cep Centrum für Europäische Politik
FREIBURG | BERLIN

cep**Study**

16 March 2023

Ban on Commission in Financial Services Markets

Summary of evidence and arguments for the current debate in the EU

Philipp Eckhardt and Dr. Anastasia Kotovskaia, LL.M.

© shutterstock/Crizzy Studio

At the end of 2022, EU Commissioner McGuinness caused controversy with her suggestions regarding the possible implementation of a ban on commission in the EU. But what is the current legal position in the EU? What has been the experience of the UK and the Netherlands regarding commission bans? Which ordoliberal and legal arguments are essential to the debate? And which regulatory approaches should the EU Commission pursue? These are the questions which this cep Study will seek to answer.

- Legislation, in the form of the MiFID Directive and the Insurance Distribution Directive (IDD), has already been established to strengthen consumer protection on the retail investment market. However, this has not settled the question of whether a ban on commission is necessary.
- As a result of commission bans in the UK and the Netherlands, access to advisory services seems to have become more difficult for many consumers, especially those who are financially less well off. In addition, there has been a shift towards non-advisory investment activities and a decline in the number of intermediaries.
- From an ordoliberal and legal perspective, commission bans are not an effective option for the EU. Instead of pulling the plug on established business models, the EU should continue to allow competition between remuneration models. Simply banning a distribution model is no solution for an information-inefficient market.
- Fee-based advisory models only work in competition with commission-based models (and vice versa) because the banning of one model leads to the inefficiency of the other.

This study is funded by a voluntary donation from MLP SE.

Table of Contents

1 Introduction ... 4
2 Existing legal position at EU level ... 5
2.1 Insurance Distribution Directive (IDD) ... 5
2.2 Markets in Financial Instruments Directive (MiFID) ... 7
2.3 Interim conclusion ... 8
3 Legal position in the UK and the Netherlands as well as individual EU Member States ... 8
3.1 The path to a ban on commission and the legal position in the UK ... 8
3.2 The path to a ban on commission and the legal position in the Netherlands ... 9
4 Experience of the UK and the Netherlands regarding commission bans ... 11
4.1 United Kingdom ... 11
4.2 Netherlands ... 12
5 Ordoliberal and legal assessment ... 14
6 Initial conclusions ... 16

1 Introduction

Shortly before Christmas 2022, the EU Commissioner for Financial Services, Financial Stability and the Capital Markets Union, Mairead McGuinness, made a high-profile advance on the financial industry. Then, with the debate on commission-based investment advice having faded into the background for a while, the Irish politician brought the controversial topic back into the limelight. This took just two letters[1,2] and a hearing in the Committee on Economic and Monetary Affairs (ECON) at the end of January 2023[3], and triggered a broad response from associations, consumer protection groups and politicians.[4] In these letters and at the hearing, McGuinness announced her intention, as part of the presentation of the "Retail Investment Strategy"[5] due in spring 2023, to adapt the rules on commission as laid down in the Markets in Financial Instruments Directive (MiFID)[6] and the Insurance Distribution Directive (IDD)[7].

The statements clearly show her sceptical view of commission-based remuneration systems. The Commissioner

- stresses the importance of bias-free advice tailored to the needs of retail investors,
- expresses doubt as to whether commission-based remuneration models are really in the interests of retail investors,
- sees a decline in product costs in the UK and the Netherlands, where commission bans are already in place,
- detects a shift in the Netherlands towards less expensive and more diverse products, a higher level of trust in financial advice and a slight increase in investment activity by retail investors,
- highlights that consumers often do not understand the potential impact that incentive-based remuneration may have on the advice given, and that, in this regard, additional information requirements may not be sufficient,
- sees that retail investors often end up with expensive products rather than, say, cheaper Exchange Traded Funds (ETFs),
- claims that retail investors have to pay an average of 35%[8,9] more for products distributed on a commission basis than for those brokered for retail investors without commission.

On a cautionary note, she only states that she knows that

---

1 Letter addressed to Markus Ferber, Member of the European People's Party (EPP) in the European Parliament, 20 December 2022.

2 Letter addressed to Guillaume Prache, Managing Director at Better Finance, 19 December 2022, available here.

3 EU Commission (2023), Opening remarks by Commissioner McGuinness at the Structured Dialogue with the European Parliament's ECON Committee, 24 January 2023, available here.

4 European industry representatives and consumer advocates, among others, spoke out. And according to media reports, there were also swift initial reactions from the political arena, with the SPD and the Greens taking a more positive view of a general ban on commissions, while the FDP expressed a rather sceptical attitude.

5 The "Retail Investment Strategy" is a package of measures planned by the Commission with the aim of increasing the participation of retail investors in the EU capital markets. It also aims to improve the market outcome for retail investors and strengthen their confidence.

6 Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directives 2002/92/EC and 2011/61/EU.

7 Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution.

8 The percentage comes from a study commissioned by the EU Commission [EU Commission (2022a), Uličná, D., Vincze, M., Mosoreanu, M., et al., on disclosure, inducements, and suitability rules for retail investors: Final report, pp. 24 and 25].

9 The authors of the study have since revised this statement. They acknowledged that, in their sample, the cost of products with inducements is not 35% higher than products without inducements, but only 24-26% (revision of 8 February 2023, see here). However, even after the revision, it is still unclear whether, among other things, the sample of products without inducements also included completely advice-free business. In any case, it is no surprise that product costs are higher for commission-based distribution models than for business that provides no advice at all.

- retail investor behaviour and the level of financial literacy varies in the EU; so it's not quite a level playing field,
- that the Dutch market is not representative of the rest of the EU, and
- there are concerns about the availability of financial advice and she does not want to jeopardise access to financial advice.

