European Securities and Markets Authority

Call for evidence

On the European Commission mandate on certain aspects relating to retail investor protection

1 October 2021 | ESMA35-43-2827

Responding to this paper

ESMA invites comments on all matters in this paper and in particular on the specific questions summarised in Annex 1. Comments are most helpful if they:

1. respond to the question stated;
2. indicate the specific question to which the comment relates;
3. contain a clear rationale; and
4. describe any alternatives ESMA should consider.

ESMA will consider all comments received by **2 January 2022.**

All contributions should be submitted online at www.esma.europa.eu under the heading 'Your input - Consultations'.

Publication of responses

All contributions received will be published following the close of the consultation, unless you request otherwise. Please clearly and prominently indicate in your submission any part you do not wish to be publicly disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESMA's rules on access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESMA's Board of Appeal and the European Ombudsman.

Data protection

Information on data protection can be found at www.esma.europa.eu under the heading 'Data protection'.

Who should read this paper?

This paper is of interest to competent authorities, investors and firms that are subject to Directive 2014/65/EU of the European Parliament and of the Council (MiFID II) and to the Regulation 1286/2014/EU of the European Parliament and of the Council (PRIIPs).

Due to its focus on investor protection issues, this paper is therefore addressed to investors and consumer organisations, to investment firms and credit institutions performing investment services and activities and to manufacturers of PRIIPs, and to any relevant trade association.

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1 Executive Summary

Reasons for publication

In the September 2020 new Capital Markets Union Action Plan, the European Commission announced its intention to publish a strategy for retail investments in Europe in the first half of 2022. As part of its evidence gathering, the Commission launched in May 2021 an extensive three-month public consultation on a wide array of aspects related to retail investor protection.

On 27 July 2021 the Commission sent to ESMA a request for advice[1] asking ESMA to assist the Commission in the development of its strategy for retail investments and to make appropriate adjustments to the legislative framework. ESMA was asked to deliver the report to the Commission services by 30 April 2022.

Contents

Section 2 sets out the various topics included in the ESMA Call for evidence. Annex I lists all the questions set out in the ESMA Call for evidence.

Next Steps

ESMA will consider the responses it receives to this Call for evidence and will finalise the draft technical advice for submission to the Commission.

ESMA will hold a public hearing in Q4 2021 and registration for the hearing will be available in the relevant section of the ESMA website in due course.

[1] https://www.esma.europa.eu/sites/default/files/library/call_for_advice_to_esma_regarding_certain_aspects_relating_to_retail_investor_protection.pdf

General information about respondent

Name of the company / organisation	Deutsche Börse Group
Activity	Regulated Market
Country/Region	Germany

2 Call for evidence

2.1 Overview

1. In the September 2020 new Capital Markets Union Action Plan, the European Commission (Commission) announced its intention to publish a strategy for retail investments in Europe in the first half of 2022 and, in May 2021, as part of its evidence gathering, the Commission launched an extensive three-month public consultation on a wide array of aspects related to retail investor protection.[2]

2. On 27 July 2021 the Commission sent to ESMA a request for advice asking ESMA to assist the Commission in the preparation of legislative proposals implementing aspects of the retail investment strategy[3]. More specifically, the Commission invited ESMA to provide advice on a number of focused areas:

   - Disclosures: identification of any significant overlaps, gaps, redundancies and inconsistencies across investor protection legislation that might have a detrimental effect on investors (i.e. which might confuse or hamper decision-making or comparability) in addition to those already identified and addressed by the recent PRIIPs level 2 work, how the different legal frameworks fit together and options as to how to remedy any identified shortcomings. ESMA was also invited to reflect on how the rules work from a retail investor perspective, in particular on whether they ensure that consumers can make informed choices, avoid information overload and overly complex information while ensuring investor protection.

   - Digital disclosures: an assessment of how regulatory disclosures and communications can work best for consumers in a digital, and in particular smartphone, age, and proposed options as to how existing rules might be adapted, such as allowing layered information.

   - Digital tools and channels: an assessment of both risks and opportunities with respect to retail investing stemming from both the increasing availability of digital tools and the increasing levels of direct investor participation, in particular via online trading platforms and robo-advisors. ESMA was invited to reflect on the appropriateness of the current regulatory requirements, with a focus on the efficiency of safeguards such as best execution requirements and risk warnings provided to clients (e.g., as in the GameStop case). ESMA was, in addition, invited to explore whether and how far value chains should be 'opened' up by the sharing of specific investor data amongst investment firms and third party providers, and how far new markets for services, such as advice via

[2] https://ec.europa.eu/eusurvey/runner/retail-investment-strategy-2021

[3] https://www.esma.europa.eu/sites/default/files/library/call_for_advice_to_esma_regarding_certain_aspects_relating_to_retail_investor_protection.pdf

platforms, might be expected to develop, bearing in mind, on the one hand, the need to protect investor rights, but also to bring down cost and allow for innovation in products and services.

3. During the development of its technical advice, ESMA intends to coordinate closely with EIOPA that received a call on similar aspects regarding protection of retail investors (investing in insurance-based investment products)[4]. ESMA will also take into account actions resulting from the call for advice sent by the Commission to the Joint Committee on a number of areas concerning the PRIIPs Regulation[5], as well as the request for technical advice sent by the Commission to the ESAs on Digital Finance, which covers topics including digital platforms[6]. Furthermore, considering the importance of the topics of the request for advice in the global financial framework, ESMA will consider in its upcoming advice the ongoing US SEC work on matters related to the use of digital engagement practices by broker-dealers and investment advisers.[7]

4. ESMA acknowledges that the importance and complexity of the topics set out in the Commission's request for advice require the involvement of stakeholders to ensure that they can adequately contribute to ESMA's work to respond to the Commission's request for advice, already at an early stage. Therefore, with a view of gathering views and qualitative/quantitative information stakeholders may have on the topics covered by the Commissions' request for advice, ESMA has decided to launch this call for evidence, the results of which will be used to shape the technical advice to the Commission.

5. Due to the tight deadline set by the Commission (April 2022) no further consultation will be possible; the engagement with stakeholders, and any limitation thereof, will be mentioned in the final report to the Commission, as also requested in the request for advice.

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.

Deutsche Börse Group appreciates the opportunity to provide feedback to this call for evidence on retail investor protection. We support the objectives of the European Commission's (EC) Capital Markets Union 2020 action plan, which places a clear focus on strengthening the role of the retail investor and making the European Union (EU) an even safer place for private individuals to save and invest for the long term. In this context, we also welcome the development of a dedicated EU strategy for retail investors.

