RESPONSE TO ESMA

SMSG response to ESMA on its Call for evidence on the EC mandate on certain aspects relating to retail investor protection

Q1: Please insert here any general observations or comments that you would like to make on this call for evidence, including any relevant information on you/your organisation and why the topics covered by this call for evidence are relevant for you/your organisation.

The ESMA SMSG is grateful that this call for evidence is giving the opportunity to build on its response[1] to the European Commission´s consultation on the Retail Investment Strategy in order to share its reflections based on the practice observed across the EU in the area of investor protection. It is indeed very valuable for stakeholders coming from different horizons to share, confront and converge most of the time towards proposals of way forward in order to fulfil the expectations of the retail investors while remaining practicable from the market participants´ perspective.

In addition, this call for evidence triggers a more than needed reflection around the reach of the investor protection´s regulatory framework. An important area of investor protection concern stems indeed from unregulated firms and products such as crypto assets. This is why it is important that regulated and unregulated firms are subject to the same requirements, as the objective is certainly not to make the regulated services/products more expensive or inaccessible, as compared to unregulated services/products. A level playing field between regulated and not regulated firms becomes even more crucial in a world where it is tempting to use digital channels to sometimes circumvent the regulatory framework.

Q2: Are there any specific aspects of the existing MiFID II disclosure requirements which might confuse or hamper clients' decision-making or comparability between products? Are there also aspects of the MiFID II requirements that could be amended to facilitate comparability across firms and products while being drafted in a technology neutral way? Please provide details.

As a preliminary and general consideration, simplification and consistency of the framework would help investors to better cope with the complexity which is inherent to financial investments. This is why the regulatory framework regarding investor protection for retail investors should be simplified, instead of making it even more complex. In addition, whatever the complexity of the inner workings of a product, the investor should be able to comprehend the promise of the investment, i.e. its objective, its risks and rewards profile.

The information provided to the investor should not give rise to any confusion as it may currently be the case regarding the understanding of costs and value[2], issue on which we will elaborate in the response to

[1] https://www.esma.europa.eu/system/files_force/library/esma22-106-3504_smsg_response_to_ec_consultation_on_retail_investment_strategy.pdf?download=1

[2] Please refer to several publications from the UK FCA in the area of asset management, inter alia: Asset Management Market Study, Final Report, June 2017; Occasional Paper 32, *Now you see: drawing attention to charges in the asset management industry*, Lucy Hayes, William Lee and Anish Thakrar, April 2018, and the related Policy Statement, *Asset Management market study remedies and changes to the handbook – feedback and final rules to CP17/18*, April 2018.

Q4. In addition every information disclosed should be of use to the investors; confusing, redundant and information without benefit for the investor should be discarded in light of the legal (MiFID) requirement of fair, clear, and not misleading information.

These principles being established, it is important to observe regularly the behavior of retail investors in reaction to the disclosure requirements. Understanding and predicting the likely effects of interventions can be difficult. Interventions motivated by good intentions may nonetheless have unintended effects. In addition, the effectiveness of particular interventions may rely in large part on the context in which that intervention occurs, such that an intervention that produces a particular set of results in one jurisdiction may not necessarily produce the same results in another. Testing illustrates how seemingly intuitive assumptions about investor behaviour may not reflect actual investor behaviour. Research and testing can help regulators uncover faulty assumptions that might otherwise have the potential to reduce the effectiveness of retail investor protection initiatives. Experimentally-lead testing is more and more a common and good practice among regulators however experimental conditions may not always align with the conditions that exist in the real world. These misalignments may be anticipated when an experiment is designed, or may only be discovered after the fact. Monitoring and evaluating how experimentally-informed initiatives operate in the real world may be a helpful tactic for identifying potential shortcomings. A good way to do so is the consumer testing which should be used to a greater extent on “real” products (and not only on simple products on which it is usually focused for budgetary reasons) in order to full grasp the pictures of both challenges and possible returns. Although maybe more challenging, such testing would be needed in order for ESMA to grasp the full picture, potentially with the NCAs involvement. The scrutiny of complaints is also helpful, the latter having been overall handled consistently as per the ESAs report published in March 2021.

The facilitation of comparison across firms and products should be “reasonable” in the sense that it should aim to bring value to the investor. The practice proved that the comparison is sometimes meaningless as for instance with regards to the difference between derivatives used for investment and derivatives used for hedging or as means of payment (i.e. some derivative contracts are not “financial instruments” under MiFID, while being covered by PRIIPs). The information should indeed not be identical in these two different cases (instruments used for investments or for hedging purposes). In other words, hedging instruments should not belong to the PRIIPs scope but, if it is decided to do so, the related information should be adapted in order to make sense to the investor.

Q3: Are there specific aspects of existing MiFID II disclosure requirements that may cause information overload for clients or the provision of overly complex information? Please provide details.

The feedback received from investors is that they are facing an actual information overload, all the more as they cannot take the time and are sometimes not even in the position to understand the massive texts and differing documents (layout, information flow, type, and structure) that are put in front of them when these are phrased in legal terms.

Further to the amount of information, the understandability of the information is indeed key and should be appropriate, with an approach of the complexity which is more consumer-centric.[3]

A striking example of overly complex information is the presentation of costs and charges. Retail clients may typically not be interested in calculation methodologies and detailed breakdowns As an example, it is difficult to make sense out of the cumulative effects on returns (both actual and future ones), and the same goes for the percentage calculations and implicit cost transactions.

Academic studies[4] have been performed which show that, due to the amount of the aggregate pre-contractual information provided to retail investors, there is a risk that investors are not able to absorb all the necessary information due to information overload. This can lead to suboptimal investment decisions.

In 2020-2021, the FCA launched a similar initiative regarding pension products and services with the objective to promote the best value for pension scheme members.
Please also see the EIOPA statement on unit-linked insurance products: https://www.eiopa.europa.eu/content/eiopa-sets-out-framework-delivering-better-value-money-consumer-centric-way_en

[3] *Complexity of Financial Products – a Quantitative and Economic Approach*, C. Koziol, P. Rossmann, S. Weitz, October 2018

[4] *MiFID II/MiFIR/PRIIPs Regulation Impact Study: Effectiveness and Efficiency of New Regulations in the Context of Investor and Consumer Protection – A qualitative/empirical analysis*, Prof. Stephan Paul from Bochum University, February 2019.

The difference between the understanding of lay investors who often get too much information that is too complex to understand, while on the other hand relatively experienced retail investors get too much information they do not need, may be fixed by amendments to the MiFID II which go beyond the scope of disclosure requirements mentioned there. The facilitation of “opt up” from the retail to the professional investor category for certain transactions or instruments or in total, provided the investor meets defined criteria along the lines recommended in the context of the 2020 HLF CMU discussions, is one avenue that the EC consultation on Retail Investment Strategy has rightly mentioned.

Q4: On the topic of disclosures, are there material differences, inconsistencies or overlaps between MIFID II and other consumer protection legislation that are detrimental to investors? Please provide details.

The alignment and consistency of the regulations is crucial to ensure that the regulatory framework actually benefits the investor.