Ms McGuinness' comments did not come as a complete surprise, however. The EU Commission conducted a consultation from May to August 2021 that included the subject of commission.[10] It also launched a Call for Evidence in May 2022[11], in which it criticised the "*low reliability and quality of the provided investment advice due to advisors' remuneration setup and product cost-structures or varying levels of investment advisor competence*".[12] And finally, in its 2023 work programme, for the 1st quarter of this year, it announced a "Retail investment package: Improving the retail investment framework".[13] By then, at least, it was clear that regulatory adjustments at EU level could be expected in 2023.

In this cep**Study**, we first want to provide an overview of the current legal position at European level (Section 2). We will then take an in-depth look at the UK and the Netherlands, which have already implemented bans on commission at national level (Section 3). In Section 4, we will examine what the experience of these two countries has been in this regard. We will then examine bans on commission from an ordoliberal and legal perspective (Section 5). In Section 6, we will draw initial conclusions and develop ideas for more targeted regulation.

2 Existing legal position at EU level

At EU level, two legal acts in particular apply which contain rules on the commission-based remuneration model. These are MiFID, which applies to financial product distribution, and the Insurance Distribution Directive (IDD), which was created for insurance product distribution. The EU legislator has laid down rules in both Directives because it sees conflicts of interest in certain remuneration structures, including commission-based models, which (may) run counter to the client's interests. The legislator has taken various precautions, which are stricter in the MiFID than in the IDD, to prevent or counteract these conflicts of interest:

2.1 Insurance Distribution Directive (IDD)

Principles of insurance distribution: Insurance intermediaries and insurance companies must "always act honestly, fairly and professionally" towards their customers and in accordance with their "best interests".[14] The remuneration of the insurance distributor must not conflict with their duty to act in the best interests of the client. In particular, he must not make arrangements, by way of

---

[10] EU Commission (2021a), Public Consultation on an EU strategy for retail investors, 11 May 2021 - 3 August 2021, available here.

[11] By way of Calls for Evidence, the Commission typically seeks initial views from stakeholders on regulatory proposals and provides early indications of which regulatory options it is considering.

[12] EU Commission (2022b), Call for Evidence, Retail investment: New package of measures to increase consumer participation in capital markets, Ref. Ares(2022)3391353, available here.

[13] EU Commission (2022c), COM(2022) 548, Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, Commission Work Programme 2023 - A Union standing firm and united, Annex I.

[14] Art. 17 (1) IDD.

remuneration[15] or the setting of sales targets, which (could) amount to the recommendation of one insurance product over another which better meets the customer's needs.[16]

Transparency requirements: Insurance intermediaries must inform the customer, in good time before the conclusion of an insurance contract, about the "nature"[17] of the remuneration they will receive in connection with the insurance contract. Furthermore, they must state whether the remuneration is to be paid directly by the customer, i.e. on the basis of a fee, or whether the remuneration is included in the insurance premium, i.e. on the basis of a commission.[18] Insurance companies are subject to the obligation to disclose the "nature" of the remuneration received by their employees.[19]

Additional requirements for the distribution of insurance-based investment products: Additional requirements apply to the distribution of so-called insurance-based investment products[20]:
Transparency: Insurance intermediaries and insurance companies must inform (potential) customers about "all costs and related charges" before concluding a contract. This includes information on the cost of advice and the cost of the insurance-based investment product, as well as on "how the customer may pay for it, also encompassing any third party payments".[21]
Dealing with conflicts of interest: Insurance intermediaries and insurance companies must take appropriate precautions to prevent or manage conflicts of interest. If these precautions are not sufficient, insurance intermediaries and insurance companies must disclose to the customer the "general nature or sources" of the conflicts of interest.[22]
Permissibility of commission: Insurance intermediaries and insurance companies must ensure that any commission or non-monetary benefit paid to or received from third parties - other than the customer - complies with the duty to act in accordance with the best interests of the customer and to prevent conflicts of interest. Such compliance may exist, firstly, where the commission or non-monetary benefit "does not have a detrimental impact on the quality of the relevant service to the customer" and, secondly, does not compromise the duty of the insurance intermediary or insurance company to act both in the "best interests of its customer" and "honestly, fairly and professionally".[23]

Option for Member States: The EU legislator has spoken out against a general EU-wide ban on commission-based remuneration models. Nevertheless, the IDD in principle allows Member States to "prohibit or (further) restrict the offer or acceptance of fees, commissions or non-monetary benefits" (flexibility clauses)[24,25] and, according to EIOPA, some Member States use these options.[26]

---

15 "Remuneration" means "any commission, fee, charge or other payment, including an economic benefit of any kind or any other financial or non-financial advantage or incentive offered or given in respect of insurance distribution activities" (Art. 2(1) No. 9 IDD).
16 Art. 17 (3) IDD.
17 This does not include an obligation to disclose the amount of remuneration received.
18 Art. 19 (1) IDD.
19 Art. 19 (1) IDD.
20 "Insurance-based investment products" are defined as "insurance products which offers a maturity or surrender value that is wholly or partially exposed, directly or indirectly, to market fluctuations". These include, for example, capital-forming life insurance policies.
21 Art. 29 (1) (c) IDD.
22 Art. 28 (1) and (2) IDD.
23 Art. 29 (2) (b) IDD.
24 Art. 22 (3) and Art. 29 (3) IDD.
25 The requirements for dealing with inducements are further specified in the Delegated Regulation (EU) 2017/2359, in particular in Article 8.
26 Cf. EIOPA (2022b), Annexes to EIOPA's final report on technical advice to the Commission on retail investor protection, EIOPA-BoS-22/021, 29 April 2022, p. 14.

