# APPENDIX 1

# General recommendations on a REFIT approach

In order to overcome the issues highlighted in the main paper, we recommend the following approach to carrying out a REFIT of MiFID II and MiFIR:

- **Sufficient testing and analysis**: According to the Commission's better regulation agenda, the review should be fact based and any proposals for amendments should be supported by consumer testing and consultations with stakeholder. Although proposed legislation is already subject to a cost-benefit analysis, our members' research in Appendix 3 has shown that besides the initial implementation costs, banks have significant running costs to consider due to MiFID II/ MiFIR obligations. Any future cost-benefit analysis should thus take into account not just initial cost impact but also accumulated costs. It should also provide evidence of the actual benefits of the legal provision as assessed against the negative impacts;

- **Transition periods between levels of legislation and issues of legal certainty**: Any changes to MiFID II which require transposition into national law should not start before all changes to MiFIR (and other relevant Level 2 and Level 3 legal acts) have been published so as to ensure legal certainty and no further double cost burdens. In this context, we also draw attention to the issues of interpretation when comparing Level 1 or Level 2 rules to ESMA's Level 3 questions and answers, or guidelines. Interpretations differ across Member States, and often lead to a sustantial increase in the requirements and costs for banks' IT systems and human resources compared to the project carried out under the banks' interpretation in good faith based on the Level 1 and Level 2 requirements. This is not only because of timing issues but also due to several key concepts not being clearly defined such as in the case of "execution on trading venues" and "algorithmic trading". Therefore, there should be a transition period stipulated for the implementation of Level 3 acts, and any guidelines provided to the market should be sufficient and appropriate in order to avoid several interpretations;

- **Harmonisation in securities markets legislation:** the review should include an analysis of the interaction between different rules within MiFID II as well as any overlapping EU legislation both in terms of requirements and timing of application. One prominent example is the inconsistent cost calculations and cost disclosures to clients required under the Undertakings for the Collective Investment in Transferable Securities (UCITS) Directive and PRIIPS Regulation, as well as, mis-alignment between the MiFIR derivatives trading obligation (DTO) and the recently revised scope of the clearing obligation (CO) under the EMIR REFIT;

- **Scope of firms:** Requirements with regard to ancillary services, for example corporate advice and custody, should be tailored to these services and not to the status of the firm. If a firm qualifies as a MiFID investment firm, it has to comply with the MiFID II/ MiFIR requirements such as client classification, cost disclosure, conflicts of interests, segregation of assets et al. If the firm is not a MiFID investment firm, these requirements should not be applicable as it creates an uneven playing field. The issue of scope also applies in the case of the impact of the unclear and inconsistent pattern of exemptions intended under MiFID II and MiFIR for those EACB members who are small and non-


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complex institutions (SNCBs) under the meaning of Article 4 (1) point 145, Capital Requirements Regulation (CRR) II. A range of typically small, simple cooperative banks and building societies have business models that are based only on deposit-taking and lending, with no provision of investment services to customers. However, they all need to undertake a limited level of activity in financial instruments (for own account) as part of their treasury function – managing any wholesale funding, liquidity, and balance sheet risks. This means that they will issue their own instruments – certificates of deposit, medium term notes, and covered bonds, buy and sell government bonds and other liquid assets, as well as transact derivatives (as end-users) to manage their intrinsic interest rate risks. Under MiFID I and MiFID II, derogations such as the 'own account exemption' have catered for such scenarios. However, MiFID II introduced some attached conditionalities and possibly unintended interactions with other parts of the text, making such exemptions no longer workable for SNCBs. Therefore, the proposed REFIT review should take into account the current exemptions regime in relation to SNCBs that do not undertake client investment business;

- **Scope of clients:** the review should distinguish between eligible counterparties/ professional clients and retail clients, with the aim of (i) removing requirements which are of little use for eligible counterparties and professional clients (such as in the case of interbank trading); and (ii) introducing opt-out possibilities (e.g. from the obligation to record telephone orders), even in the case of retail clients who are feeling patronised and/or overwhelmed under the current provisions;

- **Scope of financial instruments:** In order to ensure that reporting and information requirements are meaningful, the rules should be calibrated taking into account diversity of financial instruments covered by MiFID II. In particular, the review should take into account that instruments used for hedging purposes (such as interest rate derivatives to hedge a bank loan) need to be treated differently from financial instruments held for investment purposes. It should be critically assessed whether investor protection rules should be applicable or amended. For example, we would advocate for the loss reporting requirement to not be applicable for such instruments, whereas, the suitability rules should be applied differently and more in relation to positions which have to be hedged;

- **Technology neutrality:** Digitalisation should be a part of the review process with the ambition to make MiFID II as technology neutral as possible. In a recent report[1] the European Commission has identified that digitalisation has negatively impacted providers of retail financial services and their business models. This competitive disadvantage for co-operative banks is further emphasised due to the social element of our members' business model. The history of co-operative banks is long rooted in agricultural financing and up to this day many clients are located in rural areas which cannot be easily digitised. These types of clients depend on co-operative banks for their livelihood; and

- **Brexit:** The review should take into account the impact of Brexit on the market and ensure the competitiveness of EU players.

[1] See *'Final report on a Behavioural study on the digitilisation of the marketing and distance selling of retail financial services'*, April 2019, European Commission (prepared by LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex).


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# APPENDIX 2

## Technical recommendations: 9 priority areas

The EACB strongly believes that certain legal amendments that extend beyond the original mandate of the Commission's review exercise, are also crucial for the revision of MiFID II and MiFIR. We also consider that in a few cases, clarification by ESMA could also be relevant.

Therefore, we propose certain technical recommendations in the following legislative areas:

1) **Inducements and research unbundling**
2) **Disclosures of costs and charges**
3) **Timing and format of client disclosures**
4) **Market data and consolidated tape**
5) **Trade reporting**
6) **Trading obligation**
7) **Loss reporting**
8) **Recording of telephone conversations**
9) **Statement of suitability in case of investment advice**

We wish to clarify that these recommendations cover prioritized areas by our members and this does not necessarily mean that other areas or articles of MiFID II/ MiFIR, which we have not mentioned, should be regarded as our unconditional consent on the regulatory approach on such topics. We also acknowledge that certain recommendations could be subject to change in the case of any new developments published after the date of this paper, which may have a major impact on the understanding or application of the relevant regulation.

### (1) Inducements and research unbundling

The EACB has participated[1] in ESMA's call for evidence[2] under mandate of Article 90(1)(h) of MiFID II, which obliges the European Commission (with the assistance of ESMA) to review the impact of inducements disclosures requirements on the provision of **investment advice** or **any ancillary services** to the client (in accordance with Article 24(9) of MIFID II).

The EACB supports the fact that the inducement regime under MiFID II has been introduced as a means to prevent conflicts of interest, and the increased competition observed in research provision is also positive in theory. However, we have noted that research unbundling has decreased research available for investors. This is particularly true for research coverage of SMEs, which are significantly financed by co-operative banks (one third of market share in Europe), and thus exposing our members and their clients on a greater level to the negative repercussions of this regime.

[1] Source: EACB website.
[2] See '*Call for evidence on Impact of the inducements and costs and charges disclosure requirements under MiFID II*', 17 July 2019, ESMA35-43-1905.


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For example, this can be seen in a survey conducted by the Nordic Securities Association about the effects of research unbundling after MiFID II implementation. This survey, dated 13 June 2019, comprised of 43 respondents in the Nordics, including 34 sell-side and 19 buy-side:

- Main findings from the Nordic **sell-side** are that:
  - **More than 50% of sell-side respondents have cut down on research of small-cap equites**. At the same time, 30% have increased their coverage. **The net effect is clearly on the negative side**, particularly for Nordic small- and midcaps;
  - **85% of sell-side respondents report less liquidity in small and midcap equities**. None reported increased liquidity;
  - **High yield bond liquidity has deteriorated**, but not as much as mid- and small-cap equities; and
  - The quality of consensus earnings estimates has deteriorated significantly.

- Main findings from the Nordic **buy-side** are:
  - Buy-side largely pays for research out of own account;
  - The 'full subscription at fixed price'-contract is adopted by nearly all fund managers participating in the survey;
  - **The number of research providers used has declined sharply by about 30%**
    - **Sell-side coverage of small-caps down, mid-caps also negatively affected;**
    - No positive trend in buy-side research hiring, mostly unchanged;
    - Buy-side is cautious towards issuer-sponsored research, even when clearly marked; and
    - Clearly lower quality in consensus estimates.

As execution fees are being forced down, research coverage requires sufficient liquidity (i.e. demand for research) in order to be a profitable activity. Consequently, this has reduced the incentive to provide research coverage for less liquid instruments, and decreased liquidity for high yield bonds and small-/mid-cap equities as can be seen above. Research providers have also diverted their business towards large caps. This impacts the financing (both debt and equity financing) and efficiency of the economy, due to the increased information asymmetry in the market (highly favourable to large hedge fund managers and banks).

Besides the uneven playing field impacting SMEs, there is also a distinction made between research and corporate access[3] that has led to substantial administrative costs without contributing to investor protection. Currently, two invoices are sent out to clients: one for research costs and the other for corporate. This has increased the cost of invoicing to a significantly higher level than the fees charged, which is confusing investors who are now less reluctant to attend road-shows or accept bilateral meetings with corporates. This is another example which is not conducive to achieving the CMU objective of affiliating and incentivising access to capital markets.

[3] The broker's role in facilitating discussions between fund managers and the companies in which they invest.

It is clear that the inducement regime had positive intentions both for investors (consumer protection) and their service providers (positive increased competition), but the success of these goals is questionable. Therefore, the EACB has considered the following proposals to address these consequences:

- **Review which type of research should be under scope of the unbundling regime:** In practice, monetary inducements are disclosed within the costs and charges disclosures required under MiFID II/ MiFIR and customers have become used to the praxis of inducements being disclosed within such disclosures. Therefore, it might be complicated to propose the removal of the unbundling obligations although this could be the best solution to gain back liquidity to less liquid instruments such as SME equities or high-yield bonds. Another solution could thus be to look at different kinds of research and their unbundling rules since MiFID II (at Level 1 and 2) does not take into consideration different kinds of research indicating that such rules mainly relate to research on companies (primarily equities). It should be noted that there are many kinds of reports and types of research provided to clients, not just equity research. The research relating to fixed income, currencies or commodities (FICC) or macro-economic analyses are only mentioned at Level 3 in ESMA's Q&As[4], and it is difficult to find any potential issues in bundling, unbundling or inducements for this kind of material. Clients may receive macro-economic, currency or commodities research from many service providers, some of it for free and for a minor benefit. It would thus be useful to the industry and investors to at least clearly carve out some of the research types, for example FICC research or macro-economic, that for example is not relating to a specific company, from the research unbundling obligations.
- **Unbundling issues relating to corporate access:** Research and corporate access should not be distinguished as this confuses clients and leads to bureaucracy;
- **Clear guidance on scope of inducements rules on corporate access**: If the distinction remains in place, then guidance should be given particularly for the differences between exclusive/ non-exclusive roadshows and investor conferences on the one hand, and research on the other hand;
- **Free research subject to conditions**: The MiFID II review should result in an explicit legal basis under which research can be received for free under the condition that there are no inducement issues, i.e. a specific exemption for trading functions where there is no direct link to underlying clients. Indeed, explicit exemption from inducement rules should be granted on research used for proprietary trading or other non-client related activities, or otherwise a sufficient clarification can be given if an exemption cannot be granted. Article 13 of the Delegated Directive[5] describes the requirements with regard to inducements in relation to research. These requirements are related to investment services (to clients) which seems logical to us because these are investor protection rules. This would entail that these requirements are not applicable on investment activities like own

[4] See Section 7: Inducements (Research) of *'ESMA Questions and Answers on MiFID II and MiFIR investor protection and intermediaries topics'*, 3 October 2019, ESMA35-43-349.
[5] See Commission Delegated Directive (EU) 2017/593.


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account trading. Own account trading by investment firms takes place for example in the framework of treasury activities (hedging), market making and building stock to be prepared for further demand. This own account trading is not related to a client and therefore it makes sense to us that own account trading is not included in Article 13 of the Delegated Directive or that our understanding is clarified in this regard;

- **Free market information:** There is a need for precision of free market information which regulators have deemed to be a minor non-monetary benefit;
- **Equal treatment and interpretation** within the local market is required, including more scrutiny on buy-side adherence; and
- **Equivalence**: There is a need for a level playing field between US and EU as regards the provision of research.

As a result of the above-mentioned reasons and in accordance with the aim to strengthen the CMU, the EU should review the requirements for research unbundling and adjust them accordingly.

### (2)Disclosures of costs and charges

The same ESMA call for evidence also covers the costs and charges disclosures requirements under Article 24(4) of MiFID II, which have also had an impact on the provision of investment services and performance of investment activities of our members.

We propose the following legislative proposals:

- **Deregulation of disclosures to eligible counterparties and professional clients:** Professional clients and eligible counterparties are familiar with the way capital markets function. They have significantly more knowledge and experience than retail clients. This view is reflected in MiFID II insofar as no assessment of appropriateness has to be carried out for these types of clients. MiFID II rightly assumes that these clients have the necessary knowledge and experience (Articles 54(3) and 56(1) of the Delegated Regulation[6]). Both their need for information and their need for protection are significantly lower than those of retail investors. These client groups frequently include banks and institutional investors (which are usually classified as eligible counterparties, though sometimes as professional clients), which meet the investment firm on an equal footing. In many cases these market participants are not only familiar with the market conditions and prices of the various providers but specify the conditions of the transaction in question themselves.

  Ex-ante cost information is supposed to provide investors with transparency regarding pricing and enable them to compare different offers. These clients normally already have access to this information through other channels (especially market observation and parallel price enquiries). As a result, ex-ante cost information about an individual transaction does not usually deliver the intended benefit, but is instead regarded as an

[6] See Commission Delegated Regulation (EU) 2017/565.



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annoyance. The German Ministry of Finance also came to this conclusion in a recent position paper[7].

Professional clients and eligible counterparties generally place a large number of high-value orders compared to those placed by retail investors and attach great importance to swift order execution. Transactions with professional clients and eligible counterparties are usually concluded over the phone or by chat and immediate action is expected. Ex-ante cost information, by contrast, translates into time lags and price risk, which these client groups consider disadvantageous. Professional clients and eligible counterparties are price-sensitive and normally maintain business relations with several investment firms. It is common market practice throughout the EU for professional clients and eligible counterparties to make investment decisions quickly on the basis of parallel quotes from several brokers. They neither need nor want ex-ante cost information, especially as they have to bear the market risk for the time lag between preparation and provision of the information. The market price of the product usually changes during the period needed to provide specific ex-ante cost information before concluding the transaction. To mitigate the price risk for the bank, prices would need to be raised.

On top of that, it is often technically unfeasible to provide ex-ante cost information owing to the order channels used – e.g. via interfaces such as FIX. "Users" of the trading platform are not in direct communication with the enquiring party. It is outside the remit and responsibility of platform users to create technical ways of exchanging instantaneous ex-ante cost information between users.

Given the expertise of eligible counterparties and professional clients, it should be remembered with the principle of proportionality in mind that the provision of annual ex-post cost information about costs and charges generates a lot of additional bureaucracy. This goes not only for those preparing the information but also for the recipients, who have to review and manage documents they do not need. Experience shows that these client groups feel massively over-informed and harassed as a result of the obligation to provide annual ex-post cost information. Under Article 59 of the Delegated Regulation, all clients already receive a statement immediately after the execution of their order containing, in a durable medium, the essential information concerning the execution. Under Article 59(4)(m) of the Delegated Regulation, the client already has the option of requesting an itemised breakdown of the commissions and expenses charged – just as in the context of ex-post cost information. As a result, clients already have all relevant information at their disposal about the costs incurred. An annual summary of ex-post cost information is therefore merely a duplication of information already received and generates additional costs for all involved.

Therefore, we propose that in order to address the above issues:

[7] See '*Necessary amendments and revisions to investor protection provisions in MiFID and PRIIPs'*, German Ministry of Finance.

- **An exemption should be introduced so that ex-ante and ex-post cost disclosure requirements no longer apply to eligible counterparties and professional clients:** In our opinion, a mere option to waive these requirements would not be sufficient as both client and bank would be burdened with the administrative red tape associated with exercising the option. Given the level of professionalism of the investors in both of these client groups, this is not necessary – including from an investor protection angle. We believe it would, however, make good sense to give retail clients the option to 'switch off' cost disclosure requirements (see below);

- **An exemption from other information requirements which do not benefit these client groups but represent a bureaucratic burden**, particularly client information in accordance with Article 24(1), sentence 1 of MiFID II about the investment firm and its services, the financial instruments and proposed investment strategies and execution venues; and

- **Until the requirements amended under the review come into force, ESMA should make absolutely clear that the cost disclosure requirements for transactions with eligible counterparties and professional clients may be met through standardised information on costs** (e.g. by way of the cost grids already introduced), and in fact with regard to all financial instruments. Given the lower level of protection of eligible counterparties and professional clients, standardised information on costs is appropriate information within the meaning of Article 24(4) of MiFID II that enables these to take decisions on an informed basis as called for under Article 24(5) of MiFID II.

- **Possibility for retail clients to opt out of receiving ex-ante information on costs:** The current provisions of MiFID II do not allow any room for a differentiated approach to handling ex-ante information on costs where retail clients are involved. This fails to take account of reality, as the retail client category is highly heterogeneous. Numerous complaints from clients show that there are clients who regard ex-ante information on costs as a nuisance – for example, because they are well aware of the costs associated with an order. MiFID II should therefore allow clients to decide for themselves whether or not they want to receive ex-ante information on costs. That the above would be welcomed by many clients is backed up by various studies:
  - According to a German study by Ruhr University Bochum[8], there is a marked preference for an opt-out option across all categories of clients (62.7%) and only 42.7% of clients see any benefit in the ex-ante information on costs. In addition, 54.2% of clients regard the additional information as actually (very) bothersome. The study reveals that clients are being overwhelmed with the scale of mandatory

[8] See Paul, S., Schröder, N. and Schumacher, S. (2019), "*Impact study of MiFID/MiFIR and PRIIPs Regulation: effectiveness and efficiency of the new rules against the backdrop of investor and consumer protection – a qualitative-empirical analysis*", Ruhr University Bochum on behalf of the German Banking Industry Committee.

information (62% of respondents) indicating that they do not feel better informed with the additional disclosures (66%) and that the extensive mandatory information does not help them to better understand the content of the documents (77%). On the other hand all this extra information leads to higher regulatory costs which at the end will have to be paid by the investors; and

- A consumer survey[9] commissioned by the German Federal Financial Supervisory Authority (BaFin) also reveals a rather muted interest on the part of clients in the content of the information. In this survey, more than half of respondents (53%) who made an investment transaction after 3 January 2018 said they had not read the ex-ante information on costs. A further 5% of respondents said they did not know if they had looked at the information.

However, such an opt-out option should not of course lead to the obligation to provide ex-ante information on costs being undermined in any way. There are, after all, clients for whom such information is important when it comes to making an investment decision. The opt-out should thus be tied to objective and transparent conditions, for example, the provision of qualified information about the relevant costs prior to the client's decision for or against an opt-out, followed by the type and complexity of financial instruments being offered to the retail client.

We would like to add at this juncture that the EACB does not consider the creation of a fourth level of investors i.e. 'experienced' or 'semi-professional' clients[10]. EACB members do not distinguish between different levels of retail clients and doing so would also mean undergoing a huge change in their legal and IT systems, as well as paperwork. Besides this, it would be very difficult to provide the appropriate criteria for the distinction. The regulatory changes in this regard would constitute a review of the suitability assessment and product governance rules (target market) which could end up leading to a major overhaul of MiFID II/ MiFIR – contrary to our primary objective to focus only on targeted amendments in this review.

- **Synergies between the MiFID II regime and the PRIIPs KID and UCITS KIID:** The fact that product costs are calculated differently under MiFID II and the PRIIPs regime causes major practical problems. Among other things, there is a difference in the treatment of inducements. While product costs under the PRIIPs Regulation include inducements, inducements under MiFID II are part of service costs, so MiFID II product costs have to be disclosed without inducements. This means clients are given different information about the product costs of one and the same product (if it is both a PRIIP and a financial instrument within the meaning of MiFID II) even if both information sheets base their calculations on the same investment amount of €10,000. In an example provided by a large German bank, the same product was shown to have product costs of €246.28 or 1.38% p.a. based on an investment of €10,000 when calculated under the PRIIPs

[9] See publication on BaFin website, '*MiFID II in practice*' (7 June 2019).

[10] 'Experienced' or 'Semi-professional' clients could be described as retail investors who possess a higher level of knowledge and/or experience compared to absolute beginners in the field of capital markets.

Regulation and product costs of €111.27 or 0.56% p.a. based on the same investment amount but calculated in accordance with MiFID II. This discrepancy, which has to be explained to investors and which they find difficult to understand, results from a lack of consistency in the rules governing the calculation of costs. In future, care should be taken when developing legislation to ensure greater consistency between thematically related legislative projects. As regards the relationship between the PRIIPs Regulation and its delegated regulation, on the one hand, and MiFID II on the other, the way of achieving greater consistency would be to refrain from the presentation of costs in the KID if the product in question is a financial instrument within the meaning of MIFID II. Therefore, the customer would be solely presented with the MiFID II cost disclosures so as to avoid the above discrepancies/confusion to the client, whilst ensuring regulatory compliance.

We are also aware that the UCITS key investor information document (KIID), does not meet the requirements on costs and charges in Article 50 of the Delegated Regulation. Therefore clients are being given two documents in order to disclose additional information that is not shown in the actual UCITS KIID. Further to the solution proposed for PRIIPs – we suggest to also refrain from the presentation of costs in the KIIDs, if the product in question is a financial instrument within the meaning of MiFID II.

- **Deregulation of ex-ante information on costs regarding distance communication with retail clients (telephone-based business):**
  The existing requirements for handling ex-ante cost disclosures in telephone trading continue to pose problems in practice. It should be noted that in telephone trading clients expect their orders to be accepted and executed without delay. Because of postal delivery times, information on costs in durable media cannot be provided promptly. Clients then usually cannot or do not want to use the internet but the telephone instead (e.g. when travelling (particularly by car) or where there is a poor internet connection). At the same time, such clients are predominantly experienced in securities transactions which make a large number of (recurring) transactions. Similar problems arise if orders are received by letter, fax or a transmission medium where provision of ex-ante information on costs is not possible. A clear, practice-oriented arrangement is therefore called for since in such situations clients want to be able to opt out of receiving ex-ante information on costs. That said, banks should at least be allowed in distance marketing transactions to provide retail clients with ex-ante information on costs following a telephone conversation.

  ESMA, too, has acknowledged this problem and outlined a degree of flexibility in its Q&As on investor protection issues and intermediaries topics that helps to some extent at any rate. As yet, there is no legal provision corresponding to that, for example, with regard to KIDs under the PRIIPs Regulation or with regard to the suitability statement (Article 25(6) MiFID II) that allow for an exemption to provide cost information after the transaction in certain cases. We advocate for a similar legal provision to be added to MiFID II for ex-ante cost transparency, in order to address this regulatory gap. The existing gap in regulation continues to lead to practical problems and to annoyance on the part of clients. It should therefore be directly addressed in MiFID II. In the results of its consumer survey, BaFin


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also advocated retrospective provision of information on costs in line with the provisions on the suitability report.

For professional clients and eligible counterparties, the problems posed are even greater. Transactions with professional clients and eligible counterparties should therefore be generally exempted so that these categories of clients would not have to be provided with any ex-ante information on costs in telephone trading (see "Deregulation of disclosures to eligible counterparties and professional clients" above).

- **Deregulation of ex-ante information on costs in case of sales:**
  Pursuant to Article 24(5) of MiFID II, clients must reasonably be able to take investment decisions on an informed basis. Hence, this appears to cover only the purchase of financial products as clients only take investment decisions when they are purchasing financial products. In case of sales of investments, usually other aspects other than the costs are decision drivers (e.g. loss of liquidity, expected decreased value of the investment, etc.). This is why various provisions of the MiFID II Delegated Regulation fit purchases but not sales, particularly:
    - illustration of the cumulative effect of costs on return (Article 50(10)(1) of the Delegated Regulation); and
    - illustration of anticipated spikes or fluctuations in costs (Article 50(10)(b) of the Delegated Regulation.

  It should therefore be made clear in MiFID II that the rules on cost transparency apply only to purchases and not to sales.

- **Deregulation of obligations to provide comprehensive ex-ante and ex-post cost and charges information where service provider takes care of only trading and the clearing is done by another party:**
  In financial markets it is typical that active and bigger customers have one service provider that takes care of custody and clearing of financial instruments. These clients use many service providers for trading. They may ask a price from different service providers or use many different brokers for their trades. The broker or service provider trades the financial instrument and transfers the position through give-up or similar procedure to the clients' service provider who then clears the trade and/or has custody relationship with the client. There are different costs and fees between these parties relating to trading, clearing and custody.

  Article 24(4) of MiFID II requires that costs presented to clients should include "all costs and related charges" and "information relating to both investment and ancillary services" and "where the client so requests, an itemised breakdown shall be provided".

  The service provider who only takes care of the trade does not know what the client pays for clearing or custody. Therefore, it is impossible for the trader or broker to evaluate overall costs and charges of the financial transaction ex-ante or ex-post. In this context,


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we propose that this obligation to provide ex-ante or ex-post information would be limited to costs and charges that are charged by the service provider (as mentined above, the trader or broker and their trading fees) who is responsible to send the ex-ante or ex-post report to the client.

- **Standardised information on costs (cost grids):**
  We also believe it is appropriate that ex-ante information on costs should only have to be provided once to clients where a category of products with a virtually identical cost structure is involved. Clients would accordingly only receive ex-ante information on costs before placing an initial order in this product category. When placing subsequent orders relating to a product in the same category, clients would not receive ex-ante information on costs again, as they are already sufficiently familiar with the relevant information on costs for any new transaction. This applies mainly to products that do not contain any different product costs. Classic cases are, in particular, shares, simple bonds, or exchange traded derivatives (e.g. trade on EUREX) where there are usually neither product costs nor inducements. In our view, it is not clear from the present wording of MiFID II and the MiFID II Delegated Regulation that ex-ante disclosure of costs always have to relate to an individual transaction and to a specific individual financial instrument. As opinions on this issue have differed in the past we suggest including appropriate clarification in MiFID II.

We would like to emphasise that the EACB does generally support the Level 1 legal text of MiFID II/ MiFIR because it is the basis for disclosure requirements that provide end-clients with clear, correct and comparable information on all costs and charges relating to the provision of investment services and financial instruments. However, the above recommendations are a reflection of our experience that in some respects the current legal concept of the information requirements is overshooting the mark.

**(3)<u>Timing and format of client disclosures</u>**

- **Statements of client financial instruments or client funds in accordance with Article 63 of the Delegated Regulation:**
  Besides the information requirements with regard to costs and inducements that are dealt with in the consultation paper, there are other information and reporting requirements under MiFID II. Particularly costly for investment firms in practice is compliance with the requirement under Article 63(1) of the Delegated Regulation to send their clients at least on a quarterly basis a statement in a durable medium of the financial instruments or funds they hold for them.

  Given that clients are widely able to view their portfolio online (or contact their investment advisor where necessary), providing them with such statements is superfluous. Compliance with this new requirement introduced under MiFID II imposes a considerable cost burden on banks. This is mainly because the statement cannot be sent to many clients electronically, as they do not have an electronic mailbox. The statement has to be sent to all other clients by post, which is expensive (paper, postage, etc.). And besides cost burdens, the EACB also supports current global sustainable goals. Printing and sending these kind of materials to millions of clients around Europe is not rational from an environmental point of view.

The above quarterly reporting requirements, compliance with which entails enormous costs and printed paper materials every year, should thus be dropped in the course of the MiFID II review. Data on paperwork volumes under MiFID II can be found in Appendix 3.

- **No obligation to obtain the client's explicit consent to use of other durable media:** The formal requirement under Article 3(1) of the MiFID II Delegated Regulation to obtain the client's explicit consent to the provision of regulatory documents in a durable medium other than paper is no longer in keeping with the times and needs to be amended. All durable media should be put on an equal legal footing and allowed to be used by banks as a possible means of transmission to clients. The formal requirement under Article 3(1) of the MiFID II Delegated Regulation to obtain the client's explicit choice for the provision of regulatory documents in a durable medium other than paper should be dropped. Banks should be free to decide in which durable medium they transmit information to clients provided it may, in their view, be assumed that the information will reach them. It should thus, for example, be made clear that, where clients indicate their email address for communication purposes, sending the information by email as a PDF document or, where clients use online banking, providing a download as a PDF document are automatically sufficient. Such an adjustment of the Level II requirements would take account of two main objectives: digitalisation and sustainability. Sustainability aspects, in particular, should be taken into account in this context. Clients often criticise the flood of information, providing which uses up an enormous amount of resources (energy and, in many cases, even paper). This additional information on costs is perceived by many clients as "disinformation" and by no means delivers the intended benefit for clients in every case. The amount of information provided should therefore be reviewed and the requirement to provide the information in paper format reduced at any rate.

### (4) Market data and consolidated tape

The relevant rules on market data and the setting up of a consolidated tape (CT) were one of the main tools of MiFID II aimed at increasing market transparency. However, the EACB notes that due to the complexity of the regulation, issues of data availability, poor data quality, and the increases in the costs of market data, this objective has not been achieved. Therefore, our members strongly support the need for a CT and a comprehensive analysis of the transparency rules with respect to market data. Indeed, the EACB has also replied[11] to the ESMA consultation paper[12] in this regard.

[11] Source: EACB.

[12] See '*Consultation Paper on MiFID II/MiFIR review report on the development in prices for pre-and post-trade data and on the consolidated tape for equity instruments*', 12 July 2019, ESMA70-156-1065.

As a primary concern, our members have recorded rising costs of market data in the EU over the recent years, which are creating inefficiencies in the use of trading data by firms and investors. Indeed last June, Steven Maijoor (ESMA Chair) acknowledged that *"Following the application of MiFID II, we were made aware of substantial increases in the costs of market data, reaching at times up to 400% compared to prices charged prior to 3 January 2018".*

The rise in prices is being seen as compensating the revenue losses at trade execution services by exchanges. One of the causes for this is the fact that certain market structure features are not supporting the 'reasonable commercial basis' principle which was put in place with MiFID II. This principle refers to the provision of market data at fees that are based on a reasonable relationship to the cost of producing and disseminating that data.

Another contributing factor to the elevated price level is the ability of venues and data vendors to bundle their services into a single product offering. This means the client is 'forced' to pay for trading, messaging and/or data services in one package. In addition, within the data offering, clients often have no choice but to pay for all the streams of data, whilst they would typically only use a comparatively small set.

Furthermore, MiFID II brought with it the multiplication of International Securities Identification Number (ISIN) with around 2 million ISIN codes having been created in Q4 2017 alone. There is around 280,000 ISIN for IRS (Fixed to Floating). This massive number of ISIN makes reporting ineffective. For example, if you trade a standard 10Y EUR IRS Fixed vs Euribor 6M, the 03/04/2019, one specific ISIN will be provided, but you will get another ISIN if you trade it the following day. As the ISIN code is linked to the maturity this multiplies the number of ISINs, which is why there is a massive number of ISINs and the list keeps on growing on a daily/weekly basis.

Based on the above reasoning, we call for:

- **Market data to be based on a reasonable commercial basis**, and ideally, only the supply of raw data should be regulated in order to ensure competition on value-added data;
- **ISINs:** The characteristics of the transaction generating ISINs codes to be revised in the aim to avoid an exponential growth of those ISINs. The European Commission should launch a targeted consultation to address this issue;
- **Requirements of consolidated tape provider:** Ideally, ESMA could be the EU consolidated tape provider in the EU. However, if this is not possible then we would expect the EU consolidated tape provider to be non-profit and centrally organised by ESMA. If the CTP function in the EU is run by a third-party provider, the third party provider should not consider CTP data to be another source of income to that of a centralised data provider. For example, in the US markets you can find this kind of association, the CTA, where non-professional investors can have their data with the CTA[13] for a really low 1USD/month/network. The price is higher for broker-dealers but there is a price cap. The

[13] Source: CTA.


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EU should look at the way markets and prices are developed there and have the best and lowest fees practices possible for all market participants. According to this US association's website: *"Millions of professionals and nonprofessional investors have access to real-time prices via the consolidated tapes. Most non-professionals do not pay fees because the low cost allows for brokerage firms to include real-time prices as part of their service"*. The consolidated tape provider should aim for a hundred percent coverage in order for participants to gain full benefits from it; and

- **Implementation issues of FIRDS and FITRS**: Policymakers to do an in-depth analysis of implementation issues in both Financial Instruments Reference Database System (FIRDS) and Financial Instruments Transparency System (FITRS), in close dialogue with the market. In particular, we take the view that the concept of 'traded on a trading venue' (ToTV) is applied and whether there is a need to do further calibration for different asset classes. This is because the EACB is concerned that the current data quality is too low, and we are wary that the lack of reliability/accuracy of FIRDS creates a major impact on investment firms' 'ability to comply with MiFID II/MiFIR.

### (5)Trade reporting

The new reporting requirements in MiFID II regarding execution quality (RTS 27)[14] intend to enable investors as well as investment firms to compare and monitor execution venues and to evaluate if best execution requirements are met. However, the current reporting requirements have been drafted according to a one-size-fits-all approach which results in the publication of unhelpful data. For example, there is significantly more data available on liquid equities which are traded on a venue than for OTC derivatives. For non-standardised or bespoke products, the information, which is currently required under RTS 27, have only little or no comparative value for investors. For investment firms this fact is also problematic considering that other parts of MiFID II in fact require firms to take the RTS 27 report into account.

Therefore, in our view the European Commission should:

- **Carry out a comprehensive review of RTS 27** in close dialogue with stakeholders, considering the characteristics of different asset classes and how the instruments are traded. The necessary amendments to the RTS 27 should only apply to products where adequate and meaningful data is available, such as instruments traded on a trading venue (ToTV). In addition, the review should include considerations relating to further standardisation of the format of the report as well as the alignment of the RTS 27 requirements with the rules on cost & charges and transparency;
- **Clarify the meaning of 'execution' of a transaction:** Investment firms which 'execute transaction' in financial instruments have to **report transactions to** the competent authority. Even if the concept of 'executing transactions' is detailed in the Delegated Regulation, this still provides room for interpretation and confusion as the concept of 'execution' is not per se defined. In practice, this raises several questions, especially

[14] Draft RTS on the data to be published by execution venues on the quality of execution of transactions.

within the context of Brexit, as it is not properly defined and might be interpreted in several different ways – Does it mean booking, trading, selling? This question is even more complex for e-business especially when the trades are executed via an algorithm;

- **Review the pre-trade requirements for 'non-equity instruments':** the requirement to publish firm quotes is totally inappropriate for non-equity instruments and is rather artificial. Most of the time the quotes are published but it is almost impossible to trade on those quotes as they are generally providing for one client with specific trade characteristics; and
- **Exempt transactions with central banks including non-EU central banks from the transaction reporting:** Several central banks such as in Asia are not exempted from the transaction reporting. This raises several commercial issues which are to the benefit of non-EU investment firms.

### (6)Trading obligation

MiFID II/ MiFIR currently allows for package transactions or orders to be grouped together subject to certain conditions. The same rules require that investment firms trade package transactions with the same efficiency and timing as a single one, even though a package transaction is more complex.

For example, trading on venues for package transaction on cross assets creates some difficulties especially when one component is not ToTV as all the components of the package have to be traded in venues whereas there is no liquidity for them. In consequence, the operational treatment is not as easy and creates a complex situation with our clients which is difficult to manage.

In addition, the pre and post trade transparency regimes, as they apply to packages, have given rise to a complex array of requirements, namely:

- If executed as part of a package, the price of the swap component is likely to be off market. However, if the investment firm provides pre-trade transparency on a component it may be doing so without being able to properly identify that the price provided is not representative of the currently tradable price. This can be seen particularly in the case where the derivative component is subject to the trading obligation and the investment firm cannot execute the trading obligated component through a trading venue and flag that it was agreed as part of a package trade. The trading obligated component may be subject to pre-trade transparency by the trading venue, despite the fact that the package has already been agreed on. This pre-trade transparency may be additional to the pre-trade transparency applied to the package; and
- If a post trade deferral applies to the component of a package, RTS 2 suggests that the same deferral should apply to all components. However, in practice, it is not clear how this can be applied where the package is executed part on-venue and part OTC, as counterparts/trading venue would not know what the other participants are doing.

Therefore, the EACB recommends:

- **Clarification of the trading obligations:** The trading obligation to package transactions should only apply if (i) all legs are subject to trading obligations; and (ii) can be executed on the same venue;
- **Pre-trade transparency should not be required;**
- **Change to the post-trade transparency requirement:** Package transactions should be subject to post-trade transparency only when all the components of the package are traded on the same venue. And if the package is comprised of different components that are traded both off venue and on venue, the on venue components will be reported by the trading venues and the off venue components by the investment firms; and
- **More flexibility (in terms of efficiency and timing of the reporting) should be introduced for package transactions.**

### (7)<u>Loss Reporting</u>

Loss reporting on the basis of MiFID II (Article 62 of the Delegated Regulation), in particular for leveraged financial instruments or contingent liability transactions, is very confusing for investors. The character of these instruments entails large fluctuations. A 10% depreciation on one business day can be followed by an appreciation of 15% the next day. The loss reporting requirement (end of business day) is not suitable for informing investors and creates a lot of unrest and irritation.

In case these instruments are used for hedging purposes this is even more the case because fluctuations should be seen in relation to the underlying positions which are being hedged. For non-leveraged instruments the loss reporting is also often most detrimental since it may induce investors to make hasty decisions that are not relevant when investing in the medium and long term. Sometimes investors will be lead to disinvest at the worst moment.

Therefore, **the EACB calls for the exclusion of the loss reporting obligation** at least relating to leveraged products, warrants, derivatives and other similar products which exhibit frequent fluctuations. **Retail clients could be provided with a one-time clarification** about the possible price fluctuations of that product type. **Professional clients and eligible counterparties do not need this kind of information** as mentioned above in this document.

### (8)<u>Recording of telephone conversations</u>

The implementation of the recording requirement (Article 16 (7) of MiFID II) causes high costs for investment firms, raises data privacy concerns for clients, and has the potential to impair the confidentiality of communication between investment firms and clients. Some jurisdictions (Spain[15] and Italy) have opted for a conservative approach by providing solely by remote means

[15] In Spain, the physical interaction with clients is based on investment advice (and not execution services) mainly due to a willingness to focus network branches on higher-income value-added services by positioning banks in services which

(telephone, internet) the so-called "executive services" (e.g. reception and transmission of orders) or the execution-only services, leaving investment advice available to retail clients only at bank branches. Many clients would still like to consult easily with their investment advisor by phone, but this is not possible in many occasions. These clients need and want help to participate actively in capital markets. But certain technical issues mentioned in this paper including such obligation to record telephone conversations and make records of any discussions, ends up hindering financial advisors' ability to help the client to make good investment decisions in their best interest.

**The EACB is therefore in favour of deleting the provision, or at a minimum, clients should be allowed to waive the telephone recording requirement,** under the condition that they are provided with information regarding the risks of not being able to use a telephone recording as proof in cases of dispute with an investment firm.

**(9)Statement of suitability in case of investment advice**

The EACB supports the purpose of the suitability statement in showing the retail client the advice given and how the advice meets their preferences, objectives and other characteristics of the retail client. However, we do not understand the rationale behind issuance of the suitability statement for every investment advice as required on the basis of Article 25 paragraph 6 of MiFID II as the investment advice given has to be based on the suitability assessment in the first place.

Normally the investment advisor meets with the client and they confidentially discuss the client's portfolio. Let us consider that the client has a portfolio of equity investments, for example, 20 companies, bonds from 10 issuers, a few investment funds and derivatives to hedge the positions. The client would require the investment advisor to assess the whole portfolio and give investment advice on whether to hold, sell or replace each of the assets. This request is problematic after MiFID II because now the investment advisor would have to provide a statement of suitability relating to each investment advice. The first issue with this is that the interpretation of investment advice is broad and many discussions between the investment advisor and client could be potentially regarded as investment advice.

Therefore, **as a first step we would propose to remove from MiFID II the obligation to provide the client with the statement of suitability relating to each and every investment advice**. **If this is not possible, we would propose that all clients - including retail clients - should be able to opt-out from this requirement.** Ultimately, this article should be amended or clarified to ensure that this ineffective papering to clients is eradicated

are not so easy to replicate via internet-based platforms. There is also a risk of considering every physical interaction as investment advice, and thus banks try to avoid this legal risk by interacting only under investment advice. However, this strategy (which is sought by banks and also valued by clients who want to access high-value investment services on a face-to-face basis) is being hindered by the costs and burdens of MiFID II/ MiFIR.



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# APPENDIX 3

## Costs and resources impacts from implementation of MiFID II/ MiFIR

### Case 1 – Finland

Our Finnish member's regional banking group has 2.7 million private clients and 31% of them have invested into capital markets. The group has recorded that the costs of MiFID II are exceeding the costs of the Capital Requirements Regulation (CRR) as can be seen below:

- The project costs for MiFID II (which in addition to large IT work and retraining), included added value services created for clients relating to inducements. The total cost of the long project was around €59 million;
- Ongoing charges are on average €2 million (MiFID I and MiFID II) yearly e.g. for extra staff and other costs;
- Despite the increased use of web and mobile banking, there is still a large number of these clients who are not online and are sent a huge amount of paperwork from the regional banking group: total printing and mailing costs were €1.5 million in 2017 in total, whereas in 2018 the same amount was already spent by August 2018 alone (inclusive). Printing cost figures for 2019 are not available yet;
- In terms of the paperwork required in order to comply with MiFID II reporting requirements:
    - First ex-post reports: January to May 2019, 405,000 pages printed and sent in paper; and
    - End-of-the year reports and first quarterly report 2019: 8.8 million pages (of which 5.8 million pages were sent to customers' online accounts and 3 million pages were sent to clients in printed paper);
- 9000 of the banking group's 12,200 employees have phones that have to be recorded. These persons are involved with clients' banking, finance and/or insurance services and their phone calls have to be recorded. One active phone user's phone costs are round €100/month. There is no fixed sum that can be taken from this that would relate directly to telephone recording because the phone service is an overall service that includes the phone, phone calls and the recording. However, if one considers around €14/month/person for recording alone, this would amount to costs of approximately €1.5million per year relating to telephone recording. Although Finland has a long history of phone call recording since before MiFID II, the banking group in question has estimated that if it could use cheaper non-recording internet call lines then its savings could easily exceed this €1.5 million;
- 5400 of the 12,200 employees were retrained to use the new IT systems developed for MiFID II; and
- In a MiFID I environment, it took around 60 minutes to offer basic investment advice to one client starting to save in one investment fund. After 2018, the average duration of the same procedure has increased substantially to 90 minutes.



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**Case 2 – Austria**

A study by the Johannes Kepler University Linz "STUDIE BÜROKRATIEBELASTUNG DER BANKEN IN NIEDERÖSTERREICH 2017" (May 2018) was carried out in relation to administrative cost burdens of Austrian banks due to regulatory compliance. The study covered the administrative cost burden of three large upper Austrian banks which were selected based on their total balance sheet. To take into account the heterogeneity of the banking industry in Lower Austria, the three banks selected for the study came from regionally different business areas:

- Reference bank No. 1: total balance sheet of about €3 billion and 451 employees (FTEs)
- Reference bank No. 2: total balance sheet of about €1.6 billion and 204 employees (FTEs)
- Reference bank No. 3: total balance sheet of about €970 million and 112 employees (FTEs).

The data analysed shows that the implementation costs of MiFID II have been very high and for some banks even higher than the burden of other regulatory acts. Table 5.1 (page 49) shows that in some areas MiFID II produces more costs for Austrian banks than the Capital Requirements Regulation (CRR). The running costs including overhead and pro rata non-recurring costs (as can be seen in the table) which were caused by MiFID II exceed the corresponding costs caused by the CRR in two of the three reference banks (No. 2 and No. 3). For reference bank No. 3, the costs which were caused by MiFID II were more than twice as high as the costs caused by **C**RR.

**Case 3 – Spain**

Our Spanish member has collected the data on on-going and variable costs of investment advice under MiFID II from a regional co-operative bank in Spain. The bank has estimated an additional average personnel hourly cost of €40 after implementation of MiFID II, which translates into €43 as "year 1 variable cost" and €30 as "recurring variable costs". However, as these costs depend on "personnel intensity" and this is not linked to the total amount invested, these costs (as well as those affecting the client) affect in a disproportionate manner those clients with smaller investments, as well as the banks serving these customers.

The above additional variable costs do not even take into account variables such as printing fees, delivery by post of ex-post information, tax collection, tax reporting, and all information services permanently available to clients at branch level. The data study also does not cover fixed and overhead costs such as:

- Recurring personnel training: *According to MiFID II rules, and in order to be able to provide investment advice, an initial training of 150 hours and a yearly re-training of 30 hours is required*;
- Product development, marketing, compliance;
- Physical infrastructure (Branches, printers, document transporting and storing, IT systems etc): *this Spanish regional co-operative banking has recorded that in order to fulfil all documentation requirements under MiFID II, it needs to obtain 11 signatures from each client for all pre-contractal and contractual documentation, and it needs to print:*



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- *First year (pre-contractual and contractual): 48 sheets on average per client; and*
- *Yearly (post-contractual): 4 sheets on average per client*; and
- Operational, regulatory and legal risks.

Furthermore, the time consumed for the provision of investment advice is proving uneconomical particularly for smaller investors. The Spanish banking group recorded an average duration of 65 minutes to complete the subscription of an investment fund under investment advice (the pre-contractual and contractual), and an additional 45 minutes every year after that for post-contractual purposes (e.g. yearly optimal asset allocation, ex-post cost information etc.).

The above shows that the additional costs created by regulation such as MiFID II has made a high number of client relationships simply uneconomical, either because of income too low to justify the required investments (and involved risks) or just because there is a direct economic loss (in some cases even before taking into consideration fixed costs). Small investments generate the same costs (economical and 'frictional' such as time spent, burdensome documentation, etc.) while generating much less income for the service provider (and also less potential return for the investor). Cooperative banks such as the one in this Spanish study suffer more (due to its client base, proximity and easy access to customers), and in many cases are the only remaining 'face-to-face' financial services provider to clients in many local markets. The client is also impacted with cost burdens which impacts his/her behaviour. These are not necessarily direct economical costs to the client but rather additional transaction costs due to, for example, the time consuming, burdensome and confusing set of documents and procedures that are provided and need to be read and signed.

Therefore it is noted that in Spain the new costs - both economic and time wise - that MiFID II has brought to investment advice for retail clients are due to:

- the need to increase ex-ante and ex-post information on costs and charges;
- the need to record conversations (or alternatively, include them through written minutes in the investment proposal); and
- the requirement to comply with the "Quality enhancement criteria" which entails the periodic revaluation of suitability, a new proposal for asset allocation, third-party investment products, etc.

All this involves new documents, new information procedures (with traceability) and of course more time needed at branch level.

The above information is based on annualised data for Q1-Q3 2019.


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**Case 4 – Germany**

A recent German study by Ruhr University [1] indicates that the impact of MiFID II/ MiFIR, as well as, the packaged retail and insurance-based investment products (PRIIPs) Regulation has led to:

- Clients being overwhelmed with the scale of mandatory information (62% of respondents) indicating that they do not feel better informed with the additional disclosures (66%) and that the extensive mandatory information does not help them to better understand the content of the documents (77%). On the other hand all this extra information leads to higher regulatory costs which at the end will have to be paid by the investors;
- A decline in certain business lines such as: (i) 'telephone orders' due to the increased amount of time needed for such transaction method, which has also led to an increase in customer complaints received by German banks – the time taken to place an order/execute a transaction by telephone has increased by 50% in Germany, and (ii) retail investment advice which has declined, thus, leading to closures/reduction in bank branches; and
- Consequently, it has been observed that: (i) private banking/corporate clients have become more attractive; (ii) there has been a reduction in the area of equities; and (iii) advice-free business is becoming more important because small investors cannot afford the expensive investment advice according to MiFID II requirements. Many retail investors have switched to execution-only for cost reasons. However, some of these retail investors are not that familiar with capital markets and would more likely require investment advice from their local branch.

[1] See Paul, S., Schröder, N. and Schumacher, S. (2019), *"Impact study of MiFID/MiFIR and PRIIPs Regulation: effectiveness and efficiency of the new rules against the backdrop of investor and consumer protection – a qualitative-empirical analysis"*, Ruhr University Bochum on behalf of the German Banking Industry Committee.



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