First and foremost, MiFID and IDD´s distribution rules as far as IBIPs (insurance-based investment products) are concerned should be aligned. The IDD does not contain detailed rules on the demands and needs test, and leaves it to Member States to decide on the details of how the test is applied in practice. This results in differences between Member States. This should not be the case and, even more importantly, the IDD disclosure should be aligned with MiFID, in particular on inducement disclosure, as these overarching frameworks should provide the overall cost disclosure points and methodologies.
Second, MiFID and PRIIPs cost and performance disclosure information should be tackled as their discrepancy (MiFID uses a zero-return assumption while the PRIIP KID uses the cost disclosures tied to complex future performance scenarios resulting in diverging cost figures) creates confusion for individual investors, and could generate mistrust in the financial products itself. The retail investors carefully studying all pre-contractual disclosure documents (e.g. MiFID and PRIIP KID) will indeed be confused as to why product costs are not aligned. This regulatory misalignment should be addressed through the adoption of MiFID/IDD disclosures points and methodologies in the PRIIPs KID e.g., regarding transaction cost and future performance.

At least, cost disclosure must in future be aligned to disclosing the same cost information (i.e. MiFID and PRIIPs) to retail investors. In a sense, overarching frameworks like MiFID and IDD should provide the overall cost disclosure points and methodologies, which can be simply inserted into Key Information Documents. In any case, the current situation where the PRIIP KID uses its own cost calculation methodologies (which are different to MiFID/IDD) must be avoided at “all costs”.

In terms of comprehensibility of the terms used, it should be noted that some other regulations mandate the key terms or wording to be used, therefore limiting the ability of regulated firms to simplify their documentation or avoid jargon. The SMSG advises to make an overview of such problematic requirements (with the help of stakeholders).

In the area of sustainability, the interaction between SFDR and MiFID II is currently not clear at all, and could benefit from some clarifications.

In particular the uncertainty about the scope of services and financial instruments covered by MiFID II and SFDR is problematic. Under SFDR “a portfolio” is a financial product to which disclosure rules shall apply. SFDR refers to sectorial legislation regarding this reporting i.e., MiFID II. However, under MiFID II, portfolio management is an investment service and there is no pre-contractual document as a KID and KIID. This creates uncertainty as to in which format the SFDR information should be provided for “a portfolio”. In addition, the reference to periodic reporting information in MiFID II (article 25.6 MiFID II) suggests that information for “a portfolio” should be published monthly or quarterly and not annually, as is the case for other SFDR products e.g. investment funds and insurance products.

In addition, from an investor protection perspective, it is important to clarify if financial instruments or “a portfolio” can be referred as “sustainable” or “ESG” even if they are not article 8 or 9 products under SFDR. In this context, it should be noted that SFDR as well as MiFID II rules on suitability assessment are only applicable to investment advice and portfolio management and not to other investment services.

Furthermore, the MiFID Quick Fix has introduced a number of changes to the requirements provision of pre-contractual information to professional clients and it is not clear whether this equally applies to SFDR information.

Finally, the divergent implementation periods of MiFID II (3 August and 22 November 2022) and SFDR (1 January 2023) could create practical problems.

Q5: What do you consider to be the vital information that a retail investor should receive before buying a financial instrument? Please provide details.

What is considered as “key information” may vary between products and services. It may also vary depending on the point in time, the education and the knowledge and experience of the investor. On the two latter aspects, the more educated and financially savvy customers do not accept to be flooded with information (which certainly ties up with behavioral economics as mentioned in the next question).

From a forward-looking perspective, the key information may be conceived as a common body of key information that is disseminated about all investment products, which will help streamline, and harmonize actual key disclosures. Such presentation should be balanced as the ultimate goal is to provide investor protection, while at the same time improving retail investors’ engagement in capital markets. From a practical perspective, digital design for instance should help investors to get further information if they so wish with for example the use of drawdown menus. This key information should predominantly focus on risk and performance, costs/value for money, total actual costs and fees, and other key features (including sustainability information). The comparability of risk reward profile with investor´s objectives and needs (investment horizon, amounts available for investment…) is equally important as choosing an investment should not solely be based on cost considerations.

The UCITS-KIID for instance, may be given as a good illustration of key information regarding the investment objectives risks, performance, costs and basic information of a financial product that is presented in a manner which is deemed clear and transparent.

While the presentation of this key information through main headings is important, details may be tailor-made per product.

Q6: Which are the practical lessons emerged from behavioural finance that should be taken into account by the Commission and/or ESMA when designing regulatory requirements on disclosures? Please provide details and practical examples.

The academic works in behavioural finance start from the assumption that it is arguable that the traditional approach to investor protection (which underpins in general legal regulations of financial markets and assumes that investors act rationally) is still adequate[5]. The financial crisis has indeed revealed fundamental problems with regards to this traditional approach and put into question the paradigm of rational behavior and information obligations[6].

Recently IOSCO[7] has pointed out three main “topic areas” where behavioural insights can be useful to respond to investor protection issues: i) Disclosure design; ii) Online interfaces; iii) Timeliness of information.

On disclosure design, there is mounting evidence, drawing from behavioural economic studies, that consumers struggle to understand the costs of investment products and the impact that these have on investment returns. For instance, the UK’s Financial Conduct Authority’s (FCA) completed in June 2017 a market study about the asset management industry and found evidence that consumers “rarely engage with [the] charges associated with fund investment”. The study also found that “investors’ awareness and focus on charges is mixed and often poor,” with nearly half of retail investors not even aware that they are paying fund charges for their asset management services. According to FCA analysis of browsing data from online investment platforms, very few investors seek out information related to costs. Of all the visits to the website to look at funds, fewer than 9% of visitors looked for charges’ information, while under 3% look at documents (including the KID).

Going a step further, the UK Financial Conduct Authority published in April 2018 a discussion paper on “Drawing attention to charges in the asset management industry”. The paper drew attention to the fact that simply providing consumers with information in disclosure documents about charges, does not guarantee that they will use it in their decision-making. The paper found that clearly presenting engaging information

[5] Ben-Shahar and Schneider 2010, p. 48.
[6] *Behavioural finance and investor protection regulations*, Gerald Spindler, June 2011.
[7] IOSCO, *The application of behavioural insights to retail investor protection*, April 2019.

in a prominent way can enhance the effectiveness of disclosures. For instance, the paper found that using colour, graphics and plain language as well as warnings and impact charts helped consumers in their decision-making when making investment decisions.

Additionally, as suggested by the IOSCO survey, disclosures face substantial competition for investors' attention e.g., from a sales pitch or marketing materials. This context can help informing the development of disclosures that make the most of the limited attention they receive, or that could capture a greater share of investors' attention relative to competing factors. It could be derived from there that clear and effective warnings in PRIIPs KID documents and MiFID II disclosures would help investors to better pay attention to costs when making investment decisions.

