FSUG RISK OUTLOOK 2015 AND BEYOND

PROGRESS REPORT AND NEW RISKS FACING EU FINANCIAL SERVICES USERS

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INTRODUCTION

If policymakers, regulators, and civil society representatives are to be effective at meeting their objectives (ensuring safe and resilient markets, making markets work, protecting financial users, and ensuring consumers' needs are met), effective risk analysis and risk management is a priority. Good risk analysis and risk management allows us to:

- understand the major forces shaping market and user behaviours
- understand the root cause of market failure/ detriment
- develop mitigation or prevention strategies
- regulate and supervise more cost-effectively and efficiently and prioritise using targeted interventions

Ultimately, risk analysis is necessary to set strategic priorities and use limited resources to protect citizens. Failure to deal with detriment that has already occurred means that citizens still face a welfare loss, causing a redress deficit[1] . Failure to identify, manage or mitigate risks will inevitably result in future market failure and consumer detriment. It also results in significant ex post redress costs to the industry (if sanctions and redress are successfully applied) and costs to the regulatory authorities.

Just over two years ago, the FSUG produced its first Risk Outlook to help policymakers, financial regulators at EU and national level, and other stakeholders such as consumer organisations recognise the key risks facing EU financial users in the post financial crisis environment. Quite often a detrimental practice in one member state will be copied in other member states so we hope this Risk Outlook will be helpful as an 'early warning' system for representatives.

This second Risk Outlook report updates that report and identifies new or emerging risks facing financial users. It also provides a commentary on whether we believe that the previous risks we identified have been dealt with.

In particular, we hope that the Risk Outlook will be helpful for the new Commission to help it understand the scale and nature of the risks facing financial users and the challenges facing policymakers and regulators. Financial users face a huge number of risks across the spectrum of financial services in all member states. It is not possible to cover them all in detail. Therefore, in addition to the specific sector and product risks highlighted in this report, we have also identified a number of strategic priorities which we believe the new Commission and ESAs should focus on.

Commentary on progress

In the first Risk Outlook, we highlighted that following the financial crisis, policymakers, regulators, civil society representatives and other opinion formers faced three major challenges:

[1] A redress deficit occurs when consumer detriment is left unresolved and consumers do not get due redress for losses suffered (the redress gap) and wrongdoers escape accountability

i. restoring and maintaining financial stability;

ii. making sure major financial institutions are prudently and safely run; and

iii. making financial markets work for society.

Policymakers and regulators understandably had focused on the first two challenges. Recently we have seen much activity relating to the third challenge at EU level with the reform of MIFID, IMD, initiatives to improve long term investment and so on.

However, there does not seem to be much evidence that this activity has been translated into major improvements for financial users. Enough time has now passed. Policymakers must now ensure that making markets work for EU citizens is given the same priority.

As the most recent Consumer Markets Scoreboard [2] shows, FSUG representatives are right to be very concerned about the failure of financial services to work effectively for financial users. The Consumer Markets Scoreboard is a very powerful tool as it evaluates markets from the user perspective – not from the industry perspective. Despite the claims of industry lobbies that the financial services industry has learnt its lesson and has the interests of financial users at its heart, the research shows quite clearly that financial services continues to be amongst the very worst performing markets in the EU.

Previous attempts to make markets EU financial markets work by focusing on demand side interventions (such as information provision and/or financial capability) have had limited impact on their own. Furthermore, while self-regulation has a role and designed properly can work in certain cases, it does not have a very good track record in financial services.

Therefore, we hope there is a consensus amongst policymakers and regulators on the need for a different, more robust approach to regulating financial services and making markets work. Tough supply side interventions are needed to change the behaviours and improve the efficiency of the EU financial markets and promote a real single market that works in the interests of financial users and citizens.

If policymakers and regulators are to protect financial users in this new, more challenging era, first they should become more proactive and responsive to threats to consumer welfare rather than reactive. Early interventions to pre-empt and limit the scale of detriment are more effective at protecting consumers (and more cost-effective) than allowing detriment to occur and clearing up after the event. Of course, early interventions have to be calibrated so as not to stifle genuine innovation. But, contrary to the claims of industry lobbies, good regulation does not stifle socially useful innovation and real competition. Further information can be found in our report, *Principles and Practices of Financial*

[2] See http://ec.europa.eu/consumers/consumer_evidence/consumer_scoreboards/10_edition/index_en.htm

Services Regulation, which provides a template for policymakers and regulators to evaluate how these risks may affect financial users, and how to identify measures to protect financial users[3].

But, even the best regulation is pointless unless compliance is monitored and enforced at EU and national level. Similarly, identifying risks is of mainly academic interest unless these risks are dealt with through effective mitigation. This lack of enforcement in key areas has been one of our main concerns.

We are very strong supporters of the EU Single Market. But it is very sad to report that we see too many examples of poor practice and poor value products being exported from one Member State to another. This is not a sign of a well-functioning market. Therefore, one of the key strategic priorities we have selected is 'Better Regulation' including tougher, more consistent monitoring and enforcement of existing regulation to deal with existing market risks as well as targeted interventions to pre-empt detriment and promote a more efficient Single Market.

Next Steps

The FSUG does not have the resources to undertake the necessary research to quantify the potential scale of detriment associated with these emerging and potential risks. Therefore, we urge the Commission and ESAs to proactively evaluate these risks, quantify these risks in terms of potential consumer detriment/ welfare loss, and prioritise these risks for interventions.

We would welcome the opportunity to work with the authorities to help prioritise these risks so that financial users are properly protected.

[3] FSUG has proposed a new approach to regulation which allows regulators to identify detriment and risks and intervene effectively to target root causes of detriment, not the symptoms. Effective interventions include: market alerts, product interventions (such as banning toxic financial products), addressing potential conflicts of interest. interventions should target the root cause of detriment and market failure, not the symptoms.

UNDERSTANDING 'RISK'

Before we get into the detail of the Risk Outlook it may be helpful to describe what we mean by risk and the categories of risk we are concerned with. When we refer to risk we are talking about a set of *external* events and trends, and *internal* market behaviours, practices, and decisions which have damaged or pose a risk to the financial welfare of citizens.

Root cause analysis

If we are to be effective at mitigating the effects of detriment/ market failure, then it is imperative that we are able to identify and understand the underlying or root causes of that detriment/ market failure. If we fail to do this, we risk wasting limited resources on ineffective interventions and fail to protect citizens.

The root cause of market failure/ detriment can be found in three 'domains':

- **External factors:** socio-economic, demographic, macro economic, financial system shocks, long term financial returns, technology and information science, globalisation – mainly outside of our remit but we can do much to mitigate the effects on citizens
- **Supply side/ market factors:** business models, sales and marketing strategies, conflicts of interest/ agency problems, remuneration strategies, supply chain risks, product risks, weak system controls, poor corporate governance and corporate culture, shareholder expectations re returns on investment, anti-competitive practices and behaviours. It is in this domain where policymakers and regulators can intervene to greatest effect.; and
- **Demand side factors:** user behaviour, attitudes, confidence and trust, capability and cultural factors – these factors weaken the ability of citizens to positively influence market behaviours.

