FACTSHEET

How the EU can make financial advice fairer for consumers

What's the problem?

Europe's retail investment markets are not working in consumers' interests. However, people need to be able to invest properly to save for their retirement, build wealth, save for a house, education or other uses that are essential to them and society.

The financial products sold to consumers to fulfil these needs are underperforming. They offer low returns, which are the purpose of savings products. The lower the returns, the less reason for consumers to invest. Those who do, often manage only poor results which causes very low trust leading many to refuse to invest at all.

This harms consumers twice-over: by causing a lack of investment and by wasting money for those who do invest. For some, this can mean the difference between comfort and poverty in older age. This issue also negatively impacts the European economy. Many private companies prefer to seek funding in the more efficient US markets due to lack of private funding in the EU. This not only hurts individual investors but also hampers the overall economic performance within the EU.

Why is this happening?

The core of the problem is that in many European countries, financial advisors are little more than salespeople. They receive commission (or 'inducements') from fund managers to sell certain products, whether those are in consumers' best interests or not. Products with higher inducements are therefore more attractive to sell, but those costs mean that the product is of lower quality. This leads to "adverse selection" - a system where the worst products sell the best.

Unfortunately, consumers pay the bill for this in the form of high fees on products such as pension plans. This means that consumers who think they are receiving trustworthy financial advice from their bank are actually being subjected to a sales pitch.

This 'advice' model has led to countless mis-selling scandals across Europe, as attested to by our Price of Bad Advice campaign. These scandals are only the tip of the iceberg though, as these products ultimately lead to consumers disengaging from the market.

Would banning inducements work?

There is evidence from the Netherlands and the UK – where inducements have already been banned – that consumers have benefited from it. Indeed, the ban has led to more competition on the market and better returns, as consumers are not paying for advisors' commission in the shape of inflated fees. Despite industry scare-mongering that consumers would no longer be able to access financial advice, evidence that our German member vzbv has collected suggests the contrary.

What is the EU doing about it?

The European Commission has recognised that the current financial advice model is failing consumers. However, massive lobbying from the finance industry blocked a ban on inducements when the Commission unveiled its Retail Investment Strategy proposal in May 2023.

However, several positive aspects remain:

- **A ban on inducements when no advice was given.** Currently consumers pay inducements to financial institutions even if they do not receive, want, or need advice. (e.g., by buying investment funds via their bank online). Putting a stop to this is the bare minimum in terms of reform.
- **New benchmarks on product performance and cost.** Enforceable, harmonised rules on minimum product quality would help raise the quality of products sold to consumers. Performance and cost benchmarks are a very good step to achieving this. Setting a hard rule is key to ensure every product has a positive return after costs and inflation. This is needed to be an enforceable criterion by market supervisors and courts.
- **A review process.** The Commission proposes to revisit its proposal three years after entry into force, to see if further action is needed. A robust and ongoing review process is key to be able to raise data about the possible effect of the reform and fix any problems. This should not be delayed, and the scope should be maintained. Should the current proposal fail to meet its stated objective, just like previous attempts focussed on transparency did, we need to be able to discuss more fundamental reform of the distribution system again.

What happens next?

The Commission's proposal is currently under review by the European Parliament and Council, where policymakers are again under heavy finance industry lobbying to further dilute the remaining ambition.

Despite not proposing to ban inducements, this proposal has some potential to improve the dysfunctional financial advice market by limiting the costs consumers pay on their investments. For this purpose, it is worth defending any progress that could be made through this proposal, even if only a fundamental reform will solve the problem.

For more information and BEUC recommendations on the Retail Investment Strategy, read our position paper.