2.2 Markets in Financial Instruments Directive (MiFID)

Principles for the provision of investment services: Investment firms are also subject to the principle that they must act "honestly, fairly and professionally in accordance with the best interests of their clients".[27] And for them, too, the duty to not remunerate the performance of their staff in a way that conflicts with the duty to act in the best interests of their clients applies. In particular, they must not make arrangements, by way of remuneration[28] or the setting of sales targets, which (could) amount to the recommendation of one financial instrument over another which better meets the client's needs.[29]

Transparency requirements: Investment firms must inform their (potential) clients about all costs and related charges in good time. This requirement includes, among other things, the cost of advice, the cost of the financial instrument marketed and also any third-party payments.[30] In any case, they must be transparent about the existence, nature and amount of the commission, or the method of calculating the amount.[31]

Dealing with conflicts of interest: MiFID provides that investment firms must take appropriate precautions to prevent or manage conflicts of interest. This also includes such conflicts as those caused by the receipt of inducements from third parties. If these arrangements are not sufficient, investment firms must disclose to the client both the "general nature and/or sources" of the conflicts of interest and the steps they have taken to limit them.[32]

Permissibility of commission: Investment firms must also ensure that any commission or non-monetary benefit paid to or received from third parties - other than the client - in connection with the provision of investment services, complies with the duty to act in accordance with the best interests of the client and to prevent conflicts of interest. Such compliance may exist if the commission or non-monetary benefit "enhances the quality of the relevant service to the client" and the obligation to act "in accordance with the best interests" of the client is not impaired.[33]

Additional requirements for independent advice: Where investment firms are providing investment advice, they must indicate whether or not the advice is provided "on an independent basis" and whether the advice is based on "broad or more restricted analysis" of financial instruments.[34] If they are providing advice "on an independent basis", they must assess a "sufficient range" of financial instruments and, in particular, must not limit themselves to their own financial instruments. In addition, they are then not allowed to accept and retain "fees, commissions or any monetary or non-monetary benefits" from a third party ("commission ban"), except for instance for "minor non-monetary benefits that are capable of enhancing the quality of service provided to a client". The latter, however, must then be disclosed.[35] Conversely, therefore, inducements are now only permitted for "non-independent" advice.

Additional requirements for portfolio management: When providing the service of portfolio management, investment firms are in principle not allowed to accept and retain "fees, commissions or any monetary or non-monetary benefits" from a third party ("commission ban"). Only "minor non-

---

27 Art. 24 (1) MiFID.
28 While the IDD contains a clear definition of "remuneration", MiFID does not.
29 Art. 24 (10) MiFID.
30 Art. 24 (4) MiFID.
31 Art. 24 (9) MiFID.
32 Art. 23 (1) and (2) MiFID.
33 Art. 24 (9) MiFID.
34 Art. 24 (4) and (7) MiFID.
35 Art. 24 (7) MiFID.

monetary benefits that are capable of enhancing the quality of service provided to a client" may be permissible, but must be disclosed.[36]

Option for Member States: MiFID allows Member States to impose "additional" requirements on the matters mentioned but only "in exceptional cases". They must also be "objectively justified and proportionate" and address specific risks to investor protection or to market integrity.[37,38] According to the Commission, only two Member States - Spain and Sweden - have made use of the option to introduce additional requirements.[39]

2.3 Interim conclusion

While both the IDD and MiFID contain rules for dealing with commission-based remuneration models, there is a significant difference between them. Thus, inducements are "prohibited unless permitted" under the MiFID and must pass a quality improvement test. Under the IDD, on the other hand, inducements are "generally allowed" unless they have a negative impact on the quality of service for the customer. Thus, the inducement requirements under the IDD are "laxer". However, Member States also have more leeway to make these requirements stricter because the IDD is designed as a minimum harmonisation directive. The design options for Member States under MiFID are more limited.[40]

3 Legal position in the UK and the Netherlands as well as individual EU Member States

3.1 The path to a ban on commission and the legal position in the UK

As early as 2006, the Financial Services Authority in the UK launched a review of the financial services market. This was carried out within the framework of the so-called "Retail Distribution Review" (RDR), which examined in particular whether commission-based advice involved misaligned incentives in a way that could be considered a trigger for high levels of mis-selling.[41] Such mis-selling was found in particular in connection with residual debt insurance (payment protection insurance).[42] In this context, the Authority identified several types of distortions that resulted in sales not being made in accordance with the best interests of customers.[43] Even the disclosure of any conflicts of interest did not sufficiently protect investors. Moreover, the commission-based remuneration model and its inherent conflicts of interest were not sufficiently understood by the investor.[44] In principle, the investment landscape in the UK was considered favourable for a commission ban since a mature market with actively investing consumers had already become established, for example via compulsory occupational pension schemes.[45] Based on these findings, some regulatory adjustments were made under the RDR to strengthen the protection of retail investors. Alongside additional rules on adviser

---

[36] Art. 24 (8) MiFID.
[37] Art. 24 (12) MiFID.
[38] The requirements for dealing with inducements are further specified in the Delegated Regulation (EU) 2017/593, in particular in Articles 11 and 12.
[39] EU Commission (2022a), p. 257.
[40] Ibidem, pp. 250 and 251.
[41] Competition Commission (2009), Market investigation into payment protection insurance; Oxera (2009), Competition in secondary products: the case of payment protection insurance.
[42] Thus, many customers were pressured into buying these products, even though they were only intended to be optional. Moreover, they were also sold to clients who were not even eligible for them [Oxera (2015), Regulating remuneration systems: effective distribution of financial products, p. 20; more information here].
[43] Oxera (2015), p. 15 et seq.
[44] EU Commission (2022a), p. 294.
[45] EFAMA, EBF, EAPB, EACB, ESBG, Insurance Europe, EUSIPA (2022), Joint letter on EC Retail Investment Strategy and the importance of financial advice, 16 December 2022, available here.

qualifications and stricter transparency requirements, it was also decided that commissions could no longer be used to pay for advice.[46] These new rules came into effect on 1 January 2013. In particular, they provide that intermediaries of investment products may no longer accept commissions from the providers of the products. The ban only applies to sales to retail investors. It does not apply to all financial or insurance products but is limited to pension insurance, investment funds, savings schemes, securities, shares and structured venture capital products, among others. Real estate financing and term life insurance, on the other hand, are not covered. Ultimately, it applies to all distributors of the investment products mentioned. As a result of the ban on accepting commission, intermediaries of investment products are now only allowed to provide their advisory services in return for a fee to be paid by the client. They must therefore quote clients two separate fees, one for the investment product and one for the advisory services. Both must be disclosed to the client. Under the RDR, it was also decided that advisers must disclose whether and to what extent their advice is "independent" or "restricted". If they declare that they (wish to) provide independent advice, they must take into account a wide range of products available on the markets, whereas if they provide restricted advice they may limit their choice but must disclose and explain the limitation to the client.[47,48,49,50]

3.2 The path to a ban on commission and the legal position in the Netherlands

The Netherlands probably has the strictest commission rules in the EU.[51] They were the result of an upsurge in mis-selling that led the Dutch government and regulators to intervene, in particular to counter over-charging, prevent mis-selling, improve transparency and create a level playing field. The aim was also to achieve a clear separation of payment streams in financial distribution.[52] The mis-selling occurred predominantly in the mortgage markets, i.e. in a specific market segment.[53] According to one study, the commission-based remuneration structures of intermediaries contained financial incentives which promoted complex mortgage products issued by only a limited number of providers. Furthermore, the amount of commission was often linked to the size of the loan taken out.[54] Consumers therefore bought products that had less favourable interest rates and lower quality due to information asymmetries.[55] Finally, another mis-selling scandal was uncovered in 2006, which resulted in a loss to Dutch insurers of about € 5 billion and further fuelled the discussions about a commission ban.[56]

The first significant regulatory step was the introduction of commission ceilings in 2009. These were thus already initiated before, and independently of, the implementation of the IDD and MiFID. In 2011,

---

46 Financial Conduct Authority (2020), FCA publishes evaluation of its work on the financial advice market, press release 3 December 2022, last updated 29 November 2021, available here.

47 Oxera (2015), p. 15 et seq.

48 Financial Conduct Authority (2014), Post-implementation review of the Retail Distribution Review –Phase 1, December 2014.

49 KPMG (2021), Zukunft der Beratung: Ein Vergleich der Honorar- und Provisionsberatung aus Sicht der Retail-Kunden, Whitepaper, November 2021.

50 Versicherungsbote (2015), Finanzberatung – Provisionsverbot führte in Großbritannien nicht zu Vermittlersterben, 31 March 2015, available here.

51 The legal framework for insurance activities is provided in particular by the Financial Supervision Act (Wet op het financieel toezicht) and a number of other supplementary regulations, such as the Decree on Prudential Rules (Besluit prudentiële regels) and the Decree on Market Conduct Supervision (Besluit Gedragstoezicht financiële ondernemingen).

52 Oxera (2015), p. 24 et seq.

53 Fred de Jong (2017), A commission ban for financial advice: Lessons learned from The Netherlands, p. 5.

54 Bas, P. de, Bruggert, F. & Lijn, N. van der (2004), Marktwerking op de markt voor hypothecaire kredietverlening: analyse van de markt voor hypotheekverstrekking en de markt voor advies door tussenpersonen, ECORYS-NEI Macro & Sector Beleid, Rotterdam.

55 Fred de Jong (2017), p. 5.

56 Rijn van der Linden (2019a), Banning protection commissions - the Netherlands experience, 18 March 2014, available here.

having failed to push through stricter rules on commission at EU level, the Dutch government decided to seek a ban on commission at national level.[57] The Ministry of Finance had already confirmed in 2010 that the envisaged cultural change from product-oriented sales to customer-oriented advice had not been achieved.[58,59] As in the UK, a commission ban was therefore introduced in 2013. It prohibits advisers from receiving payments from product providers and applies, in particular but not exclusively, to complex financial products with a potentially greater impact on investors. The ban already covered a wide range of products to begin with, including life insurance, pension insurance, mortgage loans, investment fund holdings and death benefit insurance. But just one year later, in 2014, the ban was further expanded to cover other investment products, including those considered less complex, such as funeral insurance. However, typical property and accident insurance, such as motor vehicle, household, third-party liability and legal expenses insurance, remain exempt from the commission ban.[60,61] In addition, personal loans and consumer credit are not covered, and in the case of health insurance, commission is paid by the insurance companies.[62] In 2015, another innovation was implemented. This was a restriction (not a complete ban) on the right of advisers to transfer payments made by investors to the providers of the products covered by the commission ban. This rule does not however apply to any other products.[63,64,65] As part of the implementation of the IDD in 2018, the Dutch government examined whether it wanted to retain the complete ban on commission and ultimately decided that it did, thus taking advantage of the option to adhere to stricter rules than those of the IDD. In the years since, the government has repeatedly lobbied for the establishment of an EU-wide ban on commission.[66,67]

57 EU Commission (2022a), p. 292.
58 Fred de Jong (2017), p. 5.
59 Rijn van der Linden (2019b), A Ban on Commissions: The Netherlands Approach to Transparency and Remuneration.
60 Oxera (2015), p. 24 et seq.
61 EU Commission (2022a).
62 Van Bruggen Adviesgroep, What does good financial advice cost?.
63 Oxera (2015), p. 24 et seq.
64 Minister of Finance (2011), 'Uitwerking regelgeving provisieverbod', Letter to Dutch Parliament, 13 April 2011.
65 Art. 86c Besluit Gedragstoezicht financiële ondernemingen.
66 In November 2019, for example, the Financial Stability Committee spoke out in favour of this. One year later, the government reiterated this position in a parliamentary briefing relating to the EU Commission's Communication on Capital Markets Union.
67 In July 2021, the Ministry of Finance and the Supervisory Authority underlined this requirement in a non-paper [Dutch Ministry of Finance/Dutch Authority for the Financial Markets, The Netherlands' position on effective consumer and investor protection to stimulate long-term retail investment, July 2021].

4 Experience of the UK and the Netherlands regarding commission bans

4.1 United Kingdom

There is some controversy over the question of whether the commission ban in the United Kingdom has been successful, and most notably as to whether the ban has given rise to an "advice gap". The advice gap refers to the discrepancy between investors who want advice and those who can actually afford it. The assumption is that bans on commission make access to advice more difficult and that financially less well-off retail investors, in particular, (have to) do without it. The evidence for the UK seems to indicate that an advice gap exists here. Since 2009, for example, the advice levels for investment funds have declined significantly from approx. 67% to approx. only 12%. Particularly affected, however, is the market for private pension products, where a decline in advice levels of approx. 66 percentage points has been recorded.[68] This shows that an advice gap has indeed arisen since the introduction of the commission ban.[69] At the same time, it is likely that one million more consumers accessed advice in 2020 than in 2017, representing around 8% of UK adults (6% in 2017). In addition, a large number of investors (67%) state that they do without advice because they consider it to be unnecessary; they therefore do not want any advice at all and thus, strictly speaking, do not contribute to the emergence of a gap.[70,71] Ultimately, it is mainly low-income consumers who decide against advice. Most notably, where the investment amount is small, they often consider that advice fees are not cost effective,[72] although surveys from 2017 showed that only about 9% of clients are financially unable to pay for advice.[73] Just under half of investors who are potentially willing to pay for advice only do so if the costs are reasonable from their point of view.[74] At the same time, 72% of investors who received advice were satisfied with it,[75] whilst only 8% of customers in the UK are generally open to receiving regular advice.[76]

Since the introduction of the commission ban, there is an apparent tendency for fewer intermediaries to be active on the market.[77] However, the decline seems to be due not only to the commission ban but also to other factors, such as higher professional standards and increased price competition.[78,79] In general, it appears that clients with small portfolios are less attractive to financial advisers than wealthy ones. For example, the average client in the UK has assets of more than £150,000.[80] In addition, 40% of intermediaries require new clients to have a minimum level of assets as otherwise investment advice does not seem financially viable. This is probably the reason why many advisers have already turned clients away.[81] For example, according to one survey, 69% of advisers said they

---

68 Detlef Pohl (2022), Provisionsverbot: Dramatische Folgen im Königreich, Procontra, 25 July 2022, available here.

69 See also EU Commission (2022a), p. 294.

70 FCA (2020), p. 6.

71 The fact that there seems to be little interest in advice may also be partly explained by the fact that intrinsic consumer demand for financial and insurance products is often low, as markets are regularly seen as sellers' markets.

72 HM Treasury (2016), Financial Advice Market Review, Final report, March 2016, p. 7.

73 HM Treasury and FCA (2017), Financial Advice Market Review, Baseline report, p. 11.

74 Ibid., p. 22.

75 FCA (2020), p. 31.

76 FCA (2022), Broadening access to financial advice for mainstream investments. Consultation Paper CP22/24, p. 64.

77 in 2011 the number of advisers in the UK was around 40,000, in 2014 it had fallen to around 30,000 and in 2017 to around 26,000[FCA (2019), Evaluation of the impact of the Retail Distribution Review and the Financial Advice Market Review, p. 14; Wilfred Ling (2016), Problems when UK banned commissions, 4 April 2016, available here.

78 Oxera (2015), p. 22 and 24.

79 Verbraucherzentrale Bundesverband (2019), Europäische Provisionsverbote & deutsche Fehldarstellungen, Position paper from the Federation of German Consumer Organisations based on the commission bans in the UK and the Netherlands, January 2019.

80 FCA (2020), p. 3.

81 Ibid., p. 32.

had refused clients access to advice, with this being attributed to the client's financial situation in 43% of cases.[82,83] Another survey suggests that between 2013 and 2015 alone, the rate of advisers requiring minimum assets of £100,000 rose from 13% to 32%.[84] These developments indicate that access to advice has become more difficult, especially for financially less well-off clients.

With regard to the costs of financial products, we can conclude that these naturally decreased after the introduction of the commission ban due to the elimination of the commission element.[85] There are also indications that product costs in the case of certain retail investment products have fallen beyond this commission element. This is attributed most notably to a trend towards less complex and low-cost products, such as ETFs,[86] as well as increased price competition between advisers and product providers. However, the UK Financial Services Authority was unable to provide a definitive statement on whether this development also applies to existing products. At the same time, it also saw an increase in the cost of advice for consumers but refrained, in the end, from drawing any clear conclusions on whether the decreases in product costs were more or less offset by the increase in advice costs, and what effect the commission ban had therefore had on the total cost of the investment.[87,88]

The extent to which the "quality of advice" has also improved as a result of the commission ban cannot be clearly ascertained. The 2016 Financial Advice Market Review (FAMR) saw an improvement in this regard but mainly for consumers investing larger amounts. It attributed this to stricter professional standards and increased professionalism in the industry, i.e. not specifically to the commission ban.[89] In general, a large proportion of consumers (56%) are satisfied with the quality of the advice they receive, which is higher than a few years ago (48% in 2017).[90] Only 11% of investors who choose not to take advice say that a lack of confidence in the quality of advice is the main reason.[91,92]However, these figures do not indicate how the quality of advice would be rated if the commission-based distribution model were still in place in the UK today.

4.2 Netherlands

The Dutch investment landscape is different to that of many other EU countries. In the Netherlands, for example, an above-average number of private households (69%) invest in insurance and pension products.[93] Many consumers know their way around the financial world and only buy products they really need.[94] There is also a traditionally high level of capital market participation in the Netherlands and a preference for non-traditional products as well as execution-only products.[95] The commission

---

82 HM Treasury (2016), p. 6.
83 KPMG (2021), p. 20.
84 HM Treasury (2016), p. 19.
85 For example, fund fees fell by up to 50% in the first 5 years [Fonds professionell (2018), Nach Provisionsverbot: Fondskosten fallen um bis zu 50 Prozent, available here].
86 I.e. products that were already associated with no or low commissions even before the commission ban.
87 FCA (2014), Post-implementation review of the Retail Distribution Review –Phase 1, December 2014.
88 EU Commission (2018), Distribution systems of retail investment products across the European Union: Final report, 24. April 2018, p. 79.
89 FCA (2016) Financial Advice Market Review: Final report, March 2016.
90 FCA (2020), p. 31.
91 HM Treasury FCA (2017), p. 11.
92 When assessing the quality of advice, the FCA considers, among other things, the levels of satisfaction with advice received, the extent of mis-selling and whether advisers meet professional standards and qualifications [FCA (2020), pp. 29-30].
93 EU Commission (2022a), p. 60.
94 Rijn van der Linden (2019b).
95 EU Commission (2022a), p. 69.

ban has received widespread support in the Netherlands. According to the Dutch Ministry of Finance, misaligned incentives for intermediaries have been reduced as has mis-selling. In addition, it is their view that no advice gap has emerged. Although some consumers probably did refrain from seeking advice, this was because they were unwilling rather than unable to pay for it.[96] Nevertheless, the proportion of retail investors receiving investment advice is falling, according to the Dutch Financial Markets Authority (Autoriteit Financiele Markten, AFM). A consumer survey by the AFM shows that the percentage of consumers using investment advice initially - in the first three years after the commission ban came into force - fell by 3 percentage points. Many of these investors are switching to execution-only services. Their share has risen significantly - to 60% of investors - since the introduction of the commission ban although not necessarily due only to the ban. The provision of (online) portfolio management services has increased by 10 percentage points within three years.[97] Other concepts, such as guided execution services, have also developed in the Netherlands, and - compared to other Member States - there has been an above-average shift by investors towards passively managed funds. In addition, the Dutch financial regulator concludes that the ban has contributed to the growth of the robo-adviser segment. Irrespective of how this development is evaluated, it is evident that, especially outside of the conventional advisory business, fiercer competition has developed and a variety of innovations have emerged.[98] The reason for the apparent move away from advice-based sales in the Netherlands, and the increased focus of consumers on execution-only transactions, is also reflected in the advice fees that now have to be paid.[99]

Furthermore, access to investment advice is increasingly limited to wealthier client groups.[100] And surveys show that about 46% of low-income consumers would tend not to seek advice because of the cost of financial advice[101], although only about 2% are unable to afford advice.[102]

The number of intermediaries has slightly decreased since the introduction of the commission ban. However, a trend towards fewer intermediaries also existed several years earlier.[103] The decline can also therefore be attributed to factors such as stricter professional qualifications for intermediaries, increased digitalisation and the banking crisis.[104] Nevertheless, the Commission ban has arguably had a significant impact on independent financial advisers in the Netherlands: their number has dropped by 30%.[105] And the number of insurance intermediaries is also declining, although the volume of advice has not decreased.[106]

In 2018, the Dutch Financial Supervisory Authority also noted in a briefing that the "quality" of advice had seen a "broad" increase but did not elaborate on how this had been measured. On a cautionary note, at least, it pointed out that considering the consequences of the commission ban in isolation was

---

96 EIOPA (2022d), Country-by-country analysis - The Netherlands - Annex IX to the Report on the application of the Insurance Distribution Directive (IDD), EIOPA-BoS-21/584, p. 10.

97 AFM (2020), Working towards open and sustainable capital markets in Europe that serve the real economy - next steps for the CMU, A contribution by The Dutch Authority for the Financial Markets (AFM), 28 April 2020.

98 Ibid.

99 PWC 2017), The Dutch Disadvantage?, September 2017.

100 EU Commission (2022a), p. 292.

101 Nibud (2017), Rapport Keuzeproces bij financieel advies, p. 10.

102 CentERdata (2017), Consumenten en financieel advies: Consumentenonderzoek in het kader van de evaluatie van het provisieverbod, p. 14.

103 The number of authorised advisers and financial intermediaries decreased from 10,031 to 8,458 between 2010 and 2015 [AFM (2015), Trends vergunning gegevensadviseurs & bemiddelaars].

104 Fred de Jong (2017), p. 8.

105 Brokers Ireland, Submission on the Central Bank's Discussion paper on the Payment of Commission to Intermediaries, p. 7.

