

## ADVICE TO ESMA

### Response to ESAs joint consultation on cross-selling (JC/CP/2014/05)

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#### Executive summary

The SMSG welcomes the joint consultation of the European Supervisory Authorities (ESAs) on cross-selling and concur with the view that cross-selling transactions may provide real benefits to retail investors, but also offer the risk that the interests of the client is not adequately considered. We believe that the guidelines are a necessary first step to ensure fair treatment of investors by providing the necessary transparency and focusing on the need to ensure proper training of staff and to avoid remuneration policies that may distort the incentive to provide suitability and appropriateness in this kind of investment transactions.

As the SMSG finds it important that cross-selling transactions are available also for retail investors, when offered in a transparent and proper way, we stress the need to achieve a proportionate regime that balances benefits with disadvantages and we believe that the proposed guidelines fulfil this aim.

At present, supervision is probably best placed with national competent authorities, but the SMSG believes that it may in time be necessary and efficient to engage the ESAs in direct supervision of cross-selling transactions in order to secure a truly pan-European approach.

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#### I. General remarks

1. The SMSG welcomes the joint consultation of the European Supervisory Authorities (ESAs) on cross-selling. We concur with the view on cross-selling transactions expressed in recital 81 of MiFID II that »[t]hey can provide benefits to retail clients but can also represent practices where the interest of the client is not adequately considered« and for this reason find it important that guidelines are issued to provide national competent authorities with rules that are both harmonised and cover the different areas of financial services and products covered by the three ESAs.
2. The proposed guidelines appear consistent with special regulation, governing investments, insurance and mortgage credit and prevent a loophole, which, in principle, might appear when financial products are bundled. The guidelines seem proportionate as they concern dimensions such as disclosure, transparency, suitability, training and remuneration of staff, which market participants already have to adhere to when it comes to individual products. At the same time the guidelines are consistent with their main purpose to strengthen protection and facilitate consumers' decision-making.

3. Before addressing the particular questions raised by the joint consultation, the SMSG would like to provide some general observations that we find important to highlight.
4. In financial regulation, especially where retail investors are concerned, it is often better to prevent than to cure. Consequently, guidelines should be made to prevent malpractices and not so much to establish standards of prudent behaviour that may later provide a basis for sanctioning or liability, as retail investors are often not in a capacity to seek adequate redress for any wrongs they have endured. Guidelines only serve this purpose of preventing malpractices if followed diligently by both market participants and authorities.
5. In respect of market participants it is of paramount importance that they internalise these guidelines and secure the proper training of staff, especially the front office staff that deals with retail investors, and that they avoid remuneration policies that may distort proper incentives of their staff. We are pleased to see that these considerations are addressed in the draft guidelines.
6. In respect of authorities, it remains important that they abide by the principle of a single rulebook and seek to exercise their authority and supervision in a harmonised way both to achieve a uniform level of investor protection throughout the Union and to provide a level playing field for market participants which will facilitate cross-border activity and thereby increase the competition and the number of services and products offered to European investors. At this point in the development of an integrated European financial market, supervision is probably best placed with national competent authorities, but just as this joint consultation is evidence of the need for the three ESAs to cooperate through their Joint Committee to seek a unified approach, so do we believe that it may in time be necessary and efficient to engage the ESAs in direct supervision of cross-selling transactions in order to secure a truly pan-European approach. Although cross-selling transactions by their very nature often cover different sectors, the need for market supervision would indicate a special role for ESMA in this area, which may rely on the Joint Committee to facilitate the necessary cooperation with the two other ESAs.
7. The problems caused by cross-selling have mostly been explored in the still new field of behavioural finance. Although not in a position to engage in a scholarly debate on the merits of behavioural finance, we find that many empirical findings correlate with common sense perceptions and every day experience of how retail investors make choices. Especially, we are convinced that when faced with cross-selling transactions including as they do a combination of services or products, retail investors may find it more difficult to make informed decisions than when confronted with the individual products or services in isolation. This is the very reason why we support the issuance of guidelines in this area.
8. As cross-selling transactions may offer the benefits described in the joint consultation, we find it important, however, that retail investors are not precluded from access to these transactions either in the form of outright bans on particular forms of transactions or by making the transactions so costly or burdensome for market participants that they make them exclusive for non-retail investors only. We believe that what is needed is sufficient, clear and intelligible information (transparency) and, as mentioned above, sufficient training of staff to assist retail investors in this information process and the avoidance of remuneration policies that may distort this process. Given sufficient transparency and a well-trained and properly motivated staff, we believe that retail investors can enjoy the benefits that cross-selling transactions may offer.