More generally, a number of tactics have been suggested for improving the effectiveness of disclosures in encouraging informed decision-making. These tactics are intended to organize disclosures in a way that reflects the time and other constraints faced by these disclosures' intended audiences. The objective should be to direct users' attention to the most important information included in a disclosure, and to design disclosures such that the most important disclosures are also the most engaging. Firstly, important pieces of information should be placed where most consumers would be expected to focus their attention. This generally means that important information should be placed prominently and in intuitive places in a disclosure, and should be easily accessible by readers. For instance, for the PEPP KID, a mini-dashboard is placed at the top of the KID with the most important information. Secondly, while keeping in mind that even short, one-to-two page disclosures can be complex and confusing for investors, regulators should continue encouraging or seeking to ensure that disclosure providers simplify the language used in their disclosures where possible. Thirdly, graphical elements may also affect how a reader understands and uses a disclosure. For example, Oxera[8] tested graphical elements employed to help describe the risk level of an investment.

This being said, disclosure is not necessarily the best solution as illustrated by David Leiser[9] about the disclosure of the conflicts of interests around inducements. A contradictory outcome could be the result as more confidence may be attributed through the disclosure by the people who are not financially literate. It may indeed be difficult for not qualified investors to discount information from a source with conflict of interest and they would not know where to turn in order to get "neutral" information. Indeed, while disclosure is central to informed investor decision-making, disclosures and other informational resources, even if informed by behavioural insights, are not guaranteed to succeed. Standards of conduct imposed on the investment professionals on whom retail investors rely to recommend and manage investments and the regulation of investment products sold to retail investors, should continue to be part of the total mix of measures employed by regulators to further retail investor protection.

On the second topic area defined by IOSCO, namely online interfaces, we observe that while the use of online investing tools is widespread, the academic literature on online investment behaviour remains nascent. The available literature indicates that individuals tend to make different decisions when interacting with an online interface as opposed to interacting with a human or with print materials (see below Q. 21). For the purpose of disclosure and subsequent decision-making, it is worthwhile mentioning that given the availability of online comparison and choice engines individuals may be more likely to compare investments side-by-side, based on the metrics displayed by the relevant online interface, rather than reviewing investment options one-by-one. By organizing and ordering information in different ways, comparison and choice engines offer the possibility of customizing the amount of choices and information presented to fit the user's appetite for reviewing this information.

Additionally, graphical elements, the organization of information, and the use of plain language are crucially important for users of online interfaces as visual biases are especially relevant in screen environments. Oxera shows that design elements that work well in print may not necessarily work well online: users may skim through information that is presented online in a format similar to that used in print. As a recent study shows[10] users are accustomed to skipping through dense "Terms and Conditions" presented on various

[8] Oxera, *Review of literature on product disclosure* (prepared for UK FCA), 2014.
[9] *Paradoxical Effects of the Disclosure of Conflict of Interest on the Selection of a Pension Plan*, D. Leiser, N. Gadsi, N. Basher, A. Spivak, December 2010.
[10] Jonathan A. Obar and Anne Oeldorf-Hirsh, *The Biggest Lie on the Internet: Ignoring the Privacy Policies and Terms of Service Policies of Social Networking Services*, Information, Communication & Society (2018).

websites. In this respect, OECD[11] shows that requiring users to choose whether to review or skip required disclosures may increase the likelihood that this disclosure will be reviewed.

The third topic area where behavioural insights can contribute on investor protection is the timeliness of information. In fact, timeliness of information delivered to investors is relevant to investors' likelihood of reviewing and acting on that information. The challenge is to identify when an investor is most likely to be receptive to a given piece of information, something that can vary not only from situation to situation, but from person to person, and deliver information at that time. Oxera shows that while general disclosures on fees is made available at the point of sale, individuals tend to be less likely to pay attention to fees that are charged farther out in the future. So forth, one means of bringing management and other fees charged to investors' attention after purchase may be to provide fee reports at the time these fees are charged. UK FCA applied this concept to overdraft charges,[12] finding that sending consumers a text message notifying them that they had reached their overdraft limit and could avoid charges by making a deposit into the relevant account before a given cut-off time reduced overdraft fees charged by 25 per cent. The study shows that many consumers reported incurring overdraft fees largely as a result of inattention, or not realizing that they had insufficient funds in a given account to make a purchase, rather than having insufficient savings.

Strategies based upon timeliness of information can also be important tools for more general financial welfare. A field study[13] shows the relevance of the "fresh start effect". In delivering investor education materials or materials encouraging individuals to plan for retirement, choosing to present this information when individuals have reached a particular milestone: birthdays, the start of a new job or the beginning of a new year can lead people to step back from their day-to-day routine and take in new information about newly available choices.

Based on further literature on behavioural finance, several ideas may be explored around a stricter enforcement of the know-your-customer principle, where documentation may be combined with tests (more or less thorough, using psychological insights, possibly determined in liaison with supervisory authorities) which would reveal the real knowledge bias and the real risk aversion of clients.[14] Other suggestions may be made based on behavioural observations combined with practical insights: restriction of the information to the core, with two-layers information depending on whether the investor is interested or not and/or his level of knowledge and experience; consistent, comparable and retrievable information at any time; mitigation of investors' overconfidence and (maybe) through striking examples.

Q7: Are there any challenges not adequately addressed by MIFID II on the topic of disclosures that impede clients from receiving adequate information on investment products and services before investing? Please provide details.

Where inducements are being paid, disclosure is important to allow clients to receive adequate information on services before investing, along the lines drawn by ESMA in its Technical Advice published on 31 March 2020. In addition, it may be in particular recommendable to make inducements disclosures on an ISIN-by-ISIN basis, to include a clear explanation of the terms used to refer to inducements and to display on the firms´ website the specific quality enhancing services that the client is already benefiting from or that the client could benefit from. It could also be useful to observe recently drawn rules such as the ones adopted by the Central Bank of Ireland[15] with a comprehensive summary (e.g., a table) of the inducement that the firms receive on their (public-facing) website. The objective is to enhance inducement transparency for consumers prior to becoming a client of the broker and/or taking investment decisions, while it may be operationally or technically difficult for firms to provide this information in an easy way on the public-facing part of their website.

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[11] OECD, *Behavioural Insights and Public Policy: Lessons from Around the World,* 2017.

[12] UK FCA, *Sending out an SMS: The impact of automatically enrolling consumers into overdraft alerts,* Occasional Paper No. 36, May 2018.

[13] H. Dai, K.L. Milkman, and J. Riis, *The Fresh Start Effect: Temporal Landmarks Motivate Aspirational Behavior*, Management Science , 60, 2014.

[14] For an insightful exploration of the demand side of financial advice: *Is Unbiased Financial Advice to Retail Investors Sufficient? Answers from a Large Field Study*, U. Bhattacharya, A. Hackethal, S. Kaesler, B. Loos, S. Meyer, September 2011.

[15] Feedback statement CP116 Intermediary Inducements – Enhanced consumer protection measures, Central Bank of Ireland, September 2019, p. 15.

Q8: In case of positive answer to one or more of the above questions, are there specific changes that should be made to the MiFID II disclosure rules to remedy the identified shortcomings? Please provide details.

Based on the feedback received from investors and the lessons drawn from behavioural finance, the MiFID disclosure rules should concentrate on the key information as described in response to Q5 in order to make prominently appear risk and performance, costs/value for money, total actual costs and fees, and other key features (including sustainability information).

