Commission communication 2007 and European Parliament resolution 2008) and national level (e.g., Belgian FSMA since 2011).

99 Lauren E. Willis, Against Financial Literacy Education, 94 Iowa L. Rev. 197, 202-04 (2009). See Decision Technology Ltd, Consumer Decision-Making in Retail Investment Services: A Behavioral Economics Perspective, Final Report, November 2010, at 390 (acknowledging the lack of studies regarding if and to what extent it is possible to improve behavioral traits through education or information campaigns).

100 One of the topics at the 2014 Joint ESAs Consumer Protection Day was “behavioural economics/finance”. But unfortunately, none of the panelists was from the consumers' associations or specialists in this very specific area of research. In Europe, a lot remains to be done to take the sentence of Daniel Kahneman to its fullest width: “*Although Humans are not irrational, they often need help to make more accurate judgments and better decisions, and in some cases policies and institutions can provide that help*” (Daniel Kahneman, Thinking fast and slow, Farrar, Straus and Giroux, 2011, at 411).

101 See Decision Technology Ltd, Consumer Decision-Making in Retail Investment Services: A Behavioral Economics Perspective, Final Report, November 2010 (concluding that “*professional financial advice plays a key role in the market*” (at 21)). See as well Recital 36 of the draft IMD 2 (“*Due to the increasing dependence of consumers on personal recommendations [...]*”).

inevitably involve risk. Complexity may be necessary for the product to function as expected and might answer the needs of specific investors. Structured products indicators are not absolute determinants of detriment.¹⁰² As long as the product is understood by the manufacturers and distributors alike and that the product works to the best interests of the target market for which it is created and as long as the investor agrees with the risks fully and accurately disclosed to him/her, complexity should not be banned.

The stricter conduct-of-business rules, product governance arrangements and product intervention powers that we have now reviewed imply that supervisory authorities have adequate resources to supervise and intervene early enough in the process. In that respect, the increase in ESMA staff is to be welcomed.¹⁰³

We would like to conclude by reminding a very simple, although so often forgotten fact. Regulations will not be effective in meeting their objective of clients' protection on financial markets if manufacturers and distributors lack ethos in their way of doing business. As experience shows, financial and insurance institutions do know the tricks to circumvent the purpose of regulatory provisions. It is now time to restore what has been lost (if it has ever existed) in too many financial markets players : a culture reflecting a strong commitment to offer products that work in the best interests of their clients. And this can only happen with a strong and sincere will from management as it needs proper motivation and supervision. ■

102 Accord, Better Finance, Better Finance Response to the Informal Consultation of 14 May 2014 by OECD, at 3.

103 In order to keep up with the additional responsibilities and tasks that were on ESMA's plate in 2013, ESMA staff numbers grew by more than 50 % to 139 staff by the end of 2013. "Looking ahead at the long list of our responsibilities and on-going and new tasks (whether under EMIR, MiFID II or other legislative provisions), ESMA will need to continue to develop existing and attract new staff, as well as continue to improve its organisational effectiveness" (ESMA annual report 2013). See also the increase in staff at the Belgian FSMA.