Although retail investor participation increased in 2020, overall participation in the EU remains relatively low compared to other jurisdictions. To encourage EU citizens' participation in capital markets, comprehensive investor protection remains essential. In this context, we believe that the current framework may need to be revised to ensure that retail investors continue to be sufficiently empowered and protected (see our responses in this consultation paper).

Financial products and services remain complex for many retail investors. In order for individuals to manage their finances and invest appropriately, it is key that they are able to understand the risks and benefits of investments and the different options available to them. In this context, it is important to note that according to ESMA's 2021 report on the performances and costs of retail investment products in the EU, retail investors receive

[4] https://www.eiopa.europa.eu/content/call-advice-eiopa-regarding-certain-aspects-relating-retail-investor-protection
[5] https://www.esma.europa.eu/sites/default/files/library/call-for-advice-on-priips-cfa.pdf
[6] https://ec.europa.eu/info/sites/default/files/business_economy_euro/banking_and_finance/documents/210202-call-advice-esasdigital-finance_en.pdf
[7] https://www.sec.gov/rules/other/2021/34-92766.pdf

poorer terms compared to institutional investors and that transparency across EU Member States is only comparable to a limited extent. Moreover, “retail investors pay above 40% more than institutional investors across asset classes”. [1]

We believe that combining financial education with a sufficient level of transparency is key in this regard. While the primary responsibility for financial education lies with the Member States, a combined approach offers the EU the opportunity to support retail investors by ensuring adequate disclosures and appropriate transparency. Therefore, we believe that disclosures of risks and opportunities must be provided in a way that allows individuals to assess whether risks are being properly managed. In addition, transparency requirements must include the disclosure of comprehensive information about assets, the specific risks associated with them, as well as the cost of investing in those assets. Overall, this would allow retail investors to make better-informed decisions.

[1] ESMA Annual Statistic Report on performances and costs of EU retail investment products, 2021, https://www.esma.europa.eu/sites/default/files/library/esma_50-165-1710_asr_performance_and_costs_of_eu_retail_investment_products.pd

2.2 Disclosures

6. MiFID II[8] is the key legislation covering the distribution of financial instruments. Indeed, MiFID II covers the provision of different investment services (including investment advice and reception, transmission and execution of orders) in relation to any financial instruments to different categories of investors, including retail clients.

7. Rules on pre-contractual and on-going disclosure requirements are set out in MiFID II as well as in other sectoral investor protection legislation and in horizontal EU legislation. The PRIIPs legislation is particularly important in this respect because of its objective to provide short, pertinent, and clear information to retail investors and its direct impact on the distribution of retail investment and insurance-based investment products. The rules can differ from one legal instrument to another, which may render comparison of different products more difficult for investors.

8. With regard to MiFID II, Article 24(3) of MiFID II states “All information, including marketing communications, addressed by the investment firm to clients or potential clients shall be fair, clear and not misleading. Marketing communications shall be clearly identifiable as such”.

9. Article 24(4) of MiFID II further requires that appropriate information shall be provided in good time 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. In accordance with paragraph 5, this information shall be provided in a comprehensible form in such a manner that clients or potential clients are reasonably able to understand the nature and risks of the investment service and of the specific type of financial instrument that is being offered and, consequently, to take investment decisions on an informed basis. Member States may allow this information to be provided in a standardised format.

10. Further requirements on the topic of the provision of information to clients are specified in Chapter III of the MiFID II Delegated Regulation[9].

[8] In particular Article 24 of MiFID II; Articles 3 and Articles 44 to 52 of the MiFID II Delegated Regulation.
[9] Commission Regulation 565/2017.

11. On the topic of disclosures under MiFID II, ESMA has recently published its technical advice to the Commission on inducements and costs and charges disclosures under MiFID II[10] - In the advice, in relation to costs and charges disclosure, ESMA has found that the MiFID II disclosure regime generally works well and that it helps investors make informed investment decisions. However, ESMA advised the Commission, inter alia, to scale back some disclosure obligations vis-à-vis eligible counterparties and professional investors. As further specified in the following paragraphs, legislative actions in line with ESMA's advice have been taken in the context of the Capital Markets Recovery Package.

12. In its technical advice, ESMA has already expressed the view that MiFID II and PRIIPs disclosures regimes should be aligned and consistent. In this respect, ESMA did crossrefer to on-going work in the area of PRIIPs in order to ensure the mentioned alignment and consistency.

13. In the meantime, in February 2021, in the context of the review of the PRIIPs delegated Regulation 2017/653, the ESAs have published a final report on draft regulatory technical standards to amend the PRIIPs KID[11] suggesting a number of proposals aimed at improving certain sections of the KID.

14. Some of these proposals, described in section 4.7 of the abovementioned final report, have in particular sought to better align the cost disclosure requirements of the PRIIPs and MiFID frameworks.

15. Taking into account the options supported by the majority of the respondents to the Consultation paper that the ESAs had previously published on this issue[12], the ESAs have decided to keep the structure of two separate tables to be included in the cost section of the PRIIPs KID, with a first table ("costs over time") showing only aggregated figures in monetary and percentage terms, and the second one ("Composition of costs") showing a breakdown per type of costs. Table 2 would include a new column describing the nature of each cost (including where possible a calculation basis), as it was welcomed by the majority of respondents and is considered relevant I) for retail investors to better understand the cost structure and how it applies to their circumstances ii) for distributors, including in the MiFID context, to facilitate disclosures. The prescribed texts have been substantially adjusted to be more flexible, allowing for specific descriptions to reflect the differences between products. Table 2 would therefore include a column aiming at greater alignment with the cost disclosure framework for PRIIPs subject to MiFID II.

16. In this second table, the final report also suggests that, for PRIIPs falling in the scope of MiFID, reduction in yield (RIY) will not be used as the cost indicator. Instead, per each cost component, these products will show costs in EUR, after one year, as opposed to the approach currently followed in the PRIIPs Delegated Regulation (where RIY is also used).

17. Finally, the abovementioned final report also suggests amending the methodology to estimate transaction costs for the purpose of the cost section of the PRIIPs KID, in order to consider feedback received from certain stakeholders.

18. Other disclosure issues specific to PRIIPs will be discussed by the ESAs in the context of the abovementioned call for advice, received in parallel from the Commission, for the purpose of the review of the PRIIPs Regulation[13].