In addition, as mentioned in the response to Q4, the MiFID cost disclosure information should be aligned with the PRIIPs one, with the objective to take out information that are of little or no value to clients, such as cumulative effects on return, percentages, description of calculation methodologies.

Q9: On the topic of disclosures on sustainability risks and factors, do you see any critical issue emerging from the overlap of MiFID II with the Sustainable Finance Disclosure Regulation (SFDR) and other legislation covering ESG matters?

Please see our response to Q4 regarding the interaction/overlaps between MiFID II and SFDR.

Q10: Are there any other aspects of the MiFID II disclosure requirements and their interactions with other investor protection legislations that you think could be improved or where any specific action from the Commission and/or ESMA is needed?

It is important to think beyond the MiFID II disclosure requirements in order to assess and in the end improve the way they are "absorbed" by the investors. As already mentioned, consumer testing in of great help in order to evaluate if "average clients" (as defined in Article 44 2 (d) of the MiFID Delegated Regulation 2017/565) understand the information they are presented. Behavioural finance is of great value in this context in order to better decipher the investors´ reactions, biases, etc. Psychology and emotions (rather than knowledge) are often a main factor driving consumer decision-making in retail finance. Consumers frequently focus on inappropriate information when taking financial decisions, or are distracted by too much information and choice when taking investment decisions, or may be unaware about the conflicts of interests at play in advice settings.

This should not prevent from keeping up with efforts in the area of financial education, although research[16] shows that the effectiveness of financial education in having lasting effects on the knowledge (and especially the behaviour) of consumers is often limited at best. In few cases financial education may have a reverse effect as it increases confidence, without improving ability, leading to potentially worse financial decisions. These observations lead to reiterate the importance for the retail investors to be accompanied by professionals, as a useful complement to become more financially literate.

Q11: Do you have any empirical data or insights based on actual consumers usage and engagement with existing MiFID II disclosure that you would like to share? This can be based on e.g., consumer research, randomized controlled trials and/or website analytics.

Please refer to elements mentioned in Q6.

Q12: Do you observe a particular group or groups of consumers to be more willing and able to access financial products and services through digital means, and are therefore disproportionately likely to rely on digital disclosures? Please share any evidence that you may have, also in form of data.

Digital channels are important for young people, but are also an important channel from a financial inclusion point of view, as we may e.g. reach people in rural areas and suburbs where there may not be a bank or post office, but where you have 3G/4G/5G and can use your smart phone or tablet to reach your bank, investment firm or fund manager.
Therefore it does not look so much a matter of disproportionate reliance on digital disclosures. It is more a question of accessibility of digital information and services as digital channels are both a factor of inclusion (from a geographical perspective) and exclusion (mainly linked to the age and the capacity to use digital tools).

[16] BEUC, *Finance: when more education isn´t the answer*, May 2016.

It is also more a question of the overreliance not on the digital disclosures themselves but on e.g., social media influencers, as elaborated upon in response to Q16 and Q36. The latter are often non-regulated advisers who lead retail investors to invest in financial instruments without being provided with any type of KID to make their own investment decisions and/or without even being aware that regulated product information documents exist and should be provided to them.

Q13: Which technical solutions for digital disclosures (e.g., solutions outlined in paragraph 27 or additional techniques) can work best for consumers in a digital - and in particular smartphone - age? Please provide details on solutions adopted and explain how these have proven an effective way to provide information that is clear and not misleading.

Using digital channels is about using other channels to perform the same activity, while abiding by the same regulatory framework.

Amongst the technical solutions which could improve the consumer´s experience in a digital age are the following ones:

- To have clear rules to prescribe presentation formats (e.g. readable font size, use of designs and colours, etc.);
- To focus more on the information that should be provided instead of on the number of pages of this information, as the latter is not relevant in a digital context;
- To refrain from using "pop-up" boxes to provide information to clients where records need to be kept, as it is difficult to provide records of this;
- To adapt the requirement "in good time" as, in case of trading via phone, it makes more sense to send the information before the call;
- To find the right balance between the requirements to keep websites/digital information updated while at the same time providing that client's should be able to revisit old information;
- Other technical solutions have been contemplated in the SMSG advice on the ESAs survey on templates for environmental and/or social financial products under SFDR[17].

Such reflection on technical solutions should not be performed in silos, and should for instance be coordinated with the work and input provided in the context of the individual pension tracking systems.

Q14: Would it be useful to integrate any of the approaches set out in paragraph 27 above in the MIFID II framework? If so, please explain which ones and why.

Q15: Should the relevant MIFID II requirements on information to clients be adapted in light of the increased use of digital disclosures? If so, please explain how and why.

The adaptations regarding the layering of information, digital formats and nudging may potentially require adaptations of the MiFID II framework.

Q16: Do you see the general need for additional tools for regulators in order to supervise digital disclosures and advertising behind 'pay-walls', semi-closed forums, social media groups, information provided by third parties (i.e., FINfluencers), etc? Please explain and outline the adaptions that you would propose.

As a general consideration, the SMSG would like to reiterate, along the lines of its Advice to ESMA on Digital Finance issued in July 2021 that "same activity, same risk, same regulation" should apply and that "competition policies, supervision and enforcement need to be adapted, and further enhanced". It is indeed essential that unregulated platforms/channels which perform similar activities are subject to the MiFID II/UCITS regimes, including digital disclosures.

It is important to note that, for regulated investments, advertising rules are already similar regardless of the used medium (e.g. radio, printed press, online, TV…). In all of these media, the advertised information about a product or service must be "fair, clear and not misleading". We believe that these rules should be extended to all EU and non-EU providers of non-regulated products that distribute in the EU.

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[17] https://www.esma.europa.eu/sites/default/files/library/esma22-106-2993_smsg_advice_on_sustainability_templates.pdf

As regards unauthorized providers engaging in sometimes unlawful solicitation, national competent authorities should be endowed with broader powers to order if warranted the closure of their websites or to block access to them from their national territory.

Q17: To financial firms: Do you observe increased interest from retail investors to receive investment advice through semi-automated means, e.g., robo-advice? If yes, what automated advice tools are most popular? Please share any available statistics, data, or other evidence on the size of the market for automated advice.

Robo-advisors were expected to grow quickly to significant scales (in terms of users and assets under management), but data show this has not been the case.[18] Although robo-advisers have become more popular in some countries over the last few years, their use still represents a small part of the financial market (they are primarily used for investments in UCITS and ETFs).

This limited use, combined with the fact that retail clients have expressed preference for human advice,[19] makes hybrid models (use of robo-advisers accompanied by a human adviser) more promising.

Q18: Do you consider there are barriers preventing firms from offering/developing automated financial advice tools in the securities sectors? If so, which barriers?

Amongst the limitations to the development of automated financial advice tools are the clients' acquisition costs faced by independent robo-advisors which are still very high (Morningstar estimates a 10 years break-even time).[20] Additionally the fast evolution of the robo-advice market has been hampered by limited awareness of this business model and a low level of financial literacy of retail clients and their preference therefore to rely on human financial advisers in the investment decision process, at least on top of digital information, as described in the response to the previous question. The value proposition of robo advisors is complex for the average saver, who is confused by the terms "no commissions", "fee-based", "ETF", etc. Robo-advice is more successful with qualified non-professional investors who are also comfortable with a virtual only (or almost only) client relationship.

