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MiFID II - Inducements and Costs and Charges Disclosure Requirements

April 20, 2020

The European Securities and Markets Authority (“**ESMA”**) published its final report to the European Commission (the “Commission”) on inducements and costs and charges disclosures under MiFID II. The Final Report concerns technical advice in relation to certain investor protection topics under MiFID II, and focuses on the impact of costs and charges (Article 24(4)(c) of MiFID II and Article 24(9) of MiFID II) on the provision of investment services and ancillary services other than portfolio management and investment advice provided on an independent basis.

Inducements

ESMA encourages the Commission to conduct further analysis on inducements, and proposes some changes to the regime primarily aimed at improving clients’ understanding of inducements. ESMA proposes the following:

- ESMA does not recommend a ban on inducements completely for all retail products across the EU. However, the Commission should assess the impact that the MiFID II inducements regime has had on the distribution of retail investment products across the EU and what impact a ban would have on the different distribution models throughout the EU. In particular, to evaluate the impact the inducements ban has had in the Netherlands and UK (two jurisdictions which have already introduced it) and whether the ban has had any unintended consequences for retail clients;
- Consider what potential actions could be taken to counterbalance or at least mitigate the risks of unintended consequences of a ban on inducements;
- Further analysis might be appropriate in regards to the application of inducements requirements to the provision of underwriting or placing in case of IPOs;
- MiFID-like investment products, such as certain insurance products, should be subject to similar inducement rules to the MiFID II ones;

- Introduce the obligation to include, in all inducements disclosures, an explanationof the terms used to refer to inducements (for instance, third-party payments); and
- The Commission should bolster the MiFID II requirements around quality enhancing services. Firms should bring to the attention of its clients the specific quality enhancing services that the client is already benefiting from, or that the client could benefit from, to avoid inducements being spent on quality enhancing services of which the client is not aware. The list of such quality enhancing services should be easily accessible and updated on a continuous basis.

Disclosure requirements for costs and charges

Overall, ESMA finds that the disclosure regime works well, though certain aspects have not had the positive impact expected. ESMA has proposed:

- Professional clients (both *per se* and on request) should be allowed to opt-out completely of the ex-ante costs disclosure requirements, for one or more services;
- The obligation to provide the illustration of the impact of costs on return should not apply to eligible counterparties, without the need to opt out;
- The MiFID II Delegated Regulation should be amended to clarify that, as firms are required to provide the actual costs incurred by the client in the ex-post costs disclosures, they should keep records of the client's portfolio on a day-to-day basis so they can calculate and show the ex-post costs disclosures as accurately as possible;
- Where a transaction is carried out by telephone at the request of the client and it is not possible to provide the ex-ante costs disclosure in good time before the transaction, the relevant costs disclosures may be provided immediately after the transaction is concluded; and
- Implicit costs should be included in MiFID II costs disclosures.

In addition, ESMA recommends amending Article 3 of the MiFID II Delegated regulation so that, when information must be provided in a durable medium, the provision of such information by means of electronic communications shall become the norm and default option. An active choice of the client to that end, should not be required any more. Only if the client has not given the firm a valid email address, or if it explicitly requests the information in paper form, should the firm provide the information on paper.

ESMA also noted that it is not appropriate to create a new sub- category of clients – “sophisticated retail clients”. ESMA advised that issues raised regarding the application of the regime to more sophisticated retail clients should be addressed through the possibility for retail clients to be treated as professional clients on request.

The Final Report has been submitted to the Commission.

Related Professionals

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