FINANCE
DENMARK

# Retail Investment Strategy
## 28 August 2023

**Memo**

August 28, 2023

Finance Denmark (FIDA) supports the aims of the Retail Investment Strategy (RIS) to enhance retail investor participation and protection, and to ensure that investors are offered high-quality advice for products and services, which bring them value for money.

However, we are concerned with the narrow focus on costs, and we generally find that the effects of the package might not reflect the Commission's intentions. Thus, we are committed to provide alternative solutions to adjust the measures so that they more likely will result in the intended outcomes.

FIDA highlights the following key messages (developed in Annex I):

- **FIDA is concerned with the uncertainty associated with the term "cost efficient" central to the package, and particularly, the best interest test**. In terms of the best interest test, it is necessary to clarify the term "additional features" as it may have strong undesired impacts not only for recommended products, but also for the range of products available through execution services. If features like sustainability and active strategies are "additional features", it adds to a general risk of limiting the product diversity favouring large index issuers, which will harm consumers and capital allocation.
- **We welcome that the Commission has considered the industry's criticism of a full inducement ban, however, we are against the extension of the partial ban as proposed.** Particularly, as the scope of the ban does not only target execution-only, as defined by MiFID II, but extends to all non-advised sales. The proposal is troubling from the consumer's perspective complicating the client journey. Clients will need multiple custody accounts if they wish to trade both independently and through advice. Likewise, products must be separated, which will limit the products offered especially through execution services to the detriment of the consumer. As such, the effects resemble a de facto full ban for many distributors, notably full-service banks which are fundamental to the Danish market.
- **FIDA supports that products must deliver value and returns should not be eroded by unjustified costs. Yet, FIDA does not support the centralised, quantitative Value for Money-cost-benchmarks**. We are concerned that they will create "race to the bottom"-effects where low prices are prioritised over other important qualities (sustainability, alternative investment strategies, etc.), severely limiting the product diversity. This would be

harmful to consumers, to smaller issuers of innovative investment products, and to European SMEs seeking funding on the capital market.

- **FIDA urges the Commission to consider alternative solutions to the Value for Money-framework.** We highlight the successful setup on the Danish market based on the Danish implementation of POG rules and our independent Council for Return Expectations (see Annex II).
- **For the suitability test, FIDA is concerned with the required assessment of diversification**. This will add further complexity for the client in providing information on their full portfolio (incl. at other institutions), require more resources from advisors which increases costs, and it goes against the wishes of many clients, who prefer not to divulge too much information.
- **Including risk profile and ability to bear loss in the appropriateness test goes against the client's interests, as the test is conducted for clients who explicitly wish to trade independently**. Again, this adds complexity for the client, and it will require a great deal of information from them to properly assess such broad measures.
- **FIDA generally supports the proposals regarding PRIIPs, disclosures, and the relaxation of the requirements to qualify as professional.**
- **Lastly, we support that customers should be protected against misleading marketing,** but the wide scope of the marketing regulation proposed is burdensome and an assessment of the proposal against common advertising practices and existing regulation should be made.

# Annex I – Retail Investment Strategy
## 28 August 2023

**Memo**

August 28, 2023
Doc. no. FIDA-931287038-801756-v1

Finance Denmark supports the purpose of the Commission's Retail Investment Strategy (RIS) to increase retail investor participation on the European market and we find it important to ensure a high degree of investor protection. Additionally, Finance Denmark generally supports the further alignment of IDD and MiFID with regards to investor protection.

Furthermore, Finance Denmark agrees that the participation of retail investors is critical for the green transition.

RIS contains substantial proposals for amendments and additions to several legal acts within the area of investor protection, which potentially can have significant implications, and which will require market transitions for both investors and the financial sector.

Considering the impactful amendments and the related uncertainty, Finance Denmark finds it concerning that the adoption of the package assumedly is to be rushed through by summer 2024. It is Finance Denmark's assessment that it will be necessary to perform thorough analyses and negotiations of the Level 1 amendments in order to avoid having important uncertainties regarding the understanding and the scope of Level 1.

In relation to this issue, it is particularly concerning that the potentially most invasive proposals are worded in a relatively vague and broad manner, and/or that it is left to Level 2 and 3 to specify the rules, rendering it very difficult to assess the Level 1 proposals.

Moreover, Finance Denmark finds the deadline for implementation of the proposal very concerning. This concern is strengthened by the large amount of Level 2 and 3 legislation that is to be developed and implemented as well. In many cases, ESMA and EIOPA are given a mandate to develop RTS within 18 months after the entry into force of the amendments to the legal acts, which coincides with the deadline for implementation and compliance with the amendments in the Member States. This will undeniably make it difficult for the sector to adhere to new requirements as they are not specified before the implementation, and simultaneously, there is a risk that a clear legal basis and scope might be missing from Level 1. One might recall the implementation of MiFID II, when it was necessary to delay the implementation by one year, and yet, crucial delegated acts

were not published until less than a year before they were to be applied, while guidelines were not published until after the rules had been applied.

**Concerning elements – narrow cost focus and effects on competition**

Generally, Finance Denmark finds the proposal comprehensive and with potentially unintended consequences that can affect competition, price-setting and product offering on the market in a negative manner to the detriment of investors.

The proposal has a primary and narrow focus on cost efficiency. It is however unclear exactly how to define when a product is cost efficient, including how to measure the efficiency. We find it necessary to ensure that the proposal also puts emphasis on other parameters, such as quality and value-adding elements, which make part of the assessment of whether a product in fact provides value from a client perspective.

The stated concerns are developed further in the subsequent section based on the following main issues:

- Increased focus on cost efficiency in advice and the partial ban on inducements
- Cost-focused Value for Money benchmarks
- Added complexity for the investor and added administrative burdens through new requirements in the suitability and appropriateness tests

For the most central elements in the strategy, we have in italics presented preliminary assessments of how to adjust and improve the measures so that they are more in line with the main purpose of the strategy.

**Measures that Finance Denmark generally supports regarding disclosures, PRIIPs and marketing.**

The proposal contains several elements which Finance Denmark supports as they can contribute to more standardised investor information and better protection against misleading marketing communications, including by form of unregulated marketing from "finfluencers" on social media. These elements are further developed under the following subjects:

- Standardised and digital disclosures
- PRIIPs
- Less strict requirements to qualify as a professional
- Limiting the risks of misleading marketing communications
- Ensuring competent advice through new certifications
- Increased financial literacy

## 1. Concerning elements

1.1 Increased focus on cost efficiency and the partial ban on inducements

Finance Denmark supports the purpose to safeguard retail investors' interests. However, it is not Finance Denmark's perception that the the current MIFID-II inducements-regulation go against the interests of the investors, hence we are **against the extension of the partial ban on inducements. Finance Denmark also finds the one-sided focus on cost efficiency of the best interest test unsuitable and concerning**.

The concern stems from the inherent uncertainty related to the term "cost efficient", including which parameters to consider in the assessment of whether a product is in fact cost efficient. Furthermore, the assessment of cost efficiency could easily become either a subjective or comparative analysis. Both of which entail a large number of uncertainties and risks. The effects of both of these measures can be harmful for the consumers in Europe.

Finance Denmark is concerned that these two measures will affect especially small issuers, and that this could lead to a substantial decrease in the product offering with the risk that the markets become even more centralised by a few, large and global asset managers. This is seen to potentially have a negative effect for retail investors due to the smaller product offering, less innovation and, in the longer run, even increasing prices.

*Best interest-test (MiFID art. 24(1a)) and cost efficiency requirement*

The Commission is suggesting replacing the existing requirements to deliver quality enhancing services with a new best interest test (MiFID art. 24(1a)), according to which the advisor must present the most cost-effective product.

This test has a considerably wider scope than the requirement for quality enhancing services, which only apply in situations when the advisor accepts and retains inducements. The new best interest test instead makes a general requirement to be fulfilled for all investment advice and also for independent advisors. As the intention is to limit the conflict of interest stemming from inducements, **Finance Denmark recommends to make sure that the best interest test, if the test is kept in the final rules, will not be an obligation either if there is a prohibition against inducements or if an institution chooses not to accept nor retain inducements. The criterion to use an "appropriate range of products" could then be applied for all advisors working under an inducements regime.**

From the consumers' perspective, Finance Denmark finds it concerning that the main focus is on cost efficiency, since the most cost-efficient product might not

necessarily be the best product for the consumer. Other important qualities, such as sustainability objectives, specific asset management strategies and goals as well as other investment objectives and intentions are also of relevance. If the best interest test is to be solely based on the total costs, it can lead to a situation where consumers are solely recommended passively managed, index investment products, which do not take into account specific characteristics important to facilitate the green transition, nor does it consider the management methodology (active or passive) of a given fund, which is an inherent attribute of the fund. This can also entail a risk that capital is primarily allocated to a few global asset managers. If that is the case, it should be analysed how this will affect price setting, as the rules might resemble de facto price regulation. The potential societal implications for the distribution of capital and the retail investor participation in the green transition should also be analysed. For instance, a possible effect could be that it would be increasingly difficult for green start-ups in a smaller jurisdiction to attract capital.



Furthermore, as long as it remains unclear how to assess cost effectiveness, it is difficult to determine how the best interest test is to be combined with the suitability test. The suitability test already considers the most essential product characteristics, including product costs and complexity. The main uncertainty regarding the scope of the proposal stems from the use of the term "additional features", and its possible combination with the suitability test. The interpretation of this term will determine how severely the proposal could impact product offering on the market.