Based on the experience made by investors, it appears that a hybrid model where independent holistic financial planning is provided by a human and the implementation of the investment part is delegated to a robo might be more promising. The concept of "robo4" is indeed valuable, as it helps to increase the transparency of the decision process regarding the asset allocation choices.

Additionally, the co-operation between established financial institutions and fintech firms, together with an improved user-experience and an upgraded use of AI (as in the case of "conversational" robo-advisors), might boost demand for automated advice.

Q19: Do you consider there are barriers for (potential) clients to start investing via semi- automated means like robo-advice caused by the current legal framework? If so, please explain and outline what you consider to be a good solution to overcome these barriers.

No barriers of this kind have been identified.

Q20: In case of the existence of the above-mentioned barriers, do you have evidence of the impact that they have on potential clients who are interested in semi-automated means? For instance, do they invest via more traditional concepts or do they not invest at all?

Q21: Do you consider the potential risks and opportunities to investors set out above to be accurate? If not, please explain why and set out any additional risk and opportunities for investors.
Experimental studies[21] show that individuals are less inhibited online. The social friction "arising from the normal feelings of anxiety and self-consciousness of being judged" when interacting with a human are less present when interacting with an online interface. As a result, individuals may be more honest online than

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[18] https://betterfinance.eu/wp-content/uploads/Robo-Advice-Report-2020-25012021.pdf
[19] According to a survey 80 % of the clients in Germany responded that personal investment advice is important (or more); KPMG, *The future of advice*, November 2021, pp 14-15.
[20] https://international-adviser.com/robo-advisers-struggle-profit-morningstar/

[21] Jessica An, Melanie Kim, and Dilip Soman, *Financial Behaviour Online: It's Different!, Rotman school of management,* 2016.

with a human: for online investment advisors, this may mean that responses to an online know-your-client questionnaire may tend to be more honest than responses given to questions posed by a human investment advisor. But it also means that individuals may be more likely to make impulsive and biased choices - based, for example, on price information displayed on an online interface or based on financial news or other information. The relative ease with which decisions can be made online or in a mobile environment may reinforce this dynamic by allowing people to think "faster" and with more shallow attention. Recent experiences during the pandemic show individuals using online platforms as more likely to speculate and try to time the market through frequent trading. The introduction of no-fee online trading interfaces may affect this dynamic, encouraging more impulsive trading. On the other hand, these interfaces may reduce barriers to investors' regularly allocating savings to investments in accordance with a financial plan.

It is also important to note that individuals interact with online interfaces on a variety of different screens - from desktop computer monitors to mobile phones - and that a user may interact with information differently depending on the screen they use to view that information[22]. For example, users may tend to think "faster" and make quicker, shallower decisions when working on smaller screens (which may lead them, for example, to skip through warnings and make impulsive financial decisions). IOSCO reports the use of oculometric tests (recording eye movement), as well as audio and video recordings as means of testing how users interact with and review information provided within online portals, in addition to face-to-face questions.

Another major question remains the accountability of algorithms and how to explain their functioning. There are common concerns that the use of algorithms creates risks in terms of consumer protection. Consumers are not aware of the technology used by such automatisation, and they lack understanding of the underlying process from which the investment advice is proposed.

Q22: Do you consider that the existing MiFID regulatory framework continues to be appropriate with regard to robo-advisers or do you believe that changes should be added to the framework? If so, please explain which ones and why.

Q23: Do you think that any changes should be made to MiFID II (e.g., suitability or appropriateness requirements) to adequately protect inexperienced investors accessing financial markets through execution only and brokerage services via online platforms? If so, please explain which ones and why.

Regarding this question, the SMSG would like to refer to its response to the ESMA consultation on "Guidelines on certain aspects of appropriateness and execution-only" dating from 28 April 2021.

Q24: Do you observe business models at online brokers which pose an inherent conflict of interest with retail investors (e.g., do online brokers make profits from the losses of their clients)? If so, please elaborate.

The SMSG does not see any inherent conflict of interest for the types of online brokers which operate under the EU regulatory framework. With regards to the PFOF aspects, please refer to Q28.

They are subject to strict requirements and to a close supervision in their respective Member States. It may happen that there are online brokers who operate under less strict requirements but there are located outside the EU or in some jurisdictions where the enforcement is less stringent (e.g., in Malta).

On the contrary, access to self-service channels (execution only) is very appreciated by retail clients (e.g., in the Nordics, in Germany) where a large number of retail clients recourse to these services.

To ensure that an appropriate framework which does not impede to serve clients´ needs is also important in the context of the EU Digital agenda.

Q25: Some online brokers offer a wide and, at times, highly complex range of products. Do you consider that these online brokers offer these products in the best interest of clients? Please elaborate and please share data if possible.

Different practices exist in the market, which is illustrated by the fact that most of online brokers offer a wide range of products. The overall picture is that through the product governance processes, appropriateness

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[22] Shlomo Benartzi and Jonah Lehrer, *The Smarter Screen: Surprising Ways to Influence and Improve Online Behavior, Penguin* 2015.

tests and additional measures it is widely ensured that the best interests of the clients are met. However, there is a limited number of brokers that offer only a small range of riskier and more complex products.

The issue indeed lies not so much with the products themselves but with the broad target market and the inappropriate marketing practices that were used. Some highly complex products should indeed be sold to investors who are able to understand their risks. This is the reason why the appropriateness tests play a so crucial role,[23] and that a further layer of information sometimes complements them.

Indeed, while blatantly conflicted product offerings such as uncovered CFDs tend to disappear, some distributors, continue to apply insufficient product governance. They solicit an excessively large target market or fail to duly apply rigorous appropriateness tests to check effective clients' understanding of the proposed products.

Q26: One of the elements that increased the impact on retail investors in the GameStop case was the widespread use of margin trading. Do you consider that the current regular framework sufficiently protects retail investors against the risks of margin trading, especially the ones that cannot bear the risks? Please elaborate.

As pointed out during the discussion in preparation for the SMSG´ response to the short selling regulation consultation, this is a smaller problem in the EU than in the US. While we have seen in a few occasions phenomenons which may look like "GameStop" in the EU markets, they normally stop when the market place halts trading for the time which is deemed necessary. Aside from this, short-selling rules in the EU are very different from those in the US, making a major GameStop-event less likely to happen in the EU.

Q27: Online brokers, as well as other online investment services, are thinking of new innovative ways to interact and engage with retail investors. For instance, with "social trading" or concepts that contain elements of execution only, advice, and individual portfolio management. Do you consider the current regulatory framework (and the types of investment services) to be sufficient for current and future innovative concepts? Please elaborate.

Online brokers, as well as investment firms which provide online investment services, indeed explore ways of interacting with the investors with a more "social touch" for instance through the provision of guidance/inspiration, by using examples of what other investors are interested in. It can be seen as a sharing of experiences, without any prominent adviser who might show the way.

