



# **Evaluation of Directive 2002/65/EC on Distance Marketing of Consumer Financial Services**

Annex 1 - Case studies

Written by ICF Consulting Limited  
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and Consumers*

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# **Evaluation of Directive 2002/65/EC on Distance Marketing of Consumer Financial Services**

Annex 1 - Case studies

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## **List of abbreviations**

BEUC	Bureau Européen des Unions de Consommateurs (The European Consumer Organisation)
CCD	Consumer Credit Directive
CWA	Credit Worthiness Assessment
DG FISMA	Directorate-General for Financial Stability, Financial Services and Capital Markets Union
DG JUST	Directorate-General Justice and Consumers
DMFSD	Distance Marketing of Consumer Financial Services
EBA	European Banking Authority
EBIC	European Banking Industry Committee
EC	European Commission
ECB	European Central Bank
ECD	e-Commerce Directive
ECJ	European Court of Justice
ECRI	European Credit Research Institute
EEC	European Economic Community
EIOPA	European Insurance and Occupational Pensions Authority
EPD	e-Privacy Directive
ESMA	European Securities and Markets Authority
EU	European Union
EUR	Euro
FIN-NET	Financial Dispute Resolution Network
FSUG	Financial Services User Group
GDPR	General Data Protection Regulation
HCC	High Commercial Court
IDD	Insurance Distribution Directive
MCD	Mortgage Credit Directive
MFI	Monetary Financial Institutions
OPC	Open Public Consultation
PSD I	Payment Services Directive I
PSD II	Payment Services Directive II
UCPD	Unfair Commercial Practices Directive
UCTD	Unfair Contract Terms Directive
UK	United Kingdom

## **1 Introduction**

This is the Annex 1 to the Final Report of the Evaluation of the Directive 2002/65/EC on Distance Marketing of Consumer Financial Services (DMFSD), a study launched by the European Commission, Directorate-General for Justice and Consumers (DG JUST) in May 2019 and carried out by ICF Consulting Services Ltd (ICF).

This Annex provides the ten case studies that were carried out in the context of the evaluation, which were developed to compile and examine the data collected in the evaluation on:

- DMFSD provision of pre-contractual information;
- Challenges in the protection of consumers and the level playing field, the impact of withdrawing the DMFSD and existing gaps (and possible measures) on the sub-sector of intermediaries and on the market for distance selling of each of the following financial products/services: virtual currencies, peer-to-peer lending, payday loans/cash advances, savings accounts, investments, insurance (non-life and life), credit cards, money transfers and payments.

The ten case studies are:

- Case Study 1: Pre-contractual information
- Case study 2: Intermediaries
- Case Study 3: Virtual Currencies
- Case Study 4: Peer-to-peer lending
- Case Study 5: Pay-day loans
- Case Study 6: Savings account
- Case Study 7: Investments
- Case Study 8: Insurances
- Case Study 9: Credit Cards
- Case Study 10: Money transfer and payments



## **2 Case Study 1: Pre-contractual information**

### **2.1 Analysis of the transposition of pre-contractual information requirements under DMFSD**

Article 3 of the DMFSD imposes on the supplier of financial services an obligation to provide pre-contractual to a consumer, in good time prior to the conclusion of the distance contract for the provision of a financial service. This information concerns the supplier of the service, the financial service, the terms of the distance contract and the existence of a redress mechanism (see the box below).

#### **Article 3.1 of the DMFSD**

In good time before the consumer is bound by any distance contract or offer, he shall be provided with the following information concerning:

**(1) the supplier:** (a) the identity and the main business of the supplier and its geographical address; (b) the identity of the representative of the supplier established in the consumer's Member State of residence and its geographical address; (c) the identity and geographical address of any other professional dealing with the consumer; (d) where applicable, the trade register in which the supplier is entered and his registration number; (e) where the supplier's activity is subject to an authorization scheme, information on the relevant supervisory authority;

**(2) the financial service:** (a) a description of the main characteristics of the financial service; (b) the total price to be paid by the consumer (i.e. all related fees, charges and expenses, and all taxes paid via the supplier); (c) where relevant notice indicating that the financial service is related to instruments involving special risks related to their specific features or the operations to be executed or whose price depends on fluctuations in the financial markets outside the supplier's control and that historical performances are no indicators for future performances; (d) notice of the possibility that other taxes and/or costs may exist; (e) any limitations of the period for which the information provided is valid; (f) the arrangements for payment and for performance; (g) any specific additional cost for the consumer of using the means of distance communication;

**(3) the distance contract:** (a) the existence or absence of a right of withdrawal, its duration and the conditions for exercising it, including information on the payment of the service provided before withdrawal as well as the consequences of non-exercise of that right; (b) the minimum duration of the distance contract in the case of financial services to be performed permanently or recurrently; (c) information on any rights to terminate the contract early, including any penalties; (d) practical instructions for exercising the right of withdrawal indicating, inter alia, the address to which the notification of a withdrawal should be sent; (e) legal framework taken by the supplier as a basis for the establishment of relations with the consumer prior to the conclusion of the distance contract; (f) law applicable to the contract and competent courts; (g) language of the pre-contractual information and communication with the consumer.

**(4) redress:** (a) whether or not there is an out-of-court complaint and redress mechanism and, if so, the methods for having access to it; (b) the existence of guarantee funds or other compensation schemes.

The introduction of pre-contractual information requirements in the DMFSD aimed to reinforce consumer protection and to allow consumers to evaluate the financial service and make a well-informed decision<sup>1</sup>. Article 4 of DMFSD allows Member States to introduce more stringent rules on prior information requirements and foresees that where there are other provisions in EU law regulating financial services which contain

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<sup>1</sup> Directive 2002/65/EC

information disclosure requirements additional to those listed in Article 3(1), these requirements will continue to apply.

By July 2007 all Member States had transposed the DMFSD requirements on pre-contractual information. The European Commission started infringement proceedings against Spain and Luxembourg for failure to transpose within the period prescribed, the provisions necessary to comply with the DMFSD. However, following the infringement procedures both countries managed to correctly transpose the text of the Directive. Prior to the transposition of the Directive seventeen Member States<sup>2</sup> did not have any rules on information disclosure. On the other hand, eleven Member States had pre-contractual information requirements included in their general consumer protection legislation<sup>3</sup>, e-commerce legislation<sup>4</sup> or other legislation regulating financial services<sup>5</sup>. Thus, at the time of the transposition of the DMFSD most Member States had not regulated the provision of pre-contractual information for financial services sold at distance.

In terms of the transposition of Article 3 of the DMFSD, a number of Member States<sup>6</sup> have adapted the text of the Directive to their national context, while others<sup>7</sup> transposed the provisions verbatim. Most Member States made use of the regulatory choice set out in Article 4(2), either maintaining (more stringent) pre-existing national provisions or introducing more stringent measures on pre-contractual information.

Additionally, some Member States<sup>8</sup> explicitly stated that additional requirements set forth in product-specific legislation on financial services might apply. For instance, Romania required the provision of additional information related to the nature of the payment service, such as the form and procedure for expressing consent, the maximum term for performance, all the coercive measures applicable to a payment instrument and the reimbursement provisions. To clearly identify the financial service provider, Sweden required the provision of their telephone number or email address to the consumer. Similarly, Spain<sup>9</sup> requested that where a representative of the supplier established in the consumer's Member State of residence intervenes, it is necessary to provide all the information contained in Article(3)(1)(1A), including their telephone number, fax number and, where appropriate, the consumer's email address. Bulgaria<sup>10</sup> and Portugal<sup>11</sup> established that the pre-contractual information, the terms of the contract and all other communications regarding the contract shall also be given to the consumer in their own national language.

Italy has also introduced more stringent provisions on prior information requirements for financial services, as per Article 4(2). In particular, the service provider shall inform the consumer of the essential characteristics of the security requirements for the payment transaction and, in case of links with other financial services, they will expressly state the effects deriving from the eventual combination<sup>12</sup>. Slovenia establishes that any violation or non-disclosure of the pre-contractual information automatically constitutes unfair commercial practice, while Slovakia states that the obligation to inform the consumer can neither be overridden by invoking trade or professional secrets, nor limited or removed by contractual provisions<sup>13</sup>.

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<sup>2</sup> AT, BG, CY, CZ, DE, FI, FR, HR, HU, IE, IT, LT, LU, MT, PL, RO, SI

<sup>3</sup> EE, LT, SK, UK, BE, GR, NL, ES, SE

<sup>4</sup> PT

<sup>5</sup> DK

<sup>6</sup> For example, BG, DK, FI, PT, SL

<sup>7</sup> For example, HR, LT, LU

<sup>8</sup> For example, IT, RO, SK, NL

<sup>9</sup> Article 7(1) ADMCFs (see factsheet in Annex 8).

<sup>10</sup> Article 8(4) Distance Financial Services Act (see factsheet in Annex 8).

<sup>11</sup> Article 9 DL 95/2006 (see factsheet in Annex 8).

<sup>12</sup> Article 67-sexies Consumer Code (see factsheet in Annex 8).

<sup>13</sup> Article 6, Para 3 of GO 85/2004.

Article 5 of the DMFSD completes the legal framework laying down the rules on the communication of the contractual terms and pre-contractual information. Thus, this provision requires the pre-contractual information to be provided on paper or on another durable medium available and accessible to the consumer in good time before the consumer is bound by any distance contract or offer. This provision was correctly transposed by all Member States. The requirement of a timely communication of all contractual information on paper or on another durable medium was transposed verbatim by seventeen national legislators<sup>14</sup>. Many Member States<sup>15</sup> on the other hand, have imposed additional requirements for the communication the contractual terms and conditions and in some cases have also imposed a penalty where this obligation is not sufficiently met. Additionally, some Member States<sup>16</sup> have provided for additional rules on the consequences of non-compliance with the provision of pre-contractual information, including the invalidation of that the contract on the financial services in favour of the consumer.

Most Member States did not provide further clarification on the interpretation of “in good time before the consumer is bound by any distance contract or offer”. However, the Romanian transposition of the DMFSD states that the provider has to communicate the pre-contractual information and conditions in good time before the user becomes part of an agreement or an offer, and in any case within a timeframe that cannot be shorter than 15 days. According to the stakeholders consulted the timely provision of pre-contractual information depends on the type of financial contract negotiated. For example, with regard to consumer credits, the stakeholders consulted consider that this pre-contractual information should be provided rather short before the contract is actually concluded.

## **2.2 Analysis of existing jurisprudence**

The provisions of pre-contractual information (together with the right of withdrawal) is the legal obligation that have triggered most of the DMFSD-related case law at national level.

Most of existing case law was related to:

- Whether a website qualifies as durable medium; and
- The compliance with the requirement of timely communication of the pre-contractual information to the consumer in a durable medium.

In Bulgaria for example, the Bulgaria’s Sofia Regional Court<sup>17</sup> decided on a case on pre-contractual information on loans provided through a website. The loans were given by a website with a Bulgarian domain that did not contain the address of its supervisory board and whose language for communication was not indicated. The Court concluded that this constituted a minor violation of the national provisions transposing Article 3 of the DMFSD. However, the Court stated that the incompleteness contested by the consumer was insignificant and did not affect his rights, nor did it compromise his right to decide whether the applicant company has an authorisation for the service offered by the competent supervisor. The Court decided that that all of the essential information had been made public and revoked the administrative penalty initially imposed by the Consumer Protection Commission. Additionally, in another case, a Bulgarian court was asked to rule on an issue related to whether an activation of a confirmation link by a consumer - made available by the provider in the email sent to the consumer with the terms of the contract - could be considered explicit consent. According to the court, activation of a confirmation link is not sufficient to prove that the consumer was aware of the terms of the contract or that the consumer explicitly accepted them.

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<sup>14</sup> EE, AT, HR, CY, DK, FI, HU, IT, LT, LU, PT, RO, UK, BE, CZ, ES, SE

<sup>15</sup> BG, FR, EL, MT, NL, RO, SK, ES.

<sup>16</sup> For example, IR, EL, MT

<sup>17</sup> Decision No. 172218/14 July 2017 of Sofia Regional Court (Софийски Районен Съд).

In Slovenia<sup>18</sup> in 2018, a court was asked to rule on whether a credit institution had provided enough information on the risks of a loan taken in a foreign currency. The court ruled that contract terms of a credit agreement need to be written in clear and understandable language, which means that financial institutions must provide the borrowers with information that is sufficient to make informed decisions. The court concluded that the information received at pre-contractual stage did not allow the consumer to understand the currency fluctuation risks and ruled that this was against the information obligations at the pre-contractual stage, which binds all business entities to provide detailed information that allows consumers to assess the potentially significant financial consequences of those fluctuations. In a similar case in Greece, the court also ruled that providers have a duty to give information to consumers on the dangers associated with the financial services/products.

Regarding the definition of 'durable medium', an Austrian court clarified that such medium must enable the consumer to store the information for as long as this is relevant to safeguard their interests (time of contract negotiations, duration of the contract). The service provider's website must allow the unchanged reproduction of the stored information, with the consequence that the information stored cannot be unilaterally changed by the company<sup>19</sup>.

At EU level, the Court of Justice of the European Union (CJEU) has ruled several times on the definition of "durable medium". In case C-375/15, the CJEU was asked to decide whether information given through an e-banking mailbox is 'provided' (as opposed to merely being 'made available') through a 'durable medium'. The CJEU ruled that the information transmitted by a payment service provider to the e-banking mailbox of the customer constitutes information on a 'durable medium'<sup>20</sup>. However, information concerning changes to a framework contract transmitted by a payment service provider solely through an e-banking mailbox were not considered 'provided' but merely 'made available' to a payment service user. The decision was based on Article 44(1), in conjunction with Article 41(1) and Article 4(25) of Directive 2007/64/EC of the European Parliament and of the Council of 13 November 2007 on payment services in the internal market amending Directives 97/7/EC, 2002/65/EC, 2005/60/EC and 2006/48/EC.

Additionally, in the case C-49/11, The CJEU also had the opportunity to clarify the concept of 'durable medium' in the context of Article 5(1) of Directive 97/7/EC and Article 2(f) of Directive 2002/65/EC. In this case, the CJEU considered that making information accessible to the consumer only via a hyperlink to a website does not mean that that information was 'given' by that undertaking and 'received' by the consumer. Furthermore, the court ruled that a 'ordinary website'<sup>21</sup>, such as that at issue in the main proceedings, cannot be regarded as a 'durable medium' within the meaning of Article 5(1) Directive 97/7/EC nor Article 2(f) of Directive 2002/65/EC (that confirms the definition in that Article). The same approach was followed by the Court of the European Free Trade Association (EFTA) in Case E-4/09<sup>22</sup>, in interpreting the concept of 'durable medium' under Directive 2002/92.

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<sup>18</sup> VSL Sodba II Cp 1926/2017, 21 March 2018.

<sup>19</sup> EFTA-GH, Urteil vom 27 January 2010, E 4-09.

<sup>20</sup> 'Provided that the e-banking mailbox enables the payment service user to store information personally addressed to him in a way which is accessible for future reference for a period of time adequate in the light of the purposes of the information. It must furthermore allow the unchanged reproduction of the information stored, thus preventing the service provider from accessing, modifying or erasing that information. An e-banking mailbox can also constitute a suitable channel for the transmission of information in the form of electronic documents if those documents themselves comply with the requirements of being a "durable medium" and if such a system incites the user to electronically store and/or print those documents through an easily accessible function.'

<sup>21</sup> 'Content services refers to a 2007 report of the European Securities Markets Expert Group (ESME) that distinguishes between 'ordinary websites' and 'sophisticated websites' and that considers some sophisticated websites can constitute a durable medium.'

<sup>22</sup> Case E-4/09 *Inconsult Anstalt v Finanzmarktaufsicht* [2010], EFTA Court Report, p. 86.

## **2.3 Analysis of the enforcement of the transposed provisions on pre-contractual information under the DMFSD**

Member States have opted for different enforcement models. While in some Member States<sup>23</sup> the sole responsibility for the enforcement of the Directive lies with the consumer protection authorities, in other countries<sup>24</sup> this task is entrusted to the regulators of the financial services providers. Twelve countries<sup>25</sup> implemented a combined model, in which consumer rights are enforced by consumer protection authorities, while the financial regulators carry out the controls over the financial service suppliers. In some Member States<sup>26</sup> the provision of the various types of financial services and products, is regulated by different financial regulators, which also share the responsibilities for the enforcement of DMFSD.

All Member States have envisaged administrative fines for non-compliance with the requirement of communication of pre-contractual information. Only five Member States<sup>27</sup> have specifically stated that the breach of information disclosure requirements will carry a fine. The amount of the fine varied significantly across these five Member States. Whereas in Romania the maximum fine is 700 EUR, in France it can reach 15000 EUR for legal persons. Several countries<sup>28</sup> also explicitly stated that their national competent authorities may issue recommendations to the supplier to stop the infringement within a given period and refrain from repeating it in the future. In cases of serious infringement of their obligations under the DMFSD, a temporary ban of the supplier's services was envisaged in four Member States<sup>29</sup>. Some countries<sup>30</sup> have explicitly empowered consumers to treat the contract as null and unenforceable against them if the supplier has failed to fulfil his pre-contractual information obligations. Several Member States<sup>31</sup> have stated that general administrative penalties for breaches of consumers' rights apply also to infringements of pre-contractual information requirements.

## **2.4 Analysis of the coherence at EU level**

### **Relevant product-specific and horizontal EU legislation**

Pre-contractual information requirements are also included in the following product-specific and horizontal EU legislation:

- Consumer Credit Directive (2008/48/EC) (CCD)<sup>32</sup>;
- Mortgage Credit Directive (2014/17/EU) (MCD)<sup>33</sup>;
- Payment Accounts Directive (2014/92/EU) (PAD)<sup>34</sup>;

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<sup>23</sup> EE, BG, CY, FR, LT, RO, GR, SE

<sup>24</sup> AT, HR, DE, IT, LT, MT, SK, UK

<sup>25</sup> DK, FI, HU, IE, PL, PT, SL, BE, CZ, NL, ES

<sup>26</sup> For example, ES, PT, NL

<sup>27</sup> BG, HR, FR, MT, RO

<sup>28</sup> For example, IE, LT, GR, NL

<sup>29</sup> HR, LU, PT, GR

<sup>30</sup> FR, IT, MT

<sup>31</sup> AT, DE, PL, SK

<sup>32</sup> Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers and repealing Council Directive 87/102/EEC.

<sup>33</sup> Directive 2014/17/EU of the European Parliament and of the Council of 4 February 2014 on credit agreements for consumers relating to residential immovable property and amending Directives 2008/48/EC and 2013/36/EU and Regulation (EU) No 1093/2010.

<sup>34</sup> Directive 2014/92/EU of the European Parliament and of the Council of 23 July 2014 on the comparability of fees related to payment accounts, payment account switching and access to payment accounts with basic features (text with EEA relevance).

- Payment Services Directive (2015/2366/EU) (PSD II)<sup>35</sup>;
- Insurance Distribution Directive (2016/97/EC) (IDD)<sup>36</sup>;
- Market in Financial Instruments Directive (2014/65/EU) (MiFID II)<sup>37</sup>;
- Undertakings for the collective investment in transferable securities Directive (UCITS, 2009/65/EC)<sup>38</sup>;
- Alternative investment fund managers Directive (2011/61/EU) (AIFMD)<sup>39</sup>;
- Regulation on packaged retail and insurance-based investment products (EU 1286/2014) (PRIIPs)<sup>40</sup>;
- Prospectus Regulation (Regulation EU 2017/1129)<sup>41</sup>;
- Directive on Investor Compensation Schemes (97/9/EC)<sup>42</sup>;
- Directive on Deposit Guarantee Schemes (2014/49/EU) (DGS)<sup>43</sup>;
- Regulation on a Pan-European personal pension product (PEPP)<sup>44</sup>;
- Electronic commerce Directive (2000/31/EC) (ECD)<sup>45</sup>;
- Unfair Commercial Practices Directive (2005/29/EC) (UCPD)<sup>46</sup>;
- General Data Protection Regulation (EU 2016/679) (GDPR)<sup>47</sup>.

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<sup>35</sup> Directive 2015/2366/EU of the European Parliament and of the Council of 25 November 2015 on payment services in the internal market, amending Directives 2002/65/EC, 2009/110/EC and 2013/36/EU and Regulation (EU) No 1093/2010, and repealing Directive 2007/64/EC.

<sup>36</sup> Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution (recast) (text with EEA relevance).

<sup>37</sup> Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (text with EEA relevance).

<sup>38</sup> Directive 2014/91/EU of the European Parliament and of the Council of 23 July 2014 amending Directive 2009/65/EC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) as regards depositary functions, remuneration policies and sanctions (text with EEA relevance).

<sup>39</sup> Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010 (text with EEA relevance).

<sup>40</sup> Regulation (EU) No 1286/2014 of the European Parliament and of the Council of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (PRIIPs) (text with EEA relevance).

<sup>41</sup> Regulation (EU) 2017/1129 of the European Parliament and of the Council of 14 June 2017 on the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market, and repealing Directive 2003/71/EC (text with EEA relevance).

<sup>42</sup> Directive 97/9/EC of the European Parliament and of the Council of 3 March 1997 on investor compensation schemes.

<sup>43</sup> Directive 2014/49/EU of the European Parliament and of the Council of 16 April 2014 on deposit guarantee schemes (text with EEA relevance).

<sup>44</sup> Regulation (EU) 2019/1238 of the European Parliament and of the Council of 20 June 2019 on a pan-European Personal Pension Product (PEPP).

<sup>45</sup> Directive 2000/31/EC of the European Parliament and of the Council of 8 June 2000 on certain legal aspects of information society services, in particular electronic commerce, in the Internal Market (E-Commerce Directive, ECD).

<sup>46</sup> Directive 2005/29/EC of the European Parliament and of the Council of 11 May 2005 concerning unfair business-to-consumer commercial practices in the internal market and amending Council Directive 84/450/EEC, Directives 97/7/EC, 98/27/EC and 2002/65/EC of the European Parliament and of the Council and Regulation (EC) No 2006/2004 of the European Parliament and of the Council (Unfair Commercial Practices Directive, UCPD) (text with EEA relevance).

<sup>47</sup> Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation) (text with EEA relevance).

The DMFSD is generally coherent with product-specific EU legislation on the provision of pre-contractual information. However, due to an increase number of EU legal instrument regulating information disclosure requirements, a certain degree of overlap between the DMFSD and other pieces of EU legislation was identified. On the other hand, there are only minor inconsistencies between pre-contractual information obligations under the DMFSD and similar obligations under other relevant EU laws.

As mentioned above, the Consumer Credit Directive (2008/48/EC) (CCD) also contains information disclosure requirements for credit agreements. Although there is a degree of overlap between information disclosure requirements under the CCD and the DMFSD, no significant inconsistencies between both legal instruments were found. Under the CCD, consumer credit agreements concluded at a distance are subject to a mix of the pre-contractual rules applicable to consumer credit contracts concluded *inter praesentes* and those that only apply to distance contracts for financial services (see Annex II). Similarly to the DMFSD, the CCD also requires to provide information on the product type, identity and address of creditor/agent, total value and total duration of product and applicable terms, fees and interest rates, existence of withdrawal right as well as the total value of contract, the duration of contract, applicable rates and terms as well as any existing redress mechanisms. Additionally, the CCD provides for a more detailed list of information tailored to the specific characteristic of credit agreements including information on the annual percentage rate of charge together with a representative example, a possible obligation to enter into an ancillary service contract, a warning regarding the consequences of missing payments. One of the main differences between the DMFSD and the CCD is that the latter requires to provide the information in a specific format, the Standard European Consumer Credit Information (SECCI). Under the DMFSD, no specific format for the provision of pre-contractual information is required. Some of the stakeholders consulted stated that as a result of this parallel application of pre-contractual consumers might be overload with information with no added value<sup>48</sup>. However, despite existing overlaps and minor differences between both legal instruments, more than half of the respondents to the survey Business associations, consumer associations and national authorities were of the opinion that the CCD and the DMFSD are complementary and only 16% of the respondents believed that existing overlaps are unjustified.

At EU-level, product-specific pre-contractual information requirements on mortgages are provided for in Article 14 of Mortgage Credit Directive (2014/17/EU) (MCD). Similarly, to credit agreements, the requirements for mortgage credits are partly overlapping, partly more stringent than those set forth under the DMFSD. TH MCD also requires providing the pre-contractual information in a specific format, the ESIS form. All pre-contractual information requirements foreseen under the DMFSD are also contained in the ESIS. Additionally, the MCD also requires providing information on some specific mortgage elements not explicitly mentioned by DMFSD, such as detailed information on each instalment, illustrative repayment table and any additional obligations of the borrower. Nineteen Member States considered that their national legislation on mortgages sets forth more stringent rules on pre-contractual information than the rules on distance contracts for financial services. In line with the findings for CCD, about half of the survey respondents believe that there are synergies between the MCD and the DMFSD and only 14% found overlaps to be unjustified.

Both the CCD and the MCD have gone a bit further than the DMFSD by establishing that credit providers have to provide consumers with an adequate explanation of the pre-contractual information in order to place consumers in a position that enables them to better assess the proposed credit agreements<sup>49</sup>.

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<sup>48</sup> Interviews and position papers of stakeholders

<sup>49</sup> Article 5(6) CCD and Article 16 MCD.

In the context of payment services, the Payment Services Directive 2015/2366 (PSD II) states that its pre-contractual information requirements replace some of the prior information items required by the DMFSD. Thus, pre-contractual information on distance contracts for payment services are only partly regulated by the DMFSD. According to some of the stakeholders consulted, this regulatory regime might be confusing for the consumers rather than informative<sup>50</sup>. Although the pre-contractual information to be provided under the PSD II is partly the same as under the DMFSD, the PSD II also contains more detailed information related to the specific elements of payment services such as the unique identifier that executes the payment order or the form of and procedure for giving consent to initiate a payment order.

Regarding payment accounts, since the Payment Accounts Directive (2014/92/EU) (PAD)<sup>51</sup> expressly refers to pre-contractual information requirements under the CCD<sup>52</sup> and PSD, the type of information to be provided under this Directive also overlaps to some extent with the content of Article 3 DMFSD. For example, similarly to the DMFSD the PAD also requires service suppliers to provide the consumer with information on the corresponding fees for each service. However, the PAD goes a bit further and obliges the financial provider to provide the consumer with a glossary of all applicable terms and with information on the most representative services linked to a payment account, and switching services. Only 6% of the survey respondents believed that existing overlaps between the DMFSD and product-specific EU legislation in the area of payment accounts are unjustified. On the other hand, 41% of the survey respondents found synergies between the DMFSD and other legal instruments regulating payment accounts at EU level.

In the context of insurance contracts, Article 18 of the Insurance Distribution Directive 2016/97 (IDD) guarantees that consumers will be provided with relevant information about an insurance intermediary in good time before the conclusion of an insurance contract. The type of information to be provided under the IDD overlaps to some extent with Article 3(1) of the DMFSD. However, the IDD requires to provide additional insurance-specific information on for instance, the relationship between the intermediary and the insurance undertaking and whether the intermediary provides advice about the insurance products sold, existing voting rights in insurance undertakings, the nature of the remuneration received in relation to the insurance contract and other facts that might create a conflict of interest. One of the stakeholders consulted stated that the relationship between the IDD and the DMFSD with regard to the provision of pre-contractual information should be clarified as the current text of the IDD only refers to the DMFSD in the case of voice telephony communications. According to this stakeholder, it is currently unclear whether the DMFSD applies also to other circumstances or only to situations where the contract is concluded over the phone<sup>53</sup>.

Regulation 1286/2014 on packaged retail and insurance-based investment products (PRIIPs) requires providers to draw up a key information document. The key information document shall be drawn up as a short document written in a concise manner that promotes comparability. In terms of content, the Regulation provides for more stringent information disclosure requirements related to the characteristics of the product, the risk-reward profile and the consequences of cashing in before the end of the term among others<sup>54</sup>. The PRIIPs Regulation states that its provisions apply alongside the requirements foreseen under the DMFSD. According to some of the stakeholders consulted, this approach has translated in practice in the provision of largely identical information twice<sup>55</sup>.

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<sup>50</sup> Interviews and position papers of stakeholders.

<sup>51</sup> Payment Accounts Directive 2014/92/EU.

<sup>52</sup> Article 4(1) PAD.

<sup>53</sup> Survey of business associations, consumer associations and national authorities.

<sup>54</sup> Article 8 of EU Regulation 1286/2014 on packaged retail and insurance-based investment products (PRIIPs)

<sup>55</sup> Interviews and position papers of stakeholders



The EU product-specific legislation on pan-European Personal Pension Product<sup>56</sup> (PEPP) also requires the provision of a key information document to consumers. Similarly to the Regulation on the PRIIPs, pre-contractual information requirements under the PRIIPs aims at providing consumers with accurate, fair, clear and not misleading information in a concise and user-friendly manner that allows them to understand all important terms of the pension product and make comparisons. The pre-contractual information to be provided under the PEPP is very similar to that required under the DMFSD. However, the PEPP goes beyond what is required by the DMFSD and sets out more stringent information disclosure requirements. For instance, the PEPP requires information on the past performance of the PEPP saver's investment option, more detailed information on the nature and features of the product, information on PEPP retirement benefits, on PEPP savers' rights, on the conditions to modify investment option, the possible maximum loss of invested capital, conditions for returns to PEPP savers or built-in performance caps, whether the related loss is covered by an investor compensation or guarantee scheme and requirements related to the pay-out phase.