But risk also exists along a continuum.

Historic/ legacy risks: Relates to consumer detriment and market failure that has occurred in the past. The priority here is to clean up the market after the event has occurred and ensure that consumers affected obtain due redress and wrongdoers held to account. Note that unless and until consumers do obtain redress/ wrongdoers held to account, this historic risk has not been dealt with. As we explain in the FSUG Annual Report, if historic risks are not dealt with, this results in a 'redress deficit'. The Risk Outlook contains numerous examples of consumer detriment that are still to be resolved. In other words, we believe an alarming redress deficit exists in many EU member states.

Existing/ current risk: Relates to consumer detriment and market failure that is happening in the market now. Regulators should be aware of and be taking action to deal with this type of risk before the scale of market failure and consumer detriment increases. The Risk Outlook contains numerous examples of this type of risk.

Potential/ future risk: Risks which are likely to emerge as a result of major trends and changes in society, the economy and market affecting firm or consumer behaviour. The challenge here for policymakers and regulators is to understand how these major trends will affect the industry and financial users and intervene early and effectively to pre-empt market failure. Policymakers and regulators need to become more forward looking rather than just respond to events. This requires a change in approach from ex post regulation to ex ante regulation and from permissive regulation to a precautionary approach. The sections of the Risk Outlook on the new economic paradigm and root cause analysis highlight a range of external and industry trends, events, behaviours and practices which we think will result in major detriment/ market failure unless prevented through appropriate policy and regulatory interventions. Earlier and successful identification and mitigation of risks is better for financial users – and imposes less of a cost on the financial services industry and wider society too.

ROOT CAUSES OF RISK AND MARKET FAILURE IN FINANCIAL SERVICES

Risk management is most effective when it identifies the underlying causes of risks and market failure including the macro trends that influence producer and consumer behaviours. One of the most important influences will be the structural and behavioural changes brought about by the new economic and financial paradigm facing EU economies, households and financial sector.

The new economic and financial reality

As well as macro-economic events driven by the legacy of debt, the focus on systemic failures has diverted attention away from long term structural problems in the EU financial services industry. These structural problems will be exposed as the EU enters a new economic and financial paradigm defined by a range of macro and micro economic events, social changes, and political/ regulatory responses.

We have identified a range of events operating at macro and micro economic, political and commercial level which will impact on:

i) household finances and economic behaviours; and

ii) the business models in the financial services industry.

These include:

- A legacy of high debt (household, bank, and public debt) as described above;
- A period of financial repression and retrenchment;
- Severe fiscal adjustments and austerity measures;
- The transition from a previous liberal lending regime to a more restrictive lending regime governed by tougher regulatory requirements and self-imposed restraint by lenders and the market;
- A long period of low economic growth – certainly compared to the pre-crisis period;
- Sustained pressures on household finances and low real household income growth;
- A sustained period of low interest rates and returns on financial assets available to financial institutions;
- Financial institutions face margin and revenue pressures particularly with regards to core products and business lines;
- Reduced real investment returns, with a paradigm shift in risk/ reward ratios impacting on consumer and producer behaviour and attitudes. Sustained low interest rates encourage risky

investment behaviour in a ‘search for yield’ – this leaves investors vulnerable to misselling and misleading promotions;

- An uncertain political and regulatory climate, with more intrusive regulation in the pipeline – as financial user representatives we welcome a more sceptical and robust approach to regulation but this will affect business models with consequences for financial users;
- Shareholder attitudes and activism – shareholders in financial institutions are becoming more active and exercising stewardship responsibilities and greater due diligence; and
- Changing consumer attitudes, behaviours and levels of confidence.

These individual factors will combine to exacerbate existing detriments and market failure, and create new emerging risks to the welfare of financial users and citizens. These existing and potential detriments and risks are set out below.

CROSS CUTTING RISKS/ ROOT CAUSE ANALYSIS

As experienced financial user advocates, we have considered the impact of the new economic paradigm on the financial services industry and financial users. We have also considered how policymakers and regulators might respond in the face of these pressures. From this assessment, we have identified a range of emerging and potential risks and consumer detriments.

These are detriments that are not restricted to one sector but appear to be evident in the financial services industry across the board. Dealing with these risks at an EU level requires coordination by the Commission and ESAs if consumer detriment and market failure is to be tackled. These risks will also be evident at industry level within member states.

Transition risks and legacy business models: the new economic paradigm in our view will expose major structural weaknesses in the business models of many EU financial institutions including incumbent banks, life insurance companies, and investment/ asset managers. At a sectoral level, there are major problems with oversupply of providers and products[4]. These financial institutions were structured to operate in a very different economic paradigm with high returns on equity, high economic growth, easy credit, and increasing household incomes. The dislocation effects on financial institutions (and therefore on financial users, shareholders and employees) could be significant and need to be understood and managed by policymakers and regulators. In inefficient markets with high degrees of oversupply there is a risk that financial institutions will seek to maintain revenues and profit margins through exploitative practices and behaviours. Regulators will need to pay close attention to markets for evidence of detrimental behaviours and practices such as price gouging.

[4] Policymakers should recognise that oversupply (too many providers and products) can be as detrimental to the interests of financial users as too few providers or overconcentration in a market (the classical competition model)

Market inefficiencies: the combination of lower disposable incomes, lower growth, and overhang of debt will undermine consumers' ability to afford financial products. Value will be critical. In theory, competition for limited consumer spending should result in firm offering better value to consumers. However, if history is any guidance, it is more likely that firms will respond by introducing complex pricing structures, socially useless 'innovations', and hidden features to protect and grow revenues. This is all the more likely given the legacy business models described above. Ensuring markets are efficient and financial institutions are truly competitive[5] and do not destroy value at a time when household finances are squeezed must be a priority for policymakers and regulators.

Board/ Senior management responsibilities and priorities: repairing balance sheets, cost-cutting and efficiency drives, and revenue/ profit margin maintenance will be priorities for boards and senior management. There is a serious risk that senior management will ignore behaviours further down the organisational hierarchy – for example, at the point of sale, or in bank branches – resulting in consumer detriment. Senior management will need to be reminded of their responsibilities and better monitoring mechanisms will need to be out in place.

Culture of regulatory circumvention: legal engineering used by bankers and banking lawyers to systematically circumvent regulations such as tax, capital adequacy, disclosure rules in takeovers and trade embargoes, by get round regulatory control and the rule of law and challenging in a regulatory cat and mouse game.

Basic quality and levels of service: linked to the above points, basic quality and levels of customer service may deteriorate. For example, basic customer service may suffer – claims handling in the insurance sector, staffing in bank branches, dealing with consumer complaints may be de-prioritised. Regulators will need to monitor customer service standards.

System controls: pressure on business models and cost cutting means risk of senior management ignoring basic system controls leading to poor service or denial of service, risks to internet banking, risks to client assets.

Unfair contracts: consumers more likely to fall victim to unfair terms due to pressures on financial services revenues. Financial institutions may be tempted to introduce new unfavourable terms or make greater use of existing unfair terms in contracts.

Conflicts of interest/ misselling: margin and revenue pressures will force financial institutions to attempt to reduce high fixed costs and move towards variable costs. For example, we may see an even greater emphasis on reducing fixed salaries and increasing proportion of total remuneration derived from commissions and bonuses that are linked to volume of sales. This will increase the risk of conflicts of interest and risk of misselling and inappropriate recommendations by financial intermediaries and sales staff. Impacts on the welfare of employees as well.

Aggressive marketing, selling and promotion of products: linked to the above, fierce competition to acquire new business and senior management dereliction of duties may encourage aggressive marketing

[5] This is not the same as the illusion of competition created by the existence of numerous products and providers

and selling of products and services of questionable social utility (see 'Follow the money, above). Providers and distributors may be tempted to fail to disclose important information to consumers. Regulators should pay special attention to tactics such as 'scamming' which have been targeted at older people ..

Adviser/ intermediary behaviours and competence: financial advisers and intermediaries (and directly employed sales staff) may not be sufficiently well trained to understand the consequences of the new economic paradigm on consumer expectations, attitudes to risk, the need for value and so on. As a result they may end up providing sub-optimal advice to consumers.

Information intermediaries: intermediaries – especially independent not-for-profit organisations – play an important role in helping financial users make informed choices and effective decisions. However, several FSUG members have expressed concern about the independence, objectivity and quality of information on commercial websites.

Access to financial advice: many lower-medium income households will have very complex legacy problems (for example, debt problems), or small investment or pension savings. They will have a greater need for quality advice. However, commercial pressures and squeezed household incomes mean that financial institutions are likely to increasingly concentrate on providing financial advice to higher income households.

Product design/ pricing structures: likely to see greater use of pricing structures biased towards protecting interest of financial institutions which may work against the interest of financial users. Examples might include: greater use of front-end loaded charges which ensure that if financial users want to cancel or switch providers they will be penalised; or greater use of penalty charges and hidden costs. Another example is the lack of investment in accessible ATMs and e-banking services which prevent many older people from managing their own accounts or result in high charges[6].

Anti-competitive practices and behaviours: while we may see fiercer competition to acquire new business, product design and pricing structures may be used to stifle switching away from incumbent provides and therefore undermine effective competition (see above). Particular concerns about anti-competitive practices in banking sector (and to some degree in life insurance sector) due to consolidation in market and consumer confidence.

Financial 'prisoners'/ 'captive consumers': linked to the previous point, a strong theme we expect to emerge across a number of sectors is the treatment of consumers who are in effect contract 'prisoners'. They may have limited opportunities to switch to better deals (or lack of awareness of better deals and consumer rights) and as a result may be exploited and subject to unfair practices such as excessive administrative or penalty charges. Mortgage arrears, life insurance funds, personal pensions, investment

[6] To process a paper bank transfer in Belgium, a bank typically charges more than 5€ to the customer when e-banking payments are free of charge.

funds, and bank accounts are obvious areas for concern. There is a particular concern about financially excluded and other vulnerable households who may have been targeted by unscrupulous providers in the first place. Practices which exploit 'captive consumers' violate the principle of freedom of choice for consumers promoted by the Single Market Act.

Complaints and redress: revenue and profit margin pressures may encourage financial institutions to make it more difficult for financial users to obtain due redress, even more so as financial services users still do not enjoy any collective redress schemes in a majority of EU Member States..

Regulatory pressures: it is not just financial institutions that are under pressure. We are concerned that a regulatory focus on financial stability and prudential regulation and limited resources may divert attention away from consumer protection priorities. As we explain in our paper *Principles and Practices of Financial Services Regulation*, civil society groups appreciate that rescuing our economies and financial systems must be a priority. Moreover, civil society groups recognise that prudential regulation is important and that consumer protection can be a rather abstract issue if financial institutions collapse. We do not challenge the need for policymakers to work on these priorities. However, it is critical that policymakers and regulators ensure that there are sufficient resources dedicated to consumer and investor protection priorities. As we explain in this Risk Outlook, the aftermath of the financial crisis and the response of financial institutions to margin pressures will result in financial users being exposed to detrimental behaviours and practices.

Financial supervision: transparency amongst supervisors is low, effective instruments are missing and in most countries there is no consumer representation in the existing supervisory bodies, no consumer panel with substantial rights (as in the UK) and no 'super complaint' to be worked on in the formalized procedure. For example, BAFin does not disclose how it handles consumer complaints, the whole process is not transparent, both for the consumer(s) affected and for the public.

Regulatory 'capture': the new economic paradigm will put severe strain on business models and financial returns available to financial institutions. We expect industry lobbies to put regulators under severe pressure to ease up on regulatory reform and consumer/ investor protection. Regulators will have to steadfast in resisting these lobbies.

Prudential regulation 'overshoot': we recognise the priority given to restoring balance sheets but prudential reforms need to be carefully calibrated to prevent unintended consequences such as restricted access to credit, higher cost of access, higher product prices, reduced investment returns. Similarly, regulators need to be careful to avoid regulatory backlash diluting prudential reforms. This is an important illustration of why regulators have to undertake proper impact assessments when making prudential regulations.

Conflicts of objectives of Supervisors: Also, a lot of EU supervisors – including the three new ESAs – have not moved to a "Twin Peaks" approach, and have still conflicts between the industry solvency objective on the one hand, and the customer protection one on the other hand[7].

[7] See for example FIN-USE report on the consumer voice in financial services, May 2009.

Financial exclusion and access: margin pressures will lead to banks and other financial institutions increasingly focus on higher margin/ lower risk households. This is likely to lead to deteriorating financial exclusion levels and restricted access to services - in particular to customers with special needs (persons with disabilities, senior citizens, etc.[8]) More generally, we are concerned that financially excluded, lower income and other vulnerable households will be disproportionately exposed to emerging and potential risks. Regulators should also ensure there is an equality of interests – that is, they should act in the interest of all consumers, particularly the most financially vulnerable consumers, not just 'middle-classes' or wealthy consumers. It is important that analysis should understand the impact on different groups of consumers. For example, certain pricing structures may work for medium income consumers but adversely impact consumers on lower incomes or with uncertain patterns of earnings. Assuming they can access markets in the first place, financially vulnerable consumers are more likely to be ripped off and any loss has a greater monetary impact. They are less likely to know and exercise their consumer rights. Following the theory of proportionate regulation, these consumers should attract stronger consumer protection than more economically powerful consumers.

Technology and risk based pricing: technology and risk based/ differential pricing enables more precise segmentation of consumers. This can benefit lower risk, higher income consumers but disadvantage vulnerable, lower income or otherwise disadvantaged consumers.

Consumer confidence and trust: consumer confidence and trust in financial services has already been seriously damaged. **F**inancial users need to have confidence and trust if they are expected to use financial services to meet their core financial needs, and engage with financial services and make effective choices. This lack of confidence and trust may be exacerbated if we see the emergence of further detrimental practices.

Financial capability: industry practices and behaviours (complex products etc) may further undermine the challenging task of improving financial capability**.**

[8] One example from Belgium: eighteen months ago ING introduced a limit of 1.000 € to cash withdrawals from ATM allowed to customers aged 60+. They presented this measure has being necessary to protect them from the increase risk of abuse/theft of their bank card. Consumer representatives suspected that the real reason was that since the bank has to refund customers who get rob when using the ATM cash machines, they wanted to limit the risk for the bank. The measure caused such a reaction from senior customers that within half day the Ministry of Justice intervened and asked the bank to withdraw their measure on the ground that it was age discrimination.

SECTOR SPECIFIC RISKS

FSUG experts have identified a range of specific risks relating to main financial services sectors – banking, insurance and funded pensions, and securities and asset management. These risks are a combination of existing detriments which still need to be addressed, and potential or emerging risks which – with the proper interventions – can be dealt with.

The classification of risks allows the relevant Commission officials and ESAs (EBA, EIOPA, and ESMA) to identify issues that fall within their remit.

To illustrate the impact on financial users, we have included examples provided by FSUG experts from their own country.

DATA PROFILING/ INTERNET NEUTRALITY

The first major risk covers a number of different financial sectors. However, we think this is sufficiently important to warrant a separate focus.

Data profiling: the big banks are embracing data analysis as a means to pinpoint customer preferences and, as a result, also uncover incremental sources of revenue in a period of stalled revenue growth. In the past, banks primarily used data for core numbers-crunching, such as analysing customers' creditworthiness, but increasingly they are using it to explore new areas such as sentiment analysis, to determine how customers are feeling about the overall user experience. In the old days, the grocer knew each customer personally and could recommend cuts of meat based on previous purchases and knowledge of their tastes. Banks having millions of customers can now act like the neighbourhood grocer thanks to predictive analytics culled from data sets that are growing exponentially. By analysing every transaction, each service inquiry and mouse-click, banks can look for patterns of behaviour and learn how customers prefer to interact and what products they may require in the future. The banks are also using data to track consumers' shopping habits to alert them to targeted deals.

One step further is the use of the data for e-commerce.

In the USA, Capital One, which recently purchased online-only bank ING Direct and renamed it Capital One 360, offers discount deals through email and its mobile app that are customized based on the user's past purchases. To take advantage of the deals, the user simply pays with his or her Capital One credit card.

In the Netherlands, a debate over banking privacy erupted after ING Groep NV (ING)'s Dutch lender revealed plans to share customers' debit card data with companies competing for their business. The bank wants to offer customers the option of receiving discounts from companies based on their spending patterns as revealed through data analysis, said Hans Hagenaars, a director of the Dutch unit

of Amsterdam-based ING, in an interview on the Dutch radio broadcaster NOS. ING, which has issued about 8.6 million Dutch debit cards, will invite about 1,000 account holders to take part in a trial run of the service later this year, he said. ING, the second-biggest Dutch savings bank, was the first Dutch lender to announce its intentions to use the data. “If, for example, you spend a couple hundred euros each year at garden center A, it could be very attractive for garden center B to offer you a discount on your next purchase,” Hagenaars said. “And what goes for garden centers, also applies to a telecommunications provider, energy companies and supermarkets.”

His comments prompted an immediate outcry. Hundreds of people on Twitter voiced alarm at what they described as an invasion of their privacy. Dutch lawmakers, including members of the governing Liberal Party and Labor Party, urged Finance Minister Jeroen Dijsselbloem to clarify whether the plan would violate the country’s data protection laws.

The Dutch privacy watchdog joined in. Banks should show utmost restraint in profiling their customers in such a far-reaching manner, Data Protection Authority Deputy Chairman Wilbert Tomesen said in an interview with broadcaster NOS. Wednesday 21 May 2014, the Netherlands Parliament commission on Finance organised a roundtable on the use of customer information by banks. On that occasion the Financial Markets Authority (Autoriteit Financiële Markten (AFM)) considered the use of customer data by banks as sensitive?. "The biggest challenge for the financial sector in the coming years is to build a culture of safety and fairness", suggested Kockelkoren. "Customers want their bank and insurer see fair dealing also with their personal information. The risks and opportunities associated with the commercial use of customer data are highly dependent on how the client data is used. "

In Belgium, BNP Paribas Fortis reviewed at the end of last year its banking terms and conditions which govern relationships with its customers. Several articles referring to the use and transmission of customers' personal data were modified in favour of the bank's trading partners so they are allowed to offer products and services through the bank's contact database. The largest bank in Belgium could therefore transmit personal data of its customers to trading partners, in particular for direct marketing operations. According to BNP Paribas Fortis, the changes to its terms and conditions comply with the law. In June 2014, by investing 500 million euros, the Belgian KBC announced its intention to create a database able to track and analyze the behavior of its customers in real time.

1. Alec Foege, Bank Data Cashes in on Customer Feelings, http://www.cnbc.com/id/100638320
2. Steve Bousabata, Le Big Data peut donner envie au consommateur d'aimer à nouveau sa banque, http://www.lesechos.fr/idees-debats/cercle/cercle-100127-le-big-data-peut-donner-envie-au-consommateur-daimer-a-nouveau-sa-banque-1012679.php
3. Maud van Gaal, ING Plan to Share Customer Payment Data Spurs Privacy Concerns, http://www.businessweek.com/news/2014-03-10/ing-plan-to-share-customer-payment-data-spurs-privacy-concerns

Internet neutraility: the neutrality of the "internet" (namely search engines such as Google and Bing) in presenting consumers seeking more information about financial services (or any information for that matter). The "search results" that appear in a search engine are the result of a combination of parameters among which the possibility to pay to include your link at the "top" of the search results. This is quite problematic when it comes to consumers searching information about for instance "repurchase of loans". If you search for this in french (under "rachat de credit") the first search page is only showing proposals from banks and other private actors, certainly not "neutral" information to consumers. Since more and more consumers rely on the internet to "find" information about a variety of things including financial services, making sure that the search results redirect them to "trustworthy" and "neutral" information is extremely important.

BANKING SECTOR

The banking sector faces great challenges; on the one hand it has to deal with the on-going sovereign debt crisis and on the other hand it is requested to meet the new Basel III capital requirements. In any case, the banking environment is changing and this also affects all users (consumers, micro entrepreneurs and micro investors) of financial services. Specifically, according to the ECB, the net tightening of credit standards by euro-area banks surged in the fourth quarter of 2011 and in the short run, a further net tightening of credit is expected. This creates lack of funding problems for all users. The situation is even worse for member states that face serious economic problems. Greek, Italian and Spanish banks see billions of deposits withdrawn in fear of their safety.

Another serious problem is the rise of the NPL (non-performing loans) ratio. This ratio has considerably risen during the last 2 years mainly for member states in economic trouble. This deteriorates even more the bad situation of the domestic banking system of these countries and raises the systemic risk for the financial sector as a whole in Europe.

Distribution issues: banks will look to supplement core banking revenues by playing a greater role in distributing other higher margin investment/ insurance products. While these products are within the remit of ESMA/ EIOPA, EBA would need to be aware of the behaviours in bank distribution channels and coordinate interventions with ESMA/ EIOPA (see above re: consumer expert group).

Competition: In February 2012, DG SANCO published the results of a mystery shopping they carried out to assess the implementation of a code of conduct adopted by the banking sector at EU level: it shows that more than two thirds of mystery shoppers were not able to switch their bank account successfully.[9] However, competition in the banking sector is likely to be further reduced due to ongoing major consolidation, and unintended consequences of prudential regulation reforms.

[9] http://ec.europa.eu/consumers/rights/docs/switching_bank_accounts_report_en.pdf

MORTGAGES AND CREDIT

Mortgage markets

Unsuitable advice: unsuitable advice when concluding mortgage loans is still evident in member states including: failing to obtain sufficient information concerning the financial position of consumers, objectives, willingness to accept risk, knowledge and experience of consumers.

Mortgage prisoners: these borrowers will be vulnerable to application of unfair terms, treatment of borrowers in arrears, and restricted access to fair, affordable mortgage credit. In the UK, some mortgage lenders offered tracker mortgages which guaranteed to track at a set percentage below base rate. Such products are now very favourable for consumers and lenders have tried to find ways to move consumers onto other, less favourable products.

By pressuring banks to grant variable rate mortgages rather than fixed rate, the Financial Stability Board would like to ensure that the risk of rate fluctuations is no longer supported by the bank but by his client. Ensure greater financial stability, including requiring banks to better take into account the risks of loans on their balance sheets, should not lead to encourage banks to offer mortgages at variable rates rather than fixed rates. If borrowers are the only ones bearing the risk of fluctuating interest rates, this would be very detrimental for many of them; The mortgage credit is the most important financial decision in life for many households and often the longest contract (20-30 years). Those who prefer a fixed rate to a variable rate in order to protect their finances, and their housing should continue to have the choice.

Interest only mortgages (Denmark): in Denmark, since 2003, consumers could take interest only loans. They therefore do not have to pay installment for the first 10 years of the 30-year loan. After the 10 years, the loan must be paid back in just 20 years if they are not given a new loan with a new 10 year period with interest only. Many will not be given such a new loan with a instalment free period because of fallen house prices etc. Interest-only period expires for many loans in 2020. But up to 2017 the interest only period will expire for the consumers who took up the loans when house prices were at the highest. Many of these consumers are likely to have major problems because they can hardly get extended installment freedom. The will have big problems.

Approx. 9 percent of consumers will have problems when interest only period expires. This is a great risk for the individual consumer, the financial sector and society. The politicians consider how to phase out the loans. But it's hard and difficult because the Danish housing market have got used to these loans and they fear to touch the problem.

Prudential regulation overshoot (banking)/ debt financing: poorly calibrated prudential regulation risks knock-on impacts on financial users through restricted access to credit, higher cost of access, higher prices. In the long-run, access to debt financing is expected to be more expensive and more difficult for all users. Banks are expected to become more risk sensitive, ask for more collateral and more information and impose higher interest rates. This is not bad *per se*, under the assumptions that it could lead to lower risk levels for the system and that a more "responsible lending" approach will be followed.

However, if we assume that the financial sector is the main intermediary in the flow of capital to the real economy, this may lead to severe funding problems for both liquidity and investment. Thus, alternative sources of financing should also be created.

Foreign currency loans (Austria and Poland): these loans have caused severe problems for consumers in Austria and Poland provide an ideal example of the type of detrimental pricing practices and promotional strategies that can lead to consumers buying unsuitable products. In Austria, these risky loans were granted not only to professional clients but even to consumers from approximately year 1995 to 2008. Banks granted those high risk loans even to consumers who often were not aware of the risks involved. Due to the high number of existing credit agreements with consumers in Austria to the present, it is necessary to adopt individual but not compulsory solutions with borrowers in order to avoid high losses or over-indebtedness. In Poland, these loans are no longer available but there are significant problems ensuring consumers affected can obtain redress. The shock move by the Swiss authorities highlights the risks associated with foreign currency loans.

Interest rates (Slovenia and other countries): in the field of mortgages, a risk we have been noticing in Slovenia and other countries where credit interests rates are mostly variable are increasing fixed margins that, together with a reference interest rate (typically Euribor), construct the adjustable credit interest rate of a mortgage. This is the consequence of the fact that Euribor doesn't any more reflect their costs of lending. In my opinion, when granting such credit, the banks are not sufficiently taking into account whether the consumer will be able to repay his loan if the Euribor is to rise to pre-crisis levels, and even less so inform the consumers about this risk. Due to the fact that most mortgages have a maturity over 20 years, it is very likely that a rise in Euribor will endanger the consumers' ability to repay his debt or put him under a serious financial strain. Repayment problems for a large number of consumers that might as well be accompanied by judicial proceedings on grounds of inadequate review of consumer's creditworthiness by the banks might, besides huge consumer detriment, also lead to new reputational and systemic risks.

To illustrate this, typical fixed margin in Slovenia has increased from between 1-1.5% in 2008 to 3-4% today. A rise in Euribor from today's 0,4% to let's say 4% could cause a significant rise in the consumer's monthly instalment. This problem is especially serious because relatively low levels of income in the new member states lead to a relatively high burdening of household income with credit instalments. Also, due to high housing ownership levels in many EU member states and a practically non-existent rent market, young families are forced into buying residential property and taking such risky credit.

Unfair contracts (Romania): mortgages have been one of the leading products sold by banks in the boom period of 2005-2008. Therefore, in a rush to gain as many clients as possible, banks have eased the conditions of lending. This was also possible as the regulation was extremely relaxed in the area of financial consumer protection and banks easily found ways to sidestep some important safeguards. Contracts were constructed in a discretionary manner that permitted banks to change, unilaterally, the costs and other characteristics of mortgages, without the possibility for consumers to refuse (for full details on this issue, please see Case Studies in Annex I).

Unsecured credit markets

Consumers in the unsecured credit markets are subject to a number of detriments including: application of unfair terms, treatment of borrowers in arrears, access to fair, affordable credit, growth in sub-prime predatory lending, growth in predatory commercial debt management firms.

Overdraft interest rates (Germany): are much too high though funding has never been that cheap for banks. There is no capping in Germany only a high-court jurisdiction that usury starts with twice the average (which all banks can easily fulfil as the average is already quite high).

Tying practices (Germany): esp. in consumer credit where banks sell binding high-cost payment protection insurance contracts to credit customers without declaring those contracts as binding (in the contract it says “voluntary”) and without calculating their costs into the APRC

Debt collecting agencies (Germany): often working for internet or telephone providers that have trapped consumers with costs and with long-term contracts or subscriptions they didn’t mean to conclude. Often costs after an agency has been mandated are much higher than the real or predicted main claim. It is often not transparent what are the grounds for collecting the debts..

Debt advice: access to objective debt advice is a priority for households in financial difficulty due to mortgage and unsecured credit commitments. In certain member states such as the UK there has been a significant growth in the number of commercial debt advice companies who charge high fees for providing debt advice[10]. These fees are unnecessary as there are established free debt advice charities.

Flitskrediet (Flash credit): is a new form of short term consumer credit[11], similar to SMS loans in Sweden. High costs make Flitskrediet a down-market product for consumers who have already depleted their other liquidity sources or have no other possibilities of credit access. Before they used high administrative or service costs to recover their costs. But apparently since the AFM controls providers they profit by adding in small print standard terms extra costs for those who repay late or those who want very fast access to the money.[12]

Debit Cards – decision taken by employers (Romania): cards are very popular in Romania. The development of cards market was possible through the practice of paying revenues by employers in a banking account, with debit card attached. More than this, credit cards have gained ground in the last years due to certain optional facilities offered, especially installments. Still, because of lack of proper

[10] The Financial Inclusion Centre estimates that a borrower with £15,000 unsecured debt using a commercial debt management company could pay £3,000 in fees over 5 years and take an extra year to repay the debt. The reality is worse as the fees are often structured so that borrowers pay high upfront charges which are lost if the borrower cannot maintain the repayment schedule.

[11] Amounts to about 0.025% percent of the Dutch consumer credit market. The average loan size is 230 Euro, whereas most contracts have a loan sum of 100 Euro. The average maturity of the loan is 24 days.

[12] See IOO (2009). Onderbouwing van een maximale vergoeding voor flitskrediet, Eindrapport, Een onderzoek in opdracht van ministerie van Financiën, Zoetermeer

regulation and very low level of financial literacy, customers find themselves often in situations of overindebtness or in situations where they use the product in a detrimental way (details can be found in Annex I: Case studies).

Non performing loans (Greece): In Greece, the most important problem that has escalated during the years of crisis is the extraordinary amount of non-performing-loans. This amount reaches today EUR84 billion, which is about 45% of GDP. If we add loans those that have smaller-but-continuous delays of 90 days, then this amount is over EUR110 billion representing over 58% of GDP and just over 50% of total loans. The IMF has underlined this issue as well and it seems that a new recapitalization process might be needed.
This is the one side of the coin, whereas the other side of the same coin refers to overindebted consumers who cannot repay their loans. There are no exact data about numbers of consumers in distress.
SME Access to finance (Greece): the biggest problem in the entrepreneurial environment today is SMEs access to finance. There is a complete lack of liquidity due to the absolute lack of trust between enterprises which squeezes trade credit and leads to transactions in cash in several cases on the one hand, and due to the lack of flow of funds from the banks to enterprises, mainly because of the problems that the banks still face in Greece on the other. This is verified by the outcomes of the respective semi-annual survey by the ECB, where Greek SMEs are almost always first among other Eurozone countries in rating access to finance as the most important problem they face.

INSURANCE SECTOR

Solvency II: this is an important reform as insurance companies have been mispricing risks. However, the impact on financial users needs to be better understood and assessed – specifically, with regards to access, pricing, and design of insurance policies.

We are concerned that more work needs to be done to ensure that Solvency II is calibrated to maintain and promote diversity, plurality of provision and real competition in the insurance sector.

Furthermore, there is an additional challenge to calibrate Solvency II requirements with existing or planned Insurance Guarantee Scheme. It is worth mentioning that there is a lack of coherent Insurance Guarantee Schemes across Europe.

Treatment of policyholders: policyholders in the life insurance sector are particularly vulnerable to unfair treatment arising from the business risks identified above. Issues that need to be addressed in clued: unfair contract terms, contract prisoners/ captive consumers, lower transparency requirements than for MiFID-covered retail investment products.

Common usage of abusive clauses. Financial supervision does not include detail analysis of insurance contracts. There are many signs that many policy wording do not meet required standard. There should be possibility to monitor them.

Gender pricing: regulators will also need to be on their guard to prevent insurance companies and distributors/ intermediaries taking advantage of the potential disruption and confusion resulting from the application of gender neutral insuranc e premiums in December 2012. Specifically, we have concerns about the pricing of insurance products, promotions and advertising of affected insurance products, and quality of advice and information provided to consumers who may be affected by the change.

General insurance: while general insurance tends to perform better than life insurance or investment based insurance, there are a number of issues to be addressed including misleading price competition, greater use of excesses on insurance policies, claims handling experiences deteriorating, and greater use of exclusions. The loss adjustment process very often does not provide full compensation which is reduced in an arbitrary way by small amount, that does not encourage to take legal steps against insurance company.

In several EU Member States, consumer organisations have identified increasing problems with "small insurances" sold to customers. These cover very specific types of risk such as mobile phone theft, payment services fraud or cancellation of travel sold on ancillary basis at point of sales. Many products sold seem not to offer value for money. Poor product quality (many restrictions and exemptions), an unfair selling context and shoddy business models (premiums paid often go mainly to intermediaries selling them) are the main problems in this growing industry.

Bankassurance: selling insurance product very often does not provide any add-value for consumers and what is even worse it does provide illusion of insurance coverage. High commission received by banks create a huge pressure on sale and lead very often to misselling. High commission reduces insurance coverage and increase use of exclusions, that often leads to ineffective coverage. Finally, the consumers has countless useless insurance products at the bank account and/or ineffective coverage for mortgage credit. This is still a problem in Poland. On our trip to Warsaw, we were informed that some of the bigger banks, additional to their traditional banking services, sell insurance products. The Polish Ombudsman in 2013 had received 1,604 complaints relating to problems of selling these insurance products including mis-selling and denial of refunds. New regulations are being constructed but there is no agreement on how best to proceed. The uncertainty on IMD II and PRIPs has discouraged the local regulator to impose new law.

Life insurance contracts: insurance with any form of guarantee becomes more and more expensive. Insurance with investment component are sold with no or very limited information about an investment part of the product.For example, in Germany, life insurance contracts are often inflexible. 80% of the contracts are not finished and served until the end. Therefore, investors incur high losses if they are not able anymore to make their running payments. This is a prime example of product pricing structures which are designed to protect the interests of providers not meet the needs of cosumers. Note this was a major detrimental feature of the life insurance sector in the UK – for example, with-profits funds,

mortgage endowment policies. FSUG suspects that this is an issue in many other insurance markets across the EU.

Irregular management of pension insurance brokerage: in 2010 the AFM(Netherlands Authority for the Financial Markets) identified significant shortcomings in chain management of pension insurance brokerage. By 2011, AFM still regularly encounters brokers who do not comply sufficiently with the requirements of the duty of care, integrity and expertise[13].

SAVINGS

Low interest rates: as a response to the financial crisis, benchmark interest rates have been maintained at a low level for a sustained period. **S**ustained low interest rates encourage risky investment behaviour in a 'search for yield' – this leaves investors vulnerable to misselling and misleading promotions.

Confusing/complex savings products[14]: banks sell, through their networks, different products offered by other financial institutions, part of the same financial group or not. This includes "Bauspar" products, mutual funds, insurance (unit linked, index linked). In this case, it is not the products or advertising (mostly nonexistent) that is misleading, but the selling technique in banking branches. Most of these products are complex, rather difficult to understand by clients, but they are sold as common savings products. After signing contracts, many clients realize that what they contracted is not a standard deposit and that they do not have instant access to the money or they have to pay a lot of fees (see Case Studies, Annex I). Consumer protection standards on savings is weak compared to loans.

Unit linked products (Poland): Another serious problem on our trip to Poland was identified with unit linked life assurance products in Poland. FSUG members expressed their concern as to the high level of fees paid by consumers for such products, transparency, the complexity and multi-layered structure of fees. Similar detrimental aspects of these products are experienced in other Central Eastern countries. Members of the FSUG agreed to try to carry out a comparison of typical unit linked life insurance contract fee structures to increase awareness of this issue.

Vulnerability of deposits: Governments will less and less hesitate to raid people's deposits in various ways as the Troika initially tried in Cyprus, and as the EC itself declared that the DGS rules did not prevent Governments from seizing deposits below the € 100 000 if they so decide.

[13] See http://www.afm.nl/en/professionals/afm-actueel/nieuws/2012/jan/ketenbeheersing.aspx

[14] http://www.conso.ro/depozite/economisire-produse-vandute-gresit-clientilor

PRIVATELY FUNDED PENSION SCHEMES

Low growth and high unemployment rates continue to put pressure on European pension systems. Pressure is directed either to increasing pension age limits or to pension cuts. The new economic paradigm will have a range of unintended consequences for consumers.

Low financial returns and bond yields: this includes advisers aggressively promoting complex, opaque, expensive investment strategies (dynamic asset allocation, liability driven investments) and financial products (hedge funds, absolute return funds) to pension fund trustees and individuals.

Prudential regulation overshoot (pensions): possible misapplication of Solvency II style regulation to pension funds. Conversely, industry backlash may cause regulators to dilute scheme member protection by allowing schemes to under-price risk and underprovide for future liabilities (particularly in conjunction with advisers selling opaque, expensive risk management strategies).

Pensions (accumulation): a key priority for regulators is to prevent value destruction in low return environment due to high and hidden transaction costs. Pension fund trustees and scheme members are vulnerable to misselling of socially useless financial innovations, and exposure to investment volatility.

Pensions (decumulation): risks here include annuity portfolios not backed by sufficient assets, low returns on annuities encouraging pensioners to take undue risks with retirement funds, poor advice on income drawdown and equity release schemes. We fear even worse: a negative real return on pensions for pension savers and pension annuities losing real value other time because of below inflation rate increases (see below Investments/Asset Management Section). In many countries annuity market and equity release merely exist. Due to lack of data and experience available products are very expensive.

Transfer of risk and responsibility: it is expected that we will see a major transfer of risk and responsibility for retirement provision away from the state and employers pension schemes to individual citizens. Greater use of individual pensions and defined contribution type schemes is expected. This is a major public policy risk which has not been properly evaluated by policymakers or regulators. There are major concerns about the ability of the industry to provide replacement pensions that are safe, sustainable, and efficient while we challenge the view that citizens generally are capable of managing the risk involved (or even want to take on the risk involved which will impact on willingness to provide for the future).

Insurance and pensions: sometimes, in Romania, asset management companies sell pension insurance component like an optional fund pension. This confusion is maintained especially by the selling agents, driven by their desire to win a bigger commission. In this manner, these products are described like having the same objective (assuring some additional income at the retirement), but the benefits offered to the clients by these are very different. Proofs for this misleading technique could be found on forums, where consumers state that they have been convinced to buy a product they did not desire. There is also a major lack of transparency and consumer protection. For example:

- In the past, pension funds did not display the structure of their investment portfolio. Therefore, clients had no possibility to compare or asses on their own the risk level of a certain fund. The market changed its behavior and pension funds started to display details of their portfolios only after a major campaign run by Conso.ro[15] and other financial newspapers (Ziarul Financiar, Bursa).

- There is **no minimum yield guarantee** for pension funds. The amount invested could have a negative performance, not even covering inflation.

- There are few to none programs for promoting private pensions system and the rights of participants to choose their fund. **Only about 20% of all new entries into the system, during a year, make a choice**. The rest are automatically assigned by "automatic distribution". It is important that these 'default' funds are 'fit-for-purpose'.

- The EC consumer Scorecard has again (2013) ranked retail financial services (investments, pensions and securities especially) as the worst consumer services market of all: so no improvement there so far.

- The extent of consumer detriment in pensions is still unknown despite efforts from OECD and from Better Finance. But one thing is certain: it is growing . The ESAs do not comply with their obligation to "collect, analyse and report on consumer trends" (article 9 (1) of the ESAs 2010 Regulations) when it regards the real performance of consumer products and services.

Pension underprovision (Italy): from the beginning of the economic crisis the number of people suspending integrative pension payments has raised to 1.4 million. This is associated with poor labour conditions and/or raising problems of over-indebtedness, where people suspend these payments to make ends meet (these are official data as of 31 March 2014). This adds to a significant decrease of people joining integrative pensions schemes, the problem being with young people not subscribing/taking part in any of them for lack of work or poor wages. The outlook is of very grim pension conditions for an increasing number of Italians.

In Italy, at the end of 2013 the total pension funds manage 116,4 billion Euros, equal to 7.5% of GDP, which is believed to be far less than many other EU countries.

[15] http://www.conso.ro/pensii/decizie-istorica-in-pensiile-private-administratorii-vor-dezvalui-in-ce-au-investit-banii-populatiei

INVESTMENTS/ ASSET MANAGEMENT

The investment/ asset management sector is vulnerable to similar range of factors as the funded pensions sector. The recent report published by the FSUG called The Performance and Efficiency of the EU Asset Management Industry provides more details on the extent of market failure in this critical industry.

Low financial returns: range of potential risks and adverse behaviours including financial users making sub-optimal decisions about risk and reward trade-offs, providers, distributors, and advisers aggressively promoting complex, riskier products such as absolute return funds, exchange traded funds, unregulated collective investment funds to retail financial users, abuse of investment projections. In addition, financial providers and governments are still too much playing on the "monetary illusion": returns are never communicated in real terms, i.e. net of inflation[16]. Nonetheless, inflation is still quite significant (typically from 2 to 4 % annually throughout the EU Members States), especially for long term and pension savings, for which its exponential impact can be devastating over time. FSUG suspects a majority of retail long term and pension investment products are delivering negative returns after inflation and taxes. In other words, they would be destroying the real value of European households' savings. FSUG has already come up with several such cases and is now launching a research study on pension products ,with a particular focus on their long term net performance for the savers.

Destruction of value: in an era of squeezed household incomes and low financial return a priority for regulators will be to ensure the sector can deliver value for investors. Regulators must guard against hidden and high charges destroying value in a low return environment. High charges will eat up a much larger proportion of investors and policyholders contributions. For example, if future returns are 6 % per annum instead of 7 %, a 1.5 % annual management charge would eat up a full one quarter of the investment returns. Investors and policyholders would have to significantly increase their contributions to make up the difference. In addition, given that only a small minority of investment managers can consistently outperform benchmarks the value destruction of investor's portfolios could be even greater. While we have seen a significant growth in the number of investment funds on the market and a degree of cross border activity, these changes have not resulted in benefits for the ordinary financial user. Indeed, costs to the end-user have risen undermining the supposed advantages of the single market. This is a good example of how market developments can benefit the financial services industry but not the financial user and why it is imperative that policymakers adopt a different approach to regulation.

Socially useless financial innovations: the investment and pensions sector is particularly vulnerable to the development of financial innovations which overall add little real value for ordinary investors (or even destroy value and introduce unforeseen risks) – for example hedge funds. Other innovations may start off offering value for investors but over time are undermined by conflicts of interest or over-engineering. Prime examples of this trend include exchange traded funds (ETFs). There is little evidence

[16] And very rarely net of taxes, although this has been a mandatory disclosure requirement for decades for US domiciled mutual funds.

that the increasing complexity of investment markets actually delivers value for ordinary investors – but creates huge value for investment professionals in the form of advisory fees and commissions.

The role of intermediation: linked to the above two risks is the growing number of intermediaries (as well as providers and products) who extract value from investors assets and contributions. This is one of the key challenges facing regulators. There is merit in intermediaries encouraging investors to save for the future or a pension (the well documented inertia factor is a major barrier to long term savings). However, there are now many layers of intermediaries between investors and capital markets which not only extract value from investor contributions but reduce the available capital allocated to the real economy.

Technological developments: platform technology introduces additional layers into investment supply chain and unnecessary charges.

Threats to corporate governance and to economic democracy: the further marginalization of individual shareholders due to the ever increasing “reintermediation” of equity markets by financial institutions. Citizens’ or people’s capitalism is about to die to the benefit of an all-powerful financial capitalism, which has no interest in the long term sustainability of the economy and society.

The share of individual shareholders in the Western equity markets has already gone from about 50 % in the 1950s to about 10 % in the 2010s to the benefit of financial institutions, through:

- The massive “packaging” of retail investment products (for example look at the expansion of investment funds since the 1970s);
- The growth of banks’ “proprietary trading” (especially after the abolition of the US Glass-Steagall Act in 1999);
- The emergence of algorithmic trading, and, in particular of high frequency trading (HFT).

This evolution is a severe threat to the corporate governance of listed businesses as it also impacts very negatively the average holding time of shares. Investment funds for example do not hold their shares on average for much longer than a year, so they have little interest in the mid to long term sustainability of corporations and to getting much involved owners of companies as they know they will likely be gone the following year. Recent capital market reforms have largely ignored the interests of individual investors, accelerating their marginalization.

It is also a severe threat for the financing of SMEs and of innovation, as financial institutions tend to focus on the most liquid shares to the detriment of small and mid cap listings. Indeed the new “market venues” created by MiFID have only focussed on big caps. Also, many big banks are more interested in the profit margins they find in trading and in investment banking rather that in their “dull” core business of lending to the real economy and especially to the SMEs which are the only generators of jobs in Europe.

High-Commission selling (Germany) of esp. investment products: the main form of selling financial products hiding high and third-party commissions, making costs incomparable from costs of other products and not disclosing the existing conflicts of interest. Numbers of intermediaries are inevitably high, consumer detriment is definitely higher.

Investments/asset management (Romania): banks represent a very important selling channel for the mutual funds, but even the employees that sell these products don't fully understand their characteristics. So, the investors are often wrongly informed about the expected yields or the right level of fees they have to bear. Asset management market in Romania is almost entirely based on banking sales force. Even more, banks have put together product that boost sales on investment funds.

A very popular product among bank offers is the **deposit + investment fund package**. Clients receive a higher interest rate for their savings if they also buy fund units, thus encouraging the sell of investment products. But tellers in bank branches are not specialized in selling a wide range of products, especially products for which the bank is only a selling channel. For this reason, cases were customers bought fund units without being properly explained the way this products function are quite frequent.

One important issue is the fiscal obligation of declaring any revenue received during the ownership period of the investment funds units to the fiscal authorities. Most clients are not aware of this obligation and risk fines for not declaring their revenues.

There is growing evidence of major implementation / enforcement failures regarding EU financial user protection Law. In particular the MiFID provisions on "inducements" and the prevention of conflicts of interests in distribution appear poorly implemented (a 2012 voluntary survey of distributors by French Regulator AMF revealed that two thirds of respondents admitted they did not comply with the rules). Of course this is also linked to the continuous lack of real access to "private" enforcement (collective redress) for abused users in most EU Member States.

Rights of shareholders (Germany): The German Federal Court (BGH) in its so-called Frosta-decision has significantly reduced the rights of shareholders of listed German stock companies.
Since 2002, the BGH has required companies that intended to delist from the stock exchange:

1. To obtain approval from the shareholders' meeting and
2. To pay an adequate cash compensation from the company or its majority shareholder to all outstanding minority shareholders.

Consequently, minority shareholders were entitled to appraisal rights, and could initiate judicial review of the adequacy of the compensation offered.

In its Frosta decision (2013), the BGH decided on the basis of a recent ruling of the German Constitutional Court that had held that neither a shareholders' meeting nor a compensatory offer were required to protect the shareholders' rights under the German constitution in the event of a delisting or downlisting.

The "Frosta" case involved the so-called downlisting of a German stock company from the regulated market to the Entry Standard of the Frankfurt Stock Exchange. The decision to downlist was made by the management board with approval of the supervisory board. No compensation offer was made to the minority shareholders, nor has an approval of the shareholders' meeting been obtained. Consequently, shareholders demanded a ruling for adequate cash compensation. The BGH, however, ruled that neither

a corresponding resolution by the shareholders' meeting nor a compensation offer to the minority shareholders to purchase their shares was required.

Instead, the BGH ruled that

1. The delisting only concerns the market for the shares and not the corporation or the shareholder's rights, and
2. The delisting rules of the stock exchanges afford sufficient protection to the shareholders. Some German listing rules provide that a filing to delist shall only be approved if there is either a purchase offer (which, however, is not subject to court review) or a sufficient time period before the delisting becomes effective so that shareholders have a chance to sell their shares on a regulated public market. What the BGH did not take into account is that the share price regularly drops significantly after a respective offer is announced.

Stock corporations and their majority shareholders are now able to undertake a delisting under considerably simplified conditions to the detriment of the minority shareholders as

1. The requirement for a mandatory purchase offer that can be reviewed by court is no longer provided for
2. The question of the approval threshold required for a delisting has now become obsolete and delistings may well be possible even below a 75% majority

Shareholders have no right to approve/disapprove the delisting at the general meeting anymore, which also hinders them to ask the court to review the delisting and the compensation.