Q28: Are you familiar with the practices of payment for order flow (PFOF)? If yes, please share any information that you consider might be of relevance in the context of this call for evidence.

The use of payments for order flow (PFOF), where a broker (investment firm) directs the orders of its clients to a single execution venue (i.e. a trading venue as defined in Article 4(1)(24) MiFID II) for execution against remuneration, appears to be increasingly popular as a business model (in the past it seems that it was more linked to advertisement campaigns), in particular in the context of newly established online brokers (known as "neo brokers"). Being compensated by such execution venues, brokers are able to offer their services with low, or even no, direct fees to their clients. This practice remains subject to standard MIFID/R requirements of transparency to clients on retrocessions; the quality improvement test; the best execution framework; product governance; appropriateness/suitability tests; and fair marketing communication including disclosure of costs and risks.

While, on one hand, this practice seems to contribute to a very significant increase in clients investing in financial instruments and thus fosters – the highly desirable – investor participation in capital markets, on the other hand, it may raise concerns in terms of potential conflicts of interest due to payment of inducements and fulfilment of the obligations surrounding best execution of client orders (i.e., an obligation to execute orders on terms that are most favourable to the client).

First studies have emerged as described below:

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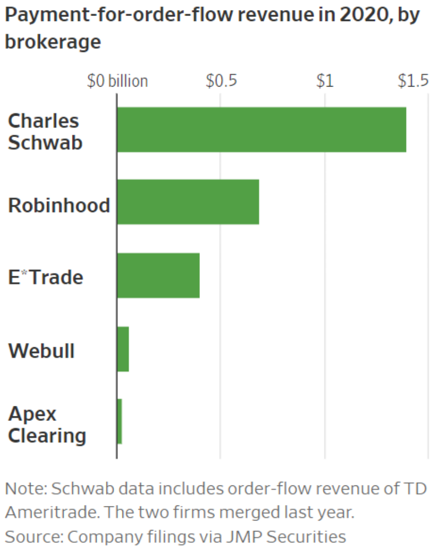
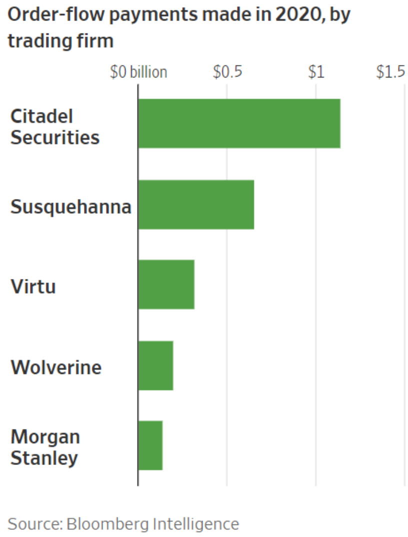
[23] See SMSG advice to ESMA on its Consultation Paper on *Guidelines on certain aspects of appropriateness and execution-only*, ESMA22-106-3280, 29/04/2021; https://www.esma.europa.eu/sites/default/files/library/esma22-106-3280_smsg_advice_on_appropriateness_and_execution-only.pdf

The independent investor protection magazine "Finanztest" (see above) published a test with four "ne-obrokers" in November 2021 with the result that the trade functioned according to their observation well. No great surcharge against the "Xetra"-trade was discovered[24], at least during the official trading hours for known shares and ETFs. Further investigation may be needed in order to take into account the potential time lag between the order positioning by the retail client and the order execution.

A recent study[25], performed by academics upon request of a neobroker and based on its own data, came to the conclusion "(…) that payment for order flow ultimately does not harm private investors. On the contrary, customers benefit from this new trading venue. Future research needs to address how these low costs impact trading activity and returns and long-term stock market participation, which might result in higher pension savings. We will focus on these questions in subsequent studies."

Although not transferable one to one, the US experience is also of interest all the more as evidence from the US is more abundant based on SEC rule 606 that requires both the payor and the beneficiaries to disclose the amounts paid to whom. The last annual data for the main players reads as follows:





Coming back to the EU, following the decision from the European Commission to insert a provision in the MiFIR text review with aims to ban these practices, while the ESMA´s call for evidence which tackles this topic is still open, the SMSG would like to plead for a thorough check about i) the use of third party payments by the broker; ii) the execution quality and the transparency to the clients of the broker; iii) the impact on liquidity and price discovery.

Once done, these technical findings should be weighed against the increase of the engagement of retail investors in capital markets, the latter being one of the most prominent objectives of the CMU, which should not hamper by higher trading commissions.

Q29: Have you observed the practice of payment for order flow (PFOF) in your market, either from local and/or from cross border market participants? How widespread is this practice? Please provide more details on the PFOF structures observed.

There is divergence in whether PFOF and other inducements are allowed or not among Member States. In particular, they are banned in the Netherlands.

Q30: Do you consider that there are further aspects, in addition to the investor protection concerns outlined in the ESMA statement with regards to PFOF, that the Commission and/or ESMA should consider and address? If so, please explain which ones and if you think that these concerns can be adequately addressed within the current regulatory framework or do you see a need for legislative changes (or other measures) to address them

[24] https://www.test.de/Smartphone-Broker-im-Test-5468655-0/

[25] *Private investors and the emergence of neo-brokers: Does payment for order flow harm private investors?* University of Southern Denmark and the WHU – Otto Beisheim

A legislative change (or other measures) would be welcome. There should be full transparency on PFOF practices, the firms involved, and flows, like in the US (SEC rule 606). Conflicts of interests should be eliminated. In addition the existing best execution rules are too vague, too complex and allow for different interpretations on PFOF. They should be simplified and made easier to comply with and to enforce.

Q31: Have you observed the existence of "zero-commission brokers" in your market? Please also provide, if available, some basic data (e.g., number of firms observed, size of such firms and the growth of their activities).

In the Swedish market, there are several popular "low-commission brokers" which are used by a large number of retail clients due to their low fees and easily available services.

In Germany there are about five "neobrokers"; the independent investor protection magazine "Finanztest" (see above) published a test with four of them in November 2021.

In France zero-commission brokerage schemes also exist (generally referred to as 'free trade campaigns'). They are essentially centered on half a dozen online brokers.

Q32: Do you have any information on "zero-commission brokers" business models, e.g., their main sources of revenue and the incidence of PFOF on their revenue? If so, please provide a description.

Q33: Do you see any specific concern connected to "zero commission brokers", in addition to the investor protection concerns set out in the ESMA statement that the Commission and/or ESMA should consider and address? Please explain and please also share any information that you consider might be of relevance in the context of this call for evidence. Please also explain if you consider that the existing regulatory framework is sufficient to address the concerns listed in the ESMA statement regarding zero-commission brokers or do you believe changes should be introduced in the relevant MiFID II requirements.

The review of zero-commission brokerage schemes should be made with due consideration of the concerned asset classes and, quite importantly, of the market models and the underlying pricing dynamics. These schemes have been an integral part of marketing strategies for decades, on a par with similar marketing policies for other financial products such as, for example, the temporary and targeted exemption by fund managers of entry costs on their investment funds.