The EU legislation on investment products and services also provides for stricter provisions on pre-contractual information than DMFSD. General investor protection rules of the Market in Financial Instruments Directive (2014/65/EU) (MiFID II) require investment companies to inform their clients of whether the advice is provided on an independent basis and whether it is given on the basis of a broad analysis of financial instruments<sup>57</sup>. Such information is not included in Article 3(1) of DMFSD. Nonetheless, some of the information to be provided under the MiFID II (e.g. information on risks and all costs and associated charges) overlaps with the rules contained in the DMFSD. In the case of undertakings for collective investment in transferable securities (UCITS), investment companies are required to draw up a key investor information document<sup>58</sup>. The European legislator followed the same approach as in the PRIIPs and PEPPs. Thus, the UCITS requires investment companies to provide information on the essential elements of the UCITS in a concise manner and in non-technical language to allow consumers to make comparisons and take an informed decision. While some of the pre-contractual information requirements overlap with the requirements foreseen under the DMFSD, the format in which the information has to be provided is different. In the context of the acquisition of securities, the Prospectus Regulation (Regulation EU 2017/1129)<sup>59</sup> requires publishing a prospectus with pre-contractual information before offering the securities to the public. A European Commission delegated act lays down the content requirements of this prospectus, which are very specific to this type of investment product<sup>60</sup>. Unlike the DMFSD, the Prospectus Regulation allows to make available the prospectus in electronic form on the websites of the issuer, of the financial intermediaries or of the regulated market. The DMFSD on the other hand, requires the pre-contractual information to be provided (and not just made available) on paper or another durable medium<sup>61</sup>. With regard to Alternative Investment Funds (AIF), EU product-specific legislation also includes some specific pre-contractual information requirements not foreseen under the DMFSD provisions, such as a description of the procedures by which the AIF may change its investment strategy, a description of the

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<sup>56</sup> Article 26 of Regulation (EU) 2019/1238 on a pan-European personal pension product (PEPP)

<sup>57</sup> Article 24 (4) (a) (i) (ii) Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU

<sup>58</sup> Article 78 of Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS)

<sup>59</sup> Regulation (EU) 2017/1129 of the European Parliament and of the Council of 14 June 2017 on the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market, and repealing Directive 2003/71/EC

<sup>60</sup> Commission Delegated Regulation (EU) 2019/980 of 14 March 2019 supplementing Regulation (EU) 2017/1129 of the European Parliament and of the Council as regards the format, content, scrutiny and approval of the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market, and repealing Commission Regulation (EC) No 809/2004.

<sup>61</sup> Article 21 of Regulation (EU) 2017/1129

AIF's liquidity risk management and the historical performance of the AIF<sup>62</sup>. Other elements required by the Directive on AIF overlap with Article 3(1) of DMFSD, such as the identity of the Alternative Investment Funds Manager, the description of all fees, charges and expenses.

Overall, the DMFSD is complementary to other horizontal EU legislation with regard to the obligation to provide pre-contractual information.

Overall, there are clear synergies between the Unfair Commercial Practices Directive (2005/29/EC) (UCPD) and the DMFSD. While the UCPD does not contain any obligation to provide pre-contractual information, it defines what is understood by misleading commercial practices by making a reference to the kind of information that shall be provided to consumers. In this context, Annex II to the UCPD expressly refers to the content of Articles 3 and 4 of the DMFSD to describe what constitutes material information that, if omitted, may lead to a misleading commercial practice.

The General Data Protection Regulation (EU 2016/679) (GDPR) complements the content of the DMFSD. While Article 3 DMFSD makes no reference to the provision of information on the collection and processing of personal data, Articles 13 and 14 of the GDPR have added additional information disclosure requirements by establishing an obligation to provide information on the processing of personal data. However, the GDPR does not provide for a format or specific requirements for the provision of information. While no inconsistencies were found between the DMFSD and GDPR in terms of the protection of personal data, the interaction between the different provisions in both legal instruments could be better clarified.

There is a certain degree of overlap between the DMFSD and Electronic commerce Directive (2000/31/EC) (ECD). In line with the DMFSD, Article 5 ECD legislates the provision of information on the identity, geographical address and all details of the service provider, public registers and supervisory authorities, requirements for regulated professions and costs. However, unlike the DMFSD, the ECD does not cover voice telephone communications and only requires the information to be provided in a way that allows the recipient to store and reproduce it (the DMFSD requires the pre-contractual information to be provided in paper or any other durable medium).

## **2.5 Analysis of the implementation of the provisions on pre-contractual information under DMFSD**

The level of compliance with providing the pre-contractual information required by DMFSD in good time appears to be moderate based on the evidence gathered in the study through the OPC, consumer survey and mystery shopping complemented with the views of the consumer associations and national authorities consulted.

Overall, 58% of the national authorities consulted consider that providers comply with the information requirements (with only 14% disagreeing with the statement). When asked about whether they agreed that consumers are provided with comprehensive and correct information at pre-contractual stage, more than 60% of the national authorities agreed (with 25% not agreeing nor disagreeing), while only one third of the consumer associations did so (one remaining third disagreed, while the other third stated that they did not agree nor disagree).

The compliance with the pre-contractual information varies with the type of information that needs to be provided (about the service/product, the supplier, terms and conditions).

Regarding the data on the characteristics of the service, the data gathered through the consumer survey indicates a level of compliance with this requirement of around 80%,

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<sup>62</sup> Article 23 of Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010

however in 20% of the cases the information was available on request. The evidence collected through the mystery shopping exercise suggests a lower, but still moderate, level of compliance with the requirement to inform consumers about the main characteristics of the service at pre-contractual stage (about 60% on average for all products/services covered, around 70% the travel insurance and current accounts, and only 45% for credit cards). According to the data collected through the mystery shopping exercise, the compliance level with the requirement to give information about the supplier to consumers is moderate-high, as on average 85% received information about the identity of the supplier, 71% about the main business of the supplier and 61% about the geographical address.

The consumer survey indicates a high level of compliance (around 74%-83% depending on the type of information, with 83% reporting having received information about the right of withdrawal and its conditions) with the requirement to inform consumers about the terms and conditions of the contract, but in 13%-20% of the cases the consumer had to request the information from the provider. The mystery shopping exercise suggests a much lower level of compliance of around 40%. The compliance level with the requirement to provide information about the right of withdrawal reported by the mystery shoppers is however around 55%.

Regarding the requirement to provide information about redress mechanisms, consumer surveys reported a compliance rate of 70%, while data from the mystery shopping suggests that only in 30% this information is provided.

Data from the consumer survey and mystery shopping suggests that pre-contractual information is commonly spontaneously disclosed to consumers<sup>63</sup>. Pre-contractual information is also usually provided in "good time" before the signature of the contract according to the consumers surveyed in the context of the OPC and consumer survey and to the results of the mystery shopping (in a significant share of the cases the information is provided by default on the website of the provider). While the majority of the national authorities consulted also agree with this, half of the consumer associations consulted consider that consumers are provided with the relevant information in good time before the consumer is bound by a contract.

More than 40% of the national authorities consulted indicated that "the information provided before the signature of the contract was not comprehensive and did not cover all relevant obligations of the consumer" as a problematic issue faced by consumers in the context of the DMFSD. Several factors affect the provision of pre-contractual information (as part of distance sales) and lead to consumer detriment, including<sup>64</sup>:

- Mode of sale/purchase: some stakeholders highlighted the deliberate omission of information during contract discussions over the phone with prospective customers. This however is not corroborated by the results of the mystery shopping exercise.
- Type of product/service: consumer associations highlighted that some providers of innovative services believe their services are exempt from the definition of financial service in the DFMSD, thus they do not comply with this provision.
- Medium used to provide the pre-contractual information: some providers use their websites or mobile applications to provide the pre-contractual information to users. However, some websites cannot be considered a 'durable medium'. This is corroborated by the results of the mystery shopping since in a vast majority of the cases the pre-contractual information was provided in the website and through no other means (e.g. email or post);

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<sup>63</sup> Consumer survey and OPC carried out as part of this research.

<sup>64</sup> Stakeholder interviews.

- Clarity and comprehensibility of the information and the appropriateness of its presentation to the means of distance communication used: studies show that providers often do not provide the information according to these requirements.

## **2.6 Challenges/opportunities raised by digitalisation on the provision of pre-contractual information**

Asymmetry of information (between consumers and financial providers) hinders the consumer decision-making process and can lead to poor choices and welfare losses or consumer detriment<sup>65,66,67</sup>. One of the main goals of consumer protection policy, therefore, is to remedy information issues.

At the time the Directive was introduced, evidence suggested that a significant share of consumers considered the information they received from financial institutions insufficient<sup>68</sup>, unclear and/or incomprehensible<sup>69</sup>. This is in line with study findings at the time<sup>70</sup>, which noted that the financial services sector is prone to information asymmetry because of<sup>71</sup>:

- Difficulties for consumers in finding information on a service/product before purchase;
- Difficulties for consumers in understanding the technical specifications of the services/products due to their low level of financial literacy and the complexity of certain financial services/products<sup>72</sup>;
- Uncertainty about how the financial service/product will perform (i.e. risk).

The use of distance means of communication and the expected increasing digitalisation of the financial sector were believed to (potentially) exacerbate these information asymmetry problems and malpractice related to information disclosure:

- They foster the development of new complex financial services/products that initially do not have easily accessible references and that may not be covered by existing legislation;
- Consumers might not receive information in a medium that allows for easy safeguarding of information on all of the agreed characteristics of the services/product, sales conditions, rights and duties of the parties, etc.

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<sup>65</sup> Micklitz, H.W., Reisch, L.A. and Hagen, K. (2011). An introduction to the special issue on 'behavioural economics, consumer policy, and consumer law'. *Journal of Consumer Policy*, 34(3), pp. 271-276.

<sup>66</sup> Cartwright, P. (Ed.) (1999). *Consumer protection in financial services (Vol. 9)*. Kluwer Law International BV.

<sup>67</sup> Muller, P., Devnani, S., Heys, R. and Suter, J. (2014). Consumer protection aspects of financial services. Brussels: European Parliament. Directorate-General for Internal Policies.

<sup>68</sup> Eurobarometer 205 (2003) found that around 50% of consumers considered it fairly difficult or very difficult to know beforehand how much borrowing money was going to cost or how well they were covered by insurance policies.

<sup>69</sup> Eurobarometer 205 (2003) found that it was fairly difficult or very difficult for 60% of the respondents to understand information and risks involved with their mortgages, for more than 50% to compare information about different banks, mortgages and bank account charges and features. Almost 60% of the respondents disagreed with the statement 'the information I get from financial institutions is clear and understandable'.

<sup>70</sup> Cartwright, P. (Ed.) (1999). *Consumer protection in financial services (Vol. 9)*. Kluwer Law International BV.

<sup>71</sup> Lumpkin, S. (2010). Consumer Protection and Financial Innovation. *OECD Journal: Financial market trends*, 2010(1), pp. 117-139.

<sup>72</sup> Arianti, B.F. (2018). The Influence Of Financial Literacy, Financial Behaviour And Income On Investment Decisions. *Eaj (Economics And Accounting Journal)*, 1(1), pp. 1-10.

Through the provisions on pre-contractual information (Articles 3, 4 and 5), the DMFSD aimed to address these needs<sup>73,74</sup> by harmonising the information that consumers should receive prior to the conclusion of a distance contract (concerning the supplier, the characteristics of the financial service/product, the contract and consumer rights and redress), including how and when the information should be provided.

Since the implementation of the DMFSD digitalisation brought opportunities but also challenges.

Digitalisation expanded the range of communication channels between consumers and providers and also increased the speed with which information is exchanged. Today, providers use a variety of tools to contact users, provide information and advice 24/7, with or without human interaction, such as websites, smartphone applications, automated chatbots and online tools that allow video, chat and voice calls with the provider. In fact, according to the consumer survey it is nowadays common for financial providers to provide pre-contractual information on their website (38% of the respondents reported that information about the financial product/service was provided by default on the website of the provider).

It is also easier for consumers to search/compare information on financial services either by conducting their own research or by using comparison websites<sup>75</sup> that compile and compare information about offers from various providers and help consumer make more informed and, in principle, better decisions (see case study 2).

Innovations on the technology behind websites, brought new means of displaying information to consumers and tools to help consumers “navigate” through long and complex documentation, search for key information, etc. contributing to deliver a seamless consumer journey experience.

At the same time, digitalisation also brought some challenges, including:

- Introduction of new and more complex financial services/products<sup>76</sup>, some of which are available (mostly) exclusively online (e.g. virtual currencies);
- Increased speed with which consumers can sign a contract and purchase a financial service<sup>77,78,79</sup>;
- New devices and applications that can be used to search, access/receive, read and analyse information, some of which have small screens such as smartphones;
- The possibility to adopt problematic or unfair practices at advertising and pre-contractual stages that to some extent exploit market failures and consumer behavioural biases related for example to difficulties in reading and analysing high amounts of information, the way they interpret and absorb information is influenced by how the information is presented (e.g., colour, font, location, etc) and provided. The European Commission’s ‘Behavioural study on the

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<sup>73</sup> As disclosure and transparency alone may not be sufficient to protect consumers when products are complex and the financial literacy of a consumer is low. See, for example, Lumpkin, S. (2010). Consumer Protection and Financial Innovation: A few Basic Propositions. *OECD Journal: Financial Market Trends*.

<sup>74</sup> Micklitz, H.W., Reisch, L.A. and Hagen, K. (2011). An introduction to the special issue on ‘behavioural economics, consumer policy, and consumer law’. *Journal of Consumer Policy*, 34(3), pp. 271-276.

<sup>75</sup> Lumpkin, S. (2010). Consumer Protection and Financial Innovation. *OECD Journal: Financial market trends*, 2010(1), pp. 117-139. Also mentioned by consumer associations and business association in their position papers. See Annex 1 - case study 2 for further details.

<sup>76</sup> Lumpkin, S. (2010). Consumer Protection and Financial Innovation. *OECD Journal: Financial market trends*, 2010(1), pp. 117-139.

<sup>77</sup> Lumpkin, S. (2010). Consumer Protection and Financial Innovation. *OECD Journal: Financial market trends*, 2010(1), pp. 117-139.

<sup>78</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services.

<sup>79</sup> This aspect was highlighted by the EBA position paper on DFMSD as well as by a few consumer associations and business associations.

digitalisation of the marketing and distance selling of retail financial services' identified several problematic practices related to the way information is presented at pre-contractual stages (see Table 1)<sup>80</sup> that are taking place recently in spite of the existing EU horizontal and product-specific legislation currently in place .

Table 1. Examples of industry misleading and unfair practices related to the way information is presented at pre-contractual stages

Stage	Practice	Description
	Benefits emphasised while costs are hidden or given lower prominence	Product features and pricing structures are not transparent, emphasising benefits while hiding costs.
	Key information missing or difficult to find	Key information about the product is not available or is difficult to find (e.g., findings from the mystery shopping carried out in the context of this evaluation (see Annex 5) shows that 13% of the mystery shoppers found it "quite difficult" or "very difficult" to find information about the products)
	Information complex and difficult to understand	Information is presented in a manner that is complex and difficult to understand, for example by using jargon or complex terms (e.g., the findings of the mystery shopping carried out in the context of this evaluation (see Annex 5) show that 14% of the mystery shoppers found that the available information about products was "quite difficult" or "very difficult" to understand)
Pre-contractual	Information layered and located in places that can be overlooked	Placement of important information in sections that can be easily overlooked by consumers
Pre-contractual	Information format not adapted to the medium used	The information provided on the mobile screen is not adapted to the size of the screen (e.g., evidence from the mystery shopping carried out in the context of this evaluation (see Annex 5) shows that 12% of the mystery shoppers using a smartphone app found the information difficult to view and read <sup>81</sup> )

Source: LE Europe (2019)

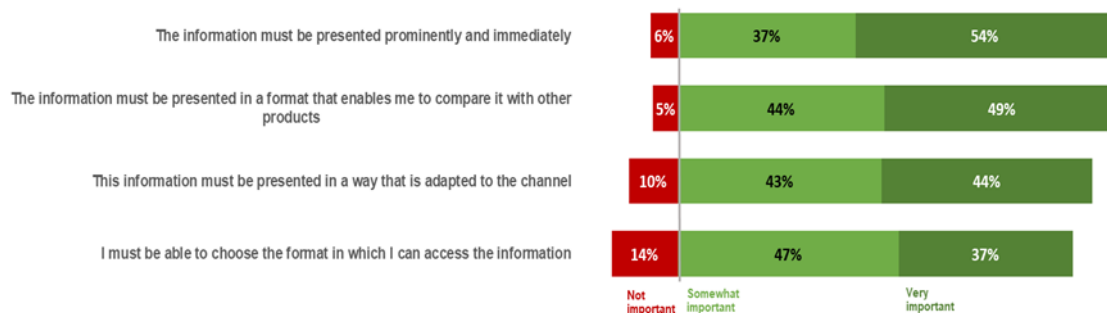
Those challenges coupled with finding from behavioural studies mean that the it is essential "to consider not just whether information is disclosed but how it is disclosed, in what format, and in what context"<sup>82</sup>. This is in line with the views of stakeholders form all groups and with the data collected in the consumer survey (see Figure 1).

<sup>80</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services.

<sup>81</sup> The sample size was 25.

<sup>82</sup> Chater, N., Huck, S. and Inderst, R. (2010). Consumer decision-making in retail investment services: A behavioural economics perspective. Report to the European Commission/SANCO.

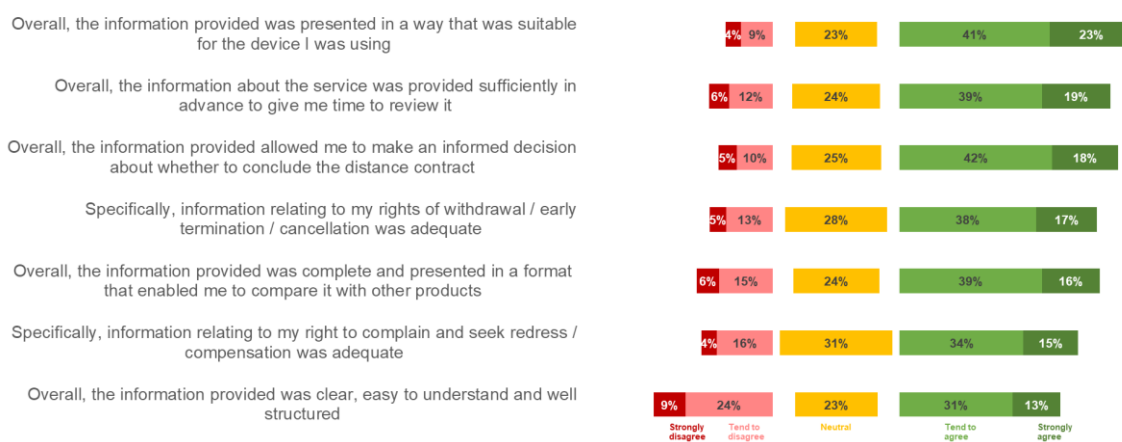
Figure 1. How important would you consider the following statements on the presentation of information?



Source: ICF (2019) consumer survey

The consumer survey shows that although generally information is made available to consumers, about 33% of the respondents considered that the information provided by was not clear, easy to understand nor well-structured and 21% of the respondents indicated that the information they received was not complete nor presented in a format enable them to compare it with information about other products/services (see Figure 2). Some of the reasons that can explain these results are, as mentioned, the emergence of complex financial products, low levels of financial literacy, consumer biases and the adoption (intentionally or not) of poor practices to disclose information by some providers.

Figure 2. To what extent do you agree with the following statements regarding the information you obtained about the financials services?



Source: ICF (2019) consumer survey

As mentioned, a current concern is the exploitation of consumer biases and poor financial literacy by some provider by adopting misleading practices, for example, by (1) using too technical/complex language when providing information, (2) emphasising benefits while giving lower prominence to costs or less favourable aspects of the service/products, and (3) making key information difficult to find by layering it or locating it in places that can be overlooked. While these practices do not go strictly against the DMFSD provision on pre-contractual information, they can hinder its relevance and effectiveness. Current research (as well as some consumer associations, national authorities, consumers and mystery shoppers) proposes remedies to deal with the behavioural biases and improve the ability of consumers to read and understand key information (e.g. simplified descriptions, avoid small print, use of icons, use of traffic

light label for financial risk<sup>83</sup>, use of tables to present the information<sup>84</sup>, minimise the use of hyperlinks<sup>85</sup>, use of pop-ups with warning messages<sup>86</sup>), and consequently promote better decisions.

The need to receive information in a way that enables comparison between services/products does not seem to be fully addressed by the DMFSD (as it is the case in some product-specific legislation<sup>87</sup>). This is becoming more relevant with the proliferation of consolidators and comparison websites for financial services. In fact, this aspect is considered important not only by consumers (including mystery shoppers) but by other consumer associations and EU and national authorities as well, and it is listed by LE Europe (2019) as one of the four key principles to improve consumer decision-making in distance selling of retail financial services. However, legal analysis of the DMFSD recital<sup>88</sup>, scope and the definitions of “distance contract” and of “supplier” (Article 2) concludes that currently the Directive might not apply to all comparison websites but only to those that have a commercial activity and participates in the process of selling financial services/products to the consumers (therefore non-commercial websites and websites that only provide links to the websites of providers seem not to be covered by the DMFSD).

Regarding comparability of information, a few consumer associations and a few consumers mentioned that having a standardised form (as imposed by some product-specific legislation) could improve the comparability of services and help consumers make more better choices. The EBA indicated that the practicality of such form should be taken into account<sup>89</sup>.

Article 3(2) of the DMFSD appears to properly address the need to adapt the information to the device used by requiring that ‘*The information (...) shall be provided in a clear and comprehensible manner in any way appropriate to the means of distance communication used(...)*’. Nevertheless, a few consumers associations, EU<sup>90</sup> and national authorities consider that further guidance on this should be provided. Similarly, LE Europe (2019) recommends that guidelines on how this should be implemented in practice should be developed and communicated to financial providers.

Similarly, stakeholders agree that the requirement that pre-contractual information is provided ‘*In good time before the consumer is bound by any distance contract or offer*’ (Article 3(1)) is very relevant. This is also highlighted by the findings of LE Europe (2019). The EBA, some national authorities and one business association indicated that it could be beneficial to define the timeline more concretely. Consumers reported that the information should ideally be provided by default, for example on the provider’s website and at least 24 hours before signature of the contract.

One point raised by some stakeholders from all groups relates to the relevance of the concept of ‘durable medium’ in a time when the most commonly used means of distance

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<sup>83</sup> Ben-Shahar (2009). European Review of Contract Law, 1; See also Becher (2009). A ‘Fair Contracts’ Approval Mechanism: Reconciling Consumer Contracts and Conventional Contract Law, 42. *University of Michigan Journal of Law Reform*, p. 747.

<sup>84</sup> See LE study and EBA Opinion, 2019. This has also been mentioned by about 5% of the mystery shoppers when asked about their suggestions to improve information disclosure.

<sup>85</sup> See LE study and EBA Opinion, 2019

<sup>86</sup> Mitts, J. (2014). How Much Mandatory Disclosure is Effective? Available at SSRN 2404526.

<sup>87</sup> One business association indicated that having the same standardised form for all financial services would be difficult.

<sup>88</sup> Recital (19) of DMFSD states that: “The supplier is the person providing services at a distance. This Directive should however also apply when one of the marketing stages involves an intermediary. Having regard to the nature and degree of that involvement, the pertinent provisions of this Directive should apply to such an intermediary, irrespective of his or her legal status.”

<sup>89</sup> One business association referred that having one form for all types of financial products might not be feasible.

<sup>90</sup> See EBA Opinion on DMFSD 2019.



communication are websites and mobile apps. Case-law seems to suggest that while some websites can be considered a 'durable medium', others cannot.

## **2.7 Extent to which the DMFSD has impacted providers and their ability to sell at distance**

When the DMFSD was implemented there was limited product-specific legislation in place. Since then, the market and the legal framework developed significantly. Currently, most of the improvements in single market can hardly be attributed to the DMFSD alone.

The DMFSD was expected to achieve the objective of contributing to consolidate the single market by providing a harmonised set of rules applicable to all distance sales of financial services in all EU countries, independently of the type of service/product (i.e., horizontal scope) and of the type of communication mean used (i.e., technology-neutral approach).

Overall, more than half of the consulted stakeholders considered that the DMFSD did contribute to increase the level of harmonisation or convergence between national legislation (35% neither agreed nor disagreed). The opinions among the three groups of stakeholders vary<sup>91</sup>, though. National authorities consulted mostly (about 80%) agreed that the DMFSD had a positive effect on the level of harmonisation of national laws, while only 40% of the business providers and consumer associations thought the same. 29% and 24% of business associations and consumer associations respectively, considered that the DMFSD had no effect on the convergence of national law on distance marketing of financial services. A few mentioning that the possibility of regulatory choices allowed in the DMFSD led to discrepancies between national legislation.

More than 70% of the stakeholders from all groups considered that the horizontal scope Directive effective (with all national authorities and consumer association agreeing). On the other hand, only a small majority of the stakeholders consulted agree that the technology-neutral approach was effective, with opinions among the stakeholders diverging. The majority of the business providers and national authorities consulted considered that this aspect of the DMFSD was effective, while the majority of consumer associations and business associations considered it somewhat ineffective (mostly due to the introduction of product-specific legislation, which on the one hand reduced the relevance of the DMFSD and on the other hand introduced different rules for different product types).

Since the implementation of the DMFSD in 2002, the proportion of sales (in the financial sector) conducted via distance channels has grown rapidly<sup>92</sup> mostly due to the increase of sales conducted over the internet. While the share of cross-border sales has been increasing slowly it is reasonable to assume that most of those sales are carried out over the internet.<sup>93</sup> This is in line with the results of the consumer survey that show that on average about 25% of the purchases of the respondents in the last 5 years were from a provider located in another Member State. There are however slight differences between product types, with investments and payment services being the ones where cross-border sales are more prominent.

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<sup>91</sup> Also in general consumer associations and business associations and providers to that responded to the OPC had less positive views than the ones consulted outside the OPC. One explanation might be that in the OPC stakeholders did not have the option of stating that they were neutral while in the consultation outside the OPC they did.

<sup>92</sup> Civic Consulting of the Consumer Policy Evaluation Consortium (2008). Analysis of the Economic Impact of Directive 2002/65/EC concerning the distance marketing of consumer financial services on the conclusion of cross-border contracts for financial services between suppliers and consumers within the Internal Market.

<sup>93</sup> Increasing digitalisation and globalisation together with European Union initiatives to promote cross-border payments (e.g., arrival SEPA) and sales will contribute to increase cross-border sales of financial services in the near future.

Stakeholders have divergent views on to what extent the DMFSD contributed to increase cross-border distance sales of financial services. The majority of national authorities tend to agree that it had a positive contribution, while more than half of the industry stakeholders and consumer association do not agree nor disagree.

The slower (than expected) uptake of cross-border (financial) sales indicates that while the DMFSD may have provided a basis for furthering the Union's efforts in promoting the cross-border distribution of financial services<sup>94</sup>, there are inherent barriers to the development of an integrated financial market which are beyond the influence of the DMFSD. Such barriers arise from both sides: consumers and business.

Evidence gathered from the desk review and stakeholder consultation<sup>95</sup> indicates that the DMFSD was effective in creating a level playing field and still is to lesser extent due to the implementation of product-specific legislation. This is because the DMFSD provides a minimum set of rules that all financial providers must follow, independently of the type of financial products they sell or the distance means of communication they use. In particular, traditional providers – amid concerns of possible legal loopholes that could lead to unfair competition from unconventional providers (e.g. FinTechs) and services – consider this a significant benefit of the DMFSD. The level playing field at EU level could be improved by ensuring maximum harmonisation of the national transposition of the Directive.

About half of the stakeholders consulted considered that the DMFSD contributed to increase competition and increase the choice of financial services.

## **2.8 Extent to which the DMFSD has enabled consumers to make better informed decisions**

As mentioned above, when the DMFSD was implemented that was limited product-specific legislation in place. Since then the market and the legal framework developed significantly. Currently, improvements in the decision-making process of consumer can hardly be attributed to the DMFSD alone.

Prior to the introduction of the DMFSD, a significant share of consumers considered the information they received from financial institutions insufficient<sup>96</sup>, unclear and/or incomprehensible<sup>97</sup>. This is in line with some studies carried out in 2003<sup>98</sup>, which concluded that the financial services sector is prone to information asymmetry because of<sup>99</sup>:

- Difficulties for consumers in finding information on a service/product before purchase;
- Difficulties for consumers in understanding the technical specifications of the services/products due to their low level of financial literacy and the complexity of certain financial services/products<sup>100</sup>;

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<sup>94</sup> Stakeholder interviews.

<sup>95</sup> More than 80% of the stakeholders consulted agreed that the DMFSD had contributed to creating a level playing field.

<sup>96</sup> Eurobarometer 205 (2003) found that around 50% of consumers considered it fairly difficult or very difficult to know beforehand how much borrowing money was going to cost or how well they were covered by insurance policies.

<sup>97</sup> Eurobarometer 205 (2003) found that it was fairly difficult or very difficult for 60% of the respondents to understand information and risks involved with their mortgages, for more than 50% to compare information about different banks, mortgages and bank account charges and features. Almost 60% of the respondents disagreed with the statement 'the information I get from financial institutions is clear and understandable'.

<sup>98</sup> Cartwright, P. (Ed.) (1999). *Consumer protection in financial services (Vol. 9)*. Kluwer Law International BV.

<sup>99</sup> Lumpkin, S. (2010). Consumer Protection and Financial Innovation. *OECD Journal: Financial market trends*, 2010(1), pp. 117-139.

<sup>100</sup> Arianti, B.F. (2018). The Influence of Financial Literacy, Financial Behaviour And Income On Investment Decisions. *Eaj (Economics and Accounting Journal)*, 1(1), pp. 1-10.

- Uncertainty about how the financial service/product will perform (i.e. risk).

The DMFSD provisions on pre-contractual information were expected to result in “better informed purchases made by consumers” and contribute to achieve the specific objective of ensuring that consumers have better access to pre-contractual information.

The majority of consumer and business associations (more than 55%, with only 6% disagreeing) consider that the DMFSD changed in practice the provision of pre-contractual information. The evidence shows diverse opinions on the effectiveness of information provision at the pre-contractual stage, but overall the majority of the stakeholders from all groups of stakeholders consider that the DMFSD contributed to increase consumer confidence, knowledge and understanding of the products purchased, by encouraging sufficient information disclosure prior to the conclusion of the contract.

A large majority of industry stakeholders consulted (above 80%) considers the DMFSD’s pre-contractual information requirements to be generally effective. The nature, timing and amount of information mandated by the DMFSD at that stage are deemed appropriate, allowing consumers to make confident and/or better-informed purchase decisions.