19. Through this Call for evidence, ESMA seeks input on significant overlaps, gaps, redundancies and inconsistencies between MiFID II and other investor protection legislation that might have a detrimental effect on retail investors. It should be noted that

[10] ESMA35-43-2126.
[11] https://www.esma.europa.eu/sites/default/files/library/jc_2020_66_final_report_on_draft_rts_to_amend_the_priips_kid.pdf
[12] https://www.esma.europa.eu/sites/default/files/library/jc-2019-63_consultation_paper_amendments_priips_kid.pdf
[13] https://www.esma.europa.eu/sites/default/files/library/call-for-advice-on-priips-cfa.pdf

this Call for evidence is focused on disclosures directly addressed to clients (typically "point of sale" ones, conceived to provide retail clients with useful and effective information on investment services and products) and does not aim at covering more general financial and non-financial issuer disclosure regimes.

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.

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.

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.

Plain vanilla corporate bonds are still de facto inaccessible for retail investors since it has not been fully clarified that these financial products are not considered as "packaged" retail investment products (PRIIPs). The exemption with regard to "bonds with no other embedded derivative than a make-whole clause" granted by Directive (EU) 2021/338 (the so-called MiFID II "quick fix") is too limited to ensure retail investors' access to plain vanilla corporate bonds.

The de facto inclusion of plain vanilla corporate bonds in the PRIIPs regulation results from (informal) comments by members of the European Commission in the past and by the consequently increasing number of bond issues availing of the wholesale bond regime with reduced prospectus requirements. The same applies to provisions for product governance defined in the "Guidelines on MiFID II product governance requirements" which also result in limited access by retail investors. Consequently, these bonds cannot be accessed by retail investors unless the issuer of the bond publishes a KID. However, this is not realistic as the issuers of these bonds are:

- Non-European firms which do not explicitly market their bonds to European retailers and therefore do not publish a KID in Europe, or
- European firms which do not want to take the risk associated with the publication of a KID. The industry standard is that issuers sell their bonds to their bank consortium and have no further interest in the reselling of these bonds by the banks in particular to retailers.

Thus, we call on the European Commission to remove existing inconsistencies in the assessment of corporate bonds and to clarify in the regulation that all plain vanilla corporate bonds are no longer considered to be PRIIPs. Accordingly, the legislator should extend the relief for simple investment products to all plain vanilla corporate bonds.

A removal of these barriers would help to reverse the significant decline in retail investing into corporate bonds since the entry into force of the PRIIPs Regulation in 2018 [1] while also reflecting the Commission's political objective of increasing retail participation in EU capital markets

[1] See BaFin Journal, April/May 2021, https://www.bafin.de/SharedDocs/Veroeffentlichungen/EN/Fachartikel/2021/fa_bj_2104_Unternehmensanleihen_Kleinanleger_en.html

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

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.

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.

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.

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)[14] and other legislation covering ESG matters?

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?

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.

2.3 Digital disclosures

20. In addition to the above-mentioned requirements on information provided to clients, Article 3(1) of the MiFID II Delegated Regulation generally requires that information is provided to clients on paper and that only provides for another durable medium under certain circumstances. In this regard, in its March 2020 technical advice to the Commission[15], ESMA had already recommended to amend the above mentioned article *"so that, when information must be provided in a durable medium, the provision of such information by means of electronic communications shall become the default option and should not require an active choice of the client, provided, however, that the client has provided the firm with a valid email address. Irrespective of this, the client should retain the right to receive information on paper. Firms should also be required to provide clear information to their clients on the consequences attached to the provision of a valid email address, and the fact that in such case no information will be provided in a paper form*".[16]

21. The EU co-legislators, taking into account the ESMA technical advice, amended MiFID II as part of the Capital Markets Recovery Package. More specifically on the aspect above, Articles 4, 24 and 25 of MIFID II were updated in order to facilitate communication between investment firms and their clients and thus facilitate the investment process itself. In light of the abovementioned changes investment information will, as a default option, be provided electronically. Retail clients will however be able to request the provision of that information on paper.

[14] Regulation (EU) 2019/2088.
[15] ESMA35-43-2126.
[16] See paragraph 193 of the above-mentioned technical advice to the Commission.

22. ESMA notes that on the topic of digital disclosures, pertinent work has been published by EU and non-EU bodies, all of which can be relevant for the ESMA technical advice. These include, for example:

- European Banking Authority (EBA) Opinion on disclosure to consumers of banking services through digital means under Directive 2002/65/EC concerning the distance marketing of consumer financial services.[17]
- Australian Securities and Investments Commission (ASIC) – Regulatory guide:

  Facilitating digital financial services disclosures.[18]
- Financial Industry Regulatory Authority (FINRA) – Regulatory notice on Disclosure Innovations in Advertising and Other Communications with the Public.[19]

23. ESMA notes that technology is transforming the way firms interact with their clients and potential clients and enables them to adopt various new approaches to communicate and provide regulatory disclosures. It is important however to ensure that these communications and disclosures remain "fair, clear and not misleading", and that customers do not receive misleading information in order to be able to make informed decisions.

24. Regulatory disclosures and communications are often lengthy, printed documents that many retail clients find difficult to understand and engage with. Communication is effective when clients pay attention to the information provided, they are able to interpret it and to incorporate the information into their decision-making process. The use of digital disclosures through interactive tools, infographics and even video content can represent a benefit for clients as these tools can be more engaging and allow to achieve the intended effect more efficiently as they are easier to understand and can provide information in a more timely and convenient manner. On the other hand, the use of digital means of communications should not result in information that is overly brief and simplified, compiled in a way that makes it unclear, ambiguous, or misleading. A (potential) client needs to be able to save relevant information (e.g. PDF) for access in the future.

25. Even the use of 'gamification' techniques can help convey complex information in a simple and rewarding way, it can demystify investing and can encourage people to save and invest their money. On the other hand, a wrong use of these techniques can push investors to take actions based on emotions rather than through rational decisions.

26. ESMA acknowledges that there may be various approaches and design concepts that firms can use in websites, email, social media, advertisements, mobile apps, and other electronic media and that through these channels firms can offer the possibility to clients to view information in narrative, tabular or even audio/video format. Especially when dealing with younger clients, the use of illustrations, cartoons, animations, pictograms, and other media has been used to tailor the user experience to specific target groups.

