Financial Advice in the EU

Mapping the Rules Protecting Individual Investors

BETTER FINANCE
The European Federation of Investors and Financial Services Users
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About BETTER FINANCE

BETTER FINANCE is the European federation representing individual savers, investors, and financial services users. Dedicated to promoting transparency, fairness, and accountability, it works to ensure that Europe's financial system serves the real economy and the best interests of its citizens. BETTER FINANCE is a European federation consisting of 40 member organisations across 25 countries. It represents millions of individual investors and other users of financial services and has operated with EU support since 2012. We empower citizens with independent information and education, advocate for fair access to financial markets, and call for policies that place people at the heart of financial decision-making. Through participation in EU advisory groups, research-based advocacy, educational initiatives, and campaigns, we strengthen investor protection, enhance financial literacy, and advocate for effective supervision and governance.

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Executive Summary

This paper examines the legal and regulatory framework governing financial advice in the European Union (EU) and assesses its effectiveness in protecting individual investors. With growing retail participation in financial markets and the increasing complexity of financial products, robust consumer protection mechanisms are critical to ensuring investor confidence and market integrity.

The study focuses on three key areas.

- First, it defines what constitutes financial advice in the EU context, according to MiFID II and IDD, following ESMA's five tests to qualify investment advice. Clear definitions and practical examples are essential for both regulatory consistency and effective consumer protection.
- Second, it maps the EU's regulatory landscape, including MiFID II, IDD, and related legislation, examining the investor journey – before, during, and after the investment – to understand the extent of protection offered, including suitability and appropriateness assessments.
- Third, it identifies gaps and challenges in the current framework, such as insufficiently effective, rules on inducements and conflicts of interest, the rise of digital advisory platforms, and regulatory fragmentation across Member States. It ends by contributing to a clearer definition of high-quality financial advice.

Introduction

As announced in the Communication on the Savings and Investments Union (SIU)[1], the European Commission aims to give European citizens broader access to capital markets and companies better financing options. This renewed policy agenda builds on the still incomplete Banking Union (BU) but also, crucially, succeeds and supersedes the largely unsuccessful Capital Market Union (CMU) agenda. It therefore foresees assessments and potential revisions of most of the European Union (EU) legislation governing the tools, products and infrastructure that European citizens use to save and invest their money, including rules governing financial advice. This research will examine how the notion of financial advice is structured in EU law and to what extent it effectively protects individual investors.

Increasing individual investor participation is essential for the growth of EU capital markets and for the long-term financial well-being of European citizens. In today's context of shifting geopolitical dynamics, rapid technological change, and pressing climate and security challenges, enhancing financial intermediation in the EU is more important than ever: ensuring that EU citizens' savings are channelled towards sustainably growing firms whose profits, in turn, generate further wealth for EU citizens.

Investment in capital markets remains out of reach for many. People may be wary of losing money, struggle to understand complex financial products, or simply distrust a system that still feels "casino-like."[2] As a result, Europeans often let their savings sit in low-yield accounts, letting others bear the risk but also reap the benefits of investing and, crucially, decide on the future of the European economy. **This is a missed opportunity**. It prevents retail investors from achieving meaningful returns on their savings, leaving them exposed to inflation, and limits the growth of companies that need diverse, long-term funding.

At the heart of these challenges lies a critical gap: the missed potential of professional advice. [3]Even those who consider themselves financially literate often require guidance to navigate increasingly complex products. As highlighted by Commissioner Albuquerque, consumers should clearly benefit from investing in capital markets, but today, many are offered products that fail to deliver real value, which undermines trust and discourages retail investors from participating.

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[1] European Commission, *Savings and Investments Union,* available at: https://finance.ec.europa.eu/regulation-and-supervision/savings-and-investments-union_en

[2] Commissioner Maria Luís Albuquerque, Keynote speech at the International Conference "Towards a Savings and Investment Union", organised by Better Finance, 28.03.2025

[3] Better Finance's previous research and public consultation on the Retail Investment Strategy highlighted that improving financial literacy not only benefits retail investors broadly but also enables them to better understand and act on financial advice.

The value of financial advice lies in its ability to bridge knowledge gaps and reduce complexity for clients[4][5]. Good advisers act as intermediaries who translate complex financial information into actionable guidance, especially when data shows that financial knowledge in the EU is, on average, low [6]. Recent studies during the COVID-19 pandemic find that clients in long-term advice relationships were better prepared financially to deal with the financial consequences of the pandemic [7]. According to the theory of financial intermediation, intermediaries create value when clients face uncertainty and complexity. In theory, advisers simplify financial products, explain their implications, and transfer knowledge to clients. This concerns not only products that regulators label as complex under MIFID II, such as derivatives, structured deposits, as well as mortgages, pensions, or insurance-products, but also those that clients themselves experience as critical. Moreover, research shows that financial advisers play an important role in the growth of SMEs[8]. For these companies, a good insurance choice can determine business survival.

Put simply, the benefit of appropriate financial advice is clear: it can help consumers manage their portfolios more effectively, reduce the impact of behavioural biases (risk aversion, short-termism, home bias…) and improve their long-term financial well-being[9] of the real economy[10].

Yet, the way individual investors perceive and use financial markets ultimately depends on the quality and trustworthiness of that financial advice they receive. Seeking financial advice unfortunately offers no certainty of actually receiving sound advice[11]. After the 2008 financial crisis, and an array of scandals in

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[4] Montmarquette, C and A. Prud'homme (2020) *More on the value of financial advisors* (Montreal, 2020); Montmarquette, C and N. Viennot-Briot, *The gamma factor and the value of financial advice*, (Montreal, 2016); Beach, B. *What it's worth, revisiting the value of financial advice, a research report from ILC-UK*, (London, 2019); Winchester DD, Huston SJ, *All financial advice for the middle class is not equal*, Journal of Consumer Policy, volume 38 (2015) pp. 247–264.
[5] F. de Jong and K. Wagensveld, '*Sustainable Financial Advice for SMEs'*, Circular Economy and Sustainability, vol. 4 (2024), pp. 777–789, available at: https://doi.org/10.1007/s43615-023-00309-7
[6] M. Demertzis, J. Mejino-Lopez, A. Lusardi and L. Léry-Moffat, '*The State of Financial Knowledge in the European Union*', *Policy Brief* 04/2024, Bruegel, 2024
[7] E. Loy, K.L. MacDonald, M. Brimble and K.L. Wildman*, The Value of Professional Financial Advice for Consumers in a Crisis: Experiences of Financial Advisers during the COVID-19 Pandemic*, Working Paper, Griffith Business School, Griffith University, Brisbane (2021).
[8] de Jong and Wagensveld, '*Sustainable Financial Advice for SMEs'*

[10] Financial Conduct Authority (FCA), *Bridging the Advice Gap: Estimating the Relationship between Financial Advice and Wealth* (London, 2025)
[11] B. de Bruin, O.O. Cherednychenko, N. Hermes, M. Kramer and M. Meyer, *Demand for Financial Advice: Evidence from a Randomized Choice Experiment*, University of Groningen Faculty of Law Research Paper No. 7/2024 (12 March 2024), available at: http://dx.doi.org/10.2139/ssrn.4756355

the past three decades[12], the mistrust in these services caught a precedent, with detrimental effects on consumers.

The qualification requirements to become an investment adviser differ across the EU. The EU framework allows Member States a margin of discretion to decide what qualification a professional must have to be certified as a qualified financial adviser. The absence of harmonised high standards among advisors has often been linked to cases where consumers receive unsuitable advice and fall victim to mis-selling[13]. Raising qualifications requirements would trigger a collective effort of the profession to enhance the knowledge and competence of advisors, potentially improving the quality of advice and reinforce public confidence in seeking advice.

Additionally,[14] can affect their objectivity, creating incentives that may create conflicts of interest and steer their advice away from what is truly in the best interest of the client. [15][16] This highlights the need of regulating inducements through a comprehensive legal framework designed to ensure transparency, address conflicts of interest and prevent inducement schemes that are lucrative for advisers precisely because they are invisible to clients. [17]

While individual investors in the EU still rely primarily on human advice delivered by banks and insurance intermediaries, the rapid growth of alternative distribution channels – such as neo brokers and other fin tech firms – signals growing scepticism, particularly among younger investors, about the value of financial advice[18]. At the same time, execution-only services and online advisory models are not without risks, especially as regards the suitability of investment decisions and the way information is presented and understood. While this development has contributed to a broader democratization of access to financial markets, it has also contributed to product proliferation, frequently accompanied by promises that exceed actual investor outcomes. There is therefore an urgent

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[12] Including, but not only, UK Competition and Markets Authority, Payment Protection Insurance (PPI) Market Investigation, available at: https://www.gov.uk/cma-cases/payment-protection-insurance-ppi-market-investigation-cc ; Interest Rate Hedging Products Mis-Selling to SMEs (UK / Ireland), [2025] EWHC 525 (Admin), available at: https://www.bailii.org/ew/cases/EWHC/Admin/2025/525.html), US Securities and Exchange Commission (SEC), Robo-Advisor Advertising, Press Release 2018-300, available at: https://www.sec.gov/newsroom/press-releases/2018-300

[13]

[14] BETTER FINANCE, *BETTER FINANCE's Key Positions on the Retail Investment Strategy proposals*, October 2023.

[15] Mullainathan, S., Noeth, M., Schoar, A.: *The Market for Financial Advice: An Audit Study*, National Bureau of Economic Research, Working Paper No 17929, 2012.

[17] Restelli F, *Shaped by the Rules: How Inducement Regulation Will Change the Investment Service Industry*, Common Market Law Review, 2021.

[18] European Commission, *Report on the Current Framework for Qualification of Financial Advisors in the EU and Assessment of Possible Ways Forward*, Commission Staff Working Document, SWD (2022) 184 final, Brussels, 30 June 2022.

need to improve the quality of both traditional and "new" forms of financial advice, in order to ensure that retail investors receive clear, suitable and reliable guidance regardless of the channel through which advice is delivered.

This research examines how financial advice is legally defined and regulated, and to what extent existing frameworks protect retail investors from misinformation and conflicts of interest. The first section reviews the definition of financial advice under European law, distinguishing it from other forms of financial information. The second section analyses the legal safeguards in place to protect investors, with a particular focus on retail investors. The third section offers a critical reflection on the remaining challenges and gaps in investor protection in light of evolving market dynamics, paving the way for a definition of high-quality financial advice and further debate. A final section concludes.

This project is intended as part of a broader effort, in which the EU system will be compared with other legal frameworks, offering a reflective perspective on how alternative approaches address similar challenges and what lessons can be drawn for improving investor protection in Europe.

Defining Financial Advice in the EU

As explained, financial advisors add value in two main ways: by lowering transaction costs and by reducing information gaps[19]. However, financial advice is not the starting point. