Financial Services Consumer Panel
AN INDEPENDENT VOICE FOR CONSUMERS OF FINANCIAL SERVICES

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DG FISMA
European Commission
Brussels, Belgium

13 May 2015

Dear Sir, Madam,

Financial Services Consumer Panel response to the Capital Markets Union Green Paper

The Financial Services Consumer Panel welcomes this opportunity to comment on the Commission's high-level proposals for the Capital Markets Union as outlined in the Green Paper.

The UK's Financial Conduct Authority (FCA) is required to set up and maintain a panel to represent the consumer interest. The Panel represents the interests of all groups of financial services consumers and operates independently of the Financial Conduct Authority. The emphasis of its work is on activities that are regulated by the FCA, although it may also look at the impact on consumers of activities that are not regulated but are related to the FCA's general duties.

In this submission, the Panel's focus is on those elements of the CMU that are either aimed directly at retail investors, for example, measures to increase retail investor participation in UCITS funds or European Long-Term Investment Funds, or those that may have an impact on consumer protection, like the potential 29th regime for personal pension products. As the Panel's remit also includes small- and medium-sized businesses as consumers of financial services, we have also responded to the proposals on SME credit information.

The Panel accepts that many of the measures being contemplated could indeed unlock investment to boost Europe's economy. However, we are concerned that no evident attempt has been made at balancing the need to raise capital for businesses in the EU with the need for an adequate level of consumer protection for retail investors, where appropriate. In particular, it is important that any reforms proposed by the Commission as part of the CMU are based on and informed by thorough consumer research.

Although the Commission highlighted "an effective level of consumer and investor protection" as one of the principles that should underpin the CMU, we were disappointed that there is no mention of consumer protection in the Green Paper itself. It is a concern that the Green Paper states that "the onus in many cases will be on the market to deliver solutions", as the market has repeatedly failed to deliver solutions that are in the consumer's best interest.

The key to a successful participation of retail investors in the CMU, and a boost in cross-border retail investment, will be increasing consumer confidence and trust in investment vehicles and the wider asset management industry.

In the Panel's view, it is paramount that measures under consideration which could impact directly or indirectly on retail investors should be subject to a thorough impact assessment process to gauge any potential negative consequences for consumers. This is particularly the case for the review of the Prospectus Directive and actions to encourage retail investment, for example through of ELTIFs or UCITS funds. As noted, consumer research will be indispensable in ensuring the Commission reaches an informed decision on any further action.

A failure by the Commission to incorporate the consumer perspective into the CMU Action Plan would be inconsistent with article 12 of the Treaty on the Functioning of the European Union, and run counter to the significant improvements to protection for consumers as investors that have been achieved under recent reforms such as MiFID 2 and the PRIIPs Regulation.

In this context, the Panel also wants to underline again its disappointment at the Commission's decision to formally withdraw its proposal for a revised Investor Compensation Scheme Directive (ICSD). A concerted effort by the EU to encourage consumers to invest would have provided the ideal background for modernising the ICSD, including a higher level of minimum compensation and more effective signposting requirements to ensure consumers are aware of the level of protection they enjoy.

We hope that the upcoming CMU Action Plan will be more explicit about the ways in which the Commission will safeguard the interests of consumers when establishing the Capital Markets Union, including the use of consumer research.

Yours sincerely,

Sue Lewis
Chair
Financial Services Consumer Panel

Q2: What further steps around the availability and standardisation of SME credit information could support a deeper market in SME and start-up finance and a wider investor base?

On balance, the Panel believes the Commission's aims on improving access to credit for SMEs is laudable. There is no doubt that, since the start of the financial crisis, SMEs have struggled more than most to raise funding, and the Commission has rightly identified improving access to finance for SMEs a priority.

We acknowledge that the establishment of effective capital markets for SMEs is a considerable challenge. The Green Paper notes that overcoming information problems and lowering the costs of access to capital markets will be the key determinants of success. It also refers to the fragmentation of key market segments, without elaborating on the precise nature of this problem.

The Panel considers it essential that more information is made available about SMEs to improve access to both bank and non-bank sources of finance. However, while steps to improve credit scoring will help at a basic level, we remain concerned about the big gap between this basic mechanism and the sophistication (and associated costs) of issuing prospectus documents.