More than three quarters of the national authorities consulted also reported that the DMFSD provisions on pre-contractual information were effective, with only 8% considering them ineffective. In particular, all consider the requirements to provide information on the provider and on the characteristics of the products and services effective.

Consumer associations are the group with less positive views on the effectiveness of the pre-contractual information, with only 54% agreeing that they have been effective (however only 8% disagreed while 38% were neutral). Based on data from the OPC, the requirements on information to be provided over the phone and about the characteristics of the products and conditions were considered by about 60% as somewhat ineffective. These views are mostly related to the fact that providers do not always comply with these requirements and also because of problems experienced by consumers in fully reading and understanding the information they receive (due to consumer bias sometimes exploited by financial provider and poor practices regarding presentation of information).

This is to some extent in line with the results of the mystery shopping exercise. Overall, 7% of the mystery shoppers considered the amount and quality of information poor and 11% fair. The mystery shoppers using smartphone apps were the ones with worst experience and the ones purchasing over the phone with the best experience as none reported that the information received was poor. At the same time, mystery shoppers found that the amount of information and its quality was better in the case of purchases with traditional providers followed by intermediaries. Of the mystery shoppers that simulated the purchase of services online domestically and cross-border and using smartphone apps considered information about:

- Products: difficult to find in 14% of the cases and to understand in 14% of the cases;
- Provider: difficult to find in 19% of the cases and to understand in 14% of the cases;
- Terms and conditions: difficult to find in 37% of the cases and to understand in 22% of the cases.

Similarly, when thinking about their last experience of purchasing financial services at a distance, the surveyed consumers generally considered:

- The information provided clear, easy to understand and well-structured (44% agreed and 33% disagree);

- The information relating to their right to complain and seek redress / compensation was adequate (49% agreed and 20% disagreed);
- The information provided was complete and presented in a format that enabled me to compare it with other products (60% agreed and 21% disagreed);
- Information relating to their rights of withdrawal / early termination / cancellation was adequate (54% agreed and 18% disagreed);
- The information provided allowed them to make an informed decision about whether to conclude the distance contract (60% agreed and 15%);
- The information about the service was provided sufficiently in advance to give them time to review it (58% agreed and 18% disagreed), with 38% indicated that the information was provided by default and in 31% of the cases more than 24h before having to sign the contract.
- The information provided was presented in a way that was suitable for the device they were using (64% agreed and 13% disagreed).

Notwithstanding the aforementioned positive views of various stakeholders on the effectiveness of the DMFSD's pre-contractual information requirements, there is evidence that the objective of reducing information asymmetries was not fully achieved (as indicated by some stakeholder from all groups). The data collected from consumers and mystery shoppers (see above) together with concerns raised by some consumer associations, national authorities and business associations, highlight that the following main points may have hindered the effectiveness of the pre-contractual provision of the DMFSD<sup>101</sup>:

- *Information overload*: too much information can be detrimental to consumers, who tend not to read lengthy documentation. The pre-contractual requirements of the DFMSD may not lead to better choices simply because consumers do not analyse the information received from providers. Some financial providers have taken advantage of this consumer behavioural bias.
- *Information not presented in a way that helps consumers to read and understand it*: the way information is 'framed' influences the capacity of consumers to read and understand it<sup>102,103</sup>. This is particularly relevant in the context of very complex financial services/products. Existing information disclosure requirements need to be adapted to emerging communication channels, notably digital devices (e.g. smartphones), with at least one in three consumers having searched and/or bought a financial product/service on their mobile phone<sup>104</sup>. While the DMFSD regulates that the information should be '*provided in a clear and comprehensible manner in any way appropriate to the means of distance communication used*', the absence of guidance on how exactly this should be implemented may have reduced the effectiveness of this provision, in particular where providers have exploited these framing biases through irresponsible practices.

The two previous aspects are of particular relevance in the context of comparison tools as the overall of information is often higher (as it is often provided for more than one product at the same time) and the presentation of comparable and comprehensive information between various products is challenging.

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<sup>101</sup> This is applicable only in those cases for which the provision of pre-contractual information is regulated by the DMFSD and not by product-specific legislation.

<sup>102</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services.

<sup>103</sup> See EBA opinion on DMFSD, 2019.

<sup>104</sup> Consumer survey/research.

## **2.9 Analysis of the impact of withdrawing the DMFSD in relation to pre-contractual information**

Since the adoption of the DMFSD in 2002, new product-specific rules have been introduced for the distribution of financial services. In general, as sectors become increasingly regulated, EU laws with a more horizontal and broader scope may lose part of its added value, as it is the case of the provisions on pre-contractual information contained in the DMFSD.

Thus, due to existing overlaps between the DMFSD and product-specific legislation, withdrawing the DMFSD would not have a significant impact on consumers' protection and the providers' ability to sell at distance. As discussed above, product-specific EU legislation already includes most of the pre-contractual information requirements foreseen under the DMFSD and adds more detailed and tailored information to be provided to consumers. Moreover, more recent product-specific EU laws better reflect the current use of digital technologies by allowing for instance, to provide pre-contractual information through a website (i.e. PSD II, PAD, IDD, UCITS, Prospectus Regulation, PRIIPs, DGS, PEPP). However, there are some aspects related to information disclosure requirements that are not covered by some of the product-specific EU laws. For example, in relation to the provision of pre-contractual information in the case of voice telephone communications (Article 3(3) DMFSD), only the IDD, CCD and MCD (which expressly refer to the DMFSD) legislate this aspect. None of the other product-specific rules make reference to the provision of pre-contractual information by voice telephone communications. Additionally, not all of the information listed in Article 3 DMFSD is always required under all product-specific legal instruments. For example, neither the IDD nor MiFiD II contain an obligation to provide information on the existence/absence of a right of withdrawal or on the right of early withdrawal. Similarly, neither the MiFiD II nor the UCITS or AIFMD establish an obligation to provide information on redress. The MiFiD II and the AIFMD do not require information on the public register and supervisory authority to be included in the pre-contractual information provided to consumers. Thus, withdrawing the DMFSD could potentially led to a slight lower protection of consumers with regard to the provision of pre-contractual information for certain financial products.

Additionally, as there are some products that are currently not covered by any product-specific legislation (e.g. savings accounts and credits below EUR 200 and above EUR 75,000), the withdrawal of the DMFSD could have a detrimental effect on consumers as pre-contractual information requirements would not be covered by any EU legal instrument.

## **2.10 Conclusions: gaps, challenges, good practices and recommendations**

At national level, the relevant provisions on pre-contractual information have been correctly transposed by all Member States and some of them have even gone beyond what is foreseen under the DMFSD by establishing more stringent information disclosure requirements. At EU level, the DMFSD is generally in line with other relevant EU legal instruments in the provision of pre-contractual information thus creating a coherent and comprehensive consumer protection framework for the acquisition of financial services sold at distance. However, some minor inconsistencies and existing overlaps between the DMFSD and the other legal instruments have created a risk of legal uncertainty and 'information overload' that may be to the detriment of the consumers' interests. In this context, there is some scope for the simplification of pre-contractual information requirements by streamlining the EU legal framework for financial services and addressing aspects related to the process, means and format through which pre-contractual information is provided to consumers.

The EBA in its opinion paper (2019)<sup>105</sup> and the LE Europe (2019)<sup>106</sup> present detailed remedies on how to address the aforementioned issues related to ensuring that the quality of information and the way it is disclosed (how, in what format, and in what context) lead to an increased capacity of consumers to understand the available information and compare it between products, and so take better decisions. These include:

- Information should be provided in a format that increases the likelihood of consumers noticing and understanding key information and implications of the agreement in terms of financial commitment.
- Drawing attention to key information and displaying it prominently.
- Information should be provided *“in plain and intelligible language and in a readable font size (ideally consumers should be able to increase it), which should easily adapt to work on any kind of device”*. Key information (e.g., fees, withdrawal conditions) should not be displayed in a smaller font size than the rest of the disclosure
- Information should ideally be in an official language(s) of the country
- Information should be provided in *“short and direct sentences, key words, boldface, bullet points, comparative tables or other such features so as to highlight relevant information and improve clarity”*.
- Technical jargons should be avoided, and if used a glossary should be provided in a visible location.
- Disclosure material should be designed in order that key information is noticeable, the size, colour, icons or graphics should be used mindfully of the context and device used.
- Navigation between pages and sections of the website where the information is provided should be easy, intuitive and not misleading. Providers should test the user-friendliness and effectiveness of this area frequently and make the necessary changes if needed.
- When scrolling mechanisms are required, providers must make sure that consumers do not conclude the contract unless they have scrolled down. They should also encourage consumers to do it using a variety of techniques.
- Information should be drafted and simplified with the *“interests, objectives, characteristics and financial capability of the target market for the product or service in question”* and using behavioural insights. Its effectiveness assessed by testing it with the target market and through analysing consumer behaviour.
- *“Chats, chat bots, Q&As, infographics, guides, interactive tools or similar approaches”* should be used to aid consumers.

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<sup>105</sup> Available at: <https://eba.europa.eu/file/147201/download?token=tUEycHID>

<sup>106</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services.

### **3 Case study 2: Intermediaries**

#### **3.1 Evolution of the market**

This case study provides an analysis of the role and relevance of intermediaries in the distance marketing and selling of financial products and services (i.e. marketing and selling online and by telephone, email and fax). Intermediaries are defined as brokers and non-exclusive sellers of financial products and services supplied by third party providers. They also include consolidation, aggregation and comparison websites and services. Intermediaries play a key role in marketing and selling, including distance marketing and selling, of a broad range of financial products and services to consumers including:

- Payment accounts
- Mortgage
- Credit / loans
- Insurance
- Pensions
- Payment services
- Investments

There are different types of intermediaries operating in the EU including: agents, who represent one or more providers of financial services; and brokers or consultants and advisers who work independently to help consumers to identify and make informed decisions about the products and services that are most appropriate for their needs. There are four core types of intermediary providing intermediation between providers of financial services and EU consumers:

- **Tied agents:** agents tied to specific providers of financial services, who are not independent and are likely to receive a salary and/or commission from the providers.
- **Multi-tied agents:** agents tied to multiple providers, who may or may not be independent, but are likely to receive commission from the providers. They may provide their services through aggregator or comparison websites.
- **Brokers:** independent intermediaries, who provide full access to their markets, and may receive a fee from consumers and/or commission from providers. They may provide their services through aggregator or comparison websites.
- **Consultants / advisers:** independent intermediaries, who provide full access to their markets, and are most likely to be receiving fees from their clients. They may provide their services through aggregator or comparison websites.

Intermediaries provide benefits for consumers in terms of reducing their search time and costs and helping them to access products and services that meet their needs. They also provide benefits for providers of financial services in terms of marketing and selling their products to consumers and facilitating entry into new markets without needing their own distribution and retail networks.

The study has found limited data on the size and scale of intermediaries operating in financial services at EU-level. However, the European Federation of Financial Intermediaries and Financial Advisers (FECIF) has provided some consolidated estimates that in 2010 there were 500,000 registered intermediaries operating in the European financial services industry and a further 700,000 professional advisors (such as accountants and lawyers) also providing financial advice to European consumers.<sup>107</sup> FECIF also reported that the number of intermediaries in 2010 had fallen significantly from previous years, by 130,000, as a result of the financial crisis and increasing

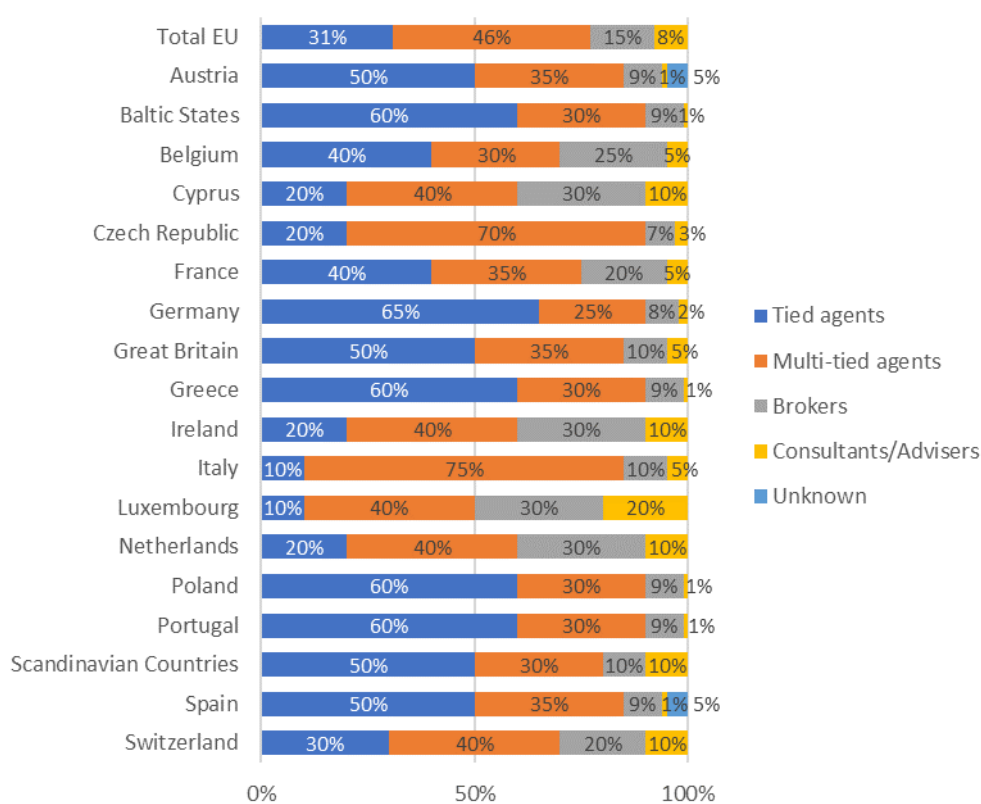
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<sup>107</sup> FECIF response to the Commission's proposals for MiFID/MiFIR 2 of 20 October 2011. Available at: <http://www.europarl.europa.eu/document/activities/cont/201202/20120221ATT38830/20120221ATT38830 EN.pdf>

regulation. The FECIF estimates suggest that most intermediaries are registered in Germany (56%), while Great Britain, Italy, Austria, Czech Republic, Spain, Switzerland and Belgium also have significant numbers of intermediaries, accounting for 34% of the European total.<sup>108</sup> The intermediaries' market share of the financial services industry was also estimated to vary significantly across EU countries. FECIF estimates range from: a 20% market share in Switzerland and the Czech Republic; between 30% and 36% in Germany, Italy and Spain; and a maximum of 51% in Benelux and 56% in the UK.<sup>109</sup>

The FECIF estimates also provide useful information on the structure of the intermediary sector in Europe. Figure 3 shows that most intermediaries (77%) are tied to one or more providers. Overall, it is estimated that 46% of intermediaries are tied to multiple financial services providers, while 31% are tied to a single provider. The other, independent intermediaries are estimated to comprise brokers (15%) and consultants and advisers (8%). Figure 3 also shows considerable variation between countries.

Figure 3. Structure of intermediaries by country



Source: FECIF White Book 2009

The latest FECIF estimates suggest that in 2017 there were approximately 695,000 advisers and intermediaries working in the investments, insurance and banking products sectors across 15 European countries.<sup>110,111</sup> These figures are not directly comparable

<sup>108</sup> FECIF response to the Commission's proposals for MiFID/MiFIR 2 of 20 October 2011. Available at: <http://www.europarl.europa.eu/document/activities/cont/201202/20120221ATT38830/20120221ATT38830EN.pdf>

<sup>109</sup> FECIF response to the Commission's proposals for MiFID/MiFIR 2 of 20 October 2011. Available at: <http://www.europarl.europa.eu/document/activities/cont/201202/20120221ATT38830/20120221ATT38830EN.pdf>

<sup>110</sup> The 15 European countries comprise Austria, Belgium, Czech Republic, Finland, France, Germany, Hungary, Ireland, Italy, Luxembourg, Netherlands, Poland, Slovakia, Spain and the UK.

<sup>111</sup> The European Federation of Financial Advisers and Financial Intermediaries (FECIF) (2017), FECIF White Book 2017. Available at: [http://www.fecif.org/html/fecif\\_white\\_book\\_2017.php](http://www.fecif.org/html/fecif_white_book_2017.php)



with the above figures from 2009 because they focus on only 15 European countries. However, the data do suggest that the number of intermediaries has continued to fall between 2009 and 2017.

With the digitalisation of financial services, three trends regarding the role of intermediaries in the sector can be identified. First the emergence of price and product/services comparison/aggregator/consolidator websites (from now on referred to as comparison websites) for financial services, fostered by the increased abundance of information and offer online. Second, easier and direct access to a wide range of financial provider reducing the need for traditional intermediaries. Third, some disruption of financial intermediation of financial services by FinTechs that offer the services such as peer-to-peer platforms. Consequently, while the importance of traditional intermediaries is falling, innovative solutions to connecting consumers and financial providers operating online have been gaining increased importance<sup>112,113</sup>.

In 2013, according to the mapping of comparison tools across seven sectors carried out by ECME Consortium (2013)<sup>114</sup>, the second largest share of comparison tools was in retail financial services. France was by far the Member State with the highest number of comparison websites in retail finance, followed by Italy, Spain and Germany.

According to EIOPA<sup>115</sup>, comparison websites vary based on a variety of aspects including:

- Purpose: they can be commercial (i.e., for profit) or non-commercial (no profit-making purpose that can be run for example by public authorities or consumer associations);
- Activities: they can provide links to the financial provider, provide quotes/rankings, propose a contract and/or sell the services/products;
- Business model (remuneration): according to ECME consortium (2013) most websites do not charge consumers and the bulk of their revenues are obtained from the providers they list by: a) charging a flat fee to list their services/products (which may be a premium fee to pay for a higher position in the results), b) cost-per-click sellers pay a fee every time a consumer is redirected to their website, b) pay per sale (providers pay when contract is concluded by the comparison website). Comparison websites may also offer their services for free to both consumers and suppliers by getting their revenues from paid advertisement. A less common business model is to charge consumers for a membership fee (this model is mostly used by consumer associations).

The Open Public Consultation for this evaluation provides further insight into the use of distance communication to access financial services. While it does not provide information directly relating to the use of intermediaries, it does help to demonstrate the significant role of intermediaries. For example, the OPC highlights the importance of comparison apps and websites in providing information to consumers of financial products. Information on comparison apps and websites was reported to have been used by one in four OPC respondents to access information on financial products and services (25%), second only to accessing information directly from providers (31%).<sup>116</sup> In 2013, a study from the EC found that 20% of the respondents to a survey that had

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<sup>112</sup> European Commission: EU multi-stakeholder working group. 2013. Multi-Stakeholder Dialogue on Comparison Tools.

<sup>113</sup> EIOPA. 2014. Report on Good Practices on Comparison Websites. Available at: [https://eiopa.europa.eu/Publications/Reports/Report\\_on\\_Good\\_Practices\\_on\\_Comparison\\_Websites.pdf](https://eiopa.europa.eu/Publications/Reports/Report_on_Good_Practices_on_Comparison_Websites.pdf)

<sup>114</sup> ECME Consortium. 2013. Study on the coverage, functioning and consumer use of comparison tools and third-party verification schemes for such tools. European Commission.

<sup>115</sup> EIOPA. 2014. Report on Good Practices on Comparison Websites. Available at: [https://eiopa.europa.eu/Publications/Reports/Report\\_on\\_Good\\_Practices\\_on\\_Comparison\\_Websites.pdf](https://eiopa.europa.eu/Publications/Reports/Report_on_Good_Practices_on_Comparison_Websites.pdf)

<sup>116</sup> OPC

used comparison websites in the last year to compare prices and features of financial services. Overall financial services did not rank very high when compared to other products/services. However, a 2013 study commissioned by the UK's Consumer Futures, found that respondents to their survey reported having used comparison website in the last two years mostly for car (81%) and home (50%) insurances, and to a less extent for travel insurance (32%, ranking 5<sup>th</sup> in all products/services considered in the survey).

Furthermore, the OPC found that the ability to compare information across products was the most important presentational element for the information that is required by the DMFSD.<sup>117</sup> In the same vein, the majority of respondents to the consumer survey indicated that having information presented in a way that allows them to compare services was very important. The London Economics (2019)<sup>118</sup> study also reported that consulted consumers considered comparison websites could *"have the potential to increase the availability of information, make it more understandable for consumers, and increase general awareness"*. This again demonstrates the need of consumers to be able to draw comparisons between different products and services, and highlights a key role and further opportunities for intermediaries to support consumers.

These aggregator/comparison websites can also contribute to some extent to consolidate the internal market<sup>119</sup>, as they can facilitate the access of consumers from one Member State to providers from a different Member States (and vice-versa) and help addressing some consumer and supply side barriers to cross-border sales. The results of the OPC and of the consumer survey highlighted some consumers-side barriers to cross-border purchases of financial services that present opportunities for intermediaries, including language barriers and difficulties understanding and comparing the information provided<sup>120</sup>. On the supply side, intermediaries are well placed to provide solutions to barriers such as entrance costs and cultural/language barriers.

### **3.2 Challenges regarding the DMFSD and differences between intermediaries and non-intermediaries**

Despite the fact that none of the articles of the DMFSD make any reference to intermediaries, Recital (19) of DMFSD clarifies that: *"The supplier is the person providing services at a distance. This Directive should however also apply when one of the marketing stages involves an intermediary. Having regard to the nature and degree of that involvement, the pertinent provisions of this Directive should apply to such an intermediary, irrespective of his or her legal status."*

Therefore, the DMFSD only applies to some comparison websites, depending on their nature and degree of their involvement in one of the marketing stages. Overall, the DMFSD provisions may not apply to websites that only provide a comparison between services/products and that may or not redirect consumers to the websites of the providers. On the other hand, the DMFSD most likely applies to comparison websites that sell the financial services/providers directly to the consumers. This is, however, an aspect that requires further clarification as highlighted by consumer associations and public authorities consulted by this evaluation. This lack of clarity can lead to situations where comparison websites do not comply to the DMFSD because they consider that it does not apply to them given their nature and level of involvement.

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<sup>117</sup> OPC

<sup>118</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. 2019. Behavioural study on the digitalisation of the marketing and distance selling of retail financial services.

<sup>119</sup> European Commission, EU multi-stakeholder working group. 2013. Multi-Stakeholder Dialogue on Comparison Tools.

<sup>120</sup> European Commission, EU multi-stakeholder working group. 2013. Multi-Stakeholder Dialogue on Comparison Tools.

For those cases to which the DMFSD applies there is a general lack of information on the impact of the requirements imposed by the DMFSD on intermediaries. However, intermediaries and providers of financial services are expected to face similar challenges in complying with the DMFSD, although it is also likely that the burdens created by some of these provisions are more significant for intermediaries than they are for other suppliers (non-intermediaries). The different ways in which intermediaries are disadvantaged are described below for each of the key provisions of the DMFSD:

- The provision of pre-contractual information is likely to be more difficult and burdensome for intermediaries because they not only have to provide this information to consumers but must also:
  - Collect and collate the required information from all relevant providers of financial services, ensuring comprehensive coverage across all products and services, and identifying any gaps and inconsistencies;
  - Present the information comprehensively and in a consistent format that enables consumers to draw comparisons between the products and services of different providers;
  - Monitor changes over time and ensure the pre-contractual information is kept up to date for all relevant products and services.
- The 'right-of-withdrawal' creates additional risks and burdens for intermediaries because:
  - It requires additional effort and resource for intermediaries to withdraw from the contractual arrangement with the supplier, as well as cancelling the contract with the consumer.
  - The return of funds to the consumer is more complicated because the intermediary must agree and arrange the return of funds from the service provider as well as from the intermediary as both will have received funds from the transaction.
  - The DMFSD does not provide any additional time for intermediaries to undertake these tasks, despite the increased complexities described above.
- The rules on unsolicited communications and services apply to intermediaries and non-intermediaries and are likely to be equally pertinent and burdensome to both groups. Similarly, the rules regarding unsolicited communications and services are therefore unlikely to create any additional impacts for intermediaries.

The results of the mystery shopping show that overall, an overwhelming share of mystery shoppers consider that the amount of information provided by intermediaries was good, very good or excellent. This is relatively similar to their (85% of mystery shoppers) assessment of the amount of information provided by traditional operators. When analysing the provision of pre-contractual information about the supplier and the terms and conditions, in both cases mystery shoppers reported having received slightly less information elements from consolidator websites when compared to the case of traditional operators.

### **3.3 The impact of withdrawing the DMFSD on intermediaries**

The impact of withdrawing the DMFSD would vary between type of intermediary and between different financial services, depending on the product specific legislation rules relating to:

- the provision of pre-contractual information to consumers;
- the 'right of withdrawal' for consumers entering contracts.

The impact of withdrawing the DMFSD on those intermediaries that currently need to comply with the DMFSD does not significantly differ from the impact on financial providers as there are just a few cases of product-specific legislation not applying to intermediaries. Some exceptions are:

- In the context of PAD, rules to be applied by some comparison websites (at least one in each Member State) are set. However, in general only “payment service providers” and “credit institutions” must comply with the pre-contractual information requirements; and
- In the context of PSD II, the pre-contractual requirements and right of withdrawal only apply to payment service providers.

### **3.4 Potential measures to improve consumer confidence and empowerment**

One important measure would be to clarify to which type of intermediaries and situations the DMFSD provisions do not apply. This should lead to higher levels of compliance and would contribute to increase consumer protection and to strengthen a level playing field between intermediaries and non-intermediaries.

Other measures that could improve consumer protection in the context of comparison websites relate to two key aspects: a) the trustworthiness, transparency, independence and coverage, and b) quality of the information provided, how it is presented to consumers.

Comparison websites can have a very important role in reducing information asymmetries and connecting consumers with providers. However, some comparison websites may adopt practices that can mislead consumers<sup>121,122,123,124</sup>, including:

- The positioning of offers in the displayed search results/list may not be random or based on independent criteria but rather depend on primium fees payed by suppliers. This can mislead consumers as they may assume that the offers are ranked based on their quality or price when it is not the case;
- The coverage of available services might be poor, while consumers may not be aware of that;
- The comparison results are influenced by the incentives the website received from the financial provider, instead being based on clear criteria and on a transparent comparison methodology.

As highlighted by the EU multi-stakeholder working group (2013) there have been important initiatives at EU, national and sectorial level to address this. Nevertheless, the London Economics study highlights that consumers still have concerns over the trustworthiness and quality of the comparison of comparison websites, suggesting that these issues could be addressed if (some) comparison websites would be offered by national institutions (one example the PAD requires that Member States “ensure that consumers have access, free of charge, to at least one website comparing fees charged by payment service providers”).

On the quality of the information provided, the way it is presented to consumers in a clear and structured way that allows them to easily compare offers and how it is up-to-date reflecting the actual offers in the market is also regarded as essential to ensure that consumers are able to analyse and understand the information received and take a good and well-informed decision.

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<sup>121</sup> Bundeskartellamt (Germany's national competition regulator). Available at: <https://webgate.ec.europa.eu/multisite/ecn-brief/en/content/bundeskartellamt-sees-need-action-comparison-websites>

<sup>122</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. 2019. Behavioural study on the digitalisation of the marketing and distance selling of retail financial services.

<sup>123</sup> EIOPA. 2014. Report on Good Practices on Comparison Websites. Available at: [https://eiopa.europa.eu/Publications/Reports/Report\\_on\\_Good\\_Practices\\_on\\_Comparison\\_Websites.pdf](https://eiopa.europa.eu/Publications/Reports/Report_on_Good_Practices_on_Comparison_Websites.pdf)

<sup>124</sup> European Commission, EU multi-stakeholder working group. 2013. Multi-Stakeholder Dialogue on Comparison Tools.

The mystery shopping exercise shows that in general mystery shoppers considered that the quality of information and the quality of the assistance offered by the operators provided by consolidators was generally slightly lower than in the case of traditional operators. Regarding specific information on service, supplier and terms and conditions:

- It was easier to find information on the characteristic of the financial products in consolidator websites than in the websites of traditional operators. However, this information was more difficult to understand in the case of consolidator websites. 12% of mystery shoppers found the information provided by consolidators on the service difficult to understand;
- The available information about the supplier was easier to find on the websites of traditional operators but was equally easier to understand in both cases. 12% of mystery shoppers found the information provided by consolidators on the supplier difficult to understand;
- The information about the terms and conditions made available by consolidators was easier to find and understand than the information provided by traditional providers. 15% of mystery shoppers found the information provided by consolidators on the service difficult to understand.

Improving the aforementioned aspects could help decreasing the share of consumers that have difficulties understanding the available information and increase their protection and help take better informed decisions.

## 4 Case Study 3: Virtual Currencies

### 4.1 Introduction

Virtual currency is a type of digital currency that is only available in electronic form<sup>125</sup>. In the US, the term "virtual currency" started being used consistently around 2009, marking the development of digital currencies and social gaming<sup>126</sup>. There is no single agreed-upon definition of VC<sup>127</sup>. In the EU, the European Central Bank defined virtual money in 2012 as "a type of unregulated, digital money which is issued and usually controlled by its developers and used and accepted among the members of a specific virtual community"<sup>128</sup>. Virtual currencies are digital representations of value are not issued nor guaranteed by a central bank or public authority and consequently they are not (conventional) fiat currency (FC). Virtual currencies are currently mostly used in online games, social networks or as a general payment method where accepted<sup>129</sup>. As these communities are by definition digital, funding methods are typically digital (e-wallets, cards)<sup>130</sup>.

Since 2013 there has been a sharp increase in the popularity and use of decentralised virtual currencies, or cryptocurrencies<sup>131</sup>. The first in its kind was Bitcoin, a decentralised digital currency system that can be traded and exchanged for goods and services at places that accept it<sup>132</sup>. It gained popularity during the financial crisis, as an alternative to the banking system. It has also been popular since bitcoin transactions can be performed in effect anonymously (however, while it takes more effort, in many cases bitcoin users can be identified).<sup>133</sup> As of mid-July 2018, the largest digital currencies by market capitalisation were bitcoin, followed by Ethereum – considerably smaller than bitcoin – ripple, bitcoin cash and EOS<sup>134</sup>. No data could be retrieved describing the most important virtual currencies in Europe, but due to the worldwide spread use of the before-mentioned currencies and the fact that most virtual currencies are new and have a negligible market capitalisation, it is probable that these same virtual currencies are the most used in the EU, as well.