27. The analysis of approaches adopted in the financial sector shows that various approaches are currently used across jurisdictions and legal frameworks. Guidance provided in the area of digital disclosures includes:

- Easy navigability of information – Recommendation to firms to ensure that clients and potential clients are able to easily identify particularly relevant sections or move around in the disclosure in a way that is meaningful to them. In practice, this can be achieved through a menu feature in an app, chapters in a video or a contents sidebar or similar on a webpage, which the client can use to immediately go to sections of the disclosure

[17] EBA-Op-2019-12 23 - October 2019.
[18] Regulation 221 – 29 March 2016.
[19] Regulatory Notice 19-31 – 19 September 2019.

(for example to benefits and risks, the cost of the product, factors affecting returns, or how to complain). Firms should consider empirical research behavioural and cognitive biases investors are subject to in order to correctly design digital disclosures in the best interest of the consumer/client.

- Retrievability of information – Recommendation for disclosures to be easy to access. For example, if a generic website address, hyperlink or other direction device that does not take a client directly to the disclosure is given, firms are required to provide instructions on how to access the disclosure and the instructions should be clear and easy to understand.
- Obligation to provide the possibility to save information – Information provided through digital means should be easily downloadable, so that clients may store it on their own device and can be able to access it in the future.
- Presentation and format – Recommendation to use format and font size that is easily readable and adapts to any kind of device (and/or enable the option for clients to increase the default font size) and that colours used in digital disclosure do not diminish comprehensibility especially if the information is printed or photocopied in black and white. Recommendation for digital disclosure to be in an easily printable format to allow consumers, if they wish to, to easily make physical prints of relevant information.
- Versioning – Recommendation to firms to retain a copy of all versions of the digital disclosures provided to clients and use technology, where possible, to maintain records of when each version was available in order to allow clients and potential clients to be able to prove which version of the disclosure they relied on.
- Limiting of security risks for clients – Recommendation to mitigate the risk of phishing and other security risks. For example, when firms deliver disclosure by email with a hyperlink to the disclosure, the email should state that the client will not be asked to provide their personal financial details online (e.g., to access the disclosure).
- Use of different means – Recommendation to use communication means that are proportionate to the complexity of services provided, such as live chats, chat bots, Q&As, infographics, guides, interactive tools, or similar approaches, to ensure that clients are adequately assisted in their interaction and commercial relationship with the firm in the digital environment.
- Monitoring effectiveness – Recommendation to firms to monitor the design and prominence of relevant disclosures by analysing client behaviour, for example by gathering feedback from clients, monitoring their activities and outcome, and following up on complaints.

28. Some of the above elements could potentially be integrated in the MiFID II framework (either through changes to the Directive and its implementing measures or through dedicated ESMA guidance). ESMA believes these new forms of digital disclosure create opportunities but also risks and is looking for input from stakeholders on practical solutions implemented by firms to deliver regulatory disclosures and information to clients with an explanation of if and how these have proven to work best when communicating with clients.

29. ESMA also looks forward to suggestions on how the MiFID II regulatory framework could be adapted to take into account technological changes in the way firms deliver regulatory disclosures and information to clients.

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.

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.

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.

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.

2.4 Digital tools and channels

2.4.1 Robo-advisers

30. Recent developments of technologies and digitalisation allowed firms to increasingly provide services through the internet. A growing number of consumers therefore use automated tools when managing their finance, to invest their[20] money, to compare costs, features and benefits of different products.

[20] In September 2018 the JC published a Report on the results of the monitoring exercise on 'automation in financial advice' (Ref: JC 2018-29). The Report followed the 2015 Joint Committee Discussion Paper on automation in financial advice and 2016 Report on automation in financials advice published by the three ESAs.

31. The increasing availability of digital tools and the increasing levels of direct investor participation, in particular via online trading platforms and robo-advisors, creates both risks and opportunities with regard to retail investing.

32. The phenomenon of robo-advice[21] had been analysed by the Joint Committee (JC) of the three European Supervisory Authorities (ESAs) and the following opportunities had been identified:

- reduced costs for both customers and financial institutions;
- easy access to more products and services to a wider range of consumers and wider client base for financial institutions; and
- improved quality of the service provided (in terms of standardised consumer experience and possibility of rapidly processing large quantities of evolving data on a real-time and ongoing basis, if needed).

33. Within its analysis, the ESAs had also identified some risks for investors, such as:

- investors having limited access to information and/or limited ability to process that information (due to the limited possibility of human interaction);
- flaws in the functioning of the tool due to errors, hacking or manipulation of the algorithm.

34. In terms of emerging business models, the ESAs concluded in 2018 that these kinds of automated services were being offered, through partnerships, by established financial intermediaries, rather than by pure FinTech firms. Some new trends seem to emerge in the follow-up analysis (such as the use of Big Data, chatbots and extension to a broader range of products), but no substantial change to the overall market had occurred since the publication of the first ESA Report in 2016.

35. ESMA has subsequently integrated its Guidelines on certain aspects of the MiFID II suitability requirements [22] (from here onwards 'suitability guidelines') to take into consideration the phenomenon of robo-advice and more specifically in relation to:

- the information to be provided to clients on the investment advice and portfolio management services when these services are provided through an automated tool (this concerns both what information should be provided and how information should be illustrated to clients);
- the assessment of the suitability (with particular attention to the use of online questionnaire with limited or without human interaction);
- the organisational arrangements that firms should implement when providing roboadvice.

36. In its suitability guidelines, ESMA had clarified that, in order to guarantee a level-playing field, it did not intend to introduce additional requirements for robo-advisers, but rather highlight certain aspects that may be of particular importance in the case of the provision of services through fully or semi-automated tools. ESMA clarified that the MiFID II requirements and the ESMA guidelines apply to all firms offering the service of investment advice and portfolio management, irrespective of the format used for the provision of these services, i.e the means of interaction with clients.

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,

[21] For the purpose of this call for evidence, 'robo-advice' means the provision of investment advice or portfolio management services (in whole or in part) through an automated or semi-automated system used as a client-facing tool.
[22] ESMA35-43-869.

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.

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

Q19: Do you consider there are barriers for (potential) clients to start investing via semiautomated 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.

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.

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.

2.4.2 Online brokers (lessons from the GameStop case)

Provision of services through online platforms

37. Technological innovation is transforming financial services at an unprecedent speed, by facilitating new business models and services and the entrance of new market participants. The digitalisation of financial services brings a host of opportunities but also raises challenges, as it can introduce new or exacerbate existing risks.

38. In fact, the retail investment frenzy relating to certain stocks that was observed in January and February this year ('GameStop case') has raised concerns around the provision of execution only and brokerage services via online platforms and has highlighted specific risks connected to some emerging business models.