We are also concerned that the Green Paper has not referred to another key demand-side issue in relation to access to finance for SMEs: the availability of investor readiness programmes. Most micro and small businesses are ill-prepared to present their businesses to potential funders and investors.

For example, in the UK the end of "Business Link", a government-funded business advice and guidance service, coupled with the absence of any adequate replacement has had a negative impact on the ability of small businesses to position themselves for investment, whether in the form of debt or equity. This is another key demand-side issue that the Commission should consider addressing as part of the CMU initiative.

Overall, the development of a Capital Markets Union with any real value for the smaller end of the SME spectrum will require a great deal of further consideration. Especially for the smallest companies, making national funding markets more effective will be an essential first step.

Q3: What support can be given to ELTIFs to encourage their take up?

By default, an ELTIF will not offer investors the possibility of redemption of their units or shares before the pre-defined end of the life of the fund, although individual ELTIFs may decide to offer retail investors early redemption, subject to a number of conditions. Given these limited redemption opportunities, it is important that investors understand the illiquid nature of the investment. Any measures to boost uptake of ELTIFs should not be at the cost of highlighting the potential risks associated with them.

Because of the long-term nature of ELTIFs, their sale to retail investors must be strictly regulated. However, the Panel accepts that for pension schemes and insurance funds they could be an attractive investment opportunity.

As regards the further role the Commission and Member States could play in supporting the take up of ELTIFs, the Panel understands particular consideration will be given to changes in tax treatment that would make such funds more attractive.

While tax advantages could be a good way of supporting the take up of ELTIFs, the key elements to encourage retail investors to invest in these funds will be cost and transparency, so that fund trustees can compare ELTIFs to alternative investments and make an informed choice.

Charges and costs, just like for any other retail investment product, will have to be clear, particularly for trustees or other governance bodies who will have to determine whether the scheme provides value for money for scheme members.

The Panel values disclosure of investment product features, in particular the associated costs, risks and returns, as a powerful way of making sure consumers can make informed choices about where and how to invest. However, disclosure is only effective if those to whom the details are provided can understand and act on the information; overly complex disclosure to consumers is counterproductive in many cases.

The ability for investors to be able to compare retail investments in order to make an informed decision is the single most important aspect which will give EU citizens the confidence to invest. It will also be important to ensure there is equal protection for those who have been mis-sold products, and regulation that is robust and swift to take action when things go wrong. Consistency across Member States is crucial. It is clear that many investors are nervous about investing in other markets because of the concern that regulation and protection may not be as robust as in their home state.

The way costs and charges associated with asset management are currently disclosed to retail investors poses particular problems. Investment costs have a significant impact on the returns associated with investment products. Consequently, retail investors need to be adequately informed about the potential costs and returns associated with their chosen investment product to enable them to make an informed choice.

However, research published by the Panel in November 2014[1] underlined the persistent problems with a lack of transparency of cost structures and poor governance in the retail investment market. Similarly, the 2014 Better Finance report on performance of personal pension products concluded that "charges substantially reduce performances [and] are often complex [and] opaque"[2].

While the second Markets in Financial Instruments Directive (MiFID 2) is likely to make a positive impact by requiring disclosure of an aggregate figure that includes transaction costs and performance fees, the potential for regulatory arbitrage and exploitation of loopholes remains.

In particular, firms may exploit the "waterbed effect" to shelter costs through charges that are outside the MiFID 2 disclosure requirement, such as blending fees or fiduciary management. The Panel has therefore recommended the creation of a single annual investment charge, with all other costs borne by the fund manager itself. Moreover, as pension products remain outside the scope of the Directive, considerable room for further improvement of the regulatory framework remains.

The Panel is fully aware that disclosure alone would not immediately change the incentives for fund managers to control those costs that can be charged against the value of funds and are consequently hidden from the investor.

One solution might be a single investment management charge; all other intermediation costs, charges and expenses incurred by the investment manager, including transaction costs, would be borne directly by the firm itself. The Panel would encourage the

[1] http://www.fs-cp.org.uk/publications/pdf/investment_discussion_paper_investment_cost_and_charges.pdf
[2] http://www.betterfinance.eu/fileadmin/user_upload/documents/Research_Reports/en/Pensions_Report_2014_FINAL_-_EN_FOR_WEB.pdf

Commission to consider imposing such a charging structure in the upcoming review of the EU legislative framework.

Q9: Are there barriers to the development of appropriately regulated crowdfunding or peer to peer platforms including on a cross border basis? If so, how should they be addressed?

The Panel supports adequate levels of protection for investors in crowdfunding and similar activities, including where such investments are transacted across Member State borders. We believe that the requirements brought in by the UK's Financial Conduct Authority, such as checks on the creditworthiness of borrowers, will bring credibility and stability to this fast-growing industry. Consumers should also be made aware of the risks of lending money via crowdfunding platforms, and the high possibility of capital losses. The biggest barrier to cross-border crowdfunding activity does not relate to regulation but to due diligence.

Retail investors already struggle to perform due diligence on borrowers or companies seeking investment funds, meaning that most consumers have to rely on their platform to some extent. Where that platform is in another EU Member State, finding out about their due diligence track record is even more difficult. This creates additional layers of information asymmetry, with the added risks to consumers who may make investment that are far riskier than they realise.

However, the Panel does consider that a basic regulatory regime is required at EU-level to guarantee a minimum standard of investor protection.

Companies seeking equity-based crowdfunding should be obliged to issue a full prospectus if they are seeking to raise more than a certain amount (for example €1 million). In the UK, some companies are already trying to raise much larger sums than these with no investor protection.

An amendment to the Prospectus Directive requiring investors to receive a prospectus before they decide to invest their money through crowdfunding would be useful. This would also necessitate common EU rules around client money and reserves for platforms. We would encourage the European Commission to consult on this issue in more detail before deciding on its next steps.

Nonetheless, any new rules in this fast growing area need to be proportionate and not stifle growth. Peer to peer lending can be a valuable part of meeting unmet demand from both savers and borrowers and offers an alternative to mainstream borrowing.

Q13: Would the introduction of a standardised product, or removing the existing obstacles to cross-border access, strengthen the single market in pension provision?

The CMU is intended to address matters relating to the flow of capital but this should not be the starting point for developing a strategy on personal pensions. The provision of value for money, properly regulated and transparent savings vehicles for European citizens should not be a secondary consideration to the use of capital generated by these products.

The Panel recognises that the demand for a new product with uniform features across borders will be more likely to succeed where the existing market is not well developed. However, it should be recognised that cross-border movement of labour is still limited and demand for a product that can be transferred by a citizen when moving to a new Member State is unproven. If consumers continue to contribute to a PPP in a Member

State, what would be the decumulation consequences if they move to a different Member State?

The major inhibitors to a successful cross-border regime for personal pensions are rooted in Member State competences in areas of taxation, insurance contract law and regulatory rules. At least in the former two there are no proposals to challenge these competences. This reduces the likelihood of success of a simple cross border product.

In the UK, auto-enrolment with guaranteed employer contributions makes workplace access to pension savings vehicles the best tool for most people currently not saving for a pension. Some of these schemes will be group personal pensions while some will be trust-based schemes. Historically, the UK was subject to major mis-selling when individuals were persuaded to open personal pensions in preference to a workplace scheme and the regime for any EU personal pension (EUPP) must not permit a recurrence of this.

It might be that such an EUPP will be developed in competition with national personal pensions (NPP). It is important that confusion is not created, as this would prevent effective choice for the consumer, whether through an individual or workplace scheme.

The advice regime for the individual will be important and should not be less robust than the existing advice rules in a Member State. If there is a pension gap in Europe, anything which reduces trust in providers and products will not help to tackle this issue. A single market for personal pensions must not undermine pre-existing products, governance, regulation or value for money.

It is suggested that there could be a 2nd regime for the EUPP. In the absence of data on what precise form this would take, we assume that this will create a standardised product regulation regime focussing on costs and charges, investment governance, communications and disclosures, key information materials and decumulation procedures may or may not be included. This could create confusion for consumers when faced with non-standardised NPPs but with regulated sales processes and competing 2nd regime products.

If an EUPP is produced, then as a minimum it must not undermine pre-existing occupational or personal pension products, it must be marketed and advised so as not to reduce consumer protection, must have effective pre-contractual and post-contractual disclosure, and will need to have fair transfer and exit charges which are not punitive. Given these constraints and requirements, it is difficult to conceive of a potential EUPP as anything other than a defined contribution product with a life-styling strategy.

Q17: How can cross border retail participation in UCITS be increased?

and

Q19: What policy measures could increase retail investment? What else could be done to empower and protect EU citizens accessing capital markets?

The Green Paper notes that "savings held in bank accounts [could] in some cases be used more productively", and that declining interest rates could incentivise households to shift wealth from savings accounts into market securities. This would be a challenge, as investors rightly see UCITS in a different light to savings accounts. UCITS carry more risk of losing capital, are opaque in their charging structure and are suitable only for longer-term investing.

The economic benefits of channelling money from savings accounts into securities are also predicated on an underlying assumption that asset managers are more efficient at channelling capital to where it is needed than are banks and other deposit-takers. This assumption needs to be tested, as it may not hold true in practice.

Moreover, channelling household savings into financing the real economy will require structural changes domestically in many Member States. For example, in the UK, there is a cultural preference for investing in property, bolstered by successive Governments' support for this market.

The Panel has been concerned for some time that, in a low interest rate environment, consumers can be prey to scams or buy inappropriate products in their search for yield. High profile miss-selling cases lead to a lack of trust. Indeed, trust in the financial services industry is low across Europe: all financial services markets are consistently towards the bottom of the table in the Commission's Consumer Markets Scoreboard, with asset management trailing by a long way.

While the Green Paper acknowledges that restoring the trust of investors is a key responsibility and challenge for the financial sector, the Commission does not offer any concrete ideas on how to achieve this. There needs to be a meaningful discussion on improving trust in the sector. Better financial literacy will not, of itself, encourage uptake of UCITS. No amount of financial literacy will help consumers compare products and restore trust in the absence of significant efforts by the industry itself to move substantially towards providing transparency and better outcomes.

It is not within the remit of the Panel to suggest changes to encourage uptake of retail investment opportunities by individual consumers. However, we do want to emphasise that boosting retail investment should not occur at the expense of adequate consumer protection.

The asset management industry already suffers from a number of shortcomings which cause detriment to consumers. The complexities of retail fund structures, combined with weak fund governance and asymmetries of information and power between the retail investor and the investment manager, have resulted in an extremely unbalanced provider-customer relationship. Put simply, nobody knows what it costs the consumer to invest in a UCIT.

The Panel believes that the Commission should await the implementation and impact of the second Markets in Financial Instruments Directive (MiFID 2) before developing any major initiative to increase take-up of UCITS. Nonetheless, current gaps in the EU's consumer protection framework should be addressed as a matter of urgency, and in parallel to any measures to increase retail investment. The Panel's recommendations to fix some of these problems are outlined below.

Disclosure of costs and charges

The Panel values disclosure of investment product features, in particular the associated costs, risks and returns, as a powerful way of making sure consumers can make informed choices about where and how to invest. However, disclosure is only effective if those to whom the details are provided can understand and act on the information; overly complex disclosure to consumers is counterproductive in many cases.

The ability for investors to be able to compare retail investments in order to make an informed decision is the single most important aspect which will give EU citizens the confidence to invest. It will also be important to ensure there is equal protection for those who have been mis-sold products, and regulation that is robust and swift to take action when things go wrong. Consistency across Member States is crucial. It is clear that many investors are nervous about investing in other markets because of the concern that regulation and protection may not be as robust as in their home state.

The way costs and charges associated with asset management are currently disclosed to retail investors poses particular problems. Investment costs have a significant impact on the returns associated with investment products. Consequently, retail investors need to be adequately informed about the potential costs and returns associated with their chosen investment product to enable them to make an informed choice.

However, research published by the Panel in November 2014[3] underlined the persistent problems with a lack of transparency of cost structures and poor governance in the retail investment market. Similarly, the 2014 Better Finance report on performance of personal pension products concluded that "charges substantially reduce performances [and] are often complex [and] opaque"[4].

While the second Markets in Financial Instruments Directive (MiFID 2) is likely to make a positive impact by requiring disclosure of an aggregate figure that includes transaction costs and performance fees, the potential for regulatory arbitrage and exploitation of loopholes remains.

In particular, firms may exploit the "waterbed effect" to shelter costs through charges that are outside the MiFID 2 disclosure requirement, such as blending fees or fiduciary management. The Panel has therefore recommended the creation of a single annual investment charge, with all other costs borne by the fund manager itself. Moreover, as pension products remain outside the scope of the Directive, considerable room for further improvement of the regulatory framework remains.

The Panel is fully aware that disclosure alone would not immediately change the incentives for fund managers to control those costs that can be charged against the value of funds and are consequently hidden from the investor.

One solution might be a single investment management charge; all other intermediation costs, charges and expenses incurred by the investment manager, including transaction costs, would be borne directly by the firm itself. The Panel would encourage the Commission to consider imposing such a charging structure in the upcoming review of the EU legislative framework.

Scope of disclosure requirements

Disclosure requirements for retail investment products will only work if the relevant EU legislation, including UCITS, PRIIPs and MiFID 2, applies across all fund structures, including unit-linked pension funds, and adopts a cost disclosure and fund governance model that aligns the interests of firms and customers.

In this regard, the Panel is disappointed that pension products are not subject to the provisions of MiFID 2 or the PRIIPs Regulation. In the UK alone, over 12 million people will be auto-enrolled in private sector defined-contribution pension schemes by 2018, but they will not benefit from the enhanced disclosure requirements on costs, risks and returns that recent EU reforms were designed to create.

The Panel is also concerned about the inconsistencies between the pre-sale disclosure requirements under the UCITS Directive, the PRIIPs Regulation[5] and MiFID 2[6]. Under

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[3] http://www.fs-cp.org.uk/publications/pdf/investment_discussion_paper_investment_cost_and_charges.pdf

[4] http://www.betterfinance.eu/fileadmin/user_upload/documents/Research_Reports/en/Pensions_Report_2014_FINAL_-_EN_FOR_WEB.pdf

[5] Regulation (EU) 1286/2014 of 26 November 2014

article 24 of MiFID 2, regulated investment intermediaries will be required to disclose transaction costs for the investment products they sell. This information must be obtained from the manufacturer of the product, which in the case of UCITS funds is the management company.

However, as manufacturers rather than distributors of investment products, UCITS funds will not be subject to MiFID 2. Nor is there a legal obligation on collective funds to report their transaction costs as part of the 'Key Investor Information Document' which they must compile under the UCITS Directive.

While the new 'Key Information Document' under the PRIIPs Regulation will require manufacturers to report transaction costs, UCITS are exempt from this legislation until the end of 2019 (and possibly indefinitely thereafter)[7].

This has created a situation where investment intermediaries will be obliged provide information to their customers on transaction costs related to collective funds, while these funds are not required to provide this information to them. To address this inconsistency, ESMA has recommended that, where a UCITS management company has not already provided transaction costs up front, investment firms should liaise with management companies to obtain the relevant information.[8]

This situation is clearly not ideal, as UCITS funds could refuse to cooperate with investment intermediaries, jeopardising the implementation of MiFID 2 and reducing the effectiveness of the new cost disclosure regime. To remedy this situation, the Panel believes that UCITS should be brought within the scope of the PRIIPs Regulation no later than the expiry of the current exemption in 2019, as this would oblige them to report their transaction costs.

Governance and conflicts of interest

Improving the way disclosure requirements work in practice will not be sufficient to prevent the many conflicts of interests that occur in the investment industry. To further strengthen accountability and stewardship, the Panel believes that the previous proposals to impose a fiduciary duty on investment managers to act in the best interests of their customers could be revisited.

In November 2014, the Panel published a discussion paper on investment costs[9]. The research found persistent weak governance in the asset management industry. Governance is frequently contracted out to commercial organisations, which are unlikely to criticise the investment manager who appointed them. Governance can also be provided by an associated group company, which shares the same ultimate owner, creating similar conflicts of interest.

Well-governed funds are more likely to provide consumers with value for money by reviewing the quality of investment management and costs on a continuing basis. Poor governance can lead to investor detriment due to the use of inadequate or excessively risky investment strategies, or unnecessarily high costs.

As a result of these problems, consumer trust in the asset management industry has been eroded and has remained consistently low. All financial services markets are consistently towards the bottom of the table in the Commission's Consumer Markets Scoreboard[10], with asset management trailing by a long way. This may be a key driver

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[6] Directive 2014/65/EU of 15 May 2014
[7] Article 32 of Regulation (EU) 1286/2014.
[8] ESMA final technical advice on MiFID 2, p. 118.
[9] http://www.fs-cp.org.uk/publications/pdf/investment_discussion_paper_investment_cost_and_charges.pdf
[10] http://ec.europa.eu/consumers/consumer_evidence/consumer_scoreboards/10_edition/docs/consumer_marke

behind the relatively low rate of retail investor participation in the EU investment market: the Commission's own impact assessment for the UCITS V Directive[11] found that only 10% of EU households are directly invested in mutual funds.

Any policy initiatives to encourage sustained participation of retail investors in funds such as UCITS and ELTIFs are unlikely to succeed unless part of a package that also aims to restore trust among consumers by addressing these governance and disclosure issues. The Panel therefore believes that further work, including legislative change, is required to make the investment industry work in the best interests of its customers, and to build trust in the industry.

Key to restoring trust in the asset management industry will be to make sure that governance arrangement are, and are seen to be, fit for purpose. To make asset managers more accountable to their customers, and to tackle conflicts of interest, the Panel has recommended an overhaul of fund governance arrangements. At a minimum, the Panel considers that there should be a full and effective separation of the UCITS management company and the depositary, in line with UK practice.

However, we believe that more far-reaching changes could be considered. In particular, the Panel would like to see the depositary subject to more stringent transparency requirements and also acquire greater responsibilities, for example an obligation to make public statements on fund performance and value for money, and – crucially - the ability to replace investment managers, where necessary. This would be similar to the arrangements for Independent Governance Committees (IGCs), which have been recently introduced in the UK.

Independent Governance Committees
Independent Governance Committees (IGCs) were introduced in the UK to improve the governance of workplace pensions, after a 2013 review found that the existing governance arrangements were often "not sufficiently independent" and did "not take into account all the key elements of value for money".

IGCs are similar to the UCITS depositary in some ways, being responsible for representing the interests of investors in assessing the value for money of occupational pension schemes and challenging providers to make changes where necessary. However, the Independent Governance Committees have statutory powers that make them far stronger than UCITS depositaries.

They have the power to request information from the fund, even where this is commercially sensitive, and the fund must also provide legal and other specialist advice. Where the IGC flags a concern, the fund must comply with the recommendations made or explain why it will not do so, and the IGC can make its concerns public. Each IGC will have to publish an annual report on its work.

Automated advice
The Panel is aware that one of the options likely to be considered to make it easier for individual consumers to become retail investors is greater use of automated investment advice.

While such services have the potential to increase access to financial advice for consumers who may have struggled to obtain advice following the Retail Distribution Review (RDR), any such process should be regulated and effectively operated at the equivalent of Level 4 or above. It is also imperative that any consumers who obtain

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[11] http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52012SC0185&from=EN#page=11

automated advice online have recourse to the alternative dispute resolution entities such as the UK's Financial Ombudsman Service.

Q18: How can the ESAs further contribute to ensuring consumer and investor protection?

The Panel supported the creation of the European Supervisory Authorities (ESAs), especially each Authority's so-called 'article 9' obligations to ensure consumer protection. However, the Panel believes the effectiveness of the ESAs has suffered from a lack of representation of the consumer interests in the regulatory process.

Composition of Boards of Supervisors
The ESA Boards of Supervisors are composed of the EU Member States' national authorities, but many of these authorities have no specific consumer protection mandate. Research by the European consumer organisation BEUC found that the financial supervisory authorities of several EU countries have no statutory consumer protection objective.

As the ESA's Boards play a prominent role in deciding their respective Authority's work programme and new regulations, the Panel believes consumers' interests should be represented consistently and adequately. Because of the differing statutes underpinning the work of national supervisors, many of the EU's national consumer protection authorities are absent from ESA Board meetings and cannot vote on policy changes or regulatory measures that are clearly relevant to their brief.

The Panel believes that national consumer protection authorities should be invited to participate in ESA Board meetings where their national financial supervisory body has no consumer protection mandate. More generally, the Supervisory Authorities should demonstrate clearly how they are meeting their Article 9 consumer protection objectives.

Consumer representation
The Panel is also concerned at the lack of direct consumer representation during the preparation of regulatory measures by the ESAs. The Supervisory Authorities' stakeholder groups are generally dominated by industry representatives.
Research undertaken on behalf of the Panel found that financial services consumer groups often lacked the resources for effective representation.

In particular, these organisations are likely to have limited access to the technical and research resources needed to participate fully in discussions and to challenge the views put forward by the financial services industry. They may also not be aware of the existence of specific stakeholder groups or the role they play in the formulation of EU financial services policy.

The Panel believes that several solutions should be implemented to redress this imbalance and to improve the representation of consumers at EU-level:

- A statutory requirement for the ESAs to provide feedback to their stakeholder groups;
- A review of remuneration and expenses to encourage the right balance of expertise on the ESA stakeholder groups;
- Increased support and resources for the stakeholder groups to carry out their own research and build up data.

Consultation process
The ESAs consultation process also poses problems for consumer group engagement. As most pieces of EU legislation now require implementing measures and technical standards to be drafted by the ESAs and adopted by the Commission, the sheer volume and scope of European financial services legislation has made it difficult for consumer groups to respond effectively to Level 2 consultations.

Not all consultations have a consumer protection element, but even responding to all relevant calls for submissions is likely to be beyond the resources of most consumer groups. The Panel would urge the ESAs to include specific sections in their consultations targeted at consumer representatives to make it as easy as possible to reply to those aspects of draft regulatory measures that have the greatest relevance for consumers.

Q20: Are there national best practices in the development of simple and transparent investment products for consumers which can be shared?

Much work has already been undertaken in the UK on developing simple financial products. In 2013, the British Government launched a 'Simple Products' initiative[12], a voluntary certification scheme commissioned by the Treasury following the 2012 Sergeant Review[13] which concluded that consumers were finding it hard to compare deals when buying a financial product because of a lack of transparency and other complexities.

All simple financial products which want to achieve certification under the scheme must comply with an agreed set of high-level principles, which cover product features, language, terms and conditions, pricing transparency, purchasing process, and regular information and product updates. To date, no investment product has received certification under the 'Simple Products' initiative.

The Sergeant Review was preceded by an earlier UK initiative, the Sandler Review[14], in 2002. This concluded that one reason that many consumers were not well served by the financial services industry was the complexity and opacity of many products. The Sandler Review subsequently called for a range of "Stakeholder" products which were simple, low-cost and risk-controlled, including a medium-term investment product related to collective investment schemes.[15]

We urge the Commission to draw on the outcome of these UK reviews and the resulting initiatives when formulating a pan-European approach to simple investment products. In principle, the Panel supports the extension of the UK's simple products initiative to cover retail investment products, and we would welcome a coordinated European approach to investigate the characteristics and limitations of simple products across all financial services.

However, it is clear from the UK experience that it is difficult to persuade firms to develop simpler products, even though the success of any simple product initiative relies entirely on the willingness of the industry to participate in the process. The Panel has concerns that parts of the asset management industry are keen to maintain complex and opaque products, as these are often more profitable.

[12] https://www.gov.uk/government/news/simple-financial-products-a-step-closer
[13] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/191721/sergeant_review_simple_products_final_report.pdf
[14] Ron Sandler, 'Medium and Long-Term Retail Savings in the UK', 2001.
[15] http://webarchive.nationalarchives.gov.uk/20130129110402/http://www.hm-treasury.gov.uk/d/Sandler_Consultation(240Kb).pdf

Moreover, given the very different nature of the markets for investment products across the EU, legislative product harmonisation (such as that resulting from the new Payment Accounts Directive) should be considered as a final option only.

However, regulatory intervention could be used to improve at least one aspect of retail investment products: cost transparency. It is clear that, before simple investment products can become a reality, a transparent and simple charging structure for the funds these products invest in must first be developed.

A product cannot be simple if a consumer cannot know how much they are paying for it. We would urge the Commission to consider the possibility of a single charge against the investment fund which covers all asset management costs. They could be relatively simple funds, such as trackers and money market funds, which have minimal portfolio turnover or transaction costs. All other costs must be taken from the business itself - not the fund. This would be simple and easy for consumers to understand and straightforward investment wrappers could easily be developed for such funds.

Q25: Do you think that the powers of the ESAs to ensure consistent supervision are sufficient? What additional measures relating to EU level supervision would materially contribute to developing a capital markets union?

In the Panel's view, the powers of the ESAs to ensure consistent supervision as laid down in their founding Regulations are sufficient. However, it does not appear that the Authorities are using their powers to the fullest extent possible. For example, they have never used their product intervention powers.

It would be prudent for the Commission to establish whether the Authorities are operating as effectively as they could within the current legal framework before proposing any changes to the overall supervisory structure.

We are also concerned that the ESA's work on consumer protection is being jeopardised by the reductions to their respective budgets in 2015, for ESMA in particular. Despite its increased responsibilities under MiFID 2 and the PRIIPs Regulation, its resources have been cut by significantly compared to the previous year. Internal resources at the ESA appear to be overwhelmingly devoted to prudential supervision; indeed, EIOPA has explicitly stated that the cuts to its budget lead directly to the "de-prioritisation" of certain work streams, including consumer protection.

It is difficult to see how the ESAs could effectively meet their consumer protection objectives under such circumstances. The Panel is especially concerned that ESMA will not be equipped to provide the necessary supervision if future measures to encourage uptake of UCITS and ELTIFs by retail investors are implemented.

A fully-fledged Capital Markets Union in the EU requires supervisory authorities that have the resources to carry out the full range of its duties and responsibilities effectively. Providing the Authorities with sufficient resourcing would also enable them to provide greater support to their stakeholder groups, thus encouraging participation from under-resourced consumer groups.

Regulatory architecture

The current supervisory structure separates regulation by sector and obliges each regulator to monitor both the prudential and conduct aspects of the sectors it regulates. In practice, we are concerned that this may lead to neglect of conduct supervision because prudential considerations either take precedence or are seen as sufficient to protect consumers through overall market stability.

The European Commission has announced that it will review the possibility of adopting the UK's 'twin peak' approach by splitting the ESAs into separate authorities responsible for conduct and prudential regulation.

We would encourage it to give further consideration to the potential merits of this approach, although we recognise this type of structural reform is a long-term option only. A dedicated conduct regulator appears to be making a difference to consumer protection in the UK, although the tensions with prudential regulation remain.

Q31: How can the EU best support the development by the market of new technologies and business models, to the benefit of integrated and efficient capital markets?

The Panel agrees with the views expressed by the Commission in the Green Paper that technological development is a key driver of the integration of capital markets. The paper refers to the development of 'FinTech' companies, noting that global investment in FinTech ventures has tripled to nearly $3 billion in the five years to 2013.

It also points out that company law has not kept pace with technological development, and there are concerns that the same applies to regulation, not least in respect to consumer protection.
The Panel concurs that regulatory activity tends to focus on traditional financial services, while overlooking the disruptive impact of innovation technologies on existing markets and their role in creating new ones. In this regard, we would like to draw the Commission's attention to a number of relevant initiatives being undertaken in the UK.

The UK's Financial Conduct Authority (FCA) in 2014 launched 'Project Innovate', in which businesses are encouraged to present innovative ideas and liaise with the FCA in understanding and overcoming compliance issues. The project will also work with stakeholders to identify areas of regulation that may need amending to help foster innovation.

Moreover, the recent UK Government Budget included plans to work with the Treasury and the Prudential Regulation Authority to investigate the feasibility of developing a regulatory 'sandbox' for financial services innovators.[16] This would involve allowing FinTech firms to test their products and ideas on consumers in a controlled environment, similarly to 'clinical trials'. Crucially, the testing is expected to include consumer products and financial services software programs.

The Consumer Panel supports efforts to improve choice and competition for consumers (and also reduce costs) by encouraging technological innovation. This will at times involve lightening the regulatory burden and removing certain barriers to allow the development of new structures, systems and services.

However this cannot come at the expense of consumer protection. New products and services must be developed with an understanding of their potential for unfair outcomes for consumers (even where the interaction may be indirect) and with robust systems and controls processes.

It remains unclear to what extent exercises such as the 'sandbox' for FinTech firms will use consumer-focused measures, including risk, response and suitability. This applies to much of the regulatory work around financial innovation, which is why the Panel would

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[16] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/413095/gs-15-3-fintech-futures.pdf

like more evidence of consumer metrics being built into technology initiatives from the outset.

The Panel would also like to underline that one of most significant uses of digital technology which has emerged is the use of automated investment advice. While such services have the potential to increase access to financial advice for consumers, any measures to increase retail investor participation through such innovative distribution channels should be accompanied by appropriate regulation.

Consumers must be able to trust that the quality of the regulated advice they receive meets the same standards irrespective of the delivery channel used. It is also imperative that any consumers who obtain automated advice online have recourse to an alternative dispute resolution scheme, such as the UK’s Financial Ombudsman Service.