It should be acknowledged that some poorly regulated entities have developed aggressive marketing practices, using crypto-assets as an appealing product but also frequently extending their service offering to more traditional asset classes such as bonds, stocks, etc.

On the other hand, when zero-commission brokerage schemes are properly implemented by duly regulated firms, they are subject to the following ethical as a general rule:

- Full transparency towards clients on the existence of retrocessions,
- Submission of the zero-commission brokerage to a quality improvement test as required by the inducement regulations,
- Best execution framework (trade benchmark with reference market prices),
- Due implementation of product governance including proper determination of target market and related distribution strategy – which helps prevent mis-selling,
- Proper implementation, as the case may be, of appropriateness or sustainability test,
- Fair marketing communication including complete disclosure of costs (specifically as concerns possible product costs beside service costs) and proper information on the risks incurred.

In addition, where zero-commission or neo-brokers provide services of safekeeping of shares, administration of shares or maintenance of securities accounts on behalf of shareholders or other persons, they are considered as intermediaries by the Shareholders Rights Directive (SRD) II. Where such intermediaries provide services to shareholders or other intermediaries with respect to shares of companies which have their registered office in a Member State and the shares of which are admitted to trading on a regulated market situated or operating within a Member State, they have to comply with the rules of SRD II and its Implementing Regulation. In particular, they have to facilitate shareholder engagement by facilitating the communication between issuers and shareholders especially around a general meeting. Some stakeholders, however, observed shortcomings at neo-brokers in terms of voting rights execution and transfer of information for shareholders. According to an upcoming study by Better Finance & DSW not only various neo-brokers do not ensure to offer these services, some even publicly state that they have no obligations to inform shareholders and facilitate their voting rights, which is contradicting the requirements of Shareholder Rights Directive (SRD II) and its Implementing Regulation.[26]

Therefore, EU authorities should assess the compliance of online brokerage platforms acting as intermediaries with the SRD II requirements and address shortcomings in the transposition of the Directive and its Implementing Regulation into national law across Member States.

Q34: Online brokers seem to increasingly use gamification techniques when interacting with clients. This phenomenon creates both risks and potential benefits for clients. Have you observed good or bad practices with regards to the use of gamification? Please explain for which of those a change in the regulatory framework can be necessary. Do you think that the Commission and/or ESMA should take any specific action to address this phenomenon?

Techniques are increasingly growing in order to make the experience more investor-friendly. For instance, virtual approaches are used as simulated experiences of trades. Watchlists are also provided to observe some stocks and the way they are evolving. These techniques are seen as part of the education provided to the investor in a way that improves his/her investment experience.

As they concern the distribution strategies, these gamification techniques are already subject to the current regulatory framework. In our view, they should notably be subject to the product governance reviews that precede any product launch. In this review a specific attention should be given to the possibility that the "gaming" approach may distort the investors ability to appreciate the incurred risks and costs. This could also be specifically be monitored by auditors and regulators when reviewing the firms' compliance with the applicable product governance requirements.

Q35: The increased digitalisation of investment services, also brings the possibility to provide investment services across other Member States with little extra effort. This is evidenced by the rapid expansion of online brokers across Europe. Do you observe issues connected to this increased cross-border provision of services? Please elaborate.

Q36: Do you observe an increasing reliance of retail clients on information shared on social media (including any information shared by influencers) to base their investment decisions? Please explain and, if possible, provide details and examples. Do those improve or hamper the decision-making process for clients?

Social media play a more and more important role, which creates a difficult situation to control and supervise. Although this phenomenon can be seen as positive as it stimulates the interest in financial services/products, young investors in particular[27] increasingly rely on social media when they make investment decisions. Prompted by the new investment apps, the access to all products, including crypto-currencies, speculative mini-bonds or other high-risk products, is much easier for these investors. Therefore it has to be made sure that the products promoted through online and social media platforms are suitable for investors who should not buy high-risk products under the pressure of online adverts or sales tactics.

Other drawbacks, such as the use for market manipulation, make necessary a strong vigilance from the supervisors. One may argue that, just as citizens should not rely primarily on medical advice by non-professionals online, investors should not rely primarily on non-professional financial advice online either.

Q37: What are, in your opinion, the risks and benefits connected to the use of social media as part of the investment process and are there specific changes that should be introduced in the regulatory framework to address this new trend?

The SMSG is of the opinion that there are very significant risks that these social media platforms are used as a vehicle by some users to help disseminate investment related information and may also pose risks for retail investment, for instance if retail investors rely on unverified information or on information not appropriate to their individual situation.

In addition, we see an increasing trend of high-risk investment products (e.g., cryptocurrencies, foreign exchange) increasingly being promoted to consumers through social media, including outright scams. Social

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[26] Better Finance & DSW Study, *Barriers to Shareholder Engagement 2.0: SRD II Implementation Study*, to be published in January 2022.

[27] https://www.fca.org.uk/news/press-releases/fca-warns-younger-investors-are-taking-big-financial-risks

media firms and national competent authorities should ensure that scams in particular are not promoted aggressively to consumers through social media, as actively resisted by the UK FCA[28].

Q38: Are you aware of the practices by which investment firms outsource marketing campaigns to online platform providers/agencies that execute social media marketing for them, and do you know how the quality of such campaign is being safeguarded?

Q39: Have you observed different characteristics of retail clients, such as risk profiles or trading behaviour, depending on whether the respective client group bases their investment decision on information shared on social media versus a client group that does not base their investment decision on social media information? Please elaborate.

Q40: Do you have any evidence that the use of social media (including copy/mirror trading) has facilitated the spreading of misleading information about financial products and/or investment strategies? Please elaborate and share data if possible.

Some National Competent Authorities in the Member States fine (often smaller) investors that have (ab)used social media or moved stock prices via platforms. In the context of an active surveillance combined with educational initiatives,[29] it is stressed that the gains made by investors are often very small compared to the fines they get[30]. (In the same vein, ESMA issued on 28 October 2021 a public statement with regards to investment recommendations made on social media platforms, where misleading information is explained and warned against.)

In addition, we also observe that certain non-regulated players or certain providers which offer non-regulated products may publish misleading or false information on social networks. For those entities/products that are currently unregulated, the challenge would be to extend to them the rules applicable to regulated investment firms/products in order to protect investors and avoid the multiplication of internet scams that have been observed in recent years. For this purpose EU regulation on investment advice (the latter being so far regulated only by MiFID) should cover all investment products and all media providing such advice.

From a more general perspective, social media platforms should take more responsibility when it comes to the spreading of misleading information, market manipulation etc., and supervisors should scrutinise this very closely. The rules need to be reinforced at EU level with respect to dissemination of investment related information via social media platforms.

Q41: Have you observed increased retail trading of 'meme stocks', i.e. equities that experience spikes in mentions on social media? Please share any evidence of such trading and, if possible, statistics on outcomes for retail investors trading such instruments.

In the case of GameStop shares in January 2021, a small proportion of investors (1%) followed this movement, amongst them clients of a major German neobroker. Similar cases happened with Nokia and Blackberry, windeln.de shares for instance. Since its insolvency, also the Wirecard share price is driven by mentions in online forums and/or blogs.