## II. The Questions raised by the joint consultation

**Question 1:** Do you agree with the general description of what constitutes the practice of cross-selling?

**Answer 1:** Yes. We thus agree with the observation that a distinction can be made between a cross-selling offer where the combined products or services are also offered individually by the market participant and, we presume, at the same point of sale, and a tied or conditional offering, but we do not believe that the difference goes beyond the fact that in the first instance information on the alternative to the cross-selling offer is available, i.e. information about the individual products or services, which it may not be in a tied or conditional offering. Thus, the distinction is more one pertaining to transparency than of form.

**Question 2:** Do you agree with the identified potential benefits of cross-selling practices?

**Answer 2:** Yes. As mentioned above, we find these benefits important and for that reason we find it important that cross-selling offers are available for retail investors, provided, of course, they are offered in the transparent and prudent way that all investment transactions should be conducted. Regarding financial benefits, it should be clear that overall costs for the consumer do not only include those at the time of purchase but also costs that might arise in the long run should to be considered, e.g. potential tariff increases for individual services included in the package or switching costs.

Apart from the benefits described in the Consultation Paper it can be added that cross-selling packages often make consumers aware of the existence and advantages of certain products which they were not familiar with before. This, if applied in a transparent way, may help raising the level of financial consciousness amongst consumers.

**Question 3:** Do you agree with the identified potential detriment associated with cross-selling practices?

**Answer 3:** Yes, which is why we find it important to issue guidelines in this area. We agree that in the absence of guidelines adopted by the ESAs there is a considerable risk that some market participants may act in this way. We also observe that while cross-selling transactions may result in long-term contractual relationships that may not suit the interest of retail investors as mentioned in para. 10, this may also arise in single product or service transactions and is thus a more general concern to be addressed irrespectively of the selling mode. We do agree that long-term relationships can be detrimental to consumers in some cases due to lower mobility, but benefits arising from long-term relationship in the retail financial services sector should not be overlooked. It allows a financial institution to provide products that are more tailored and more accurately priced to a well-known customer. The consumer can in turn acquire additional products and services with greater ease in the process, avoiding the need for extensive searches or burdensome administrative procedures.

It should also be noted that several financial market's directives already provide a necessary framework, so proper enforcement of the existing regulations should be helpful in dealing with potential consumer detriment and proper actions should be taken against any breach of those provisions.

**Question 4:** Please comment on each of the five examples above, clearly indicating the number of the example to which your comment(s) relate.

**Answer Ex. 1:** Yes, it would obviously be detrimental, unless the higher costs are somehow justified by benefits arising out of the cross-selling combination of products and services, which the market participant should be able to explain and required to disclose.

**Answer Ex. 2:** Yes, we see this as a problem of insufficient transparency.

**Answer Ex. 3:** As in Ex. 1, this would be detrimental unless somehow justified by costs connected to the unbundling of the cross-selling transaction and then only where the original transaction provided the retail investor with some benefit that depended on accepting the combined transaction.

**Answer Ex. 4:** Obviously, if indeed the charge is deemed disproportionate taking into account the various components of the combined package. However, it should be noted that this may be detrimental in a long-term commitment, but not so serious in a short-term one.

**Answer Ex. 5:** Yes, we would generally say that any transaction, cross-selling or not, that provides retail investors with products or services not suited to their needs would constitute impermissible mis-selling.

**Question 5:** Please comment on the proposed guidelines 1 and 5 (Full disclosure of information) as well as the corresponding examples, stating clearly in your response the guideline paragraph number to which your comment relates.

**Answer 5:** We consider that information disclosure alone is an important but only first step to ensure fair treatment of investors by providers and agree that sufficient transparency requires a break-down of the price between the package and its individual components in order for the retail investor to decide which to choose, as provided in Guideline 1 and 5. However, we do not believe that the market participant should be obliged to offer any or all of the individual components as a consequence of offering a package and we understand para. 15 of the summary of the guidelines as confirmation that no such obligation is intended. Where market participants do not offer one or more of the individual components, they should, if possible, disclose the price they are paying their contracting parties for a component that is provided by that contracting party.