106 EU Commission (2022a), p. 292.

virtually impossible since, for example, rules on professional qualifications had been tightened at the same time as the ban, and there was also a lack of valid data. It also stated that market participants were primarily seeing a combination of improved supervision, more stringent professional requirements, and the use of software, as key factors in improving the quality of advice, and pointed out that there was still a need for further quality improvements.[107,108] Two years later - i.e. in 2020 - the Authority again concluded that "quality of advice" had improved, although it attributed this solely to the fact that the interests of investors and advisers were now aligned.[109]

5 Ordoliberal and legal assessment

When considering whether the regulation of the various remuneration models is necessary, we must decide whether it is justified due to the existence of market failures in the markets for the distribution of financial and insurance products. Some market deficits can in fact be identified, primarily involving information asymmetries between product distributors, on the one hand, and consumers, on the other. The former usually have a knowledge advantage over the latter, which they can use to their own advantage due to the fact that financial and insurance products often possess the characteristics of credence goods, which means that their quality only becomes apparent in the medium to long term. In addition, the remuneration models being used could promote conflicts of interest and trigger false incentives for product distributors, who as a result may lose sight of the customer's interests, giving rise to the risk of mis-selling. Consequently, there is frequently found to be a need for regulation and the EU has already addressed existing market deficits by introducing, most notably via the MiFID and IDD, requirements for transparency regarding the service provided and the costs thereof, rules on dealing with conflicts of interest, provisions highlighting the client's interest and partial bans on commission. However, there is disagreement on the best way to address these deficits in the future.

Here are some suggestions for debate: In many Member States that have not imposed commission bans, the commission-based remuneration model dominates, while the fee-based remuneration model has not (yet) been able to establish itself. In the competition between distribution models, it is therefore evident that many investors in the EU still prefer one model over the other, or they are switching to new, innovative alternatives (e.g. robo-advice). Intervening in established market structures by suppressing a business model - such as by banning it - therefore always means restricting competition for the best distribution model. Ultimately, a ban on commission, for example, restricts freedom of choice for the customer who is forced to switch to another distribution channel. In a free market economy, however, it should be up to the investors to decide which distribution model they prefer. This basically requires investors to be well-informed about the strengths and weaknesses of the different types of remuneration, i.e. they must be in a position to make an "informed" decision about which type of remuneration they prefer. At the same time, it is essential for any classification of the remuneration models to be as objective as possible. The current discussion, however, is somewhat skewed. The weaknesses of commission-based distribution are frequently highlighted, while those of other distribution models are largely ignored. If we take a closer look at commission-based distribution, it is certainly true that some misaligned incentives can have a negative effect on advice. Most notably commission creates an incentive to sell as many products as possible as this can increase revenue. In addition, it creates an incentive to prefer certain products over others because they involve

---

[107] Briefing of the Dutch Minister of Finance to the Parliament of the Netherlands concerning the effectiveness of the inducements ban, 23 January 2018.

[108] This relates most notably to the distinction between the recommendations of a product provider and those of an "independent" adviser.

[109] AFM (2020).

more commission for the intermediary. In both cases, therefore, the interests of the distributor may not be aligned - at least in the short term[110] - with those of the customer. Thus, purchasing as many products as possible is often inappropriate for the consumer, and the product that promises to give the distributor the highest commission is not always - although it quite possibly might be - the most suitable product for the consumer. However, fee-based advice, which is often declared to be the more preferable distribution model, also has its pitfalls. Firstly, it provides an advice incentive. Whilst there is less incentive for the adviser to sell as many products as possible, and thus also some unsuitable ones, he may have an incentive to provide his clients with advisory services more frequently or at more regular intervals since his income derives from the advisory service itself. Secondly, financially weak clients may not be willing or able to pay a fee ex ante that covers the adviser's costs for high-quality advice. A commission ban could therefore lead to a reduction in advisory services in areas where they are particularly important. This may mean that the adviser increasingly turns to wealthy client groups - as can be observed at least to a certain extent in the UK and the Netherlands - or reduces the quality of his advice in order to continue to cover costs and/or, on the other hand, that these potential client groups turn to other distribution models, do without advice altogether and/or possibly refrain from investment activities. The latter would be detrimental to the goal of the Capital Markets Union to strengthen consumer participation in the financial markets. Thirdly, the question arises whether fee-based advisers are in practice completely immune from selling unnecessary financial or insurance products because consumers could frequently be "disappointed" if the adviser concludes that there is no need for them to buy a financial or insurance product, in which case they may ask themselves why they had to pay a fee.

With a commission ban, the legislator, whether at the EU or national level, would therefore virtually eliminate the weaknesses (as well as the strengths) of the inducement-based distribution model but would also force the consumer either to accept the weaknesses and/or the strengths of other models or do without financial and insurance advice. There will thus be an automatic privileging of all non-provision-based alternatives which, from an ordoliberal point of view, goes too far.

Instead, the legislator should pursue the goal of enabling consumers to gain a better understanding of the existing and developing distribution models, and identify their possible advantages and disadvantages, without trying from the outset to make one particular business model especially "palatable" to the consumer. This could be done most notably by investing in consumer financial education, as well as by introducing, for example, more comprehensive legislative disclosure requirements - in addition to the transparency requirements already in place - which would prompt financial and insurance distributors to explain their distribution model to potential customers in a comprehensible way.[111] With these conditions in place, consumers could decide for themselves which distribution model they trust more and there would at least be no need for legislative discrimination against any one remuneration system.

Restricting free competition between the different remuneration systems would also raise legal questions because a commission ban would also directly curtail the freedom of distributors of financial

[110] In the long run, however, he has to reckon with, among other things, damage to his reputation which could motivate consumers to change the distribution model or the distributor.

[111] When explaining the business model, however, the adviser should not be forced to state the commission amount, for example, because remuneration structures often vary widely and are therefore difficult to compare. A broker, for example, has to cover all his expenses by way of commission whereas this is not the case for other forms of distribution. Moreover, the commission level does not necessarily say anything about the quality of the recommended product. Ultimately, this could encourage consumers to purchase products with low commission even though they may not always be the most suitable for them.

and insurance products to exercise their profession and may therefore be regarded as an encroachment on the distributor's fundamental freedom of occupation. In addition, it represents an encroachment on the freedom to conduct a business.[112] There would also be a violation of the freedom of contracting parties to contractually agree on the remuneration for their professional services, which is protected by Article 12 (1) of the German constitution (*Grundgesetz*)[113].[114] In order to incorporate a commission ban into national law, the corresponding legal provision requires a legal basis. Any encroachment on the distributors' freedom of occupation must be justified as being in the overriding public interest and as complying with the principles of reasonableness, suitability and proportionality.[115]

Also open to question is whether it is possible to draw incontrovertible conclusions for the entire EU from the analysis of the outcome of commission bans in the Netherlands and Great Britain. After all, the markets in the EU member states vary significantly[116] which means that an EU-wide commission ban would also have varying effects. Thus, even if a ban on commission proves to be (partially) advantageous in some states, this does not automatically mean that it is the appropriate path for other states and their markets.[117]

6 Initial conclusions

There has been conflict in the EU for years over the most effective regulatory approach to financial and insurance distribution. The respective positions taken by those who oppose and those who support the use of commission are often irreconcilable. The European legislator has tried to defuse the conflict, most notably by way of the MiFID and IDD, and, on the one hand, contribute to adequate consumer and investor protection while at the same time respecting the fundamental freedom of the distributors of financial and insurance products to conduct a business. This has not (yet) had the desired calming effect. Member States address the issue in very different ways. The Netherlands and the UK (as a former EU Member State), for example, have opted to make their respective commission rules stricter than required by the two Directives. But, from an ordoliberal and legal perspective, is a ban on commission a valid, necessary and proportionate choice of measure for the EU? And should the Commission propose such a ban, as it plans to do probably on 3 May 2023[118]? We think not. Germany's insurance supervisory authority also does not consider a ban on commission to be a suitable approach.[119] Instead of pulling the plug on established business models, the EU should follow a different course. First, measures should be taken to strengthen the financial education of consumers in order to improve their understanding of the individual features, financial consequences and the advantages and disadvantages of the different distribution channels, and enable them on that basis to make an informed decision. The legislator should then examine whether to bring in disclosure

112 See Article 12 of the Basic Law of the Federal Republic of Germany and Articles 15 and 16 of the Charter of Fundamental Rights of the EU.

113 See for example BVerfG v. 29.06.2016 - 1 BvR 1015/15, BeckRS 2016, 48701.

114 Hans-Peter Schwintowski and Stephan Michaelis (2021), Das Provisionsverbot: Verfassungs- und europarechtliche Grenzen – anreizkompatible Alternativen, abrufbar here.

115 See for example BVerfG v. 30.07.2008 - 1 BvR 3262/07.

116 In some EU Member States - e.g. the Czech Republic and Greece - the financial assets of private households consist primarily of cash and deposits. In Germany, the Netherlands and Ireland, on the other hand, private households invest higher than average in insurance and pension products. And in yet other EU Member States, there is a mix of investments in shares, pensions and insurance products as well as investment funds [EU Commission (2022a), p. 9 and 10.

117 Rijn van der Linden (2019).

118 EU Commission (2023), Liste des points prévus pour figurer à l'ordre du jour des prochaines réunions de la Commission, SEC(2023) 2447 final, As at: 22 February 2023, available here.

119 Süddeutsche Zeitung (2023), "Wir wollen Exzesse verhindern", Article dated 27 February 2023.

requirements for the relevant players responsible for distributing financial and insurance products. All these steps must ensure that a level playing field is maintained on which no remuneration system is unjustifiably favoured or penalised right from the start. The strengths and weaknesses of all distribution models must be presented as objectively as possible.

It is therefore apparent that: The desired (efficient) market outcome - easy access to good advice and low-cost financial and insurance products - is subject to certain preconditions. Firstly, competition between advice models and distribution methods is essential. Secondly, there should be no unnecessary barriers to entry. And thirdly, institutional information efficiency should be in place so that consumers can make an informed decision. **Fee-based advisory models only work in competition with commission-based models (and vice versa) because the banning of one model leads to the inefficiency of the other.**

Authors:
Philipp Eckhardt, Financial Markets and Information Technologies
eckhardt@cep.eu

Dr Anastasia Kotovskaia, LL.M., Financial Markets and Information Technologies
kotovskaia@cep.eu

Centrum für Europäische Politik FREIBURG | BERLIN
Kaiser-Joseph-Strasse 266 | D-79098 Freiburg
Schiffbauerdamm 40 Raum 4315 | D-10117 Berlin
Tel. + 49 761 38693-0

The **Centrum für Europäische Politik** FREIBURG | BERLIN, the **Centre de Politique Européenne** PARIS and the **Centro Politiche Europee** ROMA form the **Centres for European Policy Network** FREIBURG | BERLIN | PARIS | ROMA.

The Centres for European Policy Network analyses and assesses the policy of the European Union independently of individual or political interests, in alignment with the policy of integration and according to the principles of a free, market-based system.