Q42: Do you consider that the current regulatory framework concerning warnings provides adequate protection for retail investors? If not, please explain and please describe which changes to the current regulatory framework you would deem necessary and why.

Rules applying to regulated entities e.g. as regards warnings provide an adequate protection for investors, save that some rules may need to be adjusted to make them more fit for the digital world.

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[28] https://www.fca.org.uk/news/press-releases/fca-warns-younger-investors-are-taking-big-financial-risks
https://www.fca.org.uk/news/press-releases/fca-confirms-speculative-mini-bond-mass-marketing-ban
https://www.which.co.uk/news/2020/06/fca-permanently-bans-mini-bond-ads-are-investors-still-at-risk-of-losing-money/
https://www.which.co.uk/news/2021/03/investment-scammers-run-riot-on-search-engines-while-victims-pay-the-price/
[29] Illustration from BaFin: https://www.bafin.de/SharedDocs/Veroeffentlichungen/EN/Verbrauchermitteilung/Marktmanipulation/2021/meldung_21_06_10_Windeln_de_en.html;jsessionid=AAC33E56B7B466A1BA096157836FE49C.1_cid503
[30] For an example of the amount of these sanctions in Sweden: https://www.fi.se/sv/publicerat/sanktioner/marknadsmissbruk/2021/fysisk-person-doms-att-betala-sanktionsavgift-for-marknadsmanipulation16/

A close supervisor´s scrutiny is of essence in this context (especially regarding crypto assets) and a global supervisory approach is needed, as illustrated by the recent ESMA´s statement (28 October 2021) which addresses investment recommendations made on social media platforms.

Q43: Do you believe that consumers would benefit from the development of an 'open finance' approach similarly to what is happening for open banking and the provision of consumer credit, mortgages, etc? Please explain by providing concrete examples and outline especially what you believe are the benefits for retail investors.

Digitalisation implies the mass processing of user data, which brings both advantages and risks. More data can improve the distribution and execution processes, but it must not, on the other side, be used against or without the consent of the consumer. It is important to note, in the context of the Open Finance recommendations of the Final Report of the High-Level Forum on the Future of the CMU, that the collection of user information must respect certain principles:

- first, it should be compliant with the EU GDPR and not extend further than financial data and,
- second, it must ensure that the consent of the data subject is not extorted.

Q44: What are, in your opinion, the main risks that might originate from the development of open finance? What do you see as the main risks for retail investors? Please explain and please describe how these risks could be mitigated as part of the development of an open finance framework.

The development of open finance may give rise to several risks, namely provider´s liability, mis-sellings, cybersecurity, and data protection.

The risk linked to provider´s liability and mis-selling is due to faults by design and data protection concerns, including cyber-security risks. It must be made clear that the platform manager or owner is responsible for the information provided on the platform, including for the algorithms used to calculate and display results based on user input. Although automated investment platforms bring many advantages and cost efficiency gains, this should not be construed as a limitation of liability for investment advice provided via the platform.

As regards data protection, the risk of giving direct or indirect access to non-EU third-party providers (mainly US GAFAs or Chinese BATX) to abundant and sensitive personal data should be duly analysed, together with the risk of dissemination of this data and/or its use for unauthorized purposes.

As mentioned in the SMSG advice to ESMA on digital finance and related issues (30 July 2021), another risk is the increased use of artificial intelligence (AI) in voting processes. AI is being used to provide data for voting at general meetings and it enables institutional investors to robo-vote according to pre-set instructions, or in accordance with a proxy advisor's voting policy, if the investor provides no other special instructions. Such a practice necessarily transfers fiduciary voting authority from investors to proxy advisors and consequently impacts governance and oversight of companies, as it allows investors to set their voting decisions on autopilot (set and forget). According to a study[31], 114 institutional investors voted in lockstep alignment with the two largest proxy advisors and robo-voting institutional investors in the US managed collectively more than $5 trillion in assets in 2020. The SEC therefore has issued guidance to make clear to institutional investors that fiduciary duties cannot be outsourced. In the EU, there do not yet exist any rules governing the use of AI in the area of vote execution or fiduciary duties and the SMSG suggests the Commission to analyse this phenomenon further, especially in view of the Green Deal.

Lastly, the concern of cyber-attacks is severe, in particular since more and more information is shared and stored in electronic mediums.

Q45: Which client investor data could be shared in the context of the development of an open finance framework for investments (e.g., product information; client's balance information; client's investment history/transaction data; client's appropriateness/suitability profile)?

Q46: What are the main barriers and operational challenges for the development of open finance (e.g., unwillingness of firms to share data for commercial reasons; legal barriers; technical/IT complexity; high costs for intermediaries; other)? Please explain.

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[31] *Proxy Advisors And Market Power: A Review of Institutional Investor Robovoting*, Prof. Paul Rose, The Ohio State University.

Q47: Do you see the need to foster data portability and the development of a portable digital identity? Please outline the main elements that a digital identity framework should be focusing on.

A digital investment ID could bring improvements for the onboarding processes for new clients, which currently take a long time and could be simplified by financial institutions having access to such information. The SMSG would like to encourage the adoption of the Digital ID into other processes to reduce much of the laborious and time-consuming account-opening procedures which many investors experience and which constitute a barrier to empowering investors. This data could also support the lengthy and costly Know-Your-Customer and Anti-Money-Laundering processes that accompany this process. Access to specific client data, for example, by sharing the answers to specific questions, if clients agree (there are already certain FinTech firms offering this service, e.g. Harmoney). Firms can then use this information to fit into their own questionnaires and only ask additional information which is not yet available or to verify information on which they have doubts.

Q48: Do you consider that regulatory intervention is necessary and useful to help the development of open finance? Please outline any specific amendments to MiFID II or any other relevant legislation.

In case regulatory intervention would be considered, it should be paid attention to the fact that the reference to the precedent of payment services may not fully reflect the stakes involved in the case of financial services. The latter involve far more granular information concerning both clients and products. They also generally imply the combination of a larger range of services involving a far greater diversity of players.

Moreover, in many instances, the provision of certain services is conditioned on the data subject expressing consent (which is a different legitimate basis for processing than what is necessary for the provision of a service or a contract); if the data subject disagrees with the processing of his or her data, in many instances the service will not be accessible, even if the data is not an essential or central element to the provision of the service. Therefore, digital finance regulation must ensure that a clear distinction is made between data processing that is essential to or part of the provision of the online financial service and what is needed to enhance outcomes or customer experience, which is based on the prior express consent of the data subject.

Q49: What do you consider as the key conditions that would allow open finance to develop in a way that delivers the best outcomes for both financial market participants and customers? Please explain.

To begin with, the general principles of regulating digitalisation and the use of AI in financial services should be observed, i.e. legal certainty, technology neutrality, and high standards of consumer and personal data protection.

Any reform in this area should be carefully assessed in order to avoid or mitigate possible unintended consequences, including the third country context.

This advice will be published on the Securities and Markets Stakeholder Group section of ESMA's website.

Adopted on 31 December 2021

[signed]	[signed]
Veerle Colaert Chair Securities and Markets Stakeholder Group	Henning Bergmann Rapporteur