**Question 6:** Please comment on the proposed guidelines 2, 3, 4 and 6 (Prominent and timely display of information) as well as the corresponding examples, stating clearly in your response the guideline paragraph number to which your comment relates.

**Answer 6:** We agree with the guidelines 2 – 4 and 6. In para. 16 and 20, the phrase »jargon-free« should be taken to mean devoid of financial argot, especially technical phrases taken from the theory of finance that may be difficult to understand for laymen. Special concern should be used in respect of such technical phrases where they may be misunderstood to mean no or reduced risk, which may be particularly relevant to phrases taken from portfolio theory and efficient market theory. However it should be remembered that some technical terms are required by existing legislation, so they cannot be simplified to the level of their full removal, as could be understood from para. 16. Where possible, examples should be made in final sums specifying a certain amount in euro or other currency (e.g. if you invest 100 EUR, the costs are X EUR) and risks should equally be explained with reference to final sums. In respect of para. 17, we agree but also refer to our comments re Q5.

**Question 7:** Please comment on the proposed guideline 7 (Optionality of purchase) as well as the corresponding examples, stating clearly in your response the guideline paragraph number to which your comment relates.

**Answer 7:** We agree and would prefer that web-based options remain open, so that the retail investor must actively make a choice. Where a market participant has chosen a default option, i.e. a pre-set option that the retail investor must change to avoid, the market participant must be able to justify this based on the objectives laid out in these guidelines and the generally applicable law governing retail investor advising in respect of suitability and appropriateness, cf. guideline 8.

**Question 8:** Please comment on the proposed guideline 8 (Assessment of demand and needs or suitability/appropriateness) as well as the corresponding examples, stating clearly in your response the guideline paragraph number to which your comment relates.

**Answer 8:** We agree and note that the requirements of suitability and appropriateness are no different in the context of a cross-selling offer than any other interaction between a market participant and a retail investor and should be subject to the same standards where advice is being offered. However distinction between advised and non-advised sales should be emphasised. Depending on product and distribution model, some firms limit their activity to the provision of information and specific explanation of the products, therefore advice should be viewed as a distinct service.

**Question 9:** Please comment on the proposed guidelines 9 and 10 (Training and remuneration) as well as the corresponding examples, stating clearly in your response the guideline paragraph number to which your comment relates.

**Answer 9:** As mentioned at the outset we agree with guideline 9 and note that the observable increase in complexity from offering a package rather than individual products or services entails an increase in the understanding necessary of the staff that are to face the retail investors, and market participants must ensure that their staff are trained sufficiently to possess the qualifications necessary to advise on and sell these packaged products. We also agree with guideline 10 and observe that the need to calibrate remuneration policies to avoid distorting the incentives of staff to provide proper advice and conduct is always important, also in the case of cross-selling. In respect of cross-selling where the market participant offers both bundle packages and individual products and services, remuneration policies should be neutral and not favour the sale of packages above individual sale. We do not believe that there is a case for banning remuneration policies that reward achieving certain sales targets by front office staff, nor where they include packaged offerings, but it is important to ensure that such policies do not lead staff to mis-selling, be it packages or individual products and services, and that proper training and supervision by the market participant of its staff and of the sales pressure on its staff are carried out at all times. In this respect, the SMSG believes that proper sales policies, including training, remuneration and sanctions should ideally be part of a dialogue with employee representatives where available.

**Question 10:** Please comment on the proposed guideline 11 (Post-sale cancellation) as well as the corresponding examples, stating clearly in your response the guideline paragraph number to which your comment relates.

**Answer 10:** We generally agree that a package should offer retail investors a better deal than buying the individual products and services on their own; this should be the *raison d'être* of all cross-selling. However, although not sufficiently familiar with all instances of cross-selling, we believe that a cross-selling package may entail benefits and disadvantages for the retail investor, where the latter may derive from the bundling or tying of the individual components, and that the retail investor, while being protected by the general standards of suitability and appropriateness when entering into the cross-selling transaction, should not be able to cherry-pick only the benefits of a package by first entering into the cross-selling transaction and then subsequently dismantling it. Emphasis should be on proportionality, as it is in para.

29, but not explicitly in para. 28. Thus, while we agree that rights to post-sale cancellation that apply for individual products or services should normally apply also for the combined package, we believe that a package may offer less beneficial rights in this respect where this is justifiably due to the nature of the combination of products and services and is not disproportionate so as to serve mainly as a deterrent to or a penalty for exercising these rights.

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

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