39. The Commission aims to address the challenges and risks attached to digital transformation by proposing, where relevant, adaptations to the existing legislative frameworks by mid-2022. In this context, in September 2020, the Commission published a digital finance package[23] with the aim to embrace digital finance in the EU. Following on the package, in February 2021, the Commission set out a request for technical advice[24] to the ESAs on three main issues, namely (i) the growing fragmentation of value chains in finance, (ii) digital platforms and (iii) groups combining financial and non-financial activities. ESMA is cooperating closely with EBA and EIOPA on these matters to assess the regulatory and supervisory challenges brought by these developments and the way in which they could be addressed and has launched in May 2021 a call for evidence seeking feedback from external stakeholders to inform its work on the matter.[25]

40. In the context of the 'GameStop case', the business models of "zero-commission brokers" and the practices of "payment for order flow" (PFOF) have been thrusted in the limelight. In July 2021, ESMA issued a statement[26] to warn firms and investors on about risks arising from payment for order flow. As stated in the statement "*the receipt of payment for order flow (PFOF) touches upon a number of key MiFID II obligations aimed at ensuring that they act in their clients' best interest when executing their orders. In light of the serious investor protection concerns raised by PFOF and the multiple requirements applying to it, it is in most cases unlikely that the receipt of PFOF by firms from third parties would be compatible with MiFID II and its delegated acts*". The statement outlines a number of investor protection concerns raised by PFOF connected to the requirements on conflict of interest, best execution, inducements, and cost transparency. Specific concerns regarding certain practices by "zero-commission brokers" are also highlighted in the statement.

41. In light of the above, ESMA requested NCAs to prioritise PFOF in their supervisory activities for 2021 or early 2022, especially in those Member States in which PFOF has been observed. In the context of this call for evidence, ESMA looks forward to any useful input from stakeholders on the need to adapt the current legislative framework to address these investor protection concerns.

42. The practice of PFOF isn't the only concern that arises with some online brokers. Other concerns include the broad availability of risky and complex products, margin trading with such products, the use of gamification elements to steer clients to trade these products or to trade too often and misleading marketing communications.

43. ESMA takes the opportunity of this call for evidence to gather stakeholders' view and to collect additional evidence in the area of online platforms, which a focus on PFOF and online brokers.

[23] https://ec.europa.eu/info/publications/200924-digital-finance-proposals_en
[24] https://ec.europa.eu/info/sites/default/files/business_economy_euro/banking_and_finance/documents/210202-call-adviceesas-digital-finance_en.pdf
[25] ESMA-50-164-4518
[26] ESMA35-43-2749

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.

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.

After an investigation by ESMA in 2017, insight was provided on certain shortcomings particularly in OTC markets, such as Certificate For Differences (CFD) markets. We fear that conflicts of interest for investment firms (IFs) designing and offering OTC-derivatives, such as CFDs, marketed and distributed to retail clients via their own online OTC-trading platform, are not resolved yet; leading to potential adverse effects for retail investors, who often cannot assess the perceived arbitrary price setting mechanism in CFD markets. In addition, the concept of implicit costs in these markets may often not be clear to retail investors, when zero costs are implied or advertised.

The IFs in focus, regardless of product offering, should clearly explain to retail investors what explicit and implicit costs consist of. Taking the typical OTC retail market offering as an example, the IF would deal on own account and act as market maker on their bilateral OTC-trading platform, often also as sole counterparty to retail client transactions. While not all providers are captured in ESMA's study, conflicts of interest can arise due to the IF's revenue-generating structures, as pointed out by BaFin and ESMA (see ESMA decision (EU) 2018/796 and BaFin General Administrative Act pursuant to Article 42 of Regulation (EU) No 600/2014 (MiFIR)).

It appears that the majority of such IFs designing and offering OTC products, for example CFDs, to retail clients through their own OTC-trading platform charge their retail clients an additional spread on their transaction, meaning they charge a spread mark-down on the bid price and a spread mark-up on the ask price. The spread is thereby applied to a reference price received from a third party, such as financial market data providers, who source their price feeds from the relevant trading venues. However, the IF acts as the sole market maker and thus controls the liquidity situation, including the size of the bid-ask spread, on the OTC-trading platform, and does not necessarily need to adhere to the reference price provided by third parties; hence the IF can quote wider bid-ask spreads in accordance with their economic interest and contrary to the best interest of their retail clients.

The conflict of interest stemming from adjusting prices for CFDs on their OTC-trading platform to cater for individual interests is further exacerbated, where the IF acts as sole counterparty to retail client's transactions without hedging against the market risk of these positions. In this case, the firm's profits are directly correlated with the retail client's losses, incentivising the IF to quote prices which are not in the retail client's best interest. The conflict of interest these firms face can also lead to the usage of investor protection malpractices designed to impair retail clients' ability to make informed investment decisions in order to increase their likelihood to incur losses. This has been addressed with the imposed restrictions on CFDs by ESMA and NCAs (see ESMA decision (EU) 2018/796 and BaFin General Administrative Act pursuant to Article 42 of Regulation (EU) No 600/2014 (MiFIR)). For example, misleading marketing campaigns were used by some IFs to hide the risk related to their financial instruments, while excessive leverages, discretionary and non-transparent price formation processes were employed to increase the likelihood of losses for such retail investors. Ultimately, those malpractices only served the economic interests of these firms and not the interest of retail clients.

In order to increase investor protection, it is key to address and highlight to retail investors the implicit costs they might face, be it in the sense of a bid-ask mark-up/down or because risk management aspects were not adequately addressed and reflected in the cost/price advertised. In order to allow retail investors to choose in an informed way products , increased literacy in financial market mechanisms and products need to go in tandem, in order to allow for a healthy investment culture where retail investors do not end up comparing apples and pears.

Overall, it is important to foster trading on trading venues also for retail investors, as proclaimed in the G20 objectives of shifting more trading onto multilateral trading venues. Trading venues do not face these types of conflicts of interest, and allow retail investors to participate in a brokered fashion and embedded in a mechanism of safeguards of a neutral trading platform, to reap the benefits of market transparency and market integrity also for retail investors.

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.

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.

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.

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.