We here put forward some examples which highlight the issues regarding the uncertainties on cost effectiveness and "additional features":

- If "additional features" include active management it would entail that the advisor always would have to recommend a passively managed alternative, as passively managed funds typically have lower costs.
- A one-sided focus on cost effectiveness in the best interest test combined with the obvious economies of scales effects in the asset management industry imply that the proposal will favour larger asset managers. The revised provisions might create entry barriers on the market, including, e.g., for new fintech companies.
- Sustainability objectives often entail active management which often implies increased costs; thus, a possible one-sided cost-focus can substantially decrease the likelihood that retail investors are recommended sustainable products.

Furthermore, the requirement in the best interest test that the advisor must present "an appropriate range of products" could have negative effects on the competition. This is due to the fact that the requirement to give advice based on "an appropriate range of products" is suggested to be imposed on MiFID-companies (such as banks), and hence, this requirement will also affect e.g. Alternative Investment Fund Managers (AIFMs), having extended licenses to provide investment advice only on the funds managed by themselves. Any requirement that such managers must advise on other, external products goes against the intention behind the legislation on AIFs. If the requirement is imposed, it will imply that managers of AIFs, which currently offer investment advice for their own products, will no longer be able to provide investment advice which will be directly negative for the competition on the market. **This is another argument in favour of making sure that the criterion to use an "appropriate range of products" only is to be applied for all distributors working under an inducement regime**

According to our interpretation of the proposal, the investment advisor can still offer another product which does contain "additional features", if they still offer the client the cost-efficient product without "additional features". This creates uncertainties as to how to present any "additional features". If active management for instance is an additional feature, it is not clear whether it is allowed to bring to the client's attention that passively managed funds only yield returns below that of the market.

In order to ensure that retail clients continue to benefit from qualitative services and to promote a more active, as well as ongoing, retail participation on the capital market, **Finance Denmark suggest that the criterion of recommending products without "additional features" is replaced with a criterion focusing on advisors' responsibility to deliver qualitative services, for example through various forms of follow-up actions with clients depending on the nature of the services provided, value-added tools like information tools, filtering tools, reporting etc.**

In general, Finance Denmark identifies a risk that the best interest test will limit product offering and diversity which is harmful to consumers and, in the long term, to the competition on the market.

*Partial inducement ban (MiFID art. 24a)*

It is positive that the proposal does not contain a full ban on inducements. Yet considering the extension of the current partial ban combined with the other measures in the package, also including the administrative burdens imposed on

the banks and investors in complying with the measures, the framework resembles a de facto full ban.

A full inducement ban remains an option stipulated by the 3-year review clause included in MiFID art. 24a. The review clause is worded in a way that seems biased towards a full ban. Furthermore, 3 years make up a very short period to properly assess the effects of the new legislation. It will require substantial and costly changes that are to be evaluated already after 3 years, after which the sector might once again be imposed new costly changes. In the end, the comprehensive and frequent regulatory changes will make the products more expensive for investors. Additionally, it is unclear how and based on what criteria the Commission will assess if the effects warrant maintaining only a partial ban. Therefore, it is difficult for the sector to determine what is required to avoid having a full ban imposed 3 years after the new package has entered into effect.



The partial ban targets all non-advised sales except in those cases where one or more of the client's transactions can be linked to advice. With this link to single transactions, the proposal disregards the fact that many retail investors benefit from using multiple services at their banks through which they both receive advice and trade independently. The specific parameters defining the link to advice are not defined but they will be crucial for the level of complexity in the scope of the measure and its implementation.

For consumers, the partial ban can cause a number of disadvantages contrary to the objective of ensuring better investor protection. One of these disadvantages is added complexity. In complying with the ban, banks might have to separate products sold under advice from those sold without advice, which can require the clients to hold separate custody accounts for both advice and execution only, possibly with trade restrictions on the advice account. Thus, it will be necessary for consumers to have multiple custody accounts if they wish to trade both with and without advice. **For consumers, it will affect the flexibility in their decisions on when and how they wish to trade, and potentially add additional charges for the custody accounts, while it will possibly also limit the product offering for both advice and execution only.** If the distribution costs are moved from the product to a direct fee charged by the distributor, it will in any case be less optimal for the retail investors for tax reasons[1].

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[1] Apparent from the Danish FSA's evaluation of the inducement ban's consequences (Temaundersøgelse om provisionsforbuddets konsekvenser (finanstilsynet.dk) (in Danish)) which shows tax and VAT effects for different types of portfolio management clients when the full ban was imposed on portfolio management in Denmark.

In terms of the competition on the market, the effects of the partial ban can lead to a situation in which smaller number of products from third parties are available to customers trading without advice. Inducements are the primary market mechanism that support and maintain a broad product offering being available from the distributors. The partial ban can also have significant impacts especially for the smaller issuers. The smaller issuers are typically more dependent on external distributors (thus, inducements) to ensure that their products are available to investors. The inducements are as such instrumental in ensuring that smaller issuers obtain a presence with the distributors, and this is without having the inducement influence the distributors' advisory services or marketing. **Therefore, there is a risk that the product offering will become smaller and dominated by a few, large issuers. That will limit the diversity of the products offered, which in the end will harm consumers.**



The Commission is also suggesting rephrasing the wording of the ban from "shall not accept and retain" to "shall not receive". The practical implications of this will make it impossible to offer products that contain inducements for non-advised sales or in portfolio management services. **Thus, the new wording of the ban can lead to a further limitation of the product offering – also for portfolio management – without making any significant contributions to investor protection.** It can also entail that all investment funds must be duplicated, as the funds must be structured in two versions: one with inducements and one without. This adds more complexity in the process of structuring the funds, which potentially could be costly.

**Finance Denmark requests that the rule that portfolio managers shall not "accept and retain" inducements should remain.** Passing on inducements in full to clients effectively removes the perceived conflict of interest which the Commission argues is one of the major reasons behind the extended partial inducement ban. Furthermore, by keeping the possibility to kick back all inducements to the clients, it is ensured that clients can access the full range of products available throughout all distribution channels.

Regardless of how any inducement ban will be structured in the final rules, it is necessary to include **a grandfathering clause to make sure that the ban is not applied retroactively, so that holdings obtained before the entry into force of the legal act can still contain inducements in accordance with the current legal framework.** Currently, distributors will rarely have separate units of the same fund/ISIN sold with and without advice, and thus, it is not possible to determine which fraction of the holdings can contain inducements under the new regime. This is significant considering the practicalities, as a customer's existing holdings in

the same fund containing inducements can be made up of both execution-only and advised trades.

Finally, one area where the Commission might do further analysis and market impact assessments is on the effect of the unbundling regime. We note that regulatory changes in the UK seem on their way towards a roll-back of the unbundling rules. This divergence might affect capital markets and asset allocations in Europe impacting competitiveness of European capital markets.

*Preliminary proposal:*
*Preferred option: The proposal of the best interest test is removed and the requirement to deliver quality enhancing services is maintained along with the existing rules on inducements but including common EU standards for transparency regarding the customer's access to the services.*
*Second option: The proposal is adjusted such that the best interest test only applies to institutions which receive and retain inducements. This could be based on either a national ban on inducements or if an institution chooses to opt out of receiving and retaining inducements. The wording must still allow for the practice of passing inducements on to the customers in portfolio management and for non-advised sales. It must be clarified how the best interest test interplays with the suitability test. We strongly suggest removing the point (c) in the best interest test as it is very unclear. If point (c) is maintained, the definition of the term "additional features" is crucial for the effect of the provision and a thorough analysis should be performed of the effect on the markets given the definition chosen.*

*It must be noted that, as mentioned, we are still assessing and analysing the full potential consequences of the proposal, and we maintain the right to return with revised or new proposals.*

1.2 Cost-focused Value for Money-benchmarks (MiFID art. 16-a) and undue costs in UCITS and AIFMD

Finance Denmark supports the fact that investment products must deliver value. However, it is our perception that this is already the case – at least in Denmark supported by the Danish implementation of the product governance framework. Therefore, Finance Denmark wishes to encourage the Commission to consider how the product governance regulation for distributors is interpreted and implemented in Denmark.

The Commission is suggesting introducing additional product governance requirements for products included in the scope of the PRIIPs regulation, which will create the foundation for new Value for Money benchmarks in MiFID art. 16-a

that are to be developed by ESMA and EIOPA. The Commission is suggesting that the benchmarks should be based on data on performance and product and service costs for the products reported from manufacturers and distributors. The actual benchmarks are to be developed by the ESAs, and the framework for the exact application is not determined until Level 2 and 3. Yet, they are critical to the scope of the proposal and the potential impact it will have on price setting and product offering, including whether it will become actual regulatory intervention on prices.

Finance Denmark supports that products should deliver value to consumers, including that their expected returns should not be eroded by costs. Accordingly, Finance Denmark finds it appropriate and can support determining a general principle stating that the obligation to act in the client's best interests also includes performing Value for Money-calculations as part of the distributor's product governance process.

However, Finance Denmark does not support the proposal of setting out details on how to assess if a product delivers value in a regulatory context. Finance Denmark is highly sceptical towards having centralised, EU-wide Value for Money-cost-benchmarks to be used by the institutions in each Member State to determine if products, which are distributed nationally, create sufficient value for the clients in the respective Member State. Finance Denmark is of the perception that such an approach will make it more difficult to account for the differences between Member States. **Finance Denmark strongly advises against having the legislation create cost benchmarks neither at the European level nor at a national level, but instead recommends that the Value for Money-regulation leaves room for flexibility to allow financial companies to determine methods for assessing if the products, distributed nationally, create value for the consumers in the Member State.** In this way, Value for Money-assessments can fit the market situations and business model for the country in question.