### 4.2 The evolution of the market

In 2002, when the DMFSD was adopted, virtual currencies had yet to be introduced on the market, which would happen eight years later. The pioneer virtual currency, Bitcoin, was first used for a transaction in 2010 after being invented in 2008 and operates as a peer-to-peer network. Currently, there are more than 1,500 virtual currencies although only a few have a meaningful market turnover and capitalisation.<sup>135</sup> According to Statista, the market capitalisation of Bitcoin constituted 53 percent of total market cap of all cryptocurrencies in 2019 (which is a significant decrease from the 2015 share of above 80%).<sup>136</sup>

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<sup>125</sup> <https://www.investopedia.com/terms/v/virtual-currency.asp>

<sup>126</sup> Sutter, John D. (2009). Virtual currencies power social networks, online games"

<sup>127</sup> European Parliament. (2018). Virtual currencies and central banks monetary policy: challenges ahead

<sup>128</sup> <https://dig.watch/issues/e-money-and-virtual-currencies>

<sup>129</sup> ICF former confidential study

<sup>130</sup> ICF former confidential study

<sup>131</sup> ICF former confidential study

<sup>132</sup> ICF former confidential study

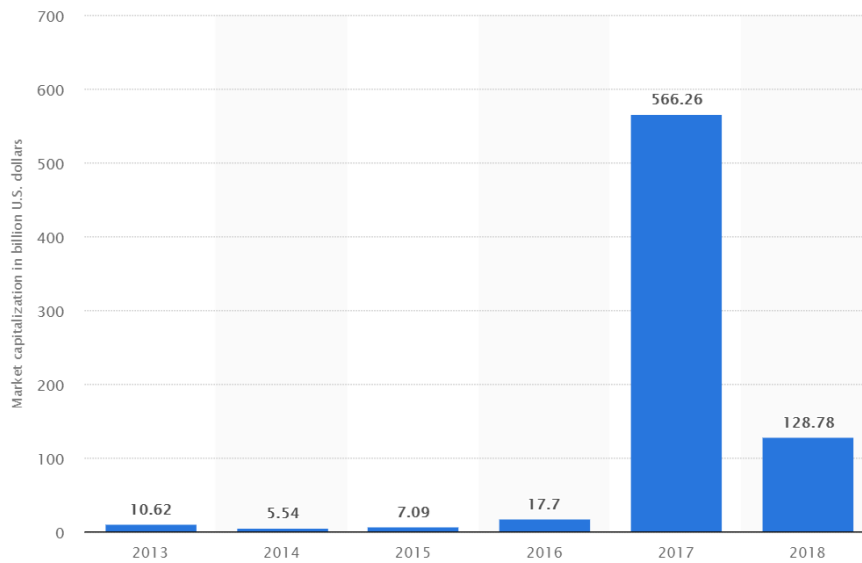
<sup>133</sup> ICF former confidential study

<sup>134</sup> <https://www.investopedia.com/news/top-5-cryptocurrencies-market-cap/>

<sup>135</sup> Dabrowski, M. and Janikowski, L., 2018. Virtual currencies and their potential impact on financial markets and monetary policy. *CASE Research Paper*, (495).

<sup>136</sup> See <https://www.statista.com/statistics/730782/cryptocurrencies-market-capitalization/>

Figure 4. Evolution of the capitalization of cryptocurrencies since 2013



Source: Statista, 2019<sup>137</sup>

Since their invention, the use of virtual currencies has been on an upward trend, with new currencies inspired by Bitcoin entering the market. The total market value of cryptocurrencies is reported to exceed EUR 128 billion worldwide in 2018 (see Figure 4), although daily transactions using virtual currency remained limited as of 2018<sup>138</sup>: "The use of VCs in day-to-day transaction remains negligible. During 2017, the number of Bitcoin transactions in the world was, on average, around 275,000 per day, compared to over nine million card transactions per day in Sweden (Söderberg, 2018) and 295 million traditional transactions per day in Europe in 2014 (EBA, 2014, p. 7)." (Dabrowski, et al, 2018)<sup>139</sup>. According to Encrybit Cryptocurrency Exchange Evaluation Survey, in 2018 33% of the cryptocurrencies traders aged between 15 and 25 years old and preferred to trade using a mobile app.<sup>140</sup>

According to the consumer survey, 29% of the respondents had purchased virtual currencies at distance in the last five years.

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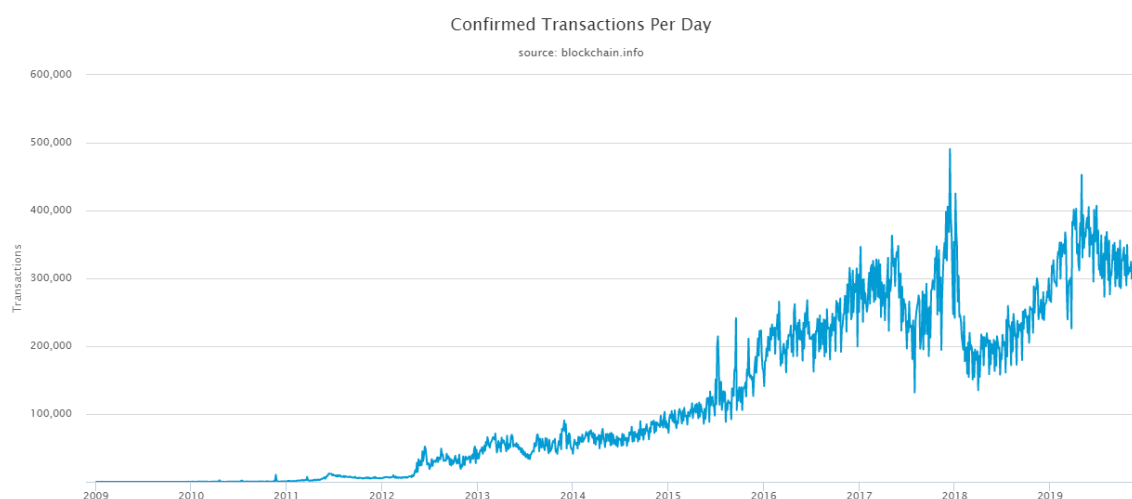
<sup>137</sup> <https://www.statista.com/statistics/377382/bitcoin-market-capitalization/>

<sup>138</sup> European Parliament. (2018). Virtual currencies and central banks monetary policy: challenges ahead

<sup>139</sup> Dabrowski, M. and Janikowski, L., 2018. Virtual currencies and their potential impact on financial markets and monetary policy. *CASE Research Paper*, (495).

<sup>140</sup> <https://medium.com/@enbofficial/encybit-cryptocurrency-exchange-evaluation-survey-2018-timeline-56b77c0d4341>

Figure 5. Evolution of confirmed transactions with Bitcoin



Source: [www.blockchain.com](http://www.blockchain.com), 2019

The future of virtual currencies is uncertain. Some experts believe that the total “market capitalisation of cryptocurrencies could explode over the next five years, rising to \$5-10 [trillion]”<sup>141</sup>. However, some significant barriers persist related to their extreme volatility and legality (three European Supervisory Authorities (the European Securities and Markets Authority, ESMA, the European Banking Authority, EBA and the European Insurance and Occupational Pensions Authority, EIOPA) and some Member States have issued informal warnings against the use of virtual currencies)<sup>142,143</sup>.

While there is no data available on the level of cross-border sales in the EU at the moment, they probably have a high proportion of total sales, since virtual currencies are independent of a particular state and even considered by experts to be a facilitator of cross-border sales<sup>144</sup>. They can be a facilitator in as much as they can offer better, faster and cheaper services and decrease compliance costs<sup>145</sup>. This is in line with the data from the consumer survey, as almost 40% of the respondents that obtained virtual currencies at distance did it from a provider in another Member State. Nevertheless, the London Economics study found that 83% of operators that offered virtual currencies were national operators being established or headquartered in the country where they provide virtual currencies.

Different players are involved in transactions with virtual currencies, including: users (a natural person or legal entity that purchases the virtual coins to use them in future transactions), miners, cryptocurrency exchanges (natural person or legal entity that offer exchange services often charging a fee), trading platforms, wallet providers (provide means to hold, store and transfer virtual coins), coin inventors and coin offerors.<sup>146</sup>

FinTech companies have been playing an important role in fostering the use of virtual currencies. Since a lot of companies active in this sector offer money transfers, they have chosen virtual currencies to streamline payments making them cheaper and

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<sup>141</sup> <https://www.investopedia.com/articles/forex/091013/future-cryptocurrency.asp>

<sup>142</sup> Rose, C., 2015. The evolution of digital currencies: Bitcoin, A cryptocurrency causing A monetary revolution. *International Business & Economics Research Journal (IBER)*, 14(4), pp.617-622.

<sup>143</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>144</sup> <https://finance.yahoo.com/news/cryptocurrency-improve-cross-border-payments-143011743.html>

<sup>145</sup> <https://www.imf.org/en/News/Articles/2017/11/01/sp103017-fintech-and-cross-border-payments>

<sup>146</sup> R, Houben, A, Snyers. (2018). Cryptocurrencies and blockchain. Legal context and implications for financial crime, money laundering and tax evasion.



faster<sup>147</sup>. Virtual currencies display another advantage for FinTech, namely the possibility to be accessible on mobile phones<sup>148</sup>. This option explores the lack of a need in the case of virtual currencies to own a bank account, use physical notes/coins, or access an ATM for financial transactions<sup>149</sup>.

According to the London Economics study, of the 200 providers covered by the study only 9% offered virtual currencies, all of which were new operators.

Table 2. Overview of baseline and endline

Indicator	Baseline	Endline
Sales	Not yet introduced on the market at the time; Bitcoin was invented in 2008 <sup>150</sup> and the first known commercial transaction using bitcoin took place in 2010 <sup>151</sup> . ECB first introduced a definition of virtual currencies product in 2012.	Market value reported to exceed USD 125 billion worldwide in 2018. In 2017 it amounted to more than USD 565 billion. The use of VCs in daily transactions is rather negligible.
Type of provider	Not yet introduced on the market at the time; see sales information on the baseline	Providers tend to be fintech companies; traditional players such as banks are less likely to offer virtual currencies <sup>152</sup>
Most used means of communication	Not yet introduced on the market at the time; see sales information on the baseline	Digital channels
Cross-border sales	Not yet introduced on the market at the time; see sales information on the baseline	No data for cross-border sales. The LE Europe reports that 83% of the operators (covered by the study) offering virtual currencies were domestic.
Main barriers	Not yet introduced on the market at the time; see sales information on the baseline	High volatility and limited historical data <sup>153</sup> Complex product

<sup>147</sup> <https://sites.duke.edu/perspective/2019/06/27/how-crypto-currency-is-changing-fintech/>

<sup>148</sup> <https://sites.duke.edu/perspective/2019/06/27/how-crypto-currency-is-changing-fintech/>

<sup>149</sup> <https://sites.duke.edu/perspective/2019/06/27/how-crypto-currency-is-changing-fintech/>

<sup>150</sup> <https://www.economist.com/the-economist-explains/2015/11/02/who-is-satoshi-nakamoto>

<sup>151</sup> <https://www.cnbc.com/2018/06/18/blockchain-what-is-it-and-how-does-it-work.html>

<sup>152</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>153</sup> European Parliament 2018. Virtual Currencies. Monetary Dialog 2018. Available at: [http://www.europarl.europa.eu/cmsdata/149902/KIEL\\_FINAL%20publication.pdf](http://www.europarl.europa.eu/cmsdata/149902/KIEL_FINAL%20publication.pdf)

	Only offered online and mostly by non-traditional operators
	Legality
	Lack of harmonised regulation

Source: ICF compilation

### 4.3 Legal framework

The European Central Bank (ECB) in 2012 published a study that analysed virtual currencies. Considering the EU legal framework, the ECB highlighted that neither the e-Commerce Directive nor the Consumers Rights Directive applies to transactions realised within a virtual community.

Additionally, the study analysed the Payment Services Directive (2007/64/EC) and its potential relevance to virtual currency schemes. The PSD, on the one hand, lays down rules on the execution of payment transactions where the funds are electronic money, but, on the other hand, it does not have directly regulated the minting of electronic money. In this sense, payment institutions should not be allowed to issue electronic money, and consequently, Bitcoin should fall outside the scope of the abovementioned Directive.<sup>154</sup> Moreover, in 2015, the ECB has stated again that virtual currencies cannot be regarded as funds, are not covered by the provisions of the PSD. The study also underlined the possibility that certain services linked to virtual currency schemes can be subject to national laws on payment services.<sup>155</sup>

The ECB concluded in its studies that the Virtual Currencies concept and the related risks mostly remain unmitigated by legislation, regulation or supervision and that such a situation remains a challenge for public authorities.<sup>156</sup>

The European Supervisory Authorities (ESAs) has been also critical on the matter of virtual currencies, and in 2018 issued a pan-EU warning to consumers regarding the risks of buying Virtual Currencies (VCs). In particular, the ESAs stressed the lack of applicable consumer protection rules to virtual currencies and warned consumers about the risks connected to the use of the virtual currencies. In practice, a consumer who either buys or hold Virtual Currencies, since they are unregulated products, he/she cannot benefit from the guarantees associated with the regulated financial services<sup>157</sup>.

Finally, it might be observed that, even though virtual currencies are not directly covered by a clear EU legal framework, the services and products depending on them may be. In this sense, if the service provider is a firm that provides investment services or financial instruments, for instance, the Market in Financial Instruments Directive (MiFID II), as well as the Undertakings for the collective investment in transferable securities Directive (UCITS), may apply. Accordingly, in such situations, it can be concluded that the information does not concern virtual currencies *per se*, but it is a corollary of the main product provided.<sup>158</sup>

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<sup>154</sup> European Central Bank, 2012, *Virtual currency schemes*

<sup>155</sup> European Central Bank, 2015, *Virtual currency schemes – a further analysis*

<sup>156</sup> European Central Bank, 2012, *Virtual currency schemes*, p. 45

<sup>157</sup> ESMA, EBA and EIOPA warn consumers on the risks of Virtual Currencies, 2018

<sup>158</sup> London Economics Europe, VVA Consulting, Ipsos NV, ConPolicy and Time.lex, 2019, *Behavioural study on the digitalisation of the marketing and distance selling of retail financial services*.

#### **4.4 Assessment in relation to the DMFSD objectives**

##### **Challenges for consumers and the impact of the DMFSD on the protection of consumers of virtual currencies**

Consumers of virtual currencies are in a particularly vulnerable position (for example, several EU agencies and public entities from Member States advise consumer against this product).

Virtual currencies are complex and risky financial products due to their high volatility and lack of historical data and also to the fact that their issuance is not regulated by central bank or public authority. Furthermore, the London Economics study identified some misleading practices when selling this product related to advertisement and provision of pre-contractual information:

- Benefits emphasised while costs are hidden or given lower prominence in advertising;
- Key information missing or difficult to find;
- Information complex and difficult to understand;
- Benefits emphasised while costs are hidden or given lower prominence in precontractual information (e.g., currency conversion charges are only prominently displayed when these rates are attractive, otherwise they tend not to be easily identifiable).

The DMFSD would be in a good position to ensure that consumers of virtual currencies receive adequate pre-contractual information as there is no product specific legislation that covers virtual currencies in all circumstances (see above) and so the provisions of the Directive would act as a safety net for consumers. However, it is currently unclear whether the definition of financial services in the DMFSD includes virtual currencies, with a few stakeholders from all groups suggesting that this should be clarified.

The DMFSD's right of withdrawal does not apply to virtual currencies as their price depends on fluctuations in the financial market outside the supplier's control.

According to the London Economics study, operators that sell virtual currencies usually do not sell other products and consequently the risk of these providers selling unsolicited services is minimum. Nevertheless, DMFSD is an important safety net for those situations where this practice may occur.

##### **Challenges for providers and the impact of the DMFSD on the distance market of virtual currencies**

Given the legal uncertainty that surrounds these financial products, a few industry stakeholders mentioned that further clarification regarding the applicability of the DMFSD to virtual currencies is needed.

The two main consequences of this uncertainty on the market are:

- Some unfair competition between virtual currencies and other financial products that have clearly to meet the requirements of the DMFSD and possibly of other product-specific legislation;
- Reluctance from some financial providers to sell these products.

#### **4.5 Existing gaps and possible measures to improve consumer confidence and Empowerment and to develop the market for distance selling of virtual currencies**

As mentioned above, it is unclear if the DMFSD definition of "financial services" covers virtual currencies and what other product-specific legislation regulates them and under what circumstances. Consequently, the main measure to improve consumer confidence

and empowerment and to develop the market for distance selling of virtual currencies is to address these legal uncertainties.

Assuming the virtual currencies are covered by the DMFSD provision on pre-contractual information, the main gaps not addressed by the DMFSD relate to the lack of concrete rules on how the information should be presented and provided and when exactly in order to make it clear, easy to understand, and timely.

## **5 Case Study 4: Peer-to-peer lending**

### **5.1 Introduction**

Peer-to-Peer lending (P2P lending) is a consumer credit product that allows businesses and individuals to borrow money, from many individuals who are ready to lend, instead of borrowing from a single source. This allows individuals or businesses to avoid the use of traditional financial institutions. Sites used for P2P lending set out the rates and terms of transactions and enable the completion of these transactions<sup>159</sup>. They also have a duty to carry out due diligence operations for each loan request with a view to protecting the interests of both parties involved in transactions<sup>160</sup>. For this purpose, typically, financial accounts and a trading track record are required<sup>161</sup>. Some other key features of P2P lending are:

- the possibility of getting a loan when refused by a bank;
- a legal requirement to pay back the loan;
- loan sizes vary greatly in size, which means that lenders of different lending capacities can take part in such platforms and invest their money; and
- loans are usually repaid through direct debit to the platform<sup>162</sup>.

### **5.2 The evolution of the market**

Europe has been leading the way in the field of P2P since the mid-2000s<sup>163</sup>. Great Britain is the country where the first P2P landing platform was created, back in 2005 (which lend less than £10 million in that year<sup>164</sup>)<sup>165</sup>. Since then, the market has been making great strides.

According to a study from 2019, as of 2017, the total amount of the P2P lending market in Europe in 2017 was EUR 3,816 million and it was forecast to reach 170% of growth, namely EUR 10,288 million by 2022<sup>166</sup>. According to Cambridge University (2018) P2P consumer lending accounted for 41% of all European alternative finance in 2017 amounting to EUR 1,292 million (which is more than twice its value in 2005 and about four times its value in 2013).

Growth prospects appeared thus strong in Europe and the same trend applies worldwide<sup>167</sup>. According to the Acuity journal realised by Sensible Investing TV, crowdfunding solutions such as P2P lending will continue to pose a threat to the established financial industry and rewrite the way consumers gain access to money<sup>168</sup>. Whether such prospects will materialise and to what extent is dependent on factors such as global interest rates, the level of competition put forward by traditional financial institutions and, last but not least, the size of the consumer market<sup>169</sup>.

In Europe, the UK has been dominant on the P2P lending market, occupying 81% of the overall European market in 2015<sup>170</sup>. The trend has been tempering over the last years, in 2016, British platforms only dominating 73% of the market share (EUR 5,5 billion)<sup>171</sup>. While the UK is the most important market for P2P lending platforms (followed by France and Germany), regions such as the Baltic region have been steadily catching up due to

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<sup>159</sup> <https://www.investopedia.com/terms/p/peer-to-peer-lending.asp>

<sup>160</sup> [https://ec.europa.eu/growth/tools-databases/crowdfunding-guide/types/p2p\\_en](https://ec.europa.eu/growth/tools-databases/crowdfunding-guide/types/p2p_en)

<sup>161</sup> [https://ec.europa.eu/growth/tools-databases/crowdfunding-guide/types/p2p\\_en](https://ec.europa.eu/growth/tools-databases/crowdfunding-guide/types/p2p_en)

<sup>162</sup> [https://ec.europa.eu/growth/tools-databases/crowdfunding-guide/types/p2p\\_en](https://ec.europa.eu/growth/tools-databases/crowdfunding-guide/types/p2p_en)

<sup>163</sup> <https://alterinvesting.com/2018/12/02/european-p2p-lending-market/>

<sup>164</sup> <https://www.orcamoney.com/zopa-review/>

<sup>165</sup> <https://alterinvesting.com/2018/12/02/european-p2p-lending-market/>

<sup>166</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>167</sup> <https://alterinvesting.com/2018/12/02/european-p2p-lending-market/>

<sup>168</sup> Sensible investing.tv. Peer-to-peer lending - a fad or the future?

<sup>169</sup> <https://alterinvesting.com/2018/12/02/european-p2p-lending-market/>

<sup>170</sup> <https://alterinvesting.com/2018/12/02/european-p2p-lending-market/>

<sup>171</sup> <https://alterinvesting.com/2018/12/02/european-p2p-lending-market/>

a convenient position between Eastern and Western Europe, a business-friendly regulation and the existence of a fintech infrastructure<sup>172</sup>. The Eastern European market (Poland, Czech Republic, Slovakia, Hungary) has also increased fast between 2015 and 2017- by 153% from EUR 71 to EUR 179 million<sup>173</sup>.

Mintos is currently the largest P2P lending platform in Europe issuing more than a billion euros in loans<sup>174</sup>. During 2017, the Latvian platform Mintos experienced significant growth, making it the peer-to-peer lending market leader for continental Europe with a 38% market share<sup>175</sup>. In the UK, a pioneer in P2P lending, in March 2019 RateSetter had the highest market share by far (74.7%), followed by Zopa and Lending Works, with 15.3% and 4.7% respectively<sup>176</sup>.

Profile wise, P2P lending providers in the EU tend to be more frequent in countries which are underserved by banks<sup>177</sup>. They are usually FinTech savvies of technological developments and adopt business models that are flexible, small-scale and customer friendly<sup>178</sup>. As of 2016, many of the EU players remained relatively small and the amount of revenue losses banks were likely to incur due to competition from FinTechs was estimated at 2-3%<sup>179</sup>.

A UK study revealed that consumer lending P2P platforms have:

- a local website and brand only in 13% of the cases;
- a global brand with local websites in 18% of the cases; and
- a global website and brand in 69% of the cases.

The same study concludes that 84% of P2P consumer lending volumes comprised of cross-border inflows and 80%.

In spite of the unequivocal growth of P2P platforms in Europe, there are gaps. A UK study suggested that both market education and amendments of regulation constitute unresolved challenges<sup>180</sup>. The same study underlined that more favourable regulation at national level would allow the industry to grow further and reach its full potential<sup>181</sup>.

The main barriers to the development of the P2P lending market are mostly on the consumer side<sup>182</sup>:

- Fears over cybercrime;
- Concerns over privacy;
- Difficulties related to confirming identity;
- Digital literacy still not fully developed, differing between jurisdictions and language groups.
- Information asymmetries that impose information costs with identifying the relevant characteristics and other details of a particular financial transaction;

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<sup>172</sup> <https://alterinvesting.com/2018/12/02/european-p2p-lending-market/>

<sup>173</sup> <https://www.finextra.com/pressarticle/79625/survey-shows-growth-of-p2p-lending-in-europe>

<sup>174</sup> <https://viainvest.com/blog/what-does-the-future-hold-for-p2p-lending-in-europe/>

<sup>175</sup> <https://www.altfi.com/wire/392>

<sup>176</sup> <https://www.statista.com/statistics/479648/peer-to-peer-consumer-lending-platforms-market-share-united-kingdom/>

<sup>177</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>178</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>179</sup> Accenture. (2016). Where Fintech Lending Will Land

<sup>180</sup> Ziegler, T., Shneor, R., Wenzlaff, K., Odorovic, A., Johanson, D., Hao, R. and Ryll, L., 2019. Shifting Paradigms: The 4th European Alternative Finance Benchmarking Report. Cambridge, UK, Cambridge Centre for Alternative Finance.

<sup>181</sup> Ziegler, T., Shneor, R., Wenzlaff, K., Odorovic, A., Johanson, D., Hao, R. and Ryll, L., 2019. Shifting Paradigms: The 4th European Alternative Finance Benchmarking Report. Cambridge, UK, Cambridge Centre for Alternative Finance.

<sup>182</sup> See [https://ec.europa.eu/info/sites/info/files/171216-crowdfunding-report\\_en.pdf](https://ec.europa.eu/info/sites/info/files/171216-crowdfunding-report_en.pdf)

- Enforcement costs incurred when checking if the terms and conditions of a transaction are executed as specified and agreed.

On the supply side, regulatory limitations can inhibit the industry to grow further and reach its full potential<sup>183</sup>. Another aspect that acts as a barrier to these platforms is the existence of government policies that favour incumbent banks, for instance large banks can often provide loans at lower interest rates than crowdfunding platforms due to government guarantees which provide them with a funding cost advantage<sup>184</sup>. A Small Business Credit Survey in the US backs up this hypothesis, having found that the principal reason why borrowers are not satisfied with online lenders is high interest rates<sup>185</sup>.

Table 3. Overview of baseline and endline

Indicator	Baseline	Endline
Sales	In the early 2000s, P2P lending platforms had yet to be used in the EU.  Europe has been leading the way in the field of P2P since the mid-2000s <sup>186</sup> . Great Britain is the country where the first P2P lending platform was launched, back in 2005 <sup>187</sup> . In 2005, the amount lent did not exceed £10 million <sup>188</sup> .	In 2017, the total amount of the P2P consumer lending market in Europe in 2017 reached an amount of 1,292 EUR millions. <sup>189</sup>  In 2017, the total P2P lending market a total of EUR 3,816 million and it is forecasted to reach 170% to EUR 10,287.6 million by 2022 <sup>190</sup> .
Type of provider	See baseline of sales	Mostly FinTech companies <sup>191</sup> .
Most used means of communication	See baseline of sales	P2P lending is more likely to be sold online than offline <sup>192</sup>
Cross-border sales	See baseline of sales	A UK study revealed that as of 2016 cross-border transactions did not make

<sup>183</sup> [https://www.jbs.cam.ac.uk/fileadmin/user\\_upload/research/centres/alternative-finance/downloads/2018-ccaf-exp-horizons.pdf](https://www.jbs.cam.ac.uk/fileadmin/user_upload/research/centres/alternative-finance/downloads/2018-ccaf-exp-horizons.pdf)

<sup>184</sup> Schich, S. and S. Lindh, 2012, Implicit guarantees for bank debt: where do we stand?, OECD Journal: Financial Market Trends, Vol. 2012/1.

<sup>185</sup> Federal Reserve, 2017. Small Business Credit Survey: Report on Employer Firms

<sup>186</sup> <https://alterinvesting.com/2018/12/02/european-p2p-lending-market/>

<sup>187</sup> <https://alterinvesting.com/2018/12/02/european-p2p-lending-market/>

<sup>188</sup> <https://www.orcamoney.com/zopa-review/>

<sup>189</sup> Ziegler, T., Shneor, R., Wenzlaff, K., Odorovic, A., Johanson, D., Hao, R. and Ryll, L., 2019. Shifting Paradigms: The 4th European Alternative Finance Benchmarking Report. Cambridge, UK, Cambridge Centre for Alternative Finance.

<sup>190</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>191</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>192</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

		for a considerable part of their business volumes <sup>193</sup>
Main barriers	See baseline of sales	<p>Fears over cybercrime, concerns over privacy and difficulties related to confirming identity</p> <p>Digital literacy still not fully developed</p> <p>Information asymmetries that impose information costs and enforcement costs</p> <p>Lack of a more favourable regulation</p>

Source: ICF compilation

### 5.3 Legal framework

Based on the EBA “Opinion of the European Banking Authority on lending-based crowdfunding”<sup>194</sup> from 2015, that P2P lending involve two aspects:

- the payments-related aspects of crowdfunding activities, and
- the lending-related aspects.

#### **Payment-related aspects**

The EBA then concludes that then the PSD I (and now one can assume the PSD II) is the “most feasibly applicable Directive” to the payments-related aspects of crowdfunding activities.

The PSD II applies if crowdfunding platforms provide any of the following services (and consequently can be regarded as payment service providers (PSPs)) as a regular occupation or business activity as required under Article 1(2) (b) of the PSD II within the meaning of Annex I of the PSD II<sup>195</sup>:

- Services enabling cash to be placed in, or withdrawn from, a payment account as well as all the operations required for operating a payment account

<sup>193</sup> Ziegler, T., Shneor, R., Wenzlaff, K., Odorovic, A., Johanson, D., Hao, R. and Ryll, L., 2019. Shifting Paradigms: The 4th European Alternative Finance Benchmarking Report. Cambridge, UK, Cambridge Centre for Alternative Finance.

<sup>194</sup> See <https://eba.europa.eu/sites/default/documents/files/documents/10180/983359/f6106173-dc94-4d22-ade8-d40fce724580/EBA-Op-2015-03%20%28EBA%20Opinion%20on%20lending%20based%20Crowdfunding%29.pdf?retry=1>

<sup>195</sup> Despite the above, in the context of the PSD I (which also affected the PSD II), the EBA identified some discrepancies in the interpretation of certain provisions across member States. For example, while some Member States consider that the commercial agent exemption of article 3 might be applicable because crowdfunding platforms act on behalf of the payer or the payee (the lender or the borrower), other Member States consider this exemption not to be applicable, because the platform acts on behalf of both the lender and the borrower without any margin to negotiate or conclude a sale or purchase of goods or services. Similarly, there are also some differences in the interpretation of some of the concepts included in the text of the Directive (e.g. the definition of some of the payment services that could be provided by the crowdfunding platforms).



- The execution of payment transactions, including transfers of funds on a payment account with the users' payment service provider or with another payment service provider; -
- Issuing and/or acquiring payment instruments;
- Money remittance;
- Payment initiation services;
- Account information services.

It is important to keep in mind that where any of the exclusions of article 3 of PSD II apply, the PSD will not be applicable to P2P, such as for Article 3 (b), (j) and (k).

Whether the MCD and CCD apply to P2P is subject to legal debate.