Yes, Deutsche Börse Group (DBG) is familiar with the practices of PFOF. In fact, we have observed that PFOF has become more popular in the retail market over the last few years and resulted in directing order flow from retail brokers to selected platforms (paying to receive and execute the order flow). PFOF is generally not a source of revenues which can easily be identified, contrary to the US where the market makers have to disclose payments they make under the SEC Rule 606. In the EU, PFOF is sometimes paid in cash on a trade-by-trade basis, in cash on a “flat fee” basis or – and this is often the case – indirectly by paying “marketing fees”, “technical maintenance fees” or similar indirect agreements. Moreover, where PFOF is usually paid by the trading venue/market maker/systematic internaliser to the broker in the equity world, issuers and asset managers pay the broker directly for the order flow for securitised derivatives (and ETFs). Indeed, while PFOF schemes were predominantly used for trading in shares in the past, online brokers and neo-brokers increasingly apply PFOF schemes also to securitised derivatives, i.e. warrants and certificates and to ETF saving plans. As issuers of securitised derivatives seem to pay considerably higher remunerations for order flow compared to equity markets, there is reason to suspect that the conflict of interest is particularly pronounced in the area of securitised derivatives. It is therefore crucial to have a holistic view on PFOF rather than targeting specific venues or infrastructures.

Payment for order flow has numerous consequences. Some aspects are developed by Better Finance in their report on “Consumer Access to EU Equity Trade Data” in March 2021 (https://betterfinance.eu/wp-content/uploads/BETTER-FINANCE-Report-Consumer-Access-to-EU-Equity-Trade-Data-25032021.pdf):

1- Conflict of interest: The investment firm (IF) executing client orders on one side but also receiving PFOF from third parties on the other side is subject to a clear conflict of interest between the broker/IF and its clients; PFOF incentivises the broker to choose the third party offering (the highest) payment, rather than the best possible outcome for the clients. This conflict of interest is often not “manageable” (as per art. 23(1) MiFID II) - rather, it is the case that the brokers involved are predominantly guided by their own interests (namely to collect the highest PFOF). In this respect PFOF compromises the duty of the IF to choose the execution venue solely based on best execution principles (and explicitly NOT by obtaining the highest amount of PFOF).

2. Non-participation to the price formation: With PFOF schemes, the client orders do not contribute to the price formation process on an exchange but are executed against the quotes set by market makers (since client orders are declared as all-or-none orders by default or the trading model only allows executions of sitting passive limit orders against the market maker). With links between brokers and liquidity providers which are closely associated with a trading venue and formalised in the exchange rules, retail investors are systematically stripped off the possibility to contribute to the price formation process by interacting in a multilateral fashion with other orders in the order book of the respective trading venue to which the orders are submitted by the broker. Investors may only be able to accept the price offered by the market maker. Since such trading models are designed to maximize the profit of the respective market maker, the retail orders are in general not displayed to the market. This is particularly harmful, where a broker only connects to one trading venue – and even increases, where this trading venue only connects one market maker. In this case, there is no competition at all in the price determination process – the investor’s order is executed at the price determined by the one venue (through the one market maker).

3. Shift of the competition paradigm: PFOF shifts competition between execution venues to attract the order flow based on best execution to another kind of competition, this one at broker level and based on the amount of payments received from venues. With trading venues not paying to receive the order flow being excluded by brokers, unlevel playing field between venues questions whether the investor’s best interest can be fulfilled. Note that traditional retail brokers also denounce the unlevel playing field between them and brokers receiving PFOF.

4. Misallocation of resources: where traditional retail brokers would invoice on the basis on the costs they incur (including access to execution venues), many retail brokers receiving PFOF actually do not fully pass on to their clients the payments they receive. Those resources could, instead of being kept at broker level, be utilized by market makers to improve the prices they offer to retail investors.

Consequently, DBG supports the initiatives taken by ESMA and the European Commission to shed more light on the practice of PFOF but also to take action. We particularly agree with the recent legislative proposal from the European Commission to ban entirely PFOF, meaning that IFs would not be able to receive payments from third parties to direct their clients' order flow to the same third parties. We believe indeed that a ban of PFOF (note that with regard to the options above, we do not think that all forms of inducements should be banned) would be most effective in the long-term. It is crucial, that such a ban would include PFOF in a wide sense including cash-payments on a trade-by-trade basis, cash on a "flat fee" basis all sorts of comparable arrangements like "marketing fees", "technical maintenance fees" or similar indirect agreements.

In addition, and because it will take some years until the application of the policy changes in MiFIR, immediate action is still required to stop regulatory arbitrage and complementary actions could be considered in the short to medium term: based on the regulatory scrutiny, ESMA might want to consider using its strengthened tools of supervisory convergence. In this context, we welcome ESMA's public statement from July 2021 calling on the industry and national competent authorities to thoroughly assess compliance with MiFID II provisions. The sharing of supervisory practices across national competent authorities would help ensure a common understanding of PFOF practices and enhance investor protection. If needed, according to the current legislation, national competent authorities have the discretion to prohibit PFOF where they find that MiFID II rules on conflict of interests and inducements are not met.

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.

Yes, DBG can confirm that PFOF is practiced in the German retail market and has resulted in directing the order flow from retail brokers to certain platforms in the last few years – those paying for the order flow. It is however difficult to quantify the extent of the retail order flow concerned, or the total of payments made under PFOF schemes in Germany. Indeed, unlike in the US where strict disclosure requirements on an aggregated level exist (SEC rule 606), there is no similar requirement in the EU. The existing disclosures corresponding to art. 24(4) MiFIDI II made ex-ante on a trade-by-trade-basis to the relevant client are not helpful to gain a systematic overview about the payments made.
Currently, brokers must disclose payments they receive in their conflict-of-interest policies under MiFID II and those are usually communicated to the clients in the ex-ante cost disclosure (prior to a transaction). However, we believe that those payment benefits are not disclosed in a comprehensive, accurate and understandable manner for end investors. This is especially harmful for clients relying on best execution policies. But it also means that assessing the extent of PFOF is difficult for the German market. We however would provide some estimates based on the information that is available to us.

For 2019, we estimate that payments to brokers sum up to approx. 35m EUR for equity markets only in Germany. Figures are estimated based on the amount paid by one of the largest market makers in Germany (according to its publicly available statements 27m EUR).

We assume that this market maker holds approximately 75 percent share of all payments. In 2020, payments by this market maker almost tripled to 80m EUR (still according to his publicly available statements), leading to estimates of 107m EUR for equity markets in 2020 (assuming he still holds 75 percent share of all statements). Based on the number of transactions of 18m in 2019 this translates into 1.50 EUR paid per transaction for shares/ETFs. For 2020 the figures are similar: 80m EUR paid for order flow and approximately 54m transactions led to about 1.50 EUR per transaction. When looking at terms and conditions of some brokers the payments even increase to 3 EUR per transaction.

For securitised derivatives when looking at disclosure requirements of different brokers/market makers payments vary between a minimum of 3 EUR and a maximum of 15 EUR. By taking the middle (7.50 EUR) payments are five times higher compared to equities markets. Assuming that for one third of all transactions in Germany (40 million in total) payments are done, total payments made in 2019 may have already reached the amounts paid for equities in 2020 (>100mn EUR). With a significant increase in 2020 due to the surge in retail flows, we estimate that figures for securitised derivatives markets are significantly higher.

These figures show that the practice is widely spread in Germany. We can confirm that local as well as cross-border market participants are making use of this practice. In fact, for undirected order flow we can observe that retail brokers select a preferred venue (one who is paying for order flow) for the routing via the best execution policy and for the ETF saving plans which are getting more and more popular in Germany. While the reference market (i.e. Xetra) offers an execution for a retail ETF saving plan without transaction costs, the majority of saving plans gets executed on venues that offer PFOF. Since the only revenue source for these venues results from the trading revenues of the respective market maker, it is questionable if investors receive the best execution price. Moreover, the market maker has a full knowledge of the setup of a saving plan, i.e. ISIN, day, time and volume of order entry, so that he can easily calculate the profit out of the transaction in advance.
In the case of self-directed order flow, we can observe that retail brokers steer investors to select a preferred venue through the design of the order entry mask or limit the choice of execution venues for retail investors to those that offer payment for order flow (pay to play model) and only consider fee-paying market makers.
In Germany, as a result, four market maker/dealer venues gained significant market share besides systematic internalisers; The market share of dealer venues in Germany increased from 6% in 2019 to 20% in 2021. If new market makers want to join, they must offer higher payments than the existing ones in order to successfully enter the market. This process results in investors facing poorer pricing options and the more competitive pricing of non-paying market makers being ignored. This holds true for the large majority of brokers in Germany.

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

DBG believes that beyond the investor protection aspect, PFOF can have an impact on the market structure, due to the segmentation of the order flow induced by PFOF: while the wholesale, institutional flow is directed to execution venues including venues operating under pre-trade transparency waivers, systematic internalisers or regulated markets/MTFs with lit order books, retail flow quasi exclusively goes to ‘retail venues’ and systematic internalisers where the flow is directed to selected market maker(s). With the growth of the retail market in the EU (the volume of retail flow has doubled in some EU countries since 2019), potential detrimental effects of the segmentation of institutional versus retail flow might become prominent. We are referring here in particular to the price formation process whose efficiency depends on the optimal mix and interaction of informed and non- informed flow. The theory of market microstructure (see M. O'Hara, 1998, Market Microstructure Theory and L. Harris, 2002, Trading and Exchanges: Market Microstructure for Practitioners) shows that different types of market participants interact on the trading platform: mainly informed investors and non-informed investors (including liquidity traders but also noise traders disturbing temporarily the price determination process). In the absence of non-informed traders, informed traders cannot find a counterpart to trade, and implicit costs (bid-ask spreads) increase significantly to cover the information asymmetry risk. Hence, non-informed traders are essential to guarantee price efficiency and reducing their participation on multilateral, lit venues increase costs and is detrimental to the price formation process. The case is particularly acute in the US where the retail flow is exclusively executed against market makers, whilst representing on some days half of the traded volume for the relevant instrument. Mittal and Berkow (2021) (see H. Mittal and K. Berkow, 2021, The good, the bad and the ugly of payment for order flow, Best Ex Research) show that although retail investors do receive better prices being executed against market makers, they would actually have achieved better execution had their orders been executed on exchanges. This result comes from some specificities of the US market but also because by increasing the liquidity on exchanges, retail flow does contribute to increasing depth and to better price formation process. Notwithstanding the fact that the EU is different from the US, we believe that the US present a case study useful to analyse potential consequences of the segmentation of order flow in the EU, and the impact on price formation in the future.

As stated in our response to Q28, we believe that only a ban of PFOF will ensure that retail flow and institutional flow can interact on all venues as flows will be directed for all market participants to the execution venues guaranteeing best execution, supporting an optimal mix of flows and participating to the price formation process. Hence, we very much support the recent legislative proposal by the EU Commission.

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).

As explained in our response to Q24, IFs designing and offering OTC-derivatives, such as CFDs, for marketing and distribution to retail clients via their own OTC-trading platform typically charge retail clients additional implicit costs hidden in the bid-ask spread. They are therefore able to promote zero-commission for trade, execution and market data to retail clients. As these types of "zero-commission brokers" in the OTC-derivatives space hide the true costs of trading, they increase the difficulty to make informed investment decisions for retail clients

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.

DBG would like to point out that there is no clear definition of what constitutes a "zero-commission broker" and that ESMA has not defined in this consultation a definition thereof. Hence, for the purpose of answering this question we would refer to any broker that does a) not charge any transaction fee or b) only a very low amount such as for example 1 EUR per transaction or c) allows free trading for a low monthly fee (e.g. 5 EUR).

As an exchange, DBG is not familiar with the detailed business models of zero-commission brokers but has noticed, that that such providers have gained importance in Germany in the last few years. Typically, zero-commission brokers would offer only one venue to their clients for execution, or a limited number of venues or a wider range of venues with some available for free (those paying for the flow) and others available for a significant fee (those not paying for the flow).

Zero-commission brokers source their revenues from:

1. Order commissions

Whilst brokers claim 'trading at no cost or for 1 EUR per transaction', not all types and sizes of transactions are offered for free or 1 EUR. Most zero-commission brokers do charge fees for specific asset-classes, issuers, asset-managers or trading-venue related costs. For most of the (German) zero-commission brokers, only a fraction of the instruments offered can be purchased at zero or very low costs. One "zero-cost" broker for example charges 1 EUR "third party fee" for each transaction. Another one charges 0,99 EUR for each transaction in shares and most of the ETFs. Hence, besides transaction fees, zero-commission brokers do charge commissions which are a relevant source of revenue.

2. Payment for order flow

PFOF received for each order is another source of revenue. Payments are made by asset managers (for ETFs), issuers (for securitised derivatives) or trading venues (for equities). Unfortunately, there are no publications on the overall impact of PFOF on the brokers business-models (see also our response to question 29).

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.

In the specific case of IFs designing and offering OTC-derivatives, such as CFDs, to retail clients via their own unregulated OTC-trading platform, the zero-commission brokers are actually charging retail investors implicit costs via the bid-ask spread. The IFs are often able to set prices on their OTC-trading platform based on their own discretion, which gives rise to concerns over their ability to adhere to the best execution requirements and act in the best interest of their clients.

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?

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.

Role of social media

44. In addition to the above, the 'GameStop' case has also raised concerns around the use of social media as a source of information on which retail clients base their investment decisions. In this context, in February 2021 ESMA issued a statement[27] urging retail investors to be careful when taking investment decisions based exclusively on information from social media and other unregulated online platforms, if they cannot verify the reliability and quality of that information. As part of this call for evidence, ESMA welcomes any useful input on the impact on retail investors` behaviour of information shared on social media.

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?

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?

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.

[27] ESMA70-155-11809.

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.

An increasingly observed phenomenon is the emergence of fraudulent websites copying the brand of regulated markets to deceive retail investors. These fraudulent websites emerge regularly and typically use an amended version of the regulated market's name, often also parts or logos of the regulated market's website, to create a trustworthy image for their fraudulent intentions or to even pretend an affiliation to the regulated market. Using this image, these fraudulent websites often present themselves as innovative online brokers to retail investors. It is assumed that these websites are promoted via social media or placed in retail forums to gain retail investors' attention. Once retail investors have registered, it is assumed that either their personal data or financial data are used against their will to the benefit of the fraudsters.

These fraudulent websites may undermine the trust of non-professional retail investors in the regulated markets. They also require regulated markets to constantly monitor the internet for frauds and to take legal actions if possible. As the initiators of these frauds, who are often located outside of the EU, can be hardly legally pursued in third countries, the legal actions are limited to the extent that only a shutdown of fraudulent websites can be achieved.

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.

Risk warnings

45. An additional aspect on which ESMA is gathering input on concerns the effectiveness of the warnings provided to retail clients when accessing MiFID investment services other than investment advice or portfolio management (''non-advised services'').

46. According to Article 25(3) of MiFID II, when providing 'non-advised services', firms are required to ask the client or potential client to provide information regarding his knowledge and experience relevant to the specific type of product or service offered or demanded to enable the firm to assess whether the envisaged investment service or product is appropriate for the client. Where the firm considers that the client does not have the necessary knowledge and experience to understand the risks involved in relation to the specific investment service or product offered or demanded, it shall warn the client accordingly. A warning is also required where a client or potential client does not provide the necessary information on his knowledge and experience, or where insufficient information is provided. Articles 55 and 56 of the MiFID II Delegated Regulation further specify the information to be asked from clients and set out the record-keeping requirements.

47. Moreover, ESMA is currently developing guidelines on certain aspects of the MiFID II appropriateness and execution only requirements, which will cover some aspects related

to the effectiveness of warnings, which are expected to be finalised in Q3 2021. A consultation paper on the Guidelines has been launched by ESMA in January 2021[28].

48. As part of this call for evidence, ESMA welcomes any additional feedback on the effectiveness of warnings in ensuring sufficient protection for retail investors when accessing `non-advised` services.

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.

The suitability and appropriateness requirements as per Art. 25 (2) and (3) MiFID II require investment firms to assess, if their clients are sufficiently knowledgeable in the financial product they seek to acquire. Pursuant to Art. 55 Commission Delegated Regulation (EU) 2017/565, this assessment shall include the client's knowledge and experience in the type of product or transaction envisaged, including their complexity and the risks involved. Should the IF conclude that the client does not possess sufficient knowledge and/or experience it shall issue a warning towards the client.

DBG considers this as a reasonable approach to strike a balance between ensuring a sufficient level of investor protection while not prohibiting retail clients from the access to financial instruments.

[28] ESMA35-36-2159.

2.4.3 Open finance

49. Open finance, i.e. the sharing and use of customer-permissioned data held by financial institutions with third-party providers, can lead to increased competition with a positive effect on innovation and the development/availability of better financial products; it can also make it easier for investment advisers to gather information on a customer and offer a more targeted advice. It could help ensure access to basic financial services to a wider range of retail consumers.

50. Open finance could be seen as an opportunity to build on the concept of open banking, extending it to a wider range of financial services and products. Along with the revised Payment Services Directive (PSD2)[29], open banking introduced a secure environment that enables customers to consent to third parties to access their payment account information or to make payments on their behalf.

51. Open banking has brought innovation and enhanced competition in the banking and payment services areas. As an example, one of the areas that sees an application of open banking is consumer lending. In fact, the sector is becoming increasingly digital. The sharing of relevant data enabled by the open banking architecture facilitates the performance of more accurate risk assessments and a better evaluation of consumers' creditworthiness. This can bring benefits, including, inter alia, faster screening and approval procedures and reduced administration costs.

52. On the other hand, the misuse of client data – including the use of client data without consent – can lead to increased risk of fraud and incorrect advice to clients (where incomplete or outdated data is shared and used) and generally lead to poor consumer outcomes. It is therefore important that open finance is developed in order to offer consumers new services and products while limiting the risks of misuse of data, data breaches, privacy and security risks associated with the sharing of consumers' financial data.

53. In this context, the Commission communicated in the September 2020 its intention to propose legislation on a broader open finance framework through its digital finance strategy for the EU.[30] In fact, the Commission announced the objective that "*by 2024, the EU should have an open finance framework in place, in line with the EU Data Strategy, the upcoming Data Act, and Digital Services Act. This will be coordinated with the review of the Payment Services Directive*".

54. Therefore, a legislative proposal for a new open finance framework will be presented by the Commission by mid-2022, building on and in full alignment with broader data access initiatives.

55. Through this Call for evidence, ESMA seeks opinions and observations in relation to open finance on whether and how value chains should be 'opened' up to allow the sharing of specific investor data amongst investment firms and third-party providers.

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.

[29] Directive (EU) 2015/2366.

[30] COM(2020) 591 final

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.

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.

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.

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.

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.

3 Annexes

3.1 Annex I - Summary of questions

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.

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.

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.

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.

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

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.

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.

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.

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)[31] and other legislation covering ESG matters?

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?

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.

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.

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.

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.

[31] Regulation (EU) 2019/2088.

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.

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.

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.

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

Q19: Do you consider there are barriers for (potential) clients to start investing via semiautomated 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.

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.

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.

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.

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.

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.

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.

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.

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.

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

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).

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.

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?

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?

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?

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.

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.

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.

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.

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.

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