Furthermore, Finance Denmark finds the approach stipulated in the proposal concerning, assuming that our interpretation of Level 1 is correct. Generally, the new requirements and centrally developed benchmarks are primarily focused on costs and performance. It is uncertain to us exactly what effect these benchmarks will have, and we are concerned about the effect cost benchmarks will have on the product offering and development of new and innovative products, including investment products with specific features such as sustainability objectives. If the effects of the benchmarks become resemblant of regulatory intervention on price setting and product offering, it also entails a risk that it will impact

the competition and price setting mechanisms negatively, making it more expensive for the retail investors to invest.

We acknowledge that qualitative parameters are difficult to measure and compare, but we do find it concerning if absolute quantitative costs and performance are the only parameters included in the new requirements for Value for Money-calculations. **We strongly recommend ensuring enough flexibility to allow for other, more qualitative quality parameters.** If the Value for Money framework remains based on an entirely quantitative focus, one must bear in mind that historical performance is not an adequate measure in the product governance process and it should be based on expected returns and be forward looking and also that expected returns represent one possible outcome in a larger spectrum of outcomes, and that a higher expected return can make up for a larger (volatile) spectrum with the risk of a larger negative outcome.



**When setting upcoming requirements for distributor Value for Money assessments, we suggest that distributors should be allowed to count delivery of qualitative services to customers as value adding services when doing Value for Money-calculations for products distributed through distribution methods where such qualitative services are provided.** By qualitative services we are here referring to the type of services which currently can be seen as quality enhancing services according to ESMA-guidance[2] on how to interpret Article 11(2)(a-c) of the MiFID II Delegated Directive, which lays down the conditions to be met in order for inducements to be considered to be designed to enhance the quality of the relevant service to the client.

In other words, Finance Denmark is of the opinion that one should aim to ensure a regulatory alignment between a) how distributors already today are required to assess value of services for the purpose of receiving inducements and b) how to assess value of services for the purpose of distributor Value for Money-calculations of products. When taking this approach of regulatory alignment on how to assess "value", Value for Money-calculations would then allow for that inducement-bearing products can be seen to deliver more value than non-inducement bearing products due to the delivery of quality enhancing services. From a product governance perspective, this could motivate a price difference between products carrying inducements and products which do not.

With regards to undue costs in UCITS/AIFMD, RIS prescribes that the firm will need to potentially compensate the clients for having charged "undue costs" also

[2] See "ESMA35-43-349 - Questions and Answers On MiFID II and MiFIR investor protection and intermediaries topics", Section 12, Question 8.

measured against common benchmarks. Reimbursement would be very difficult in several situations, e.g., where funds may have been merged or closed, several investors has fully or partly redeemed or subscribed during the period. Hence, if kept in the regulation, a materiality threshold must be implemented. Moreover, if the requirement to reimburse is maintained, the reimbursement should be to the fund, not the investors, since the management company will not in many cases be able to identify the end-investors of the investment fund and reimburse investors in a fair manner. The costs that are deemed necessary for a UCITS to operate varies from country to country due to the different operational set-ups used by the management companies (for instance, a Transfer Agent does not exist in the operation of Danish UCITS). Hence, another complicating factor behind common European benchmarks is the different costs due to differences in the operational set-ups in the management of investment funds from Member State to Member State. One more practical European solution might be a non-exhaustive list of costs that are not undue.



Considering the structure of the new benchmarks, which is yet to be defined, Finance Denmark is concerned if it will be possible for the ESAs to develop benchmarks with sufficient complexity and granularity to encompass the broad spectrum of different products on the market. PRIIPs define a very broad range of different types of products. Therefore, flexibility is needed such that the Value for Money-assessments of the products can vary depending on the type of product in question. Additionally, the risk of a long time lag is of concern, considering that it, each time new benchmark data is to be launched, will take time to obtain data, create the new benchmarks, and then it will take time for firms to do and verify value-for-money calculations making use of the new data in the product governance process. If the benchmarks are not sufficiently granular and timely, it can lead to misleading conclusions in the product governance process and the exclusion of otherwise efficient products.
Moreover, Finance Denmark also finds it concerning that distributors must report distribution costs to the ESAs, as this is administratively burdensome and these are in many cases are dependent on characteristics specific to each individual client, such as the client's invested amount, risk profile, investment behaviour etc.

Furthermore, regarding the distributors' Value for Money reporting, Finance Denmark finds it inappropriate that the Commission is suggesting that distributors are to perform Value for Money calculations not only when they recommend a product through advice, but also if the product merely is available in non-advisory services. Considering the fact that banks today ensure that clients have a broad product offering available by making thousands of products accessible through

online platforms, such a requirement risks limiting the product offering in an unnecessary manner, and such a requirement indeed seems disproportional. If manufacturers (e.g., UCITS Fund Companies) are required to perform Value for Money-calculations for their products, regardless of how they will be distributed, Finance Denmark finds that distributors (e.g., banks) should only be required to make Value for Money calculations for the products that they recommend to the client through advice. Products that the distributor only "offers" but does not "recommend" should, as such, be exempt from Value for Money-calculations. **We recommend limiting the requirement for distributors to perform Value for Money-calculations to apply only to products which are recommended in advisory services, while the products that are merely offered on trading platforms are exempt from the distributors' required Value for Money-calculations, since these products already are part of the manufacturers' required Value for Money-calculations.**



As an important sidenote, we would argue that RIS grants the opportunity to consider the scope and make precisions of the MiFID II product governance rules. More specifically, we wish to draw attention to a previously stated point regarding review obligations under the product governance requirements (paragraph 68 of the guidelines). In Annex IV to the Final report on guidelines on MiFID II product governance requirements, ESMA also acknowledged that problems arise regarding review obligations for manufacturers when they advise corporate issuers on product launches under the Level 2 requirements. ESMA recommends the Commission to consider softening the review obligation applicable to a firm that has advised a corporate issuer on the launch of a new product. We believe that the review in relation to RIS would be the time to address this problem.

*Preliminary proposal:*
*Finance Denmark fundamentally disagrees with the creation of centralised cost and performance benchmarks, as we understand them to be proposed by the Commission. We do not believe that the cost and performance benchmarks can be fashioned in neither a sufficiently granular nor precise enough manner for them to apply to all PRIIPs retail products. Furthermore, we find it difficult to comprehend how benchmarks are to be made for distribution costs as well as for different cost structures across different jurisdictions.*

*Therefore, situation, where the MIFID-regulation is interpreted in such a way that distributors (e.g. banks) are required to perform Value for Money calculations in such a way that products' costs are not tested against any cost-benchmarks but instead products are, as a part of the product governance processes, tested against estimations for a products' expected return.. In Annex II, we include a*

*concrete proposal for amendments to such a framework. The proposal provides an example of how the rules could be adjusted to enhance the focus on Value for Money in product governance processes without any overly prescriptive measures and without benchmarks but leaving room to account for other measures of quality than only costs and performance. We argue for flexibility in the regulation in order to allow the distributor Value for Money-calculations to be based on a consideration of reasonable benefit(s) expected to be provided by the investment, were e.g.* ***expected returns*** *for different asset classes is one aspect to be considered in the calculations. With regards to undue costs in UCITS and AIFs, reimbursements should have a materiality limit and reimbursements should be flexible, allowing for reimbursements either to be made to the fund or to investors. One European solution instead of benchmarks might be a non-exhaustive list of costs that are not undue.*



1.3 Added complexity for the investor and added administrative burdens through new requirements in the suitability and appropriateness tests (MiFID art. 25)

The Commission is proposing an amendment to art. 25 adding a requirement in the suitability test obliging the advisor to assess the diversification needs for the client's entire portfolio, which includes any holdings at other institutions. Adding a requirement to assess portfolio diversification also based on external holdings will generally make investment advice less flexible and more expensive.

Although diversification is important, Finance Denmark finds that the proposal, in the way it is presented now, will worsen the investors' opportunity to seek specific advice. It is not unusual that clients, especially wealthy clients, prefer that their investment advisor does not have a full overview of their entire portfolio. Some clients also actively choose to place their invested assets with several institutions, hence, they will experience this requirement as a limitation of their freedom to choose how they manage their assets, if they are forced to provide the advisor with full insight into their assets. Additionally, it is worth noting that some clients already find it somewhat condescending that they must provide full insight into their financial situation to receive investment advice.

The distributor will often only have a limited overview of the client's full portfolio. If the investment advisor is to collect information on the client's full portfolio, it will naturally also require that the client is willing to provide this information. Apart from making the investment advice process more complicated for the client, it will also entail additional administrative burdens for the advisor as well as creating a more time-consuming process, which can make it unprofitable to offer investment advice to less wealthy clients.

Adding to these concerns, we note that Recital 34 of the omnibus directive states that the advisor must also take into account the client's non-financial assets. From a practical perspective, this seems a very cumbersome and inappropriate task which will require not only great time and resources from the advisor, but it will also make the process substantially more complex and intrusive for the client having to provide such information. It is also very unclear exactly what to include as non-financial assets.

It must also be possible to conduct the additions to the suitability test using "robo-advice" or digital solutions. In terms of online self-service platforms, the new requirements can make it more difficult to provide robo-advice. Even currently, the existing comprehensive requirements imposed on clients to provide information make the experience both difficult and time-consuming for the clients. Furthermore, the requirements – both in the best interest test and in terms of diversification needs in the full portfolio – will require that the current robo-advice services are developed extensively. Where the solutions have been required to make a recommendation based on an assessment of experience and knowledge as well as ability to bear losses and risk aversion, they will now need to be able to assess the client's entire portfolio with regards to the degree of diversification.

In this regard, one must bear in mind that it is not uncommon for retail investors to intentionally seek advice only for a portion of their portfolio. Retail investors often divide their investable assets based on purposes, such as "savings for wedding", "for a rainy day", "retirement", etc. Retail investors therefore have varying risk aversion for different portfolios based on their purpose, rather than having one general level of risk aversion for the entire portfolio. The latter is usually reserved for sophisticated and very wealthy investors. In the same manner, it is often the retail investor's experience that their ability to bear losses on different parts of their portfolio also varies, e.g., for retirement funds versus travel and leisure budgets.

Finance Denmark supports the introduction of a "suitability light" regime for "well-diversified, non-complex and cost-efficient" products for which it is not necessary to assess the client's knowledge and experience with the relevant product nor their diversification needs. **We however believe that this option should be available through non-independent advice as well to create the best regulatory framework for retail investors and to ensure a level playing field and fair competition on the market**. If the option is reserved only for independent advisors, it will cause asymmetries in the competitive conditions on the market, and there does not seem to be any appropriate justification as to why this should only be limited to independent advisors from an investor protection argument. Finans Denmark has

for a long time advocated for a lighter advisory process for some clients investing in safeguarded products both to make a better client journey and to facilitate digital solutions, and the scope of the proposal is a missed opportunity in this regard.

In terms of the appropriateness test, which applies when clients trade complex products independently, the Commission is proposing to include assessments of the client's risk profile and ability to bear losses. Generally, this will complicate the process for clients, in particular since this applies to clients that explicitly wish to trade on their own. When a client intentionally has chosen to trade independently, it goes against the interests of that client to demand making an ongoing assessment of their ability to bear losses and risk profile. Ability to bear loss and risk profiles are measures that are meaningful at the portfolio level and not for single transactions or for a single asset class. These parameters are thus only assessed in a meaningful manner for the client's portfolio and should therefore only remain part of the suitability test.



It is also uncertain whether this will require that the appropriateness test should be conducted continuously, since factors like risk aversion and ability to bear loss vary with time. A client might also have a lower degree of risk aversion for a specific trade, e.g., for hedging, than the client might otherwise have. Thus, such a single trade would deviate from the assessment done at the portfolio-level in the appropriateness test, and consequently, it would become more complex for clients that wish to make such trades. An alternative scenario could be that the client wishes to trade a very risky product, but only as a small fraction of an otherwise well-diversified portfolio.

Finally, problems may arise in those situations where a client is represented through a power of attorney. According to the current rules, the appropriateness test should be conducted by the person with delegated power of attorney. If it is not clarified, distributors will have to register several appropriateness tests for the same client, both for their own investments and for those where they trade on behalf of someone who has delegated them power of attorney.

In terms of both the suitability and the appropriateness tests, we also find that it would be relevant to use the occasion to ensure better interaction between the rules for product governance and advice and appropriateness. Currently, Finance Denmark finds that the proposal can limit the options to switch between banks, as it is not certain whether the new bank will be able to recommend the client to keep part of their investments, which the new bank does not perform product governance on.

Moreover, it would also be a good opportunity to clarify the framework for reverse solicitation, including the interaction between the requirements for appropriateness test and product governance.

It could also be worth investigating how the interaction should be when clients choose smaller providers of investment services, which are dependent on the client's regular bank in terms of infrastructure. This could be a smaller independent advisor, which does not offer custody accounts or execution of orders. In such a situation, it is unclear whether the independent advisor will be limited by the "regular bank's" (with the custody account) product governance and client categorisation, as the bank is responsible for delivering investment services to the client in terms of executing the transaction itself.



## 2. Measures which Finance Denmark generally supports

### 2.1 Standardised and digital disclosures (MiFID art. 24b)

The proposed MiFID art. 24b stipulates a requirement to present inducements separately and in a standardised way as part of the ex-ante and ex-post cost disclosures, as well as making it mandatory to describe their purpose and to quantify their impact on the expected returns. The precise standardisation and terminology are to be developed by ESMA/EIOPA. Finance Denmark supports this standardisation, and the Danish Financial Supervisory Authority already has similar demands for Danish distributors. Although we reiterate our standing position that retail clients cost disclosures should be further simplified.

### 2.2 PRIIPs

Generally, Finance Denmark supports the proposals to the PRIIPs-regulation. We do however want to take the opportunity to repeat our long-standing position to have defined the scope for the PRIIPs-regulation in particular regarding corporate bonds issued by non-financial issuers. We do not believe that single bonds issued by non-financial issuers should be within the scope as they are not packaged investment products, but instruments issued to raise capital. Furthermore, for PRIIPs products, which are within the scope of the MiFID product governance rules but out of the scope of the SFDR regulation, there are problems due to the lack of alignment in the regulation in terms of the description of sustainability in the way that it is presented in ESMA's guidelines on product governance.

### 2.3 Less strict requirements to qualify as a professional

The criteria for clients who wish to opt up from retail to professional (currently MiFID Annex II) are suggested to be relaxed. The wealth criterion is reduced from 500,000 EUR to 250,000 EUR on average over a three-year period, and a fourth

criterion is proposed related to relevant education. Finance Denmark has continuously raised the need for more flexibility in the opt-up criteria. Thus, we welcome the proposed amendments. The amendments place added emphasis on knowledge and experience, which we support, yet we do recommend specifying how the client's education and experience is to be assessed in practice. We would also suggest a revision of the transaction criteria so as to make them specific to the asset class in question.



2.4 Limiting the risks of misleading marketing communications

The Commission is proposing a number of new provisions with the purpose of limiting the risk that consumers are misled by marketing especially through digital channels, where benefits and risks are not presented in a balanced way. Finance Denmark generally welcomes the purpose of protecting consumers against misleading marketing. In particular, we appreciate that the new MiFID art. 24c and the amendments to art. 69(2) also address the risks associated with digital marketing, especially from the so-called "finfluencers", as unregulated advice from such third parties can be harmful for consumers.

Additionally, Finance Denmark fully supports the clear division of responsibility between manufacturers and distributors in terms of marketing communication (developed by the manufacturer) and the distribution strategy (set out by the distributor), which is included in MiFID art. 24c(4).

However, although in support of the purpose of protecting consumers against misleading marketing, Finance Denmark finds that both the proposed definition of "marketing communications" ("in any form and by any means") in Article 4 of MIFID and article 2 of IDD and the definition of a "marketing practice" ("any strategy, use of a tool or technique") are very broad. This is hardly proportionate and can have major effects on the interpretation and application of the substantive requirements in MIFID II and IDD.

Such broad definitions could have large unintended consequences, e.g. leading to unproportional burdens related to record keeping requirements (the new article 24c (7) of MIFID and article 26 (7) of IDD) and the new requirements on annual management reporting on the use of marketing communications and strategies aimed at "marketing practices" (article 24c (5) of MIFID and article 26 (5) of IDD).

We therefore propose that the scope of these provisions should be reviewed, and we also propose a review of the relationship between the suggested new

MiFID II rules on marketing communications and other legislation such as distance marketing rules and prospectus regulation.
As an example, art. 24c(2) establishes that marketing communication must present the key elements of the respective product or service in a clear way, making it easy for the consumer to understand the key characteristics and risks associated with the product/service. We are concerned about the practical consequences if this also applies to, for instance, simple online branding of an investment service provider without mention of a specific product or service. The very wide definition of "marketing communications" can in combination with the added requirements to e.g., documentation create quite substantial administrative burdens, which do not add any value to investors.

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Furthermore, Finance Denmark perceives a risk that "marketing communication", cf. MiFID art. 4(1(66)), might also encompass part of the same information and ways to communicate such information as "announcements" in art. 2(k) of the Prospectus regulation, such as "screen announcements" published by an investment company briefly before or just after a capital market transaction or a term sheet for a capital market transaction, which is shared with an investor, containing the terms for the transaction. Such announcements are already regulated through art. 22 in the Prospectus regulation and in the Commission Delegated Regulation (2019/979) art. 13-17 and should therefore not be supplemented or imposed new rules in MiFID. We therefore suggest that an addition is made in art. 4(1(66)) with a reference to "a communication that falls within the scope of advertisement as defined in the Prospectus Regulation article 2(k)" as an exemption.

2.5 Ensuring competent advice through new certifications

The proposed new Annex V to MiFID sets out requirements for professional education of investment advisors to strengthen their competences and to ensure that the consumers receive high-quality investment advice. Finance Denmark supports this measure.

2.6 Increased financial literacy

The Commission wishes to strongly encourage Member States to further financial literacy, which we fully support. Increased financial literacy among consumers make for an important element in the process of safeguarding the financial well-being of consumers and in strengthening them to make well-informed financial decisions.

# Annex 2: DK practice on Value for Money

**Danish practice and market conditions related to Value for Money (VfM)**

- In Denmark, a supervisory practice aiming at or supporting VfM requirements exists based on the product oversight and governance rules (POG) stipulated in MiFID II and ESMA's guidelines, as well as the requirement under UCITS to act in the client's best interest.

- The Danish FSA interprets the current regulatory POG framework in such a way that in order to act in the client's best interest and mitigate conflicts of interests, investment firms should have proper POG processes in place ensuring VfM for investors.

- There is a strong supervisory focus on the quality enhancing services framework and the obligation to evaluate whether costs erode expected returns for investment firms, as well as on VfM for UCITS' delegating services to third parties.

- In addition, the industry has established an independent entity: the Council for Return Expectations. The Council sets out an industry-wide framework for expected returns used e.g., as part of the VfM process. The expected returns are generated semi-annually and include 10 asset classes, which are supplemented with standard deviations on the estimates as well as covariances documenting the risks associated with the asset classes.

- The return expectations serves as an anchor both in the internal processes in investment firms and distributors by determining the expected returns for a broad range of asset classes while also supporting the supervisory efforts in the following way: If investment firms present the expected returns to their clients, the Danish FSA asks them to be able to justify the expectations they present, including if they deviate e.g. from those set out by the Council[3].

- The Danish practice (strengthened VfM focus in POG, UCITS and Council for Return Expectations) helps secure that investors in Denmark are not

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[3] Undersøgelse af negative renter og investeringstilbud 2023 (finanstilsynet.dk) (In Danish)

offered products which are expected to have very low or even negative returns, which has concrete impact on the market. One example of this impact is that the industry restricted access to certain bond products during the low interest rate-environment of previous years to protect investors.

- On the basis of the Danish practice, Finance Denmark has drafted a proposal to ensure VfM through POG for both manufacturers and distributors (see Annex 1 below).

- The impacts of the Danish practice much resemble how we understand the intentions of the Commission with regard to ensuring value for money. It takes into account expected returns (and not only costs), which allows the framework to be applicable to a wide range of products and services of differing complexities and features, in addition to providing a strengthened approach to POG rules which are subject to supervision.

- The Danish Council for Return Expectations is not an explicit part of the FIDA proposal, which focuses solely on the Danish implementation of MiFID II.



**The Danish Council for Return Expectations – an additional feature of transparency**

In Denmark, the setup regarding Value for Money is strengthened through the Council for Return Expectations, which semi-annual publishes return expectations for 10 asset classes.

The Council was established in 2018 by Finance Denmark and Insurance & Pension Denmark. It consists of three independent experts who are elected for 3 years, currently Professor Jesper Rangvid (chair) from Copenhagen Business School, Professor at Aarhus University, Torben M. Andersen, and professional board member, Peter Engbjerg Jensen. The Council sets its expectations based on confidential input provided by a broad range of international market participants The contributing participants receive no financial remuneration for their input. The Council performs its own due diligence process with respect to the market participants they receive input from.

The semi-annual publications of return expectations are followed by a press statement explaining the considerations of the Council. These expected returns

are used across the industry (MiFID and IDD firms) as an anchor including in the VfM process. These do not include costs since this would impact competition in the markets and only the most important asset classes.

The investment firms are by industry self-regulation recommended to test the products using the returns from the Council. They are allowed to use own calculations but should in this case document and explain why they might deviate from the Council's expectations. Also, firms should combine the different asset classes to best reflect the risk profile of the product.

The motivation behind the Council's setup is:

- To create un-biased and market-based estimates of future returns.
- To provide an anchor in the VfM assessments without dictating the industry and without expecting to be able to cover all products available.
- To make sure that the industry refrains from competing on expected returns.
- To help smaller players in the market for whom generating expected returns would be a huge and disproportional burden.
- To give transparency to consumers and generate trust in the industry by having an independent council generating common return expectations.
- Deliver a common framework for an important part of the VfM assessment without distorting competition and markets.



**Key features of the Danish approach to Value for Money**

In Denmark, the supervisory approach from the Danish FSA to POG works quite well and as does the retail market in general. Retail participation is high on the Danish investment market and as is the number of high-quality products that historically have delivered high value considering both returns relative to costs as well as product diversity. As a concrete example of the well-functioning POG requirements, the industry restricted access to certain bond products during the low interest rate-environment of previous years. In a European context, the Danish fund industry as a whole offers some of the lowest costs and highest performing products for investors[4] with wide use of inducements. See the fact sheet on the Danish market included in annex 2 below.

We would like to stress the following key features of Danish approach to VfM:

[4] esma 50-165-1677 asr performance and costs of eu retail investment products.pdf (europa.eu)

- Overall value of a product is considered difficult to quantify and is assessed broader than merely expected returns.

- Even if expected returns are numerical, they are still only estimates based on risk models containing uncertainties[5].

- There are also services embedded in products and in distribution that are not quantifiable. The Danish practice takes into account that value is subjective and thus a service might be of high value to one client while of no value to another.

- The overall service effectively provided to investors as well as its quality and expected performance are used as metrics for determining value, one example is the current requirement in the rules for investment advice to consider clients' sustainability preferences in addition to purely financial criteria.

- It ensures specific distinction between manufacturers and distributors. Regarding costs, this distinction is made between product costs (MiFID ex-ante product costs) and the total costs of ownership (MiFID ex-ante product + service costs) (as defined in MIFID delegated regulation 565/2017, article 50 and annex 2), which measures the total ex-ante costs paid by retail investor. Total costs of ownership include product costs as well as the costs of distribution and advice (service costs).

- The Danish practice includes VfM in POG rules for distributors but not in the dialogue with retail clients (i.e., in the suitability regime), thereby keeping the process as simple as possible for the investor.



[5] Expected returns comes with known uncertainty measured by standard deviations on estimates but also unknown uncertainties which are not captured by the risk model and therefore the standard deviations on estimates.

# Annex 2.1: Concrete proposal for amendment for a balanced Value-for-Money approach

This proposal is based on the Danish high-level implementation of the VfM concept in the product governance framework. It does to a large extent reflect how existing rules are followed already in the well-functioning Danish retail market with relatively high retail participation.

It only regards POG rules, and thus does not take into account the Danish Council for Return Expectations or the strengthened supervisory process in Denmark.

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To ensure that the anchoring of the concept is strong and has a sufficient position in the governance arrangements for the investment firm, it could be considered to emphasize in MiFID II art. 9(3), that:

"*… the management body shall define, approve and oversee a policy to services, activities, products and operations offered or provided, which ensures that the intended benefit to the client is taken into consideration.*"

The anchoring with the management body could be supplemented by amending art. 16 on Organizational requirements. More specifically, it could be outlined in art 16(3), third subparagraph, that:

"*… the target market of the product is not only specified, but also the benefit to the identified target market shall be assessed as part of the approval process, and that it shall be ensured that the distribution strategy is consistent with the identified target market and the benefit assessed.*"

Furthermore, the VfM-concept should also be anchored with the distributor, which could be ensured by amending art. 16(3), sixth subparagraph. In the six subparagraphs, it could be emphasized that:

"*… the distributor shall have a process that ensures that it assesses the benefit to the client by the process it operates to offer or recommend financial instruments.*"

By anchoring the Value-for-Money concept in art. 9 and 16 of MiFID II, it will also be relevant to make slight amendments to the delegated directives articles on product governance (art. 9 and 10):

*"… the Value-for-Money concept could be a consideration of reasonable benefit(s) expected to be provided by the investment, when considering the risk/reward profile and the total costs to the customers as defined in MIFID Delegated Regulation 565/2017, article 50 and annex 2. The benefit(s) should be reasonable, relevant and of a qualitative and/or quantitative nature, meaning that a benefit is not necessarily a return expectation but could also be services. "*

By designing Value-for-Money in this manner, it will also create a link to the inducement regime and the quality enhancing services would automatically, among other things, be part of the benefit assessment.

For product manufactures, it could be added to art 9:
(2) *"…the procedures and measures shall ensure that the investment firm operates in a professional manner and taking the clients best interest into consideration in the manufacturing and taking into account the value – both monetary and non-monetary – that the product intents to create, and ensuring it is proportionate to the invested amount."*

(6) *"… the concept of Value-for-Money should be part of the management reporting."*

(9) *"… ensuring that it is considered and described what the benefits are for the intended target market under due consideration to the identified target market's needs, characteristics and objectives."*

(10) *"… that the stress scenarios shall take all costs and charges into consideration including an estimated cost figure linked to distribution."*

(12) *"… an assessment of expected return after all costs and charges."*

(14) *" …outlining that in the review process, it shall be reviewed whether the benefits are still relevant for the identified target market and reasonable compared to the costs and charges."*

The Value-for-Money concept will also need to be built into the distributor's product governance. This could be done by amending art. 10:

(2) *"… should ensure that the arrangements have a professional design and take into account the best interests of the client, and that the product and the ser-*

*vices provided provide benefit(s) for the investor. Furthermore, it could be emphasized that when assessing whether the products offered or recommended are compatible with the needs, characteristics and objectives of the identified target market, the distributor should, when taking into account the product costs as well as distributor service costs for the product, and the benefit(s) provided to the client, make an assessment of whether the product and services cumulatively provide Value-for-Money, also taking into consideration the expected investment horizon of the client."*

(3) "*… the management of conflicts includes considering the Value-for-Money, meaning assessing whether costs and charges incurred by the client compared to the intended benefit(s) are reasonable, relevant and of a sufficient qualitative and/or quantitative nature taking into account both monetary and non-monetary nature."*

(5) the review process should include "*… assessing whether the intended benefit(s) are reasonable and relevant, including whether they have sufficiently materialized."*

(8) "*… the Value-for-Money concept should be included in the management body's effective control."*

The Value-for-Money framework could involve an ongoing obligation for the distributor to ensure the relevance and reasonableness of the benefit(s), as a benefit never utilized would be difficult to review as reasonable and relevant.

# Annex 2.2: Trends in Danish retail investment markets

This paragraph provides insight into the Danish retail investor markets anno 2022:

1) Trends in Danish retail investment markets.
2) Finance Denmark case study 2019-2022: Key take aways from some European studies to be able to put the Danish takeaways into a European perspective.

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## 1. Trends in the Danish retail investment market

The Danish market is dominated by full-service banks[6] that provide non-independent investment advice to bank customers. Also, the Danish market has a well-matured pension system where Danes typically pay 15-18 pct. of their wage income through employment pension schemes. The participation outside the pension system of Danish savers should be seen in this context.

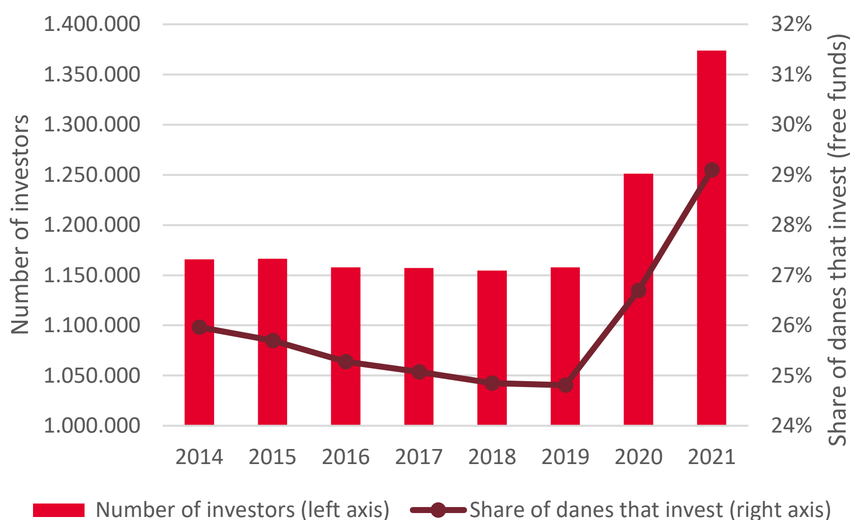
For the average Dane, deposits constitute 19 pct. of the investable wealth (excluding real estate assets) while the EU average is 37 pct[7]. Given the structure of the pensions system, with mandatory payment through employment pension schemes, 66 pct. of investable assets are placed in pension savings, whilst investments of free assets in shares, investment funds and bonds constitute 17 pct. on average. We focus on investments of free assets in this memo since this part of the total portfolio reflects investor choice.

*Source: Tax register data 2020*

[6] Full-service banks are defined as banks that offer traditional banking services such as deposits but also mortgages, pensions and investment services on products that are produced by the bank or by companies within the bank's corporate structure.
[7] Microsoft Word - Household Participation_Country statistical profiles.docx (efama.org)

Figures from 2021 show that 29 pct. of the Danish population had actively invested free assets in 2021. Having been stagnant for many years until 2020, Covid-19 kickstarted retail investments and this development remained dominant in 2021.

**Number of investors and the portion of Danes investing 2014-2021**




*Source: Tax register data, all Danes having invested free assets*

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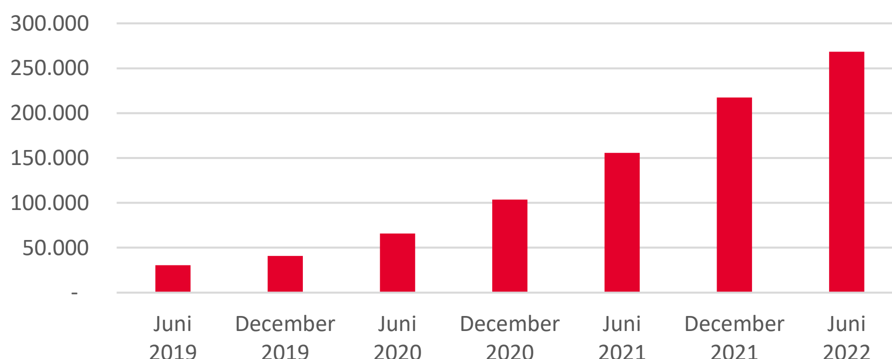
Covid-19 aside, a political initiative has also supported the developments. The so-called "savings in shares account" is targeted to small retail investors since it is easy to use, and it gives a significant tax incentive. The account had a limit of 50.000 DKK when it was launched in 2019, and the limit was raised to 100.000 DKK by 1st of July 2020. After the cap was raised, the number of accounts rose by 200.000 over 2 years.

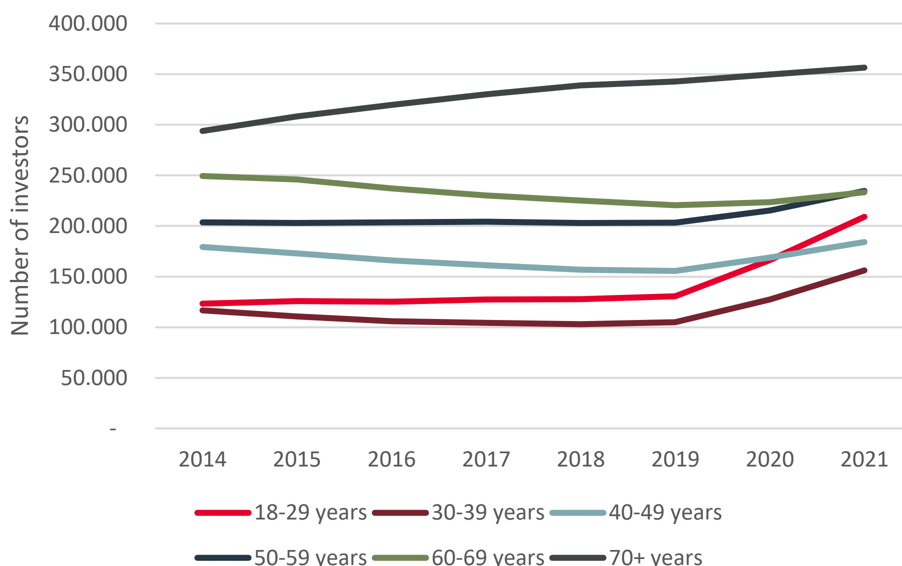
**Number of accounts 2019-2022**




*Source: Data supplied to Finance Denmark by Euronext*

Not surprisingly, the number of investors grow by age groups as savings grow through life. However, numbers from 2020-21 clearly show a sharper rise in the younger generations.

**Number of investors by age groups 2014-2021**




*Source: Tax register data, all Danes having invested free assets*

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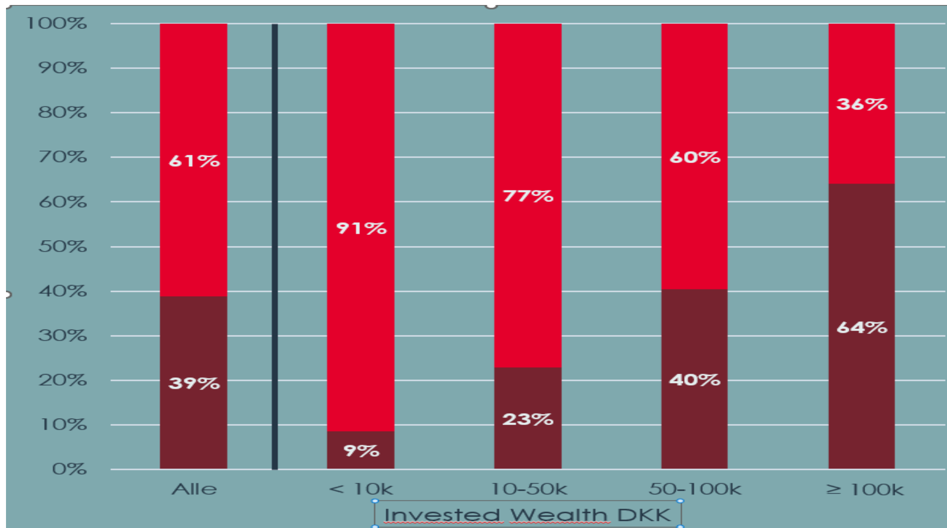
Calculations on the new investors every year from 2014-2021 show that only 5 pct. of new investors disinvest after one year. This illustrates that getting investors engaged will have lasting effects on overall retail participation.

The chart below illustrates the share of investments in funds (brown) and shares (red) in different invested wealth brackets. It clearly shows that the Danish investors increasingly invest in funds, as the invested wealth increases. However, it also shows that "small investors" primarily invest in single shares. The latest academic research on tax register data shows that retail investors do not diversify enough and that they stand to lose 1,5 pct. in yearly returns due to under-diversification of their free assets[8].

[8] danske-investorers-spredning-af-aktierisiko.pdf (danskebank.com). We can provide an unofficial English translation upon request.




*Source: Tax register data*

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In addition to register data, Finance Denmark has closely followed the product offerings of full-service banks by conducting a yearly case study of their investment product offerings since 2018. The next part of the annex "Finance Denmark case study 2019-2022" elaborates the following points:

- Full-service banks primarily offer their own products, but also provide externally produced investment products (third party products).
- There is an increase in third party investment products offered through full-service banks.
- There is an increase in investment products sold without inducements attached.
- Total costs are decreasing on investment funds across asset classes, however, some costs might have increased as direct fees towards the distributers.
- Customers who chose portfolio management have significantly lower overall risk.
- Customers who chose portfolio management have on average 8 pct. of their investments in single shares as of 2022, while customers who invest in shares based upon advice or execution have 47 pct. in single shares. When also assessing investments in investment funds, customers who chose portfolio management have on average 35 pct. of their capital invested in equity exposure, while customers who invest in shares based upon advice or execution have on average 63 pct. in equity exposure.
- The results support that the product offerings in full-service banks are dynamic and trends towards more third-party products, less commission based on inducements and more low-cost products.

- Product governance rules are considered a cornerstone in these dynamics since the banks evaluate their offerings on an ongoing basis.

# 2 Finance Denmark case study 2019-2022

Finance Denmark has gathered data since 2019 on all retail investors having less than 10 million DKK in investable non-pension assets through the 6 largest full-service banks. Measured on the balance sheet or deposit, they constitute approximately 80 pct. of the market[9]. It should be noted that the case study does not include client holdings in other banks nor holdings placed through investment banks providing execution-only services.



Two data sets were used:
- Portfolio management (managed by the bank due to an agreement between the retail customer and the bank), and
- Execution-only and Advice (managed by the retail client. Could be based upon the retail customer's initiative or due to advice given by the bank)

Only investors with less than 10 million DKK in investable assets were included, to avoid skewing the results. Unfortunately, investments based on execution-only and advice could not be separated in the study.

The following measurement is done in both data sets 2019-2022:

- Client assets by asset type
- Client assets in investment products with and without inducements attached.
- Client assets in investment products which were produced by a third party or internally by a close affiliate.

**Results**

The study shows that 750 billion DKK were invested through the banks in 2022, where 40 pct., 300 billion DKK, were invested through portfolio management agreements, and 60 pct., approximately 450 billion, were invested upon through non independent advice or execution-only. Surveys of Danish retail clients support that roughly 80 pct. are delegating or seeking advice and 20 pct. are execution-only clients. However, looking at the whole market including strictly execution service banks the total use of execution service is much higher (we estimate around 40 percent).

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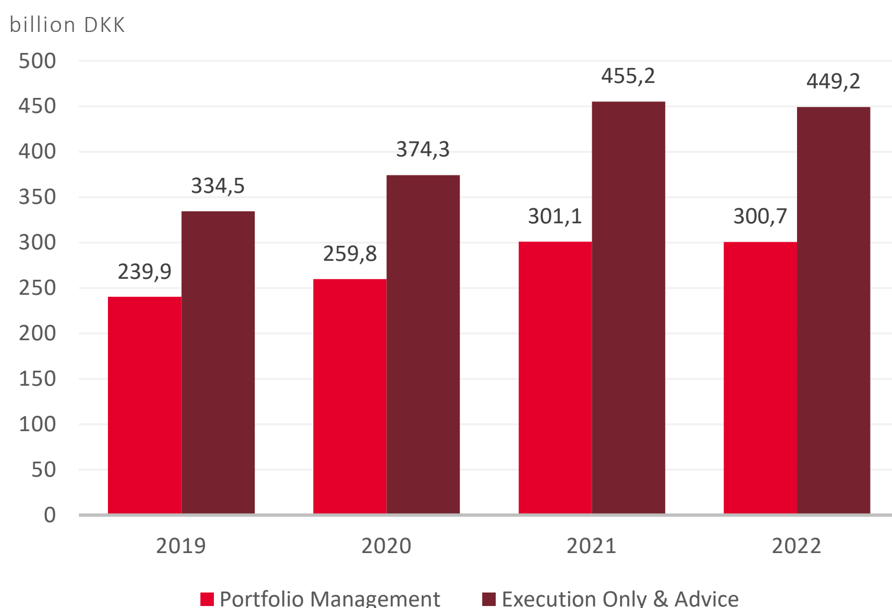
[9] Danske Bank, Nordea Bank, Jyske Bank, Sydbank, Nykredit Bank and Spar Nord Bank.

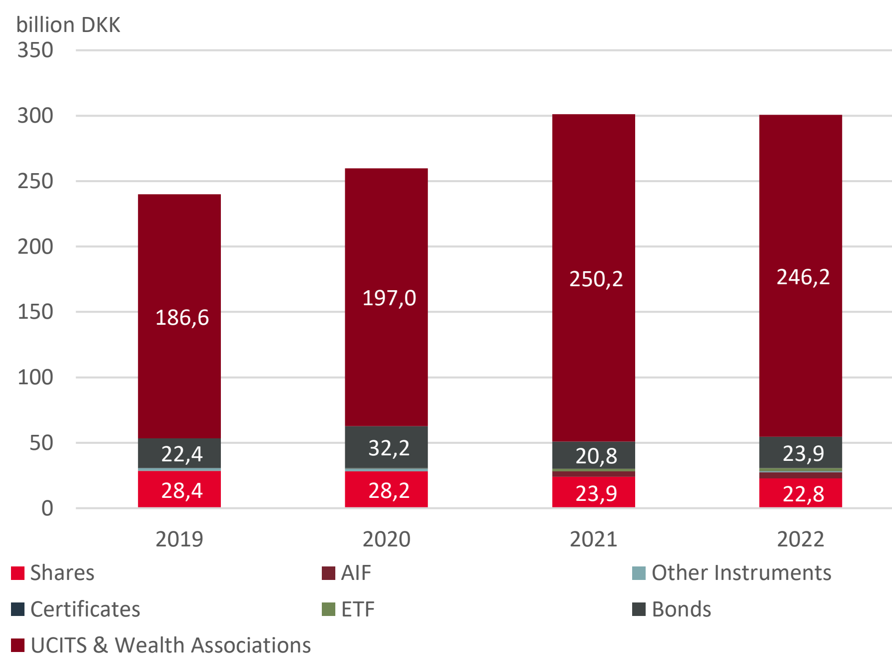
**Retail clients' assets in portfolio management, execution-only and advice**




*Source: Finance Denmark survey of the six largest full-service banks in Denmark*

Of the 300 billion DKK invested through portfolio management, the vast majority, 246 billion, were invested through UCITS investment funds.

**Portfolio Management by asset type**




*Source: Finance Denmark survey of the six largest full-service banks in Denmark*

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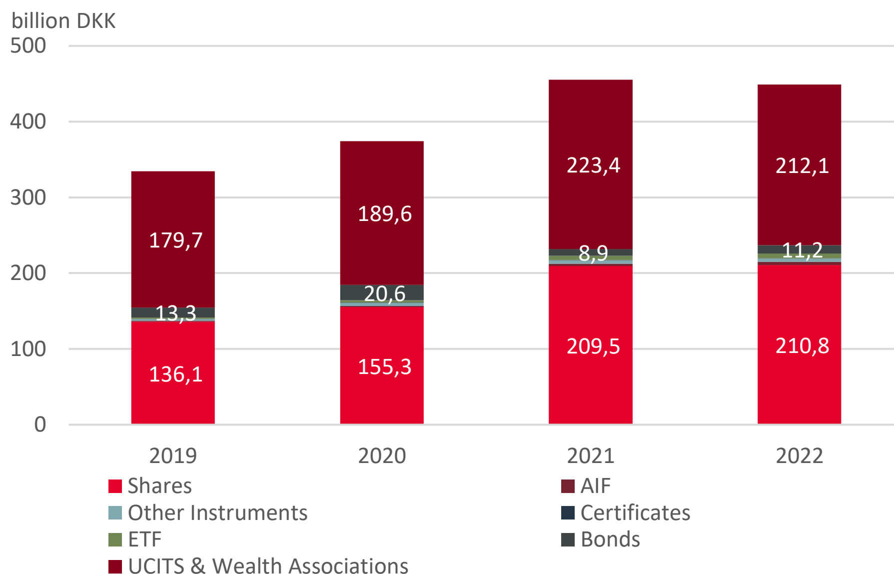
Of the 449 billion DKK invested through execution-only and advice, only half were invested through UCITS funds and almost 50 pct. and a growing percentage are invested in single shares.

**Execution and advice by asset type 2019-2022**

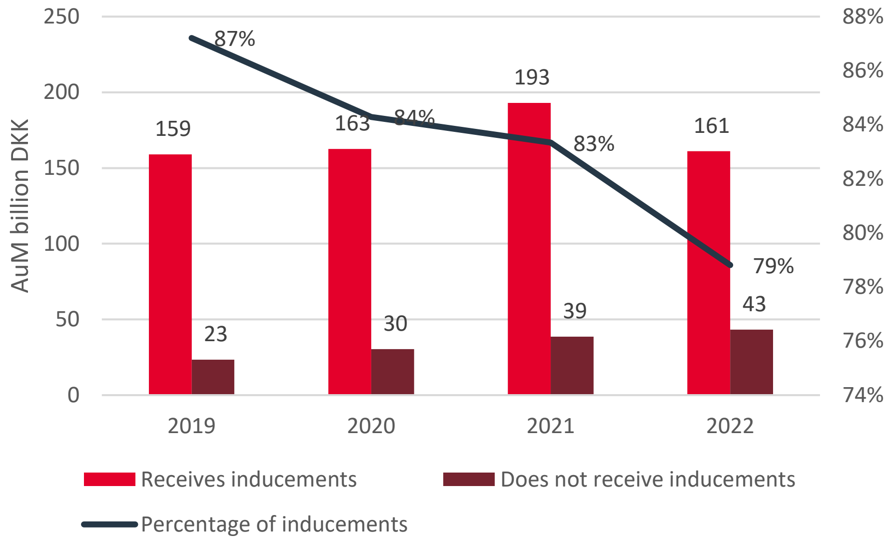



Source: *Finance Denmark survey of the six largest full-service banks in Denmark*

Looking at the funds and focusing on the risk exposure, the differences between portfolio management and execution-only and advice widen. Looking at 2022, the average equity exposure in portfolio management was roughly 50 pct. while 75 pct. in the advice and execution-only segment.

Looking solely at advice and execution-only where inducements are allowed, there is a yearly drop since 2019 in the invested assets in investment funds with inducements attached. This can be explained either in client flows towards products without inducements or by funds that remove inducements as way of payment.

**Investment funds with and without inducements attached 2019-2022**




*Source: Finance Denmark survey of the six largest full-service banks*

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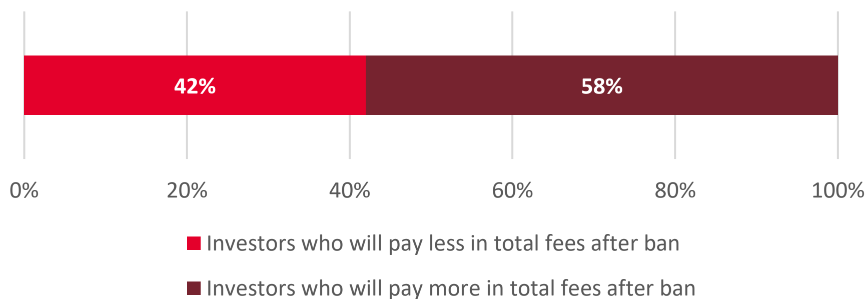
Portfolio management data indicates that the banks primarily sell their own or affiliated produced investment products and that the share of externally produced products is low and without a trend over the period.

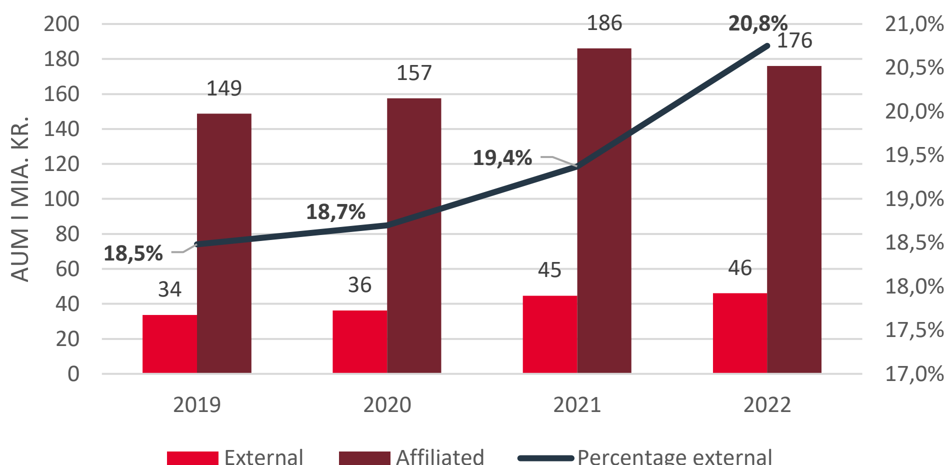
Finance Denmark has estimated that 58 pct. of fund investors will pay more should they pay an annual fee of 180 euros directly to the distributor for investment advice and suitability tests instead of through inducements. This estimate does not take tax and VAT into account which would result in an even larger percentage being better off paying through inducements.




*Source: Estimate from Finance Denmark based on client holdings from tax registers and average market inducement rate*

Looking at advice and execution-only, the share of externally produced products grow every year since 2019. The result implies that the retail investors buy more investment products produced by competing investment banks and their affiliates than previously, 20,8 pct. in 2022.

**Execution and Advice - AuM put in affiliate investments**




Source: *Finance Denmark survey of the six largest full-service banks in Denmark*

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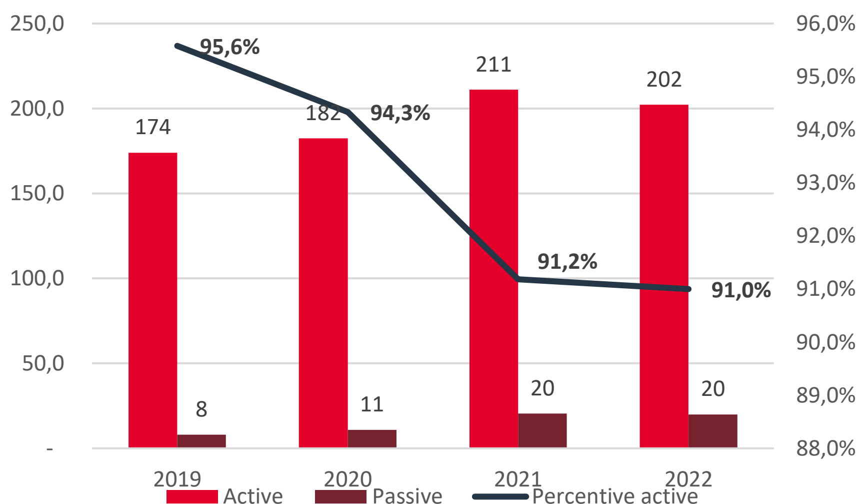
**Execution and Advice – investment funds overall strategy (Active/Passive)**

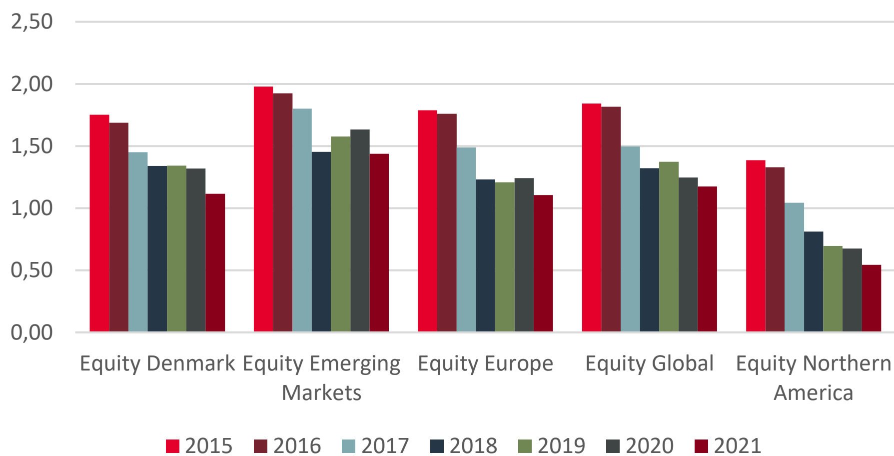



Source: *Survey of the six largest full-service banks in Denmark*

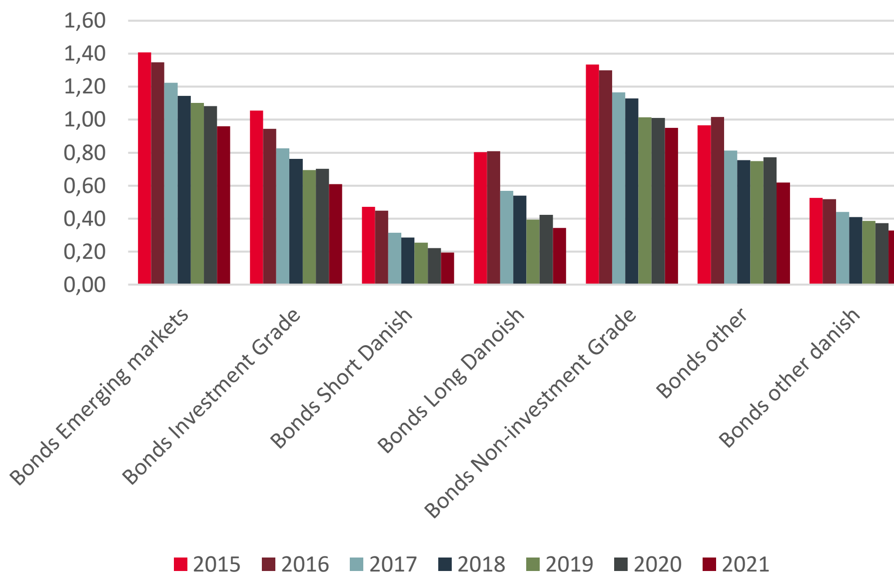
Looking at execution and advice we also see a trend towards more passive and low-cost investment funds and looking at the average product costs of the retail investor, it has fallen over a long period across asset classes. There might have been a shift towards more direct payment for distribution services that is not captured by the product costs alone.

Focusing only on the product costs of investment funds offered to retail clients, we see a strong falling trend in the costs in the period 2015-2021. These are actual cost data from funds annual accounts gathered yearly since 2015 by Finance Denmark. The total cost measure is a Danish measure which includes all fund costs components. Entry and exit costs are spread over 7 years for comparability reasons. There is a clear falling trend throughout the period 2015-2021 within almost alle fund categories in the Danish retail funds.

**Total cost (AuM weighted) - Equity funds targeted retail clients**




**Total cost (AuM weighted) - bond funds targeted retail clients**

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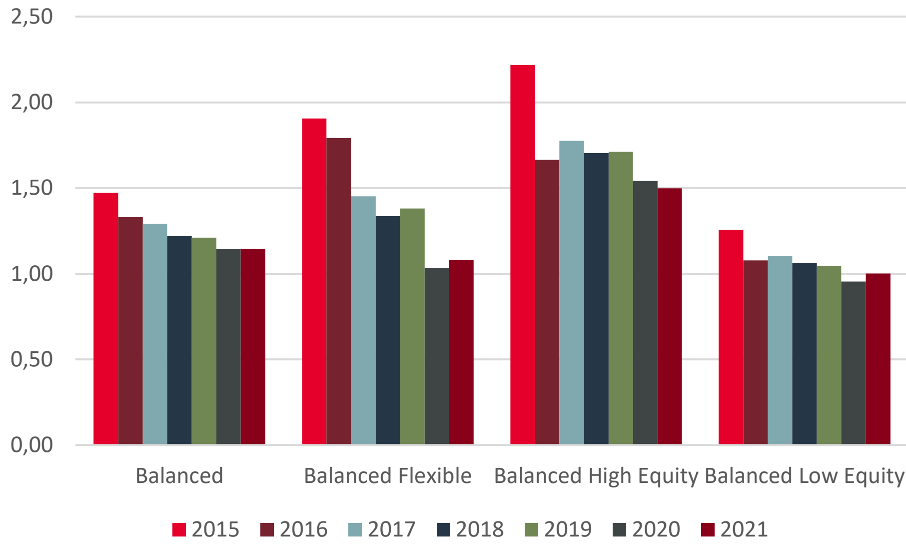
**Total cost (AuM weighted) - balanced funds targeted retail clients**




Source: *Finance Denmark funds statistics*

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