The EBA did not analyse whether the DMFSD applies. The EC in 2016 did and concluded that the DMFSD generally applies to payment-related aspects of P2P lending (as long as the P2P acts as a supplier or intermediary)<sup>196</sup>. This is particularly relevant for those situations not under the scope of the PSD II (as per its Article 3), such as:

- "(b) payment transactions from the payer to the payee through a commercial agent authorised via an agreement to negotiate or conclude the sale or purchase of goods or services on behalf of only the payer or only the payee";
- "(j) services provided by technical service providers, which support the provision of payment services, without them entering at any time into possession of the funds to be transferred, including processing and storage of data, trust and privacy protection services, data and entity authentication, information technology (IT) and communication network provision, provision and maintenance of terminals and devices used for payment services, with the exclusion of payment initiation services and account information services"; and
- "(k) services based on specific payment instruments that can be used only in a limited way, that meet one of the following conditions: (i) instruments allowing the holder to acquire goods or services only in the premises of the issuer or within a limited network of service providers under direct commercial agreement with a professional issuer; (ii) instruments which can be used only to acquire a very limited range of goods or services; (iii) instruments valid only in a single Member State provided at the request of an undertaking or a public sector entity and regulated by a national or regional public authority for specific social or tax purposes to acquire specific goods or services from suppliers having a commercial agreement with the issuer".

Furthermore, this evaluation concludes that the following EU legislation also applies: 1) Unfair Commercial Practices Directive (UCPD); 2) Unfair Terms in Consumer Contracts (UCTD), 3) e-Privacy Directive (EPD); 4) General Data Protection Regulation (GDPR).

### ***Lending-related aspects***

The EBA also concludes that the Consumer Credit Directive (CCD) and the Mortgage Credit Directive (MCD) do not apply to the lending-related aspects either, unless the lending is done by a creditor (i.e., a natural or legal person who grants or promises to grant credit in the course of his trade, business or profession) and therefore not by consumers ("any natural person who, in distance contracts covered by this Directive, is acting for purposes which are outside his trade, business or profession").

While the EBA did not analyse whether the DMFSD, UCTD and UCPD apply to lending-related aspects, the same reasoning followed for CCD and MCD can be applied to these directives as their definitions of "financial supplier, "supplier or seller" or "trader" are similar to the definitions of "creditor" in CCD and MCD.

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<sup>196</sup> EC. 2016. Commission Staff Working Document: Crowdfunding in the EU Capital Markets Union

Consequently, if a natural person is acting in his/her professional/commercial capacity when lending money against an interest rate through a P2P platform then the CCD, the MCD, the DMFSD, the UCTD and the UCPD apply to the financial transaction, otherwise they do not.

In case of transactions between consumer and suppliers or creditors, the CCD and MCD would regulate most of them and the DMFSD would only be relevant for covering:

- Pre-contractual information and right of withdrawal for consumer credits (agreed through the P2P platform) below EUR 200 and above EUR 75,000;
- Pre-contractual information on the right of withdrawal and right of withdrawal for mortgages which right of withdrawal is covered under the DMFSD and not under the MCD.

There is, however, some lack of clarity on which circumstances a natural person lending money through a P2P platform against the payment of an interest rate can be considered to be acting in a commercial capacity or as a consumer. This uncertainty is exacerbated due to the fact that often P2P lending platforms do provide mechanisms for individuals to state whether they are lending money as individuals or as traders.

This uncertainty has extensive legal implications on whether consumer law applies and has been the object of analysis in the EC study<sup>197</sup>. According to that study, national laws have different conditions and thresholds (related for example to the remuneration, frequency, duration of the transaction(s)) to define an activity as private or commercial. In order to address the legal uncertainty caused by this fragmentation and lack of EU harmonised guidelines, two options could be considered according to the study: a) the clear definition at EU level of the indicators that distinguish consumers from traders, and/or b) acknowledgement of a new type of economic operators (i.e., 'microentrepreneurs' or 'prosumers') which are "*private individuals who provide, produce or trade goods or services not related to their habitual business, trade or profession*"<sup>198</sup>.

Regarding the lending-related aspects, this evaluation concludes that the following EU legislation also applies to lending contracts done through a P2P platform: 1) e-Privacy Directive (EPD); and 2) General Data Protection Regulation (GDPR).

## 5.4 Assessment in relation to the DMFSD objectives

### Challenges for consumers and the impact of the DMFSD on the protection of consumers

The main challenge in the context of the P2P consumer lending relate to information asymmetries<sup>199</sup> and some prevailing non-compliance of financial providers with the requirement to provide pre-contractual information as reported by the London Economics study<sup>200</sup>. While there is no data publicly available on the most common complaints of P2P lending consumers in the EU, according to the UK financial ombudsman, the problems faced by consumers of these services are similar to those they see in complaints from more traditional areas of credit. They are mainly:

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<sup>197</sup> Hausemer, P., Rzepecka, J., Dragulin, M., Vitiello, S., Rabuel, L., Nunu, M., Rodriguez, A.D., Psaila, E., Fiorentini, S., Gysen, S. and Meeusen, T., 2017. Exploratory study of consumer issues in online peer-to-peer platform markets. *European Commission (EUR 2017.4058 EN)*. Available at: [https://ec.europa.eu/newsroom/document.cfm?doc\\_id=45244](https://ec.europa.eu/newsroom/document.cfm?doc_id=45244)

<sup>198</sup> Hausemer, P., Rzepecka, J., Dragulin, M., Vitiello, S., Rabuel, L., Nunu, M., Rodriguez, A.D., Psaila, E., Fiorentini, S., Gysen, S. and Meeusen, T., 2017. Exploratory study of consumer issues in online peer-to-peer platform markets. *European Commission (EUR 2017.4058 EN)*. Available at: [https://ec.europa.eu/newsroom/document.cfm?doc\\_id=45244](https://ec.europa.eu/newsroom/document.cfm?doc_id=45244)

<sup>199</sup> See [https://ec.europa.eu/info/sites/info/files/171216-crowdfunding-report\\_en.pdf](https://ec.europa.eu/info/sites/info/files/171216-crowdfunding-report_en.pdf)

<sup>200</sup> According to the study it is very common that in P2P lending services key information missing or difficult to find. Other aspects of possible misleading/unfair practices that can lead to consumer detriment were either not observed or were encountered only in 1-2 instances.

- Consumers borrowed money under a peer-to-peer arrangement without realising it.
- Some borrowers are unsure about the recourse they have to the lender.
- Some borrowers complain that they were not informed about the withdrawal period.
- Problems with fees, charges and the general administration of loans mainly because they were not explained or are considered unfair by consumers. In particular, a significant share of these problems related to fees and charges applied when consumers want to repay the loan earlier.

The aforementioned problems due to lack of information or misleading practices of the provider can lead to poor decisions by some consumers, which might make use of the right of withdrawal to revert their ill decisions.

According to the same study, P2P lending providers do not usually sell other services/products and consequently the risk of them providing unsolicited services to consumers is very low.

The impact of DMFSD protecting consumers of P2P lending is however very limited:

- On payment-related aspects, consumer protection is addressed by PSD II pre-contractual requirements, right of withdrawal and ban on unsolicited services. There are however a few cases to which the PSD II does not apply (as detailed in the previous section) and the DMFSD could apply functioning as a safety net. Unsolicited communications are regulated extensively by the EPD and GDPR.
- On lending-related aspects, consumer protection is either not addressed by any EU consumer law or it is addressed primarily by the CCD and MCD, with the DMFSD being relevant only to the cases already mentioned above.

### **Challenges for providers and the impact of the DMFSD on the distance market of financial services**

Currently, as per above the impact of the DMFSD on the consolidation of the single market for P2P lending is limited. Regarding payment-related aspects, other EU horizontal and product specific legislation already address this objective in most of the circumstances. On lending-related aspects of credit agreements between consumers (C2C) EU consumer law (including the DMFSD) does not currently apply. On lending-related aspects of credit agreements between business and consumers, the CCD, the MCD and the UCPD apply in most of the cases and so DMFSD only covers a few situations.

### **5.5 Analysis of existing gaps and possible measures to improve consumer confidence and empowerment and to develop the market for distance selling of these products.**

On payment-related aspects the key legislation is PSD II, while DMFSD acts as a safety net for those cases excluded from the scope of the PSD II.

The London Economics study identified some problems related to the availability and accessibility of information on the P2P platforms analysed. These two aspects are covered by both the PSD II and DMFSD and addressing them would require a more effective enforcement of the PSD II and the DMFSD.

On credit agreements done through a P2P platform (i.e., lending-related aspects):

- If the agreements are between two consumers, then they are not covered by the DMFSD nor by CCD nor MCD;
- If the agreements are done between a consumer and a supplier/trader/creditor they are covered by the CCD/MCD and DMFSD. In these cases, as highlighted by the UK financial ombudsman the main complaints relate to lack of information –

which again points to the need for a more effective enforcement of the CCD/MCD and DMFSD requirements on pre-contractual information – and difficulties of consumers entering into contracts without knowing it. This last aspect may be related with the complexity of the service (i.e., using/understanding the financial product or the functioning of the platform) or with malpractices of the providers in terms of getting the consent/agreement of the consumer. Consequently, consumer protection could be improved by introducing clear requirements on: a) how the information should be presented to consumers in a way that they read it and fully understand, b) how to use warning pop-ups and other mechanisms to ensure that the consumer is fully aware of their obligations and c) how to ensure that the consent is given consciously (by for example not allowing pre-ticked boxes).

Consumer protection and consolidation of the single market in the context of P2P lending could still be improved by:

- Providing harmonised EU guidelines on when an individual can be considered to be acting as a consumer or in its commercial capacity (even if it is not his/her primary activity as in the case of 'microentrepreneurs' or 'prosumers'). This would improve clarity regarding which legislation applies to the credit agreements done through the P2P platforms and would help consumers to be more aware of their rights and providers to comply with the relevant rules and expand their activity cross-border;
- Ensuring that consumers know whether they are borrowing money from a consumer or from a trader. This would help consumers to know about their rights.

These aspects are however beyond the influence of the DMFSD.

## **6 Case Study 5: Pay-day loans**

### **6.1 Introduction**

A personal loan is a sum of money granted to an individual consumer, for their personal use, according to their creditworthiness (e.g. ability to pay).

A payday loan, which can also be known as a cash advance loan or a short-term high cost loan is a small amount, short-term (up to one year) and high-cost personal loan, which falls into the wider category of consumer credit products.<sup>201</sup>

In essence, the loan process involves a lender making immediately available to the borrower a small amount of money, for a short period of time, based on the consumer's ability to pay, not the collateral they offer for the granted loan, with the lender being compensated with a higher than average interest rate for the risk taken.

Although traditionally this was carried out through post-dated checks, the borrower would receive cash and would give the lender a check post-dated to the date of his next payday for the principal amount plus fees, having therefore a maturity of up to one month, the term "payday loan" is currently used as a blanket term for a myriad of consumer credit products that embody its characteristics of short duration and high cost, its connection to a given future income or "payday", as become unnecessary<sup>202</sup> and in certain cases may have slightly longer maturities than the traditional month but always under one year.

These loans are highly accessible with limited and relaxed borrower checks and a swift lending process composed of credit application, delivery and collection, that fits well with at distance transactions, namely entirely online or by SMS<sup>203</sup>, with borrowers submitting key information (e.g. personal information, relevant financial information), the lender assessing the borrowers creditworthiness and accepting the risk, with the amount borrowed being added and withdrawn from the borrower's bank account directly.

### **6.2 The evolution of the market**

There is no information about what share of the EU consumer credit market corresponds to payday loans neither at the baseline nor currently.

Nevertheless, studies suggest that the payday day industry in Europe has developed rapidly over the last two decades<sup>204,205</sup>, and particularly after the advent of the 2008 economic crisis, since it put enormous pressure on traditional lenders (e.g. banking institutions) to shore up capital reserves, cut costs, saving money and ultimately taking less risk reducing the offer of small unsecured loans. Private equity firms and tech savvy lenders were quick to exploit this gap though the use of technology to provide credit products quicker than the traditional payday lenders could.

The integration of technology in the field of financial services, including the development of lending decision engines, allowed for low-cost and swift decision-making and a near immediate access to credit when compared to other options. Payday loans are considered to be particularly appropriate to distribute online or over the phone, using

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<sup>201</sup> European Credit Research Institute (ECRI), 2019, *Price rules in consumer credit: should the EU act?*

<sup>202</sup> Consumer Finance Association. Competition Commission Market Investigation into Payday Lending pp. 32-33

<sup>203</sup> Directorate General for Internal Policies. (2014). Consumer protection aspects of financial services (Study, IP/A/IMCO/ST/2013-07, February) pp 58 - 61

<sup>204</sup> Data available for Estonia, Finland, Latvia, Lithuania and the United Kingdom suggests that the annual average variation at constant prices of this market between 2008 and 2015 to have been on average 21.2% per year.

<sup>205</sup> Over time national regulators and legislators intervened in regulating some market practices in some EU Member States, including the Lithuania (where the market shrank significantly in 2016) and the Netherlands (where it shrank to a volume of 300 thousand euros in 2013), France and Finland.

mostly automated processes. According to the consumer survey, in the past 5 years 33% of the respondents had purchased a payday loan at the distance, with payday loans representing about 12% of all the credits purchased at the distance by the respondents in the last 5 years.

Information on this market is mostly available for the UK, which is the largest market for this type of consumer credit product.

As stated in the London Economics (2019)<sup>206</sup> study in 2017, in the UK, 37% of households with a total income of between EUR 17,069 and EUR 34,138 had a payday loan, 22% of households with an income between EUR 34,138 and EUR 56,897 embarked on a payday loan while 14% of households with an income of more than EUR 56,897 took out a payday loan.

In the UK, traditional payday lending was offered by a heterogeneous mix of providers including both traditional credit institutions (e.g. banking institutions) but also privately owned companies, that offered small amount short term loan products as a part of a multiline offer (e.g. doorstep lenders, pawnbrokers, log back loans, check cashing shops among others).<sup>207</sup> This status quo changed significantly with the entrance in the market of online payday lenders in the UK in 2004<sup>208</sup>.

In 2012, most payday loans granted in the UK were purchased online (83% of users took a loan online and 12% both online and on the high street<sup>209</sup>) and the average amount borrowed online was higher than the average amount borrowed by other means.<sup>210</sup>

A similar trend is expected to have happened in other EU countries, as the UK online payday lenders expanded quickly to other European countries in subsequent years. For example, Finland reported the start of an "SMS- loan" market or "Flitskrediet" market around 2005.<sup>211</sup>

This is in line with the data of the London Economics study, which shows that of the providers of payday loans analysed, 74% are new operators and that 76% are active only online.

The cross-border volumes of payday loans in the EU could not be determined, however the speed and streamlining of lending processes and the development of communication technologies allowed for the emergence of large operators which offered this product in multiple markets worldwide, such as Wonga<sup>212</sup>. This is in line with the data from consumer survey, as one third of the respondents that obtained a payday loans at distance did it from a provider in another Member State.

Nevertheless, of the providers of payday loans analysed in the study an overwhelming majority (92%) were national operators, while 8% were cross-border operators.

The main barriers to the development of this market relate mostly to the high interest rates charged which makes this product very uninteresting for a large majority of the consumers. On the supply side, the main barrier relates to the risky profile of consumers

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<sup>206</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>207</sup> Beddows, S. and McAteer, M. "Payday lending: Fixing a Broken Market", The Association of Chartered Certified Accountants, 2014 <https://www.accaglobal.com/content/dam/acca/global/PDF-technical/other-PDFs/pol-tp-pdlfab-payday-lending.pdf>

<sup>208</sup> Office of Fair Trading, "Review of high cost consumer credit", June 2010

<sup>209</sup> Competition & Markets Authority "Payday lending investigation – Final Report", 2015

<sup>210</sup> <https://www.theguardian.com/business/2013/oct/18/wonga-buys-german-payment-firm-billpay>

<sup>211</sup> Talousvaliokunnan Mietintö 15/2012vp page 1-2 as consulted here [https://www.eduskunta.fi/FI/vaski/Mietinto/Documents/tavm\\_15+2012.pdf](https://www.eduskunta.fi/FI/vaski/Mietinto/Documents/tavm_15+2012.pdf)

<sup>212</sup> <https://www.theguardian.com/business/2013/oct/18/wonga-buys-german-payment-firm-billpay>

of this kind of credit and the tight national regulations restricting the supply of payday loans.

*Table 4. Overview of baseline and endline by indicator*

Indicator	Baseline	Endline
Sales	No data available	No data available  12% of the credits obtained at distance by consumer survey respondents  33% of the consumer survey respondents that have purchased at least one financial service online
Type of provider	Traditional operators	74% new operators and 26% traditional operators
Most used means of communication	No information available	76% online only
Cross-border sales	No information available	No information available  One third of the payday loans obtained at distance by respondents of the consumer survey were from a provider in another Member State.  92% of the providers analysed by LE Europe study were national operators while 8% were European operators.
Main barriers	High interest rates  Risky profile of consumers  Low digitalisation and digital literacy	High interest rates  Risky profile of consumers

*Source: ICF compilation*

### **6.3 Legal framework**

The following legislation is applicable to Payday loans: the Distance Marketing of Financial Services Directive (DMFSD)<sup>213</sup>, the e-Commerce Directive (ECD)<sup>214</sup>, the Unfair

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<sup>213</sup> Directive 2002/65/EC of the European Parliament and of the Council of 23 September 2002 concerning the distance marketing of consumer financial services and amending Council Directive 90/619/EEC and Directives 97/7/EC and 98/27/EC

<sup>214</sup> Directive 2000/31/EC of the European Parliament and of the Council of 8 June 2000 on certain legal aspects of information society services, in particular electronic commerce, in the Internal Market ('Directive on electronic commerce')

Commercial Practices Directive (UCPD)<sup>215</sup>, the General Data Protection Regulation (GDPR)<sup>216</sup>, the Consumer Credit Directive (CCD)<sup>217</sup> and the 6) e-Privacy Directive (EPD).<sup>218,219</sup>

The CCD and the DMFSD are the key legislative pieces regulating pre-contractual information requirements and the right of withdrawal for payday loans provided using distance means of communication. They fully overlap on these requirements for financial services sold at distance<sup>220</sup>. The CCD takes precedence for payday loans under its scope, namely payday loans above EUR 200, while the DMFSD covers the payday loans outside the scope of the CCD, i.e. payday loans below EUR 200.

The EPD and the GDPR are the key legislative instruments regulating unsolicited communications. And the UCPD and the DMFSD protect consumers from unsolicited services.

## **6.4 Assessment in relation to the DMFSD objectives**

### **Challenges for consumers and the impact of the DMFSD on the protection of consumers**

This type of product is often associated with higher than standard APR's, irresponsible lending and aggressive advertising which led some to conclude that payday loans lead to financial quicksand for consumers by facilitating the entry into a wheel of ever greater indebtedness and financial difficulty.

On the matter of above average APR's, Euro area statistics show that bank interest loans of loans below 1 year loans in length and loans between 1 and 5 years varied since 2010 between 5% and 6% a year, payday loans were reported to have APR's of triple digits in multiple countries, namely the UK.<sup>221</sup>

By its own nature this product is particularly appealing to those consumers that are in a lower income bracket, do not possess enough disposable income and/or do not have a sufficient level of savings to face a sudden and unforeseen expenditure. Often these consumers are in a vulnerable position, over-indebted and not creditworthy.<sup>222</sup>

In 2013, the UK OFT research into the payday lending market showed that 28% of borrowers had to roll over/refinance their debt at least once, 5% had to do so four or more times, 58% of borrowers had taken more than one loan and 15% had done so

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<sup>215</sup> Directive 2005/29/EC of the European Parliament and of the Council of 11 May 2005 concerning unfair business-to-consumer commercial practices in the internal market and amending Council Directive 84/450/EEC, Directives 97/7/EC, 98/27/EC and 2002/65/EC of the European Parliament and of the Council and Regulation (EC) No 2006/2004 of the European Parliament and of the Council ('Unfair Commercial Practices Directive') (Text with EEA relevance)

<sup>216</sup> Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation) (Text with EEA relevance)

<sup>217</sup> Directive 2008/48/EC Of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers and repealing Council Directive 87/102/EEC

<sup>218</sup> Directive 2002/58/EC of the European Parliament and of the Council of 12 July 2002 concerning the processing of personal data and the protection of privacy in the electronic communications sector (Directive on privacy and electronic communications)

<sup>219</sup> LE Europe, VVA Consulting, Ipsos NV, ConPolicy and Time.lex, 2019, *Behavioural study on the digitalisation of the marketing and distance selling of retail financial services*.

<sup>220</sup> There is only one identified exception: Article 5.6 CCD provides for an additional requirement to provide consumers with an explanation of the pre-contractual information that shall be adapted to circumstances of the situation in which the credit agreement is offered, the person to whom it is offered and the type of credit offered. This obligation is not foreseen under DMFSD.

<sup>221</sup> See: <https://www.euro-area-statistics.org/bank-interest-rates-loans?cr=eur&lg=en&page=0&charts=M..B.A2B.F.R.A.2250.EUR.N+M..B.A2B.F.R.A.2250.EUR.N+M..B.A2B.I.R.A.2250.EUR.N&template=1> and Idem 10

<sup>222</sup> LE Europe, VVA Consulting, Ipsos NV, ConPolicy and Time.lex, 2019, *Behavioural study on the digitalisation of the marketing and distance selling of retail financial services*.



more than five times. With an overall 32% of loans being repaid late or none at all.<sup>223</sup> In Lithuania in 2013, 39% of loans were issued to citizens under 25 years old and a significant amount of these were repaid by their relatives<sup>224</sup>, with a 37% of loans granted being rolled over or refinanced.<sup>225</sup>

At the national level, regulatory action with provider registration, APR limitations, fee limitations, advertising limitations and improved consumer complaint and redress mechanisms seem to have a positive effect on improving responsible lending practices through realigning of incentives away from abusive practices, in countries such as the Netherlands<sup>226</sup> and the UK<sup>227</sup>, but unsustainable lending practices still exist.

By March 2019, the complaints against payday lenders in the UK has soared to a five-year high with 40.000 complaints being presented to the Financial Ombudsman Service, an 130% increase from the previous year<sup>228</sup>. Mostly related to irresponsible lending and repayment problems.

This shows that it is essential to ensure that consumers a) received and understand pre-contractual information about the supplier, the characteristics of the payday loan and the terms and conditions of the contract, b) have the right of withdrawal of ill and rushed decisions, c) are protected against unsolicited communications from payday loan providers.

### **Pre-contractual information**

The consumer survey shows that respondents that considered obtaining credits at a distance found information requirements important. Furthermore, the overwhelming majority of those respondents are eager to have the information presented in a format that enables comparison with other products, prominently and immediately and in a way that is adapted to the channel, as well as to be able to choose the format in which they can access the information.

The same respondents indicated that the required information about the service and supplier and the terms and conditions was often (75% - 92% depending on the information element) made available even if only upon request. Information on the applicable law, options and procedures for compensation claims and on the availability of funds was reported to be available in a fewer cases (around 65%). The respondents assessed the information they received as follows:

- It was clear, easy to understand and well structured (52%)
- It was complete and presented in a format that enabled them to compare it with other products (61%)
- It was provided sufficiently in advance to give them time to review it (61%)
- It allowed them to make an informed decision (62%)
- It was presented in a way that was suitable for the device they were using (70%)
- Information relating to their rights of withdrawal / early termination / cancellation was adequate (60%)
- Information relating to their right to complain and seek redress / compensation was adequate (52%)

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<sup>223</sup> Office of Fair Trading. Payday Lending. Annexe A - Quantitative Findings. OFT1481a. March 2013

<sup>224</sup> Lietuvos Bankas. Vartojimo Kredito Rinkos Apžvalga 2013 m. ISSN 2335-836X. Vilnius. 2014

<sup>225</sup> Financial Conduct Authority "<https://www.fca.org.uk/data/consumer-credit-high-cost-short-term-credit-lending-data-jan-2019>" 2019

<sup>226</sup> <https://www.stibbe.com/en/news/2017/april/ban-on-advertisement-of-high-risk-financial-products-to-retail-parties-in-the-netherlands>

<sup>227</sup> Directorate General for Internal Policies. (2014). Consumer protection aspects of financial services (Study, IP/A/IMCO/ST/2013-07, February) pp 58 - 61

<sup>228</sup> <https://www.bbc.com/news/business-48268474>

This shows that while the majority of the respondents is relatively satisfied with the quality of the information and the way and when it was presented and provided, there is a considerable share of respondents that was neutral or not satisfied with these aspects. In particular, 30% of the respondents considered that the information was not clear, easy to understand or well structured.

The London Economics study<sup>229</sup> also looked into the prevalence of some selling practices in the payday loan market and concluded that:

- Often key information is missing or difficult to find;
- Sometimes, information is complex and difficult to understand and layered and located in places that can be overlooked;
- Sometimes, benefits are emphasised while costs are hidden or given lower prominence in precontractual information.

The problems with the lack of information are clearly non-compliant with CCD and the DMFSD requirements. Other problems related a) poor quality of information and/or b) difficulties to understand the information due to its complexity or the way it is presented to consumers c) and/or how information is made available are not (fully) regulated by the CCD and the DMFSD and do not necessarily constitute a non-compliance with these two directives.<sup>230</sup>

Additionally, payday loans are marketed as fast credit and often providers make it quick and easy to purchase. Advertising tactics tend to be aggressive, with providers competing heavily for new customers mainly on issues of speed of the lending process,<sup>231,232</sup> offering gifts and discounts and time-limited options.<sup>233</sup>

The speed of the purchase process of payday loans may imply that providers do not comply with the DMFSD and the CCD requirement that consumers must be provided with pre-contractual information "in good time before the consumer is bound by any distance contract or offer."

### **Right of withdrawal**

As mentioned, the process of purchasing a payday loan tends to be relatively quick and easy with providers often using aggressive tactics that contribute to impulsive purchasing decisions.

Furthermore, regardless of their income bracket, consumers tend to be overly optimistic about their ability to repay or find new financial shocks in the near future. In the case of lower income brackets and young households the lack of disposable income may position them in a weaker bargaining position and their immediate necessity might outweigh long-term analysis, while aggressive marketing may incentivise inadequate expectations<sup>234</sup>.

The potential for ill-informed and rushed decisions is considerable in the payday loan market, and the right of withdrawal allows consumers the necessary time to analyse the

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<sup>229</sup> LE Europe, VVA Consulting, Ipsos NV, ConPolicy and Time.lex, 2019, *Behavioural study on the digitalisation of the marketing and distance selling of retail financial services*.

<sup>230</sup> As even if both indicate that information should be clear and concise, they do not provide concrete indicators to measure compliance with these requirements.

<sup>231</sup> <https://www.euro-area-statistics.org/bank-interest-rates-loans?cr=eur&lg=en&page=0&charts=M..B.A2B.F.R.A.2250.EUR.N+M..B.A2B.F.R.A.2250.EUR.N+M..B.A2B.I.R.A.2250.EUR.N&template=1>

<sup>232</sup> <https://www.ferratumgroup.com/contact>

<sup>233</sup> LE Europe, VVA Consulting, Ipsos NV, ConPolicy and Time.lex, 2019, *Behavioural study on the digitalisation of the marketing and distance selling of retail financial services*.

<sup>234</sup> Skiba, P. and Tobacman, J., "Payday Loans, Uncertainty and Discounting: Explaining Patterns of Borrowing, Repayment, and Default", 2008 and Idem 26

information about the payday loan and the terms and conditions of the contract and re-assess their decisions, and cancel the contract if they conclude that the payday loan agreement is not adequate for them.

### **Unsolicited communications and services**

There is no evidence of particular challenges related to unsolicited services. On unsolicited communication there also is hard data, however, given the aggressive marketing practices of payday loan providers reported in various studies and reports, it is reasonable to assume that some providers do not comply with this provision as also suggested by some sources<sup>235</sup>.

### **Challenges for providers and the impact of the DMFSD on the distance market of financial services**

The DMFSD contributed to a level playing field in the area of consumer credits until the implementation of the CCD in 2010 and contributed to set consumer protection standards in the context of pre-contractual information and right of withdrawal for distance sales of financial products that were followed by the CCD and other product-specific legislation. For payday loans below EUR 200, it still plays a decisive role in creating a level playing field between providers.

The requirements imposed by both Directives led to a level playing field in payday loan market between responsible and irresponsible lenders, traditional and new operators independently of the means of communication used. One important example is the impact of the requirement to provide information in good time, which by slowing down the purchase process reduced the competitive advantage of those providers that offer faster transactions because they did not perform creditworthiness checks.

Payday loans have a high potential to be sold cross-border and the existence of a harmonised legal framework that applies in all Member States might have reduced barriers to both consumers and suppliers.

However, there are significant barriers to the development of this market cross-border. The main barrier is the national legal diversity applicable to payday loans. For example, the legal limit to the maximum APR allowed in a payday loan varies from Member State to Member State, advertisement rules differ among Member States, with some countries such as the Netherlands banning the advertising financial products, legal restrictions on the operation of suppliers are in force in some countries such as the prohibition of payday loans sales at certain times of the day.

Market in a context of a level playing field with reduced barriers to cross border activity, it seems clear that the level of harmonization and of enforcement of the consumer protection rules both inside and outside of national borders must be addressed.

### **6.5 Analysis of existing gaps and possible measures to improve consumer confidence and empowerment and to develop the market for distance selling of these products.**

There are compliance issues with some of the re-contractual information requirements of DMFSD (i.e., provision of all the required information in good time) by payday loan providers. As it was stated above the number of lower income bracket consumers of payday loans is significant. However, evidence shows that consumers experience difficulties in understanding the available information. While the DMFSD states that information should be "provided in a clear and comprehensible manner in any way appropriate to the means of distance communication used" it does not provide concrete indicators/guidelines on how these should be implemented in practice and on how to assess the compliance of financial providers with these requirements, that are to a great

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<sup>235</sup> See for example: [https://assets.publishing.service.gov.uk/media/54ebb75940f0b670f4000026/Appendices\\_\\_\\_glossary.pdf](https://assets.publishing.service.gov.uk/media/54ebb75940f0b670f4000026/Appendices___glossary.pdf)

extent subjective. Remedies to this, as the ones provided by the EBA opinion on DMFSD<sup>236</sup> and LE Europa (2019)<sup>237</sup>, could be considered.

The clarification of what “in good time” concretely means would ensure that consumers effectively have time to analyse the provided pre-contractual information and reduce the probability of impulse buying by granting consumers a suitable timeframe to reflect on the information provided, which is especially relevant in the case of vulnerable consumers facing aggressive (and even misleading) marketing strategies pushing them to acquire a payday loan as fast as possible.

As DMFSD does not require a creditworthiness assessment, financial providers do not have to do it for payday loans below EUR 200. This might contribute to irresponsible lending and is an important gap in protecting consumers.

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<sup>236</sup> Available at: <https://eba.europa.eu/file/147201/download?token=tUEycHID>

<sup>237</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services.

## **7 Case Study 6: Savings account**

### **7.1 Introduction**

A savings account is an interest-bearing deposit account held at a bank or another financial institution which provides a small interest rate. The financial providers may limit the number of withdrawals that consumers can make from their savings account each month.<sup>238</sup> Savings accounts provide instant ("sight deposits") or time-limited ("time deposits") access to funds.<sup>239</sup>

Savings accounts are a relatively basic financial product and can potentially offer many benefits as it is a relatively risk-free product that offers a return on the deposited money. Savings accounts typically constitute the most common mean for households to invest financially.<sup>240</sup>

### **7.2 The evolution of the market**

In 2015, savings accounts constituted 35% of all financial savings of EU household<sup>241</sup> and in 2016, 44% of Europeans had a saving account<sup>242</sup>. These were most popular in the Netherlands (89%), Sweden (88%) and Greece (80%) and the least popular in Romania (8%), Hungary (10%) and Italy (13%)<sup>243</sup>. This represents an average annual growth of 2.8 percentual points. However, this trend is expected to have decelerated or even reverted in some countries as a consequence of the recent very low/negative interest rate.<sup>244</sup>

As of 2008, the most significant financial product offered by banks through distance marketing were: other loans (21%), and savings accounts (also 21%).<sup>245</sup> In the recently conducted Global Banking Survey by Deloitte (2018)<sup>246</sup> - in which EU countries such as UK, Spain, Netherlands, France and Germany were included- it is shown how respondents still prefer traditional channels (54%) when opening a new savings account, while 30% and 11% do it online and through mobile apps respectively, being the rest 5% contracted through a contact centre by phone.

Eurostat reported that since 2008 the number of banks in the EU has been continuously decreasing, mainly as a result of mergers in the banking sector. At the end of 2017, there were 27% less banks than in 2008<sup>247</sup>. This shows a clear trend of digitalisation of traditional operators.

As of 2019, a study on financial services in seven Member States<sup>248</sup>, showed that the great majority of financial providers that engage on the distance selling of savings accounts were traditional operators (76%) - usually well-established commercial banks proposing other financial services and products as well -, the rest (24%) being new operators, which tend to offer their services mostly online.

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<sup>238</sup> Investopedia. Savings account. Available at: <https://www.investopedia.com/terms/s/savingsaccount.asp>

<sup>239</sup> European Commission (2006). Current accounts and related services. Available at: [http://ec.europa.eu/competition/sectors/financial\\_services/inquiries/interim\\_report\\_2.pdf](http://ec.europa.eu/competition/sectors/financial_services/inquiries/interim_report_2.pdf)

<sup>240</sup><sup>240</sup> ECB 2015 Working Paper Series Financial literacy and savings account returns. Available at: <https://www.ecb.europa.eu/pub/pdf/scpwps/ecbwp1852.en.pdf>

<sup>241</sup> Better Finance (2015) Press release: Bank Savings accounts in the EU hit by financial repression.

<sup>242</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>243</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>244</sup><sup>244</sup> See [https://www.eulerhermes.com/en\\_global/economic-research/insights/Europe-s-low-interest-rates-have-an-impact-but-not-the-way-you-think.html](https://www.eulerhermes.com/en_global/economic-research/insights/Europe-s-low-interest-rates-have-an-impact-but-not-the-way-you-think.html).

<sup>245</sup> CPEC (2008). Analysis of the Economic impact of Directive 2002/65/EC.

<sup>246</sup> Deloitte (2018) Val Srinivas and Anguss Ross, Accelerating digital transformation in banking

<sup>247</sup> Eurostat (2019) The European Economy since the start of the millennium.

<sup>248</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

These new providers (e.g., FinTechs) are imposing some changes in the market of savings accounts as they generally offer higher interest rates than traditional banks and convenient means to open accounts.<sup>249</sup> This is a global trend that is causing financial start-ups to begin an interest battle to acquire new customers, diversify revenue and gain market share.<sup>250</sup> However, as many millennials are increasingly changing traditional savings accounts for new financial products, the evolution of savings accounts sales both by distance and through other means, might indicate a decreasing trend<sup>251</sup>.

The digitalisation of traditional providers and the emergence of FinTechs has particular interest in the case of cross-border sales and is expected to increase competition in the financial market in the EU as it is easier for providers to reach customers from other Member States and for customers to a) compare the return and conditions offered by savings accounts around the EU and b) open savings accounts cross-border as they do not need to be physically present in the country of the financial provider anymore.<sup>252</sup> Data from this London Economics study (2019) shows that 25% of the operators that offer savings accounts were EU operators. Nevertheless, according to the latest data available from the Eurobarometer<sup>253</sup>, in 2016 only 1% of the consumers surveyed purchased a savings account in another EU Member State. Data collected through the consumer survey for payment accounts, shows that only 6% of the respondents have opened or tried to open an account cross-border, while 26% would consider it to find better deals. The remainder 68% would not do it for a variety of reasons that will be explored below.

As of 2013, when online banking penetration was increasing, still the highest proportion of new savings accounts contracts was done face-to-face. Online via a desktop or laptop was the second preferred and at the time the use of the mobile or table for this purpose was imperceptible.<sup>254</sup> In 2019, the consumer survey conducted in the context of this evaluation, shows that of the consumers that acquired savings accounts through means of distance communication in the last five years, the majority did it over the internet using desktop, laptop or tablets (50%), followed by smartphones (31%), postal services (10%), and phone calls (9%).

As a general trend, FinTechs are offering not only savings accounts with higher rates than traditional banks, but also more innovative approaches when compared to a relatively limited offer of savings accounts options by traditional providers.<sup>255</sup> A recent illustrative example of new savings products is the smartphone application Vault, by the FinTech firm Revolut, which turns spare change into savings, both in currencies and crypto-currencies.<sup>256</sup>

Although selling and purchasing savings accounts through distance means (in particular online) offer some advantages when compared to purchasing/selling savings accounts at the branch, there are still barriers that inhibit distance sales of savings accounts.

On the main barriers at the baseline it is important to highlight: a) the limited digitalisation of traditional providers and the insignificant share of FinTechs at the time, and b) from the consumer side a study the lack of access to technology (PC/Internet),

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<sup>249</sup> BEUC. (2015). Savings accounts in Europe: A dormant market?

<sup>250</sup> Forbes (2019) Why FinTech companies keep launching their own banking products

<sup>251</sup> The balance (2019) Surprising millennial banking trends. Last visited: 7 October 2019.

<sup>252</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>253</sup> Eurobarometer. 2016. Special Eurobarometer 446: Financial products and services.

<sup>254</sup> PWC (2014) Cash Savings – An International Comparison

<sup>255</sup> Forbes (2019) Why FinTech companies keep launching their own banking products

<sup>256</sup> Fintech Futures (2018) Revolut unveils new savings solution, Vaults

particularly at home, followed by security and privacy concerns, especially after September 11.<sup>257</sup>

Currently, from the consumer side the main barrier to open savings accounts using a distance mean of communication is mostly a prevailing preference for face-to-face communication (the results from the consumer survey show that of those consumers that searched for a payment account using a distance mean of communication and that purchased the service, almost half decided to do it face-to-face). Other barriers include fears over cybercrime and lack of trust in new non-traditional operators. From the supply side, some traditional providers make the application to purchase saving accounts predicated on the relationship of the consumer with the provider (i.e., being a customer already or not)<sup>258</sup>. For instance, sometimes it is required that the consumer become a customer of the provider to have access to specific benefits or products<sup>259</sup>.

When it comes to cross-border purchases/salles there are additional barriers. From the consumer side the main barriers indicated by the 68% of respondents to the consumer survey that would not consider purchasing a payment account from a provider in another Member State were:

- Preference over face-to-face contact (30%);
- Satisfaction with the services and conditions offered in their country/area (27%);
- Unsureness about their rights or where to turn to get redress in case of a problem (28%);
- Language barriers (15%).

On the supply side, a BEUC study found that some providers do not offer their savings accounts to non-residents.

A study by INSEAD OEE Data Services (2015) and one by BEUC (2015) showed that national markets still differ widely in terms of the savings account conditions offered, distribution and regulatory treatment. Some specific characteristics such as taxation benefits for savings accounts opened in the country of residence but not in other Member States, clearly hampering market integration.

This is line with the results from the consumer survey which shows that of those 6% of respondents that opened or tried to open a payment account in another Member State, one third did not manage to access the offers in that country because the website was blocked or they were redirected to a domestic or global website and 2% managed to access the offers but could not finish the transaction. 40% had problems understanding the information provided. Of those that manage to open an account more than half considered the process difficult.

*Table 5. Overview of baseline and endline*

Indicator	Baseline	Endline
% Sales at distance	Low (no quantitative data available)	46% in 2018 <sup>260</sup>
Type of provider	Mainly traditional providers	Well established banks (76%)

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<sup>257</sup> IPTS, Joint Research Centre EC (2003) Adoption of Internet Services in the Enlarged European Union, Lessons from the banking industry.

<sup>258</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>259</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>260</sup> Global Banking Survey by Deloitte 2018.

		New operators such as FinTechs (24%)
Most used means of communication	Face to face (no quantitative data available)	1) Face-to-face (54%) 2) Desktop, laptop or tablet (30%) 2) Smartphone (11%) 3) Telephone (5%)
Cross-border sales	Almost non-existent (no quantitative data available)	Very limited (1% of total sales)
Main barriers	<p>Low digitalisation of providers</p> <p>Low digital literacy of consumers and preference for face-to-face</p> <p>Regarding cross-border:</p> <ul style="list-style-type: none"> <li>- Lack of a harmonised regulatory framework regarding the selling stage, contract stage and complaints/redress and tax</li> <li>- Entrance cost</li> <li>- Cultural barriers</li> <li>- Uncertainty about rights and redress mechanisms</li> </ul>	<p>No significant barriers to distance marketing except for the prevailing preference for face-to-face</p> <p>Regarding cross-border:</p> <ul style="list-style-type: none"> <li>- Different tax regimes;</li> <li>- Entrance costs</li> <li>- Information difficult to access and to understand</li> <li>- Burdensome process</li> </ul>

Source: ICF compilation

### 7.3 Legal framework

The following legislation is applicable to Savings Accounts: 1) Distance Marketing of Financial Services Directive (DMFSD); 2) e-Commerce (ECD); 3) Unfair Commercial Practices Directive (UCPD); 4) General Data Protection Regulation (GDPR); 5) Deposit Guarantee Scheme Directive (DGSD); 6) e-Privacy Directive (EPD), under certain circumstances<sup>261</sup>.

As per the legal analysis done in the context of this evaluation:

- The DMFSD is the key Directive regulating pre-contractual information requirements for savings accounts, as they are more stringent than the ones imposed by the DGSD (Article 16);
- The DMFSD is the key Directive regulating the right of withdrawal for savings accounts as the DGSD does not provide for this right;
- The EDP and GDPR are the key pieces of EU legislation regulating unsolicited communications (even if DMFSD, ECD and UCPD also regulate this aspect);

<sup>261</sup> According to Article 3 EDP applies only when the product is provided by means of publicly available electronic communications services.



- The DMFSD together with the UCPD are the main Directives regulating unsolicited services in the context of financial services and therefore savings accounts.

#### **7.4 Assessment in relation to the DMFSD objectives**

##### **Challenges for consumers and the impact of the DMFSD on the protection of consumers**

Based on the data collected for payment accounts in the consumer survey, the information about the service, supplier and terms and conditions is usually provided (79%-95% depending on the information element considered) and often it is provided spontaneously by the provider. According to the same survey, only between 48%-54% of respondents considered that pre-contractual information on payment accounts was:

- Presented in a way suitable for the used device (54%);
- Provided sufficiently in advance (50%)
- Allowed to make an informed decision (48%)
- Presented in a format that allowed to compare different payment accounts (48%);
- Included adequate information on the right to complaint and seek redress (44%) and on the right of withdrawal (43%);
- Clear, easy to understand and well structured (43%).

Furthermore, the London Economics study found that in the pre-contractual phase of savings accounts:

- Often key information was missing or difficult to find (e.g., regarding the possibility to purchase the savings accounts fully online or territorial restrictions);
- Sometimes the information provided is complex and difficult to understand (e.g., on the duration of the offer);
- Often the precontractual information provided emphasised benefits while costs are hidden or given lower prominence;
- Sometimes the information was layered and located in places that can be overlooked and provided in a format not adapted to medium used.

These findings show that although compliance with the DMFSD requirements is medium-high, the effectiveness of the DMSFD in protecting consumers could increase if it would cover unaddressed aspects related to the provision of information that can prevent consumers of savings accounts of making well informed decisions. This includes aspects related to the quality of the information provided, how it is presented in a way that helps consumers properly read it, understand it and compare it with information about other alternative accounts and when and how it is presented.

There is no data on the challenges with the practical implementation of the right of withdrawal for savings accounts. However, almost one quarter of the respondents of the consumer survey considered that the time allocated to review the information about the payment account was not enough and that they felt pressured into making a quick decision. Consequently, there are some risks that consumers of savings accounts enter into a contract based on an ill and rushed decision, and that the right of withdrawal is needed to ensure that these customers have the possibility to cancel these ill-informed contracts.

Regarding unsolicited communications and services there are no grounds which indicate particular challenges related to savings accounts. Nevertheless, according to the LE Europe (2019), most of the operators offering savings accounts also offer other financial products and services, which makes the provision of unsolicited services a possibility.

Other challenges found by the London Economics study related to elements not covered by the DMFSD including potential harmful practices on advertising current accounts as benefits are often emphasised while costs are hidden or given lower prominence, and to a minor degree missing product-specific contact information sections (e.g.: chat

boxes) and the existence of different applications based on customer-provider relationship (emphasising the benefit for existing customers).<sup>262</sup>

### **Challenges for providers and the impact of the DMFSD on the distance market of financial services**

The evaluation considers that the DMFSD plays an important role in creating a level playing field in the context of savings accounts as it ensures that both traditional providers and non-traditional providers have to comply with the same rules, even if the savings accounts offered by them have different characteristics (e.g., as mentioned some FinTechs offer savings accounts in a virtual currency).

The impact of the DMFSD on cross-border sales of savings accounts is very limited as key consumer and supply barriers are beyond the influence of the DMFSD (e.g., lack of harmonisation of tax regimes, or preference for domestic providers).

### **7.5 Analysis of existing gaps and possible measures to improve Consumer Confidence and Empowerment and to develop the market for distance selling of these products.**

Based on the evidence collected, there are a few aspects unaddressed by the DMFSD and other EU legislation that can hinder the consumer decision process and lead either to poor decisions or to lack of trust in distance marketing channels and preference to conclude contracts face-to-face. As mentioned above, this includes rules (including indicators that allow to assess compliance with these requirements) on the quality of the information to be provided at pre-contractual stage and how and when it should be presented in order to ensure that the consumer is aware and understands relevant information about the supplier, the service and the terms and conditions. Remedies to this are provided, for example, by the EBA opinion on DMFSD<sup>263</sup> and LE Europa (2019)<sup>264</sup>.

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<sup>262</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>263</sup> Available at: <https://eba.europa.eu/file/147201/download?token=tUEycHID>

<sup>264</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services.

## 8 Case Study 7: Investments

### 8.1 Introduction

The **investor** is a person who extends money or financial instruments to an investment firm for the purpose of investment in financial instruments. The investor transfers money or securities to the investment firm, which will subsequently engage in a speculative activity, the investment.<sup>265</sup> Investment products include:

- **Stocks** (also known as "shares" or "equity") are a type of security that signifies proportionate ownership in the issuing corporation. This entitles the stockholder to that proportion of the corporation's assets and earnings.<sup>266</sup> Most companies issue common stock, which comes with voting rights, giving shareholders more control over the business. Preferred stock typically does not offer appreciation in value or voting rights in the corporation. However, this stock typically has set payment criteria; a dividend that is paid out regularly, making the stock less risky than common stock.<sup>267</sup>
- **Bonds** are securities representing the debt of the company or government issuing it. When a company or government issues a bond, it borrows money from the bondholders; it then uses the money to invest in its operations. In exchange, the bondholder receives the principal amount back on a maturity date stated in the indenture, which is the agreement governing a bond's terms.<sup>268</sup>
- An **exchange traded fund** (ETF) is an investment fund that invests in a basket of stocks, bonds, or other assets. ETFs are traded on a stock exchange, just like stocks. Investors are drawn to ETFs because of their low price, tax efficiency and ease of trading.<sup>269</sup>
- A **mutual fund** is an investment company that pools money from many investors and invests it based on specific investment goals. The mutual fund raises money by selling its own shares to investors. The money is used to purchase a portfolio of stocks, bonds, short-term money-market instruments, other securities or assets, or some combination of these investments.<sup>270</sup>
- An **option** is a contract in which the writer (seller) promises that the contract buyer has the right, but not the obligation, to buy or sell a certain security at a certain price (the strike price) on or before a certain expiration date, or exercise date. Options contracts are used both in speculative investments, in which the option holder believes he/she can secure a price much higher (or lower) than the fair market value of the underlying on the expiration date.<sup>271</sup>
- **Forex** (Foreign Exchange or FX) is the trading of one currency for another. Foreign exchange transactions can take place on the foreign exchange market, also known as the Forex market. The forex market is the largest, most liquid market in the world, with trillions of dollars changing hands every day. There is no centralized location, rather the forex market is an electronic network of banks, brokers, institutions, and individual traders (mostly trading through brokers or banks).<sup>272</sup>
- **Virtual currency** is any form of currency that only exists digitally, that usually has no central issuing or regulating authority but instead uses a decentralized

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<sup>265</sup> Legal Analysis

<sup>266</sup> Investopedia, 2019, available at <https://www.investopedia.com/terms/s/stock.asp>

<sup>267</sup> Investopedia, 2019, available at <https://www.investopedia.com/terms/s/shares.asp>

<sup>268</sup> Farlex Financial Dictionary, 2012

<sup>269</sup> BlackRock, available at <https://www.blackrock.com/us/individual/education/ishares-etfs>

<sup>270</sup> FINRA, available at <https://www.finra.org/investors/insights/mutual-funds>

<sup>271</sup> Farlex Financial Dictionary, 2012

<sup>272</sup> Investopedia, 2019, available at <https://www.investopedia.com/terms/f/foreign-exchange.asp>

system to record transactions. Under some circumstances they can be considered investments (see case study 3).

## **8.2 The evolution of the market**

Eurobarometer surveys show that the percentage of respondents that own shares, bonds or investment funds has decreased between 2003 and 2016 (it was 28% in 2003, 22% in 2011 and 18% in 2016).

There is no data available about investments purchased at the distance when the DMFSD was implemented. In 2008, a Civic report shows that for the consulted banks involved in distance marketing, stocks/shares and bonds were the third most relevant financial service. Eurostat data for 2016-2018, shows that in that period the percentage of EU population<sup>273</sup> that bought or sold shares, bonds, funds or other investment services over the internet was relatively low (4% in 2016 and 5% in 2018 but grew significantly (about 13% to 25% in two years). The consumer survey shows that of the respondents that bought at least one financial service at a distance in the last five years, 40% had bought bonds, stocks, future and options, 29% virtual currencies and 20% other investments. Of the financial services purchased, investments were the fourth most common service acquired.

According to the Eurobarometer surveys, in 2003 8% of the investments owned by the respondents were bought in another Member State, which dropped to 6% in 2011 and went slightly up to 7% in 2016. The consumer survey suggests that in 2019, 34% of respondents that purchased investments using a distance means of communication did it from a provider located in another Member State.

Data available for some EU Member States for 2009 shows that the main providers of investment products were mainly banks (above 50% of market share), followed by investment companies and investment advisors.<sup>274</sup> In recent years, while the market is still dominated by traditional operators, FinTechs have gained ground by bringing innovative and disruptive conceptions of investment and trading. Worldwide, while in 2003 only 1% of the retail investment market was done through FinTech operators, in 2015 that percentage rose to 8%.<sup>275</sup> Currently the most common online investment platforms are fund supermarkets, online brokers and banks offering their own online platform. A fund supermarket is an online platform that allows an investor to invest in a wide range of funds from many different fund providers using just one account. An online broker, on the other hand, is another type of order execution broker that generally targets highly sophisticated and self-directed investors and, in many cases, primarily focuses on complex products while providing little research or guidance service. Retail investors also have another option to access online investment platforms thanks to a number of banks offering their own online platforms for investment.<sup>276</sup> Innovative services introduced by FinTechs in the area of retail investment include robo-advisory platforms and alternative funding platforms (e.g., P2P investment platforms and social trading platforms).

On the channels used to purchase/sell investments at distance, there is no data for 2004. In 2008 the majority of banks (67%) surveyed by Civic (2008) provided a combination of channels to conclude contracts.<sup>277</sup> Based on the consumer survey, respondents that purchased investment products at the distance did it mostly over the

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<sup>273</sup> Population aged between 16 and 74.

<sup>274</sup> Chater, N., Huck, S. and Inderst, R., 2010. Consumer decision-making in retail investment services: A behavioural economics perspective. *Report to the European Commission/SANCO*.

<sup>275</sup> See <https://caia.org/aiar/access/article-1021>.

<sup>276</sup> European Commission, 2018, Distribution systems of retail investment products across the European Union

<sup>277</sup> Civic Consulting, GHK, Van Dijk, 2008, Analysis of the Economic Impact of Directive 2002/65/EC concerning the distance marketing of consumer financial services on the conclusion of cross-border contracts for financial services between suppliers and consumers within the Internal Market

internet (48% online in a website and 19% by email); 24% used the phone and 5% by post.

There is no specific data for barriers to domestic and cross-border purchase/sales of investment products at the distance. However, it is reasonable to assume they were similar to the barriers to distance marketing of financial services in general. On the consumer side those included concerns over lack of information, concerns over who to turn in case of complains and to seek redress, and a preference for face-to-face contact and for domestic providers and language barriers. On the supply side those included lack of regulatory harmonisation (including tax regimes), entrance costs and low demand.

According to the consumer survey, of the respondents that considered purchasing an investment product using a distance mean of communication 62% finalised the transaction using a distance mean of communication, while 17% finalised it face-to-face and 21% decided not to purchase the investment product. The main reasons indicated by those that decided not to purchase the product were: concerns about purchasing financial services at the distance and there was no physical branch of the provider (24%), the information provided was not sufficient for making an informed decision, the provider was deemed to request too many personal details (14%) or the provider was from another MS (10%). This data suggests that the preference for (the possibility of) face-to-face contact and lack of information are still barriers to distance marketing of investments (domestic and cross-border).

Regarding cross-border transactions of investments, there is a clear preference for domestic providers. Other aspects play also a role as suggested by the results of the consumers survey, as 38% of the respondents that considered purchasing an investment at distance would not do it from another EU Member State because they are unsure about their rights or where to turn to get redress in case of a problem (39%), they are satisfied with the services and conditions offered in their country/area (35%), they prefer face-to-face contact (17%) or because of language barriers (9%).

There is no concrete data on supply-side barriers, but regulatory differences between Member States related to tax regimes for example, entrance costs, need to adapt to different cultural aspects (e.g., language) may play a role.

In the mystery shopping exercise, in about 30% of the cases the mystery shopper did not manage to access the website of a provider in another Member States as the website was block or redirect them to a domestic or global website. This is in line with the data collected in the consumer survey, as 56% of the respondents that had tried to purchase investment products cross-border reported that the website was blocked (20%) or they were redirected (33%) or they did not manage to conclude the transaction (3%).

*Table 6. Overview of baseline and endline by indicator*

<b>Indicator</b>	<b>Baseline</b>	<b>Endline</b>
Sales	No data available for distance sales	5% has purchased an investment product online in 2018
	28% Eurobarometer respondents owned shares	
Type of provider	Banks mostly	Still traditional operators with FinTechs gaining some terrain

Indicator	Baseline	Endline
Most used means of communication	No data available	Data from consumer survey: online in a website (48%), followed by phone (24%), email (19%) and 5% post.
Cross-border sales	No data for distance sales  7% of the investment products owned by Eurobarometer respondents were purchased in another Member State	Consumer survey:  34% of the investments purchased at distance were obtained from a provider in another Member State
Main barriers	Preference for face-to-face contact  Lack of information  Concerns over who to turn to in case of problems  Lack of digitalisation and digital literacy	Preference for face-to-face contact  Preference for domestic providers  Concerns over who to turn to in case of problems

Source: ICF compilation

### 8.3 Legal framework

The following legislation is applicable to Investments: 1) Distance Marketing of Financial Services Directive (DMFSD); 2) Directive on investor compensation schemes (ICSD); 3) Market in Financial Instruments Directive (MiFID II)<sup>278</sup>; 4) Regulation on markets in financial instruments (MiFIR)<sup>279</sup> 5) e-Commerce Directive (ECD); 6) Undertakings for the collective investment in transferable securities Directive (UCITS); 7) Prospectus Regulation 2017/1129<sup>280</sup>; 8) Alternative investment fund managers Directive (AIFMD)<sup>281</sup>; 9) General Data Protection Regulation (GDPR); 10) e-Privacy Directive

<sup>278</sup> Article 1.1 This Directive shall apply to investment firms, market operators, data reporting services providers, and third-country firms providing investment services or performing investment activities through the establishment of a branch in the Union. 'Investment services and activities' means: (1) Reception and transmission of orders in relation to one or more financial instruments; (2) Execution of orders on behalf of clients; (3) Dealing on own account; (4) Portfolio management; (5) Investment advice; (6) Underwriting of financial instruments and/or placing of financial instruments on a firm commitment basis; (7) Placing of financial instruments without a firm commitment basis; (8) Operation of an MTF; (9) Operation of an OTF [...].

<sup>279</sup> Article 1 para 2 This Regulation applies to investment firms, authorised under MiFID II and credit institutions authorised under Capital Requirements Directive when providing investment services and/or performing investment activities and to market operators including any trading venues they operate

<sup>280</sup> (7) The aim of this Regulation is to ensure investor protection and market efficiency, while enhancing the internal market for capital. The provision of information which, according to the nature of the issuer and of the securities, is necessary to enable investors to make an informed investment decision ensures, together with rules on the conduct of business, the protection of investors [...].

<sup>281</sup> This Directive aims at establishing a framework capable of addressing the potential risks which might arise from the activities of AIFMs and ensuring the effective monitoring of those risks by the competent authorities within the Union. It is necessary to provide for a stringent regulatory and supervisory framework which leaves no gaps in financial regulation. In that regard reference is made to the existing due diligence requirements applicable to professional investors pursuant to the relevant regulation applicable to such investors.

(EPD), 11) Packaged retail investment and insurance products Regulation (PRIIPs),<sup>282</sup> under certain circumstances.<sup>283</sup>

In terms of other instruments at EU level, the European system of financial supervision (ESFS) was introduced in 2010, consisting of the European Systemic Risk Board (ESRB) and 3 European Supervisory Authorities, out of which, of relevance for the investments market are the European Banking Authority (EBA) and the European Markets and Securities Authority (ESMA). This system is currently under review and in mid-2019 the European Parliament and Member States agreed on the core elements of reforming the European supervision in the areas of EU financial markets.

ESMA and EBA issue guidelines, technical standards, opinions and provide reports and statistics on various topics related to investor protection under MiFID II/MiFIR intended to achieve a high level of harmonised protection for investors by ensuring good conduct from firms that sell or advise consumers to buy financial instruments. For example, ESMA and the EBA recently developed complaint handling guidelines for the investment and banking sectors<sup>284</sup> in order to provide EU consumers with a single set of complaints handling arrangements.

### **Pre-contractual information**

The provisions on the pre-contractual information are covered by all the mentioned product-specific legislation, the DMFSD and ECD. The MiFID II, the UCITS, the PRIIPs and the AIFMD contain very detailed pre-contractual information requirements and include most of the information foreseen under DMFSD but in a more targeted manner. They also impose specific information requirements adapted to the characteristic of the investment products they regulate.

The MiFID II lays down a pre-contractual information list tailored to the specificities of the investment product aimed at giving the clients the time to read and understand it before taking an investment decision. For instance, the financial providers are required to inform the consumer about the description of products and related policies on asset protection, conflicts of interest and execution of orders<sup>285</sup>. However, contrary to the DMFSD, the MiFID does not include a requirement to provide information on the public register where the supplier is registered and on the relevant supervisory authority, on the identity of the investment firm and geographical address in which the supplier is registered, on the existence/absence of a right of withdrawal and on the right to terminate the contract early and on redress mechanisms.

The UCITS requires investment and management companies to draw up a short document containing key information for investors (such as the description of the investment objectives, costs and associated charges, the risk connected to the investment) and demands the publication of the mentioned document.<sup>286</sup> However, unlike the DMFSD, the UCITS Directive does not foresee any provision on redress and on the law applicable to the contract.

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<sup>282</sup> According to Article 3 EDP applies only when the product is provided by means of publicly available electronic communications services.

<sup>283</sup> PSD2, Art. 3 (Exclusions): This Directive does not apply to the following: [...] (h) or by investment firms, credit institutions, collective investment undertakings or asset management companies providing investment services and any other entities allowed to have the custody of financial instruments; CRD, Art. 3 (Exclusions): This Directive does not apply to contracts: financial service (any service of a banking, credit, insurance, personal pension, investment or payment nature). UCPD: This Directive addresses commercial practices directly related to influencing consumers' transactional decisions in relation to products. It does not address commercial practices carried out primarily for other purposes, including for example commercial communication aimed at investors, such as annual reports and corporate promotional literature.

<sup>284</sup> EBA, 2018, Guidelines for complaints-handling for the securities (ESMA) and banking (EBA) sectors, applicable from 1<sup>st</sup> of May 2019

<sup>285</sup> Articles 23, 24 and 25

<sup>286</sup> Articles 78, 79, 80 and 81 of UCITS. See also Art. 63, art.64, Chapter IX and Schedule A of Annex I.

Similarly, Article 23 of AIFMD foresees pre-contractual information on several aspects tailored on alternative investment funds. However, as opposed to DMFSD, the Directive does not require to provide information on the public register where the supplier is registered, on the relevant supervisory authorities, and information on redress.

The PRIIP covers a standard range of investment products typically offered by a bank to consumers, for example, in order to save for a specific objective such as a house purchase or for a child's education. Those selling or advising on these investment products have to provide the Key Information Document (KID) to an investor before any agreement is made. KIDs should be a maximum of 3 pages and provide clear information on a product allowing the investor to take an informed investment decision. When an investment product is very difficult to understand, the provider has to ensure the KID contains the following warning: 'You are about to purchase a product that is not simple and may be difficult to understand'. Article 14 PRIIPs allows for the provision of information on paper, using a durable medium or by means of a website. DMFSD only foresees the use of paper or another durable medium. PRIIPs also list the conditions under which the information can be provided through a website.

The Prospectus Regulation also aims at enabling investors to make informed investment decisions. It ensures, together with rules on the conduct of business, that the pre-contractual information is published in a prospectus in an easily analysable, concise and comprehensible form.<sup>287</sup> To this end, the Regulation provides for a list of necessary information that should be included in the prospectus<sup>288</sup>, while also foreseeing the obligation to draw up a summary<sup>289</sup> with the key evidence of the nature and the risks of the issuer, the guarantor and the securities that are being offered or admitted to trading. The approved documents remain publicly available in electronic form for at least 10 years after the publication on the relevant websites.<sup>290</sup> The latter mentioned provisions are therefore in line with the DMFSD that requires to provide the information in paper or any other medium available and accessible to the consumers.<sup>291</sup>

The Directive on investor compensation schemes provides that Member States should ensure that each investment firm takes appropriate measures to make available, to actual and intending investors, the information necessary for the identification of the related investor-compensation scheme - of which the investment firm and its branches within the Community are members - or any alternative arrangement provided. That information must also be made available in a comprehensible manner<sup>292</sup>.

### **Right of withdrawal**

The right of withdrawal is expressly foreseen in Article 6 DMFSD and ensures consumers have a period of 14 calendar days to withdraw from the contract concluded without penalty and without need of providing any justification. However, according to Article 6.2, the right of withdrawal shall not apply to financial services whose price depends on fluctuations in the financial market outside the suppliers' control, such as services related to units in collective investment undertakings.

Moreover, the Prospectus Regulation states that the publication of a supplementary prospectus<sup>293</sup>, entitles investors in some circumstances to a right of withdrawal that

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<sup>287</sup> A prospectus contains the information an investor needs before making a decision whether to invest in a company's securities (such as shares, bonds, derivatives), such as company's main line of business, its finances and shareholding structure and the securities that are being issued and/or admitted to trading

<sup>288</sup> Article 6

<sup>289</sup> Article 7

<sup>290</sup> Article 21

<sup>291</sup> Article 5 DMFSD

<sup>292</sup> Article 10

<sup>293</sup> Article 23 requires a supplement when new elements arise between the time when the initial prospectus is approved and the closing of the offer period or the time when trading on a regulated market begins



needs to be exercised within two working days or any longer period specified by the issuer. Additionally, article 17 also provides for a minimum of two days after the final offer price and/or amount of securities to be offered to the public has been filed, during which the investor can withdraw his acceptance of the purchase or subscription of securities.

### **Unsolicited services and communications**

The EPD and the GDPR lay down a complex set of measures aimed at countering unsolicited commercial communications, which go beyond the ones set in the DMFSD. Additionally, the UCPD and the DMFSD provide for rules about unsolicited services.

## **8.4 Assessment in relation to the DMFSD objectives:**

### **Challenges for consumers and the impact of the DMFSD on the protection of consumers (past, current and expected future)**

#### ***Pre-contractual information***

A recent study<sup>294</sup> shows that information on nearly all investment products is available on intermediaries' websites in the different Member States, however the documentation provided is not systematically transparent (especially regarding costs to be supported by the investor after the acquisition of said products). Specifically, for some products, e.g. bonds and equities, information needs to be retrieved from a "central" tariff sheet displaying all types of fees across the institution's services. For other products, e.g. funds, the Key Information Document (KID)<sup>295</sup> contains the essential information of the product, including costs and charges. Moreover, information on investment products is not standardised across Member States and sometimes proves difficult to understand. According to stakeholders consulted for this evaluation, information provided needs to be concise and understandable for the average consumer and more guidance for certain complex types of products should be provided by the traders in order for consumers to really understand how they operate.<sup>296</sup>

More than 60% of respondents to the consumer survey indicated that it was very important to them to receive pre-contractual information about the supplier, the product and the terms and conditions. The overwhelming majority (88%-95%) of the respondents also indicated that it was important that the information is presented prominently and immediately in a format that enables comparison with other products and in a way that is adapted to the channel and that they are able to choose the format in which they can access the information.

According to the same respondents, most have received information about the supplier, the investment products and the terms and conditions of the contract (78% to 96% depending on the information element surveyed). The majority (between 53% and 65%) also agrees that the information provided was clear, easy to understand and well structured, was complete and presented in a format that enabled comparison, it was provided sufficiently in advance to give sufficient time for review, it allowed for making an information decision and was presented in a way that was suitable for the specific device on which it was accessed. Nevertheless, more than 31% of respondents considered that the information provided was not clear, easy to understand or well-structured and 21% considered that the time allocated to review the offer was not enough and felt pressured into making a quick decision.

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<sup>294</sup> European Commission, 2018, Distribution systems of retail investment products across the European Union

<sup>295</sup> The Key Investor Information Document (KID) is a document that provides information about investment funds, in order to help a potential investor, compare different investment funds. It is required by both UCITS Directive and PRIIP Regulation.

<sup>296</sup> Stakeholders interviews and Open Public Consultation

Data from the mystery shopping exercise where mystery shoppers simulated the purchase of stocks online or by phone, shows that:

- 26% of the mystery shoppers found that information about the stocks was difficult to understand, while 10% consider it difficult to find;
- In 12% of the cases the information about the supplier was difficult to understand and in 15% difficult to find;
- 29% of the mystery shoppers found the information about the terms and conditions of the contract difficult to understand and 27% found it difficult to find.

The aforementioned evidence shows that while compliance with pre-contractual requirements tends to be relatively medium-high, in some cases consumers find the information difficult to understand. This may be related to the fact that investment products tend to be complex products and also because the information received is not easy to analyse and understand.

Another important aspect is related that many users of online services rely on comparison websites for offers of different providers of investment products such as online services of banks, fund supermarkets and online brokers. Consequently, the trustworthiness and quality of the information provided on these websites may be an issue as the products shown can be linked to a given service provider.<sup>297</sup>

### ***Right-of-withdrawal***

In the overwhelming majority of cases the price of investment products “depends on fluctuations in the financial market outside the supplier’s control which may occur during the withdrawal period”. Consequently, the right of withdrawal stipulated in the DMFSD generally does not apply to investment products. This exemption prevents speculation by retaining the product in the event of favourable price developments or by exercising the right of withdrawal in the event of unfavourable price developments.<sup>298</sup>

As highlighted above, the Prospectus Regulation contains its own withdrawal rights – these arise where during an offer a significant new factor, material mistake or material inaccuracy related to the information in the prospectus arises. In these circumstances, a supplement to the prospectus must be published providing the new information and investors have a two-day window in which to withdraw any acceptances where the securities have not yet been delivered.<sup>299</sup>

There is no evidence of problems related to the right of withdrawal for investment products.

### ***Unsolicited communications and services***

There is no evidence of challenges related to unsolicited communications and services for investment products.

### **Challenges for providers and the impact of the DMFSD on the distance market of financial services (past, current and expected future)**

Due to extensive products-specific legislation in the area of investments (some since the implementation of the DMFSD), the impact of the DMFSD in creating a level playing field and contributing to consolidate the cross-border market is assessed to be negligible.

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<sup>297</sup> European Commission, 2018, Distribution systems of retail investment products across the European Union

<sup>298</sup> Interviews and surveys of enforcement authorities, Member States, consumer associations and industry representatives.

<sup>299</sup> Interviews and surveys of enforcement authorities, Member States, consumer associations and industry representatives.

## **8.5 Analysis of existing gaps and possible measures to improve consumer confidence and empowerment and to develop the market for distance selling of these products.**

A few important aspects seem poorly addressed by the current legislative framework for retail investment products:

- Information is difficult to analyse and understand which can lead to poor investment decisions. Remedies to this suggested by the EBA opinion on DMFSD<sup>300</sup> and LE Europa (2019)<sup>301</sup> could be taken into account,
- Trustworthiness and quality of the information given by comparison websites and of the advice provided by financial operators. For example, the BEUC's campaign "The price of bad advice" advocates for trustworthy financial advice and calls on EU policymakers to ban sales incentives for investment products and complex financial products, as it is already the case in the Netherlands and UK<sup>302</sup> in order to ensure that advice (both human advice and robo-advice) is not biased but rather trustworthy and of good quality.<sup>303</sup>

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<sup>300</sup> Available at: <https://eba.europa.eu/file/147201/download?token=tUEycHID>

<sup>301</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services.

<sup>302</sup> According to the BEUC study, UK removed the bias in financial advice by banning commissions for retail investment products and transitioning to a fee-based system of financial advice, together with much stronger professional requirements for advisers.

<sup>303</sup> Interviews and surveys of enforcement authorities, Member States, consumer associations and industry representatives.

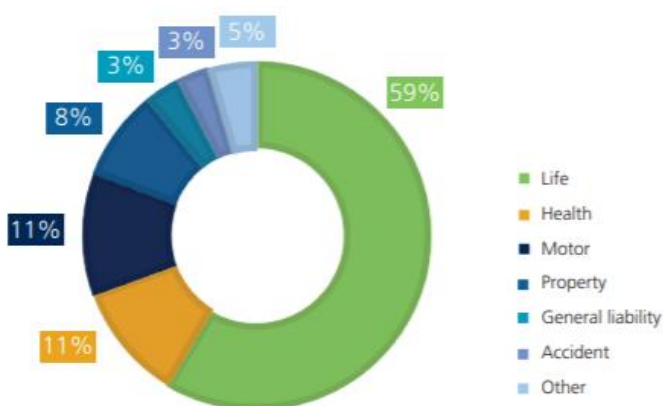
## 9 Case Study 8: Insurances

### 9.1 Introduction

An insurance is a contract, represented by a policy, in which an individual or entity receives financial protection or reimbursement against losses from an insurance company. Insurance policies are used to hedge against the risk of financial losses, that may result from damage to the insured or his property, or from liability for damage or injury caused to a third party<sup>304</sup>.

Insurances comprise life-insurances and the non-life insurances. Life insurance policies can take form of individual or group contracts, and they can be products offering protection, savings products or a combination of both<sup>305</sup>. Non-life insurances include health insurances, travel insurances, property insurances, motor insurances, accident insurances and general liability insurances. See for an overview of the distribution of gross written premiums per type of insurance in 2017.

Figure 6. Gross written premiums in Europe in 2017



Source: Insurance Europe, 2018<sup>306</sup>

### 9.2 The evolution of the market

A 2008 study found that the market size of distance marketing of insurance products and services was difficult to measure, since there were no standardised EU-level statistics issued on the proportion of sales coming from distance means of communications. Nevertheless, the literature and the data collected from a survey to national associations revealed that insurance contracts via distance marketing in the EU27 was not yet widespread among consumers and accounted for only 1.8% of their members' total premium income<sup>307</sup>.

A study conducted by Finaccord shows that online channels in France, Germany, Italy, Poland, Spain and the UK represented 42% of motor and household insurance policy purchases in 2012, compared to 35% in 2008.<sup>308</sup> The Eurostat data available indicates that the percentage of the population that has purchased at least one insurance product over the internet has been growing steadily since 2016 at around 9% per year (11% in 2016, 12% in 2017, and 13% in 2018). According to London Economics study (2019)

<sup>304</sup> INVESTOPEDIA, Last visited: 29 September 2019 <https://www.investopedia.com/terms/i/insurance.asp>

<sup>305</sup> Insurance Europe (2017) European Insurance – Key Facts

<sup>306</sup> Insurance Europe 2018. European Insurance – Key Facts 2018. Available at: <https://www.insuranceeurope.eu/sites/default/files/attachments/European%20insurance%20-%20Key%20facts%20-%20October%202018.pdf>

<sup>307</sup> Financial study 2008

<sup>308</sup> Finaccord, 2013, Aggregation Metrics: Consumer Approaches to Insurance Comparison Sites in Europe.

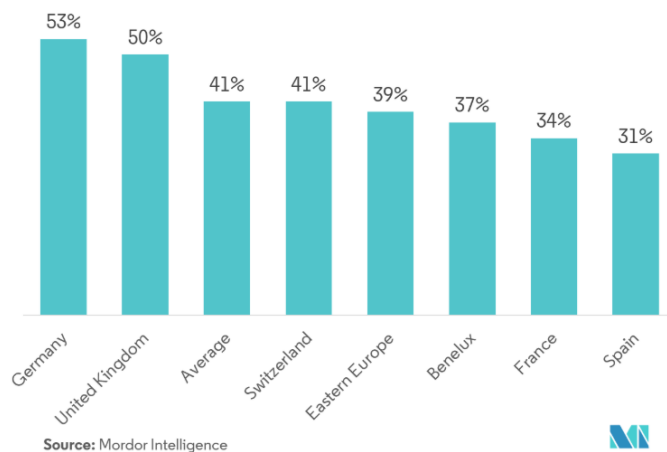
motor insurances and travel insurances are the insurances mostly sold online (directly or through price comparison websites).<sup>309</sup> This is to some extent in line with the data collected through the consumer survey, as from the total insurances purchased by the respondents in the last five years, the majority was motor insurances, followed by travel insurances and home/property insurances.

According to a recent study from Mordor intelligence<sup>310</sup>, the online insurance channel in Europe grew significantly between 2000 and 2015 (about 22%, which is considerably higher than growth of the overall market in the same period, i.e., 15%) and in 2015 it represented 8.2% of the total business. The same study indicates that the online insurance market in Europe is forecasted to grow 7.6% between 2019 and 2024.

Traditionally, insurers sell their products either directly or through a variety of distribution channels, of which the most commonly known are brokers, agents and *bancassurance*. The diversity in distribution channels benefits consumers, who have better access to products. Banks were and still are the main life distribution channels in many European countries today but have a much more modest share in non-life insurances. Intermediaries (agents, and to a lesser extent, brokers) are the largest distribution channel for non-life.<sup>311</sup>

Following the digitalisation trend, banks and insurance companies are investing heavily in digitalising their sales and customer services in the hope of making cost savings and engaging more closely with their existing customers. Furthermore, new market players (such as InsurTechs and third-party comparison websites), which often provide their services/products online only, are also gaining ground. According to Mordor (2019)<sup>312</sup>, in 2016 there were more than 439 insurers with online channels, 214 major aggregators, and 47 top InsurTech companies operating in Europe.

Figure 7. Preference of customers to buy insurance through price comparison websites, by country, in 2016



Source: Mordor Intelligence, 2019<sup>313</sup>

<sup>309</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>310</sup><sup>310</sup> Mordor Intelligence 2019. Europe Online Insurance Market - Growth, Trends And Forecast (2019-2024). See: <https://www.mordorintelligence.com/industry-reports/europe-online-insurance-market>

<sup>311</sup><sup>311</sup> Insurance Europe 2018. European Insurance — Key Facts 2018. Available at: <https://www.insuranceeurope.eu/sites/default/files/attachments/European%20insurance%20-%20Key%20facts%20-%20October%202018.pdf>

<sup>312</sup><sup>312</sup> Mordor Intelligence 2019. Europe Online Insurance Market - Growth, Trends And Forecast (2019-2024). See: <https://www.mordorintelligence.com/industry-reports/europe-online-insurance-market>

<sup>313</sup><sup>313</sup> Mordor Intelligence 2019. Europe Online Insurance Market - Growth, Trends And Forecast (2019-2024). See: <https://www.mordorintelligence.com/industry-reports/europe-online-insurance-market>

According to Eurobarometer surveys, between 2005-2016 the cross-border purchases of insurances was limited. In 2019, according to the consumer survey, only 8% of the respondents that have searched for an insurance using a distance mean of communication had purchased it in a Member State, while 28% would consider it in order to find better deals. The remainder of 64% would not consider doing so. According to the same survey, of the total insurance products purchased by the respondents solely using distance means of communication in the last five years, 23% were bought from a provider from another Member State.

A study carried out in 2008 did reveal that for the insurance sector, telephone, fax and post were the more conventional means of distance marketing, even if combined with an online channel. The Internet was mostly used for marketing purposes, or to gather further information on the product. The conclusion of the contract was rarely done online, since contractual information was mostly sent by postal mail<sup>314</sup>.

According to the consumer survey the distance means of communication used by the respondents to purchase an insurance were: online in a website (44%), followed by email (28%), by phone (23%) and by post (3%).

Overall, the main barrier to domestic distance sales of insurances relate to the preference of consumers for face-to-face purchases. As indicated by stakeholders consulted by Suter et al. (2017)<sup>315</sup> websites are sometimes used as an information channel by consumers, which then prefer to conclude the contract face-to-face. Data collected through the consumer survey suggests that one quarter of the respondents that bought an insurance product after using a distance mean of communication to search for information did it face-to-face.

48% of the respondents that searched for information about insurances using a distance mean of communication decided not to purchase the insurance in the end. The main reasons were:

- Concerns about purchasing a service at the distance and there was no physical branch of the provider (42%);
- The product did not suit them (28%);
- The information was not enough to take an informed decision (13%).

On the supply side, Suter et al. (2017) highlights that the *“insurance industry has not yet managed to propose an effective digitalised distribution chain including pre-sales, sales and post-sales phases”*.

- On cross-border sales of insurances, Suter et al. (2017)<sup>316</sup> indicates the following as main consumer-side barriers:
- Concerns over having to go through an insurance claiming process in another country and in an unknown language;
- Fear that foreign insurers do not meet legal requirements, and the perception that foreign providers would not provide coverage in their home country;
- Concerns over lack of information;
- Language barriers;
- Difficulties with solving problems with the contract;

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<sup>314</sup> GHK, CIVIC Consulting, van DIJK Management Consultants (2008). Analysis of the economic impact of Directive 2002/65/EC

<sup>315</sup> Suter, J., Duke, C., Harms, A., Joshi, A., Rzepecka, J., Lechardoy, L., Hausemer, P., Wilhelm, C., Dekeulenaer, F. and Lucica, E., 2017. Study on consumers' decision making in insurance services: a behavioural economics perspective. Retrieved from the EU Law & Publications website: <https://publications.europa.eu/en/publication-detail/-/publication/b86d7f2d-9e77-11e7-b92d-01aa75ed71a1/language-en>.

<sup>316</sup> Suter, J., Duke, C., Harms, A., Joshi, A., Rzepecka, J., Lechardoy, L., Hausemer, P., Wilhelm, C., Dekeulenaer, F. and Lucica, E., 2017. Study on consumers' decision making in insurance services: a behavioural economics perspective. Retrieved from the EU Law & Publications website: <https://publications.europa.eu/en/publication-detail/-/publication/b86d7f2d-9e77-11e7-b92d-01aa75ed71a1/language-en>.

- The perceived complexity of completing a cross-border purchase.

The main barriers from the supply side include different national rules on the terms and conditions of insurance contracts, applicable legal requirements regarding coverage and tax regimes. This leads to entrance costs, compliance costs and legal uncertainty that make cross-border sales less attractive. Additionally, the need to adapt marketing strategies and the difficulty of assessing risks in foreign markets can also constitute important barriers to cross-border sales.<sup>317</sup> In fact, according to the consumer survey, 43% of the respondents that had tried to purchase insurance products in another Member State did not manage to access the website of the provider in that Member State either because it was blocked or because they were redirected. Data from the mystery shopping exercise for travel insurances indicates that the website was blocked in 5% of the cases the uses were redirected to a domestic or global site in 28% of the cases.

Table 7. Overview of baseline and endline by indicator

Indicator	Baseline	Endline
Sales at distance	Distance marketing in the EU27 was not yet widespread among consumers and accounted for only 1.8% of Insurance Europe members' total premium income	Growth of 22% between 2000-2015 About 13% of the EU population has purchased at least one insurance online in the last year
Type of provider	Traditional providers (insurance companies, banks, etc.)	Traditional providers are still more relevant Non-traditional providers such as InsurTechs and third-party comparison websites gaining relevance
Most used means of communication	Face to face, phone, fax, postal mail	Face to face, Online (44%), email (28%) and phone (23%)
Cross-border sales	3% in 2005 (overall)	23% of the total insurances purchased by the consumer survey respondents using distance means of communication in the last five years
Main barriers	Lack of trust Lack of information Language barriers Lack of offer	Regulatory differences between countries Difficulty of assessing risks in foreign markets

Source: ICF compilation

<sup>317</sup> European Commission (2017) Study on Consumer's Decision-Making in Insurance Services: A Behavioural Economics Perspective

### 9.3 Legal framework

The following legislation is applicable to Insurances (life and non-life): 1) Distance Marketing of Financial Services Directive (DMFS); 2) Insurance Distribution Directive (IDD); 3) Unfair Commercial Practices Directive (UCPD)<sup>318</sup>; 4) EU Regulation 1286-2014 on packaged retail and insurance-based investment products (PRIIPs); 5) E-Commerce (ECD); 6) General Data Protection Regulation (GDPR); 7) Unfair Contract Terms Directive (UCTD)<sup>319</sup>; 8) e-Privacy Directive (EPD),<sup>320</sup> under certain circumstances.

#### Pre-contractual information

The Insurance Distribution Directive (IDD) sets a detailed list of pre-contractual information to be provided before the conclusion of an insurance contract (Article 18) as well as the conditions and means through which the mandatory information must be disclosed. The IDD establishes similar pre-contractual information requirements as the ones foreseen under DMFSD and adds additional insurance-specific requirements. By way of example, Articles 20 and 23 respectively list information for non-life insurance products and regulate the conditions for the use of the different means of communication in providing pre-contractual information (website, telephone selling).

Moreover, similarly to the DMFSD, the ECD and the PRIIPs, the IDD establishes that Member States shall ensure that all information (related to the subject of IDD, including marketing communications, addressed by the insurance distributor to customers or potential customers) shall be fair, clear, not misleading and accessible free of charge.

The PRIIPs also contains very detailed pre-contractual information requirements and it requests all PRIIP manufacturers to publish the key information document (KID) which constitutes pre-contractual information. Article 6 PRIIPs states that the KID shall be a stand-alone document, and shall not contain cross-references to marketing material, establishing a higher standard in comparison to the DMFSD. Moreover, it also limits the maximum number of pages (when printed) for the pre-contractual information provided.

Overall, the IDD and PRIIPs have more stringent pre-contractual information requirements than the DMFSD. The only exception are the information requirements related to the right of withdrawal as this right is not foreseen in these two EU legislative pieces and insurances that fall under the category of insurances to which the IDD does not apply (Article 1(3)).

#### Right of Withdrawal

The right of withdrawal for most of insurances is only foreseen in Article 6 DMFSD. Travel and baggage insurance policies or similar short-term insurance policies of less than one month's duration are excluded according to Article 6.2. of the DMFSD.

#### Unsolicited services and communications

The DMFSD, UCPD, GDPR, ECD and EPD lay down a complex set of measures aimed at countering unsolicited commercial communications. Additionally, the DMFSD and the UCPD provide for rules about unsolicited services.

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<sup>318</sup> COMMERCIAL PRACTICES WHICH ARE IN ALL CIRCUMSTANCES CONSIDERED UNFAIR: *Requiring a consumer who wishes to claim on an insurance policy to produce documents which could not reasonably be considered relevant as to whether the claim was valid, or failing systematically to respond to pertinent correspondence, in order to dissuade a consumer from exercising his contractual rights.*

<sup>319</sup> [...] whereas the main subject matter of the contract and the price/quality ratio may nevertheless be taken into account in assessing the fairness of other terms ; whereas it follows, inter alia, that **in insurance contracts**, the terms which clearly define or circumscribe the insured risk and the insurer's liability shall not be subject to such assessment since these restrictions are taken into account in calculating the premium paid by the consumer.

<sup>320</sup> According to Article 3 EDP applies only when the product is provided by means of publicly available electronic communications services.



## **9.4 Assessment in relation to the DMFSD objectives:**

### **Challenges for consumers and the impact of the DMFSD on the protection of consumers**

Data from the consumer survey shows that most of the respondents that search for insurances using a distance mean of communication received information about the supplier, service and the terms and conditions (63% to 89% depending on the information element surveyed). The same respondents assessed the pre-contractual information they received as follows:

- It was clear, easy to understand and well structured (41%);
- It was complete and presented in a format that enabled them to compare it with other insurances (57%);
- It was provided sufficiently in advance to give them time to review it (61%)<sup>321</sup>;
- It allowed them to make an informed decision (63%);
- The information relating to their rights of withdrawal / early termination / cancellation (55%) and relating to their right to complain and seek redress / compensation was adequate (48%);
- It was presented in a way that was suitable for the device they were using (64%).

The London Economics study and the mystery shopping exercise looked into the information provided to or received by consumers at pre-contractual stage for travel insurance sold at distance.

- The London Economics <sup>322</sup> data shows that:
- Often key information missing or difficult to find;
- Often benefits emphasised while costs are hidden or given lower prominence in precontractual information;
- Often information format not adapted to medium used;
- Sometimes information complex and difficult to understand (e.g., what was covered or not) and it was layered and located in places that can be overlooked.

The mystery shopping exercise shows that the mystery shopper usually obtained the required information, however:

- 14% of the mystery shoppers considered the information about the travel insurance difficult to understand and 10% consider that it was difficult to find;
- 22% of the mystery shoppers found the information about the supplier difficult to understand and 21% found it difficult to find.
- 30% of the mystery shoppers found the information received about the terms and conditions difficult to understand and 35% that it was difficult to find.

Together, these findings show that the quality of information, the way it is presented, its accessibility and when it is made available to consumers are still not optimum and can lead to poor decisions from consumers and/or to a preference for face-to-face sales so that more clarity can be obtained directly from the salesperson.

While the IDD and the DMFSD indicate that the information should be clear, understandable, accurate and provided in good time, they do not provide specific rule on how this should be implemented

No challenges were identified with the right of withdrawal not unsolicited communications and services.

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<sup>321</sup> The French Prudential Supervision and Resolution Authority, some insurance providers have interpreted that an e-mail or text message during the phone call fulfils the pre-contractual information requirement (Article 3(1), Article 4 and Article 5.1. of the DMFSD).

<sup>322</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

### **Challenges for providers and the impact of the DMFSD on the distance market of financial services**

The current impact of the DMFSD in the consolidation of the single market of insurances sold at distance is negligible as the IDD and the PRIIPs are the key provisions regulating this market.

Nevertheless, as EIOPA highlighted that with digitalisation and the increased influence of InsurTechs and price-comparison websites, it is possible that new products/services/selling frameworks might emerge and that the DMFSD will be the necessary safety net to avoid possible legal loopholes (because the IDD and PRIIPs do not apply to those new circumstances).<sup>323</sup>

According to an interview made to BIPAR, the DMFSD did not play an important role increasing cross-border access and transactions. On the contrary, IDD or IMD had a positive effect on cross-border access since insurers were provided with a passport.

### **9.5 Analysis of existing gaps and possible measures to improve consumer confidence and empowerment and to develop the market for distance selling of these products.**

The quality and accessibility of information as well as how and when it should be provided to consumers remain challenges. While the DMFSD and product-specific legislation do refer to these subjective aspects, they do not define specific guidelines/indicators on how these should be implemented in practice. Remedies such as the ones proposed by EBA<sup>324</sup> in its opinion paper on the DMFSD and by LE Europe<sup>325</sup> could be considered.

As comparison portals are gaining importance in the distance marketing of insurances, to the lack of clarity in which circumstances and to which comparison websites the IDD and the DMFSD apply are current gaps.

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<sup>323</sup> EIOPA (2017) Insurtech Roundtable: how technology and data are reshaping the insurance landscape

<sup>324</sup> Available at: <https://eba.europa.eu/file/147201/download?token=tUEycHID>

<sup>325</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services.

## 10 Case Study 9: Credit Cards

### 10.1 Introduction

Credit cards are payment cards that enable cardholders to make purchases and/or withdraw cash up to a certain prearranged credit limit. The credit granted may either be settled in full by the end of a specified period (a charge card, essentially a delayed debit card), or settled in part, with the balance comprising a form of credit on which interest is usually charged (a revolving credit card).

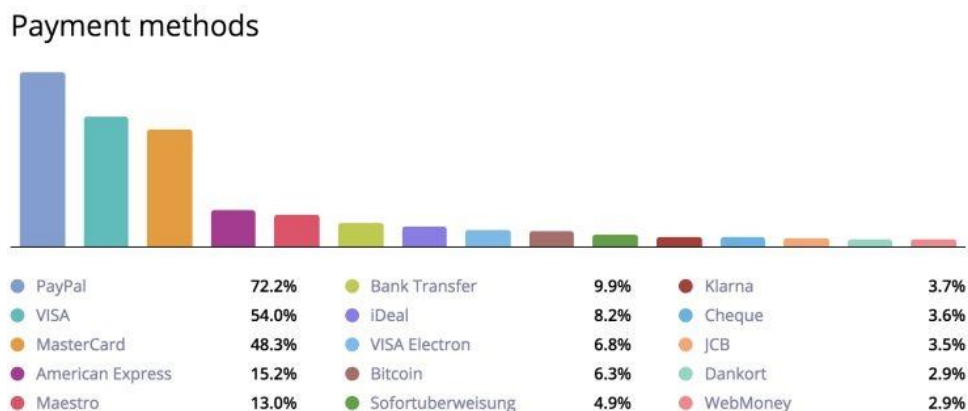
Given that transactions with a credit card are not necessarily directly and immediately charged to the payer, the card scheme's rules and the processing of the transaction, and therefore also the card acceptance environments, can be broader as compared to transactions with a debit card.

The flexibility of credit cards is valued by consumers because it allows consumers to defer payments and spread large expenses over several months. Ultimately, however, this flexibility can be detrimental for consumers, as they generally have continued access to credit if they make minimum payments on their debt. This practice is very likely to play to the disadvantage of consumers, since it rests on several behavioural biases likely to lead consumers to accumulate debt over a long period of time<sup>326</sup>. Consumers may consequently end up in situations where they are making minimum repayments that simply cover the interest and fees, without ever reducing the debt (i.e. persistent debt)<sup>327</sup>. This is highly profitable for credit providers<sup>328</sup>, particularly given the very high cost of a credit card.

### 10.2 The evolution of the market

According to the Eurobarometer surveys, the percentage of the consumers with a credit card had increased between 2003 (45%) and 2016 (49%). An economic study carried out in 2009 for the Commission, reported that credit cards were the third most popular distance marketing product offered by banks. Nevertheless, its popularity is decreasing due to new online payment methods (e.g., digital wallets, tokenization, biometric payments) and products (e.g., hybrid payment cards) that emerged with digitalisation of the financial sector and with the entrance of new players in the market (i.e., FinTechs and comparison websites) and partially due to its complexity.<sup>329</sup>

Figure 8. Popularity of payment methods in Europe



<sup>326</sup> These behavioural biases are: over-optimism: overestimating one's ability to maintain a zero balance; myopia: overvaluing the short-term benefits of a credit transaction and neglecting the future impact; and cumulative cost neglect: dismissing the cumulative effect of a large number of small credit options.

<sup>327</sup> According to the UK Financial Conduct Authority, a persistent debt is defined as a situation where, over a period of 18 months, a consumer pays more in interest, fees and charges than on the principal of the debt.

<sup>328</sup> European Parliament, 2018; BEUC, 2019.

<sup>329</sup> Deloitte (2019) The Future of Credit: A European perspective Summer 2019

Source: *ecommercenews.eu*<sup>330</sup>

In 2011, the Eurobarometer survey shows that the vast majority of respondents that obtained a credit card directly from a provider did it face-to-face (77%), while 16.5% did over the internet and 5.5% through a phone call.

A 2018 study from Deloitte<sup>331</sup> which analysed the credit card market in some EU Member States, concluded that 44% of respondents concluded the contract in a bank branch, while the majority used distance means of communication: 38% did it online (using a variety of devices except a mobile), 11% did it using a mobile and 7% did it through a contact centre (telephone). The consumer survey shows that of the total financial services purchased by respondents at distance in the last five years, around 6% were credit cards.

When the DMFSD was implemented the overwhelming majority of credit cards was provided by traditional banks.<sup>332</sup> Currently, based on the LE Europe study, credit cards are still mainly issued by traditional operators and the bigger banks. In the seven Member States selected for the study, of the 38% of providers of retail financial services offering credit cards online, 79% were traditional operators and 21% were new operators (i.e., FinTechs and other innovative operators).

According to the Eurobarometer surveys for EU-15, between 2003 and 2016 the percentage of respondents that had obtained their credit cards in another Member State decreased from 5% in 2003 to 1.7% in 2011 (most likely due to the financial crisis) but then between 2011 and 2016 it increased more than 40%, reaching 2.3% in 2016. According to the consumer survey, 12% of credit cards obtained by the respondents at a distance in the last five years, where provided by a financial operator located in another Member State. The credit card providers studied by LE Europe (2019) were mostly domestic (74%), while 26% were EU operators.

The consumer survey conducted for the purpose of this evaluation suggests that in the case of credit cards, consumers considered different means of communications for purchasing the aforementioned product. The most popular means of communications appeared to be the Internet, using a desktop, laptop or tablet (46%), followed by smartphones 32%, phone calls (12%) and postal services (9%). The LE Europe (2019) study concluded that 73% of providers of credit cards used both offline and online channels for sales purposes, 25% only online channels (mobile and desktop) and 1% only mobile or only desktop channels.<sup>333</sup>

Barriers to obtain credit cards at distance are likely to be similar to the barriers to obtain credit using distance means of communication. The consumer survey shows that 32% of the respondents that obtained a credit card after searching for one using a distance mean of communication, did it face-to-face with the provider. Preferences for face-to-face over distance means were also the main reason why respondents decided not to finalise the transaction (e.g., 42% of the respondents that did not finalise the transaction justify their decision with concerns about purchasing financial services at the distance and there was no physical branch of the provider). On the supply side, the LE Europe study shows that in some cases the process of obtaining a credit card can only be partially conducted online<sup>334</sup> and has to be finalised face-to-face.

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<sup>330</sup> Available at: <https://ecommercenews.eu/top-3-payment-methods-per-european-country/>

<sup>331</sup> Deloitte (2018) Accelerating Digital Transformation in Banking

<sup>332</sup> London Economics 2014. Study on The Functioning of the Consumer Credit Market in the EU

<sup>333</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>334</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

Regarding cross-border purchases, 63% of the respondents to the consumer survey that considered obtaining credit at distance would not do it cross-border mainly because they were unsure about their rights or where to turn to get redress in case of a problem (32%). 27% would not do it because they are happy with the services offered in their country and 25% would not do it because they prefer face-to-face contact. Of the 9% that tried/did obtain a credit at distance in another Member State, a significant share (around 60%) did not manage to access the offers as the website was blocked or they were redirected to the domestic or global site of the provider.

In line with this evidence, the mystery shopping exercise shows that 20% of the mystery shoppers that simulated an application for a credit card in another Member State did not manage to access the website of the provider in that Member State. Additionally, 25% of the mystery shoppers had problems filling in their residence and did not manage to proceed with the transaction.

Table 8. Overview of baseline and endline by indicator

Indicator	Baseline	Endline
Sales	No data available regarding distance marketing In 2003, 45% of the EU population had credit card	In 2016, 49% of the EU population had a credit card. In 2018, 56% of the credit cards were negotiated at distance
Type of provider	Traditional banks mainly; followed by brand cards.	Mostly traditional banks with new players such as FinTechs on the rise
Most used means of communication	Mostly offline In 2011, 15% did over the internet and 5% over a phone call	Mostly at distance. In 2018, 38% online (using a variety of devices except a mobile), 11% mobile banking and 7% did it through a contact centre
Cross-border sales	2% of Europeans had obtained a credit card from a provider in another MS in 2003	In 2016, 1% had obtained a credit card from a provider in another MS
Main barriers	No data available specific for credit cards, but overall the main barriers were: Lack of trust and low digital literacy Lack of offer due to low digitalisation and possible regulatory uncertainty and disparities	Preference for face-to-face Concerns over redress Limited cross-border offer

Source: ICF compilation

### 10.3 Legal framework

The following legislation is applicable to credit cards agreements: 1) Distance Marketing of Financial Services Directive (DMFSD); 2) Consumer Credit Directive (CCD); 3) Payment Services Directive (PSD II), 4) e-Commerce Directive (ECD); 5) Unfair

Commercial Practices Directive (UCPD); 6) General Data Protection Regulation (GDPR); 7) ; 6) e-Privacy Directive (EPD)<sup>335</sup> under certain circumstances.

Pre-contractual information requirements and right of withdrawal are, for most credit cards, regulated primarily by the CCD. Exceptions are credit cards with a credit limit below EUR 200 or that require the credit to be repaid within three months and only insignificant charges are payable.

In some cases, the PSD II applies (although according to recital 40, without prejudice to Directive 2008/48/EC) to credit cards that were granted in order to facilitate payment services and that grant credit of a short-term nature and for a period not exceeding 12 months.

Consequently, only in a very few cases the CCD or PSD II may not apply, and the DMFSD might be the only Directive covering pre-contractual information requirements and right of withdrawal. Those are:

- credit cards with a limit below EUR 200 that were not granted in order to facilitate payment services or that grant credit of a long-term nature and for a period exceeding 12 months; or
- credit cards that require the credit to be repaid within three months and were not granted in order to facilitate payment services.

Unsolicited communications are regulated by the EPD, the DMFSD and GDPR. Unsolicited services are regulated by the UCPD and DMFSD (which Article 9 was amended by the UCPD), and to some extent by PSD II in those cases within its scope.

#### **10.4 Assessment in relation to the DMFSD objectives**

##### **Challenges for consumers and the impact of the DMFSD on the protection of consumers**

The consumer survey shows that respondents that considered obtaining credits at distance consider information requirements important. Furthermore, the overwhelming majority of those respondents consider it important to have the information presented in a format that enables comparison with other products, prominently and immediately and in a way that is adapted to the channel, as well as to be able to choose the format in which they can access the information.

The same respondents indicated that the required information about the service and supplier and the terms and conditions was often (75% - 92% depending on the information element) made available even if only upon request. Information on the applicable law, options and procedures for compensation claims and on the availability of funds was reported to be available in a fewer cases (around 65%). The respondents assessed the information they received as follows:

- It was clear, easy to understand and well structured (52%)
- It was complete and presented in a format that enabled them to compare it with other products (61%)
- It was provided sufficiently in advance to give them time to review it (61%)
- It allowed them to make an informed decision (62%)
- It was presented in a way that was suitable for the device they were using (70%)
- Information relating to their rights of withdrawal / early termination / cancellation was adequate (60%)
- Information relating to their right to complain and seek redress / compensation was adequate (52%)

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<sup>335</sup> According to Article 3 EDP applies only when the product is provided by means of publicly available electronic communications services.

This shows that while the majority of the respondents is relatively satisfied with the quality of the information and the way and when it was presented and provided, there is a considerable share of respondents that was neutral or not satisfied. In particular, 30% of the respondents considered that the information was not clear, easy to understand or well structured.

The LE Europe (2019) has also assessed the prevalence of some selling practices in the credit card market and concluded that often key information is missing (e.g., display of price ranges rather than an exact price) or difficult to find. Furthermore, sometimes information was found to be complex and difficult to understand, to emphasise benefits while costs were hidden or given lower prominence (e.g., use of teaser rates and the use of large fonts and bright colours), to be layered and located in places that could be overlooked, and to be in a format not adapted to medium used.

The data collected through the mystery shopping exercise for credit cards shows that:

- Information about the characteristics of the credit card were difficult to find in 12% of the cases and in 9% of the cases it was difficult to understand;
- Information about the supplier was difficult to find in 21% of the cases and difficult to understand in 8% of the cases
- Information about the terms and conditions was difficult to find in 33% of the cases and difficult to understand in 22% of the cases.

While the CCD, PSD II and the DMFSD indicate that the required information elements should be clear and comprehensible and presented in a “good time”. Only the DMFSD clearly mentions that the information should be adapted to the device used.

These findings suggest that while the provision of pre-contractual information is considered relevant by consumers of credit cards, the information received does not always allow for an informed decision, for a variety of reasons, including lack of compliance with these requirements and difficulties in finding and understanding the provided information (in particular on terms and conditions).

This evaluation identified no evidence of difficulties with the right of withdrawal. Of the 86 respondents to the consumer survey that purchased a credit at distance in the last five years, 10 cancelled the contract within the period covered by the right of withdrawal and none of them experienced problems.

Regarding unsolicited services, the Financial Services User Group argued that practices such as sending credit cards to consumers who have not requested them or increasing the limit of the card without it being explicitly requested happen occasionally. These practices go against the DMFSD and UCPD and require a to be more effectively monitored and enforced.

No challenges were identified in the context of unsolicited communications.

Other potential challenges related to credit cards sold using a distance means of communication are highlighted by the LER Europe (2019) study<sup>336</sup>:

- It is very common to find credit cards associated with product bundling, and it was found in some cases that consumers were not properly informed about it.<sup>337</sup> In France, it was found that for some credit products, including credit cards, the option “subscribe to an add-on insurance” was already ticked in the contract, regardless of not being compulsory. In the Czech Republic, several consumers

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<sup>336</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>337</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

were issued a credit card when contracting other financial products without having knowledge of it.<sup>338</sup>

- The availability of information tools for consumers still remains a challenge in the case of credit cards sold by distance means of communications (e.g. lack of chat boxes).

### **Challenges for providers and the impact of the DMFSD on the distance market of financial services**

As a reaction to the increasing number of new providers, traditional banks started cooperating with FinTechs to offer new products. In addition, it is expected that product combinations and cooperation will become more complex and important in the near future, with the entry into the market of traditionally non-financial operators.<sup>339</sup> An example of this practice is Amazon Credit card, which offers discounts for purchases using their card. Ensuring a level playing field is therefore very relevant in order to prevent unfair competition and that minimum protection standards are in place. The role of the DMFSD in the market of credit card sold at distance is currently very limited (due to the CCD and PSD II) but might become more prominent if new credit cards emerge that are outside the scope of the CCD and of the PSD II.

The impact of DMFSD on cross-border sales is very limited as the main consumer (e.g., preference for face-to-face, preference for domestic suppliers) and supply barriers (e.g., tax regimes, entrance costs) are beyond the influence of the DMFSD.

### **10.5 Analysis of existing gaps and possible measures to improve consumer confidence and empowerment and to develop the market for distance selling of these products.**

Aspects related to the quality of information and how and when it should be presented and provided do not seem adequately regulated by the DMFSD not by the two products-specific legislation that covers credit card agreements sold at distance. Several remedies have been proposed to address these shortcomings that are common to most of financial services sold through distance means of communication by stakeholders and researches, including the EBA<sup>340</sup> and the LE Europe (2019)<sup>341</sup>.

Furthermore, measures to improve the effectiveness of enforcement should be considered as evidence shows compliance levels below optimum in some aspects related to for example, the availability and clarity of information on terms and conditions and cases of provision of unsolicited services

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<sup>338</sup> European Parliament (2018) Consumer Credit: Mis-selling of Financial Products

<sup>339</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>340</sup> EBA 2019. Opinion on the DMFSD. Available at: <https://eba.europa.eu/eba-publishes-opinion-disclosure-consumers-buying-financial-services-through-digital-channels>

<sup>341</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services



## **11 Case Study 10: Money transfer and payments**

### **11.1 Introduction**

Money transfer and payments refer to all the tools and procedures enabling the transfer of funds from payers to payee, at the same time it refers to online and mobile payment.

Non-cash transfers and payments refer to: cheques, credit transfers, direct debits, card payments and alternative online payments.

A credit transfer is "Payment service which allows the payer to instruct the institution holding its account to transfer funds to the beneficiary. It is a payment order or a sequence of payment orders made for the purpose of placing funds at the disposal of the beneficiary. Both the payment order and the funds described therein move from the PSP of the payer to the PSP of the payee, i.e. the beneficiary, possibly via several other credit institutions as intermediaries and/or one or more payment and settlement systems.<sup>342</sup> These payments are processed by the main payment and settlement systems. The instruction can be done face-to-face or through a distance means of communication.

A direct debit is "A payment service for debiting a payer's payment account, potentially on a recurrent basis, where a payment transaction is initiated by the payee on the basis of the payer's consent given to the payee, to the payee's PSP or to the payer's own PSP."<sup>343</sup> These payments are processed by the main payment and settlement systems. The instruction can be done face-to-face or through a distance means of communication.

A card payment is an instruction from a customer using a payment card (i.e., debit card, credit card or delayed debit function) to transfer money to another entity through a payment card scheme in exchange for good or services. In 2019 there are several national payment schemes, but cross-border card payments are dominated by two international payment card schemes: VISA and MasterCard.<sup>344</sup> E-money payments are not included. Generally, card payments are done online or face-to-face.<sup>345</sup>

E-money payments is "a transaction whereby a holder of e-money transfers e-money value from his/her own balance to the balance of the beneficiary, either with a card on which e-money can be stored directly or with e-money accounts."<sup>346</sup> These include payments with cards on which e-money can be stored directly or with e-money accounts. Consequently, e-money payments can be done face-to-face or at distance.

Other alternative online (including mobile) payment methods offered by P2P platforms or other innovative online platforms which are not included in any of the previous payment methods.

The DMFSD only applies to service agreements and not to operations. Therefore, this case study focuses on payment services agreements done using distance means of communications. Consequently, it covers agreements done at distance for:

- current accounts (as they allow for credit transfers and direct debit);
- payment cards (debit, with delay debit function and credit);
- e-money accounts;
- other payment service agreements.

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<sup>342</sup> ECB. Payment statistics: methodological notes. <http://sdw.ecb.europa.eu/reports.do?node=1000002018>

<sup>343</sup> ECB. Payment statistics: methodological notes. <http://sdw.ecb.europa.eu/reports.do?node=1000002018>

<sup>344</sup> European Central Bank. 2019. "Card payments in Europe Current landscape and future prospects: a Eurosystem perspective" Available at: [https://www.ecb.europa.eu/pub/pdf/other/ecb.cardpaymentsineu\\_currentlandscapeandfutureprospects201904~30d4de2fc4.en.pdf](https://www.ecb.europa.eu/pub/pdf/other/ecb.cardpaymentsineu_currentlandscapeandfutureprospects201904~30d4de2fc4.en.pdf)

<sup>345</sup> However it is also possible to do card payments over the phone.

<sup>346</sup> ECB. Payment statistics: methodological notes. <http://sdw.ecb.europa.eu/reports.do?node=1000002018>

## **11.2 The evolution of the market**

The share of Eurobarometer surveys' respondents (EU-15) with at least one: a) current account was relatively the same in 2003 and in 2016 (80%), and b) credit card increased from 45% to 49% in the same period.

According to the Global Findex Database, the percentage of individuals (aged 15+) with a debit card increased 19pp since 2001: it was 68% in 2011, 81% in 2014 and 87% in 2017.

Data from the ECB database shows that the number of e-money accounts (from credit institutions) increased more than 60% in 4 years (in the period 2014-2018), while the total number of payment accounts remained stable. The number of accounts from non-credit payment institutions also increased at a rate of 4% per year since 2014.

There is very limited data on the number or share of agreements for debit cards and payment accounts (other than e-Money accounts) that were done using a distance mean of communication for the period of analysis. The available data on payment services shows:

- In 2011, distance contracts for credit cards represented 23% of the total credit card contracts signed by Eurobarometer respondents. In 2018, 64% of the respondents to a Deloitte survey (some EU countries only) concluded a credit card contract at distance.
- In 2011, distance contracts for current accounts represented 8% of the total current account agreements signed by Eurobarometer respondents. Consumer survey shows that of the total respondents 33% concluded a contract for a current account using a distance mean of communication in the last five years.
- In 2007 the number of registered clients of PayPal in the EU (the biggest e-wallet provider) was around 35 million. E-money accounts and other payment accounts (from non-credit institutions) represented 45% of the total payment accounts in 2014 and over 60% in 2017. These payment accounts are opened online usually using e-wallet services.

No data is available on the percentage of distant payment service agreements that were done with a provider in another member state. Overall the Eurobarometer surveys show that the share of cross-border sales was and still is very limited for current accounts (3.8% of total current accounts in 2016) and credit cards (2.3% of total credit cards in 2016). After a significant drop between 2003 and 2011 (most likely due to the financial crisis), cross-border sales increased about 26% for current accounts and 40% for credit cards between 2011 and 2016.

A study from 2004 found that the use of cross-border facilities was not widespread in the reporting e-money schemes. Although the EU "single passport" (mutual recognition arrangements) under the EU directive on the prudential supervision of the business of electronic money institutions allowed any authorised and supervised institution to provide services in other EU countries, including the issuance of e-money, the existing e-money products still did not operate on a cross-border level.<sup>347</sup>

Based on the consumer survey (2019), while the percentage of respondents that obtained a current account or a credit card from a provider in another Member State was around 21%, more than one third of the respondents that contracted another type of payment service at distance did it from a provider in another Member State. The LE Europe (2019) mapping of payment service providers suggests that the majority are

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<sup>347</sup> Committee on Payment and Settlement Systems, 2004, Survey of developments in electronic money and internet and mobile payments

national operators (71%), while 25% are European operators and the remaining USA operators.

At the baseline the majority of payment service providers were traditional operators, mostly banks. In 2004 there were less than 6 e-wallet providers in Europe, of which the majority was founded between 2002 and 2004. Since then, the number of online and mobile digital wallet providers has increased considerable (especially around 2015) and other FinTech providers emerged offering other alternative payment services online (e.g., P2P platforms). Currently, the digital payment sector is the sector with the highest number of FinTechs (88%)<sup>348</sup> with all the big technology giants, from Apple to Samsung and Google, entering in the payments market. Traditional operators, such as banks, also offer digital payment services. According to LE Europe (2019), of the providers surveyed that offered payment services 64% are traditional operators, while 36% are new operators.

Regarding preferred distance means of communication, the consumer survey (2019) suggests that 90% of payment services (other than bank accounts and credit cards) obtained by the respondents in the last five years were finalised online (including email) and the remainder by phone. Roughly 46% of the surveyed consumers obtained payment services on the internet, using a desktop, laptop or tablet and 34% on a smartphone.<sup>349</sup>

Historically, traditional operators have offered money transfers and payment services to their customer pool, starting with offering the service through means such as giro cards and cheques<sup>350</sup>.

Since the implementation of the DMFSD, much has changed in the payment service landscape in Europe and in the world. The rapid evolution of e-commerce, digitalisation and emergence of FinTech companies brought with new business models and innovative services/products such as E-wallets, in-app purchases and P2P payments, have arrived on the market. In particular, mobile payment services provided both by traditional payment service provider and emergent e-wallet services are gaining in importance as more and more Europeans use a smartphone.

At the baseline, the low digitalisation and digital literacy were the main barriers to both demand and supply of payment services at distance. Concerns over online payment security also played a role. Quickly however, digitalisation and digital literacy increased significantly and today there seem to be few barriers to distance marketing of financial services domestically.

Regarding cross-border sales, both at the baseline and currently consumers seem to prefer domestic providers, citing concerns over lack of information and who to turn to in case of problems as well as language barriers. This is in line with the consumer survey (2019), as 46% of the respondents that were considering obtaining a payment service reported that they would not do it from a provider in another Member State because one of those reasons.

Currently, not all payment services providers offer services cross-border. According to the consumer survey, of the respondents that tried to obtain a payment service cross-border, 42% did not manage to access the offers as the website was blocked or they were redirected to the domestic or global site and 6% did not manage to complete the transaction. Other problems reported by the respondents were related to difficulties understanding the information (29%). Data collected in the mystery shopping exercise for money transfers, shows that 16% of the mystery shoppers did not manage to access

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<sup>348</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

<sup>349</sup> Results of the Consumer Survey

<sup>350</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

the offers of a provider in another Member State because the website was blocked or they were redirected to a domestic or global website. This evidence suggests that there are still unaddressed barriers at supply side, which are likely to be related to different tax regimes and entrance cost due to cultural differences (including language) and lack of knowledge of the market, in addition to the burden of having to comply with divergent consumer protection requirements in the 28 Member States (reportedly, in most of the cases, even on-line banks have to set up a subsidiary in every country and adapt their products to local regulation and context).<sup>351</sup>

Table 9. Overview of baseline and endline by indicator

Indicator	Baseline	Endline
Sales	No data available for distance	E-money accounts represent 60% of the total accounts
Type of provider	Mostly traditional (banks)	Mostly traditional but new providers have a significant share
Most used means of communication	No data available	Consumer survey: 90% online and 10% phone
Cross-border sales	No data available	No data available Consumer Survey: 33% from another Member State
Main barriers	Digitalisation and low literacy Security concerns Lack of information, concerns over who to turn to in case of problems, language barriers	Lack of information, concerns over who to turn to in case of problems, language barriers Different tax regimes and different cultures

Source: ICF compilation

### 11.3 Legal framework

The following legislation is applicable to Money Transfer and payments: 1) Distance Marketing of Financial Services Directive (DMFSD); 2) e-Commerce Directive (e-CD); 3) Unfair Commercial Practices Directive (UCPD); 4) General Data Protection Regulation (GDPR); 5) Payment Accounts Directive (PAD); 6) Payment Services Directive (PSD2); 7) e-Privacy Directive (EPD).

Electronic payment, electronic money and mobile payment have been supported by several initiatives in EU which aimed at the preparation of a regulatory framework to address issues of emerging payment instruments and solutions.<sup>352</sup>

The European Bank Authority (EBA) supervises and regulates in the area of payments and electronic money and ensures that payments across the EU are secure, easy and efficient. Its regulatory output in this section includes technical standards and guidelines under the revised Payment Services Directive (PSD2); the mandate conferred on the

<sup>351</sup> European Banking Federation, 2016, European Banking Federation's response to the European Commission Green Paper on Retail Financial Services

<sup>352</sup> Andreas Huber, 2004, Mobile payment – A comparison between Europe and the US.

EBA in the Interchange Fee Regulation (IFR); the EBA Guidelines on the security of internet payments; and the EBA's views on financial innovations in the payments sector, such as 'virtual currencies'.

Regarding pre-contractual information requirements and right of withdrawal the key legislative instrument in the context of payment services is the PSD II. Additionally, information requirements for payment accounts are also regulated by the PAD.

Both PSD II and PAD have more stringent and specific pre-information requirements, and so the DMFSD functions as a safety net in case an innovative payment service emerges that is not covered by it.

PSD II sets a detailed list of pre-contractual information that must be provided under the different situations of payment and transactions (i.e. information on the service provider and supervisory authorities, a description of the payment service, interest and exchange rates<sup>353</sup>). As in the DMSFS, the PSD II requires that the information must be provided on paper or another durable medium and in good time.

PAD also provides for new elements for information disclosure for distance payment account contracts<sup>354</sup> and in Article 7 requires that Member States shall ensure that consumers have access, free of charge, to a least one website comparing fees charged by payment service providers for at least the services listed in the Directive. This Article sets the rules on the type of information that these websites need to provide to consumers

Unsolicited communications are regulated by the EPD, the DMFSD and GDPR. Unsolicited services are regulated by the UCPD, PSD II and DMFSD (which Article 9 was amended by the UCPD).

#### **11.4 Assessment in relation to the DMFSD objectives**

##### **Challenges regarding consumers and the impact of the DMFSD on the protection of consumers**

The overwhelming majority of respondents to the consumer survey considered that obtaining a payment service at distance indicated that receiving information about the supplier, the service and the terms and conditions was important (96%). The majority also stated that they considered very important that the information is presented prominently and immediately and in a format that enables them to compare the service with others. When asked about their experiences:

- the overwhelmingly majority received information about the supplier, service and contract, but around 20% of the respondents indicated that they did not receive information about the potential risks associated to the service, the existence of additional taxes or costs that the consumer has to pay to someone other than the supplier, options and procedures for small compensation claims;
- 35% indicated that information was not clear, easy to understand or well structured, 21% reported that the information was not in a format that enabled them to compare the service with others, 29% considered the time allocated for them to review the offer was not enough and felt pressured into making a quick decision.

The mystery shoppers that simulated obtaining a money transfer contract reported the following experiences:

- 13% found the information about the service and the supplier difficult to understand and 19% had difficulties finding it;

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<sup>353</sup> Articles 51 and 52 PSD2

<sup>354</sup> Including fee information, information on the most representative services linked to a payment account and information on switching services.

- 12% found the information about the terms and conditions difficult to understand and 56% had difficulties finding it.

In terms of common potentially harmful practices adopted by service providers, the LE Europe (2019) study found that:

- Often key information was missing or difficult to find;
- Sometimes benefits are emphasised while costs are hidden or given lower prominence in pre-contractual information
- There are no effective practices to accelerate consumer purchase decisions were not found.

No evidence on challenges related with the right of withdrawal was identified. Of respondents to the consumer survey that signed for a payment service agreement at distance in the last five years, 17% cancel the contract within the period covered by the right of withdrawal and none of them experienced problems.

There is no evidence of consumer challenges with regard to unsolicited communications and services.

### **Challenges regarding providers and the impact of the DMFSD on the distance market of financial services**

The emergence of new online players (FinTechs, including large platform operators (“big techs”)) with new business models and innovative payment services, posed challenges to traditional providers that had to adapt their business models in order to keep their competitiveness. Until the implementation of the Payment Services Directive, the DMFSD ensured that these new players had to follow a minimum set of rules when offering their services to consumers, acting as a safety net for consumers but also creating a level playing field for traditional providers and non-traditional operators (which could not benefit from loopholes to provide their services faster or cheaper than traditional providers). After the implementation of the PSD, the role of the DMFSD regarding payment service agreements has significantly reduced and with the implementation of the PSD II it is now negligible.

### **11.5 Analysis of existing gaps and possible measures to improve consumer confidence and empowerment and to develop the market for distance selling of these products**

The evidence from the consumer survey, mystery shopping exercise and LE Europe (2019) study shows some issues with the compliance with the provision of pre-contractual information. Measures to improve the effectiveness of enforcement should therefore be considered.

Furthermore, two aspects do not seem fully addressed by the current legislative framework, which if improved, could lead to better decisions and higher levels of consumer protection.

First, the information should be clear and understandable. The DMFSD, the PSD II and the PDA all indicate that pre-contractual information should be in line with these requirements. However, they do not define concrete guidelines and indicators on what these subjective elements mean in practice and how providers and regulators can assess compliance with them. In this context, remedies suggested by the EBA<sup>355</sup> and LE Europe (2019)<sup>356</sup> could be considered.

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<sup>355</sup> EBA 2019 Opinion of the European Banking Authority on disclosure to consumers of banking services through digital means under Directive 2002/65/EC.

<sup>356</sup> LE Europe, VVA Europe, Ipsos NV, ConPolicy and Time.lex. (2019). Behavioural study on the digitalisation of the marketing and distance selling of retail financial services

Second, the information should allow consumers to compare payment services. While the DMFSD does not define this as a requirement, the PSD II and the PAD do. However, only the PAD states how the information about fees should be structured and enables comparison between payment accounts. Since the PAD only covers a subset of payment services it would be important to have guidelines on how financial providers should structure key information in order to help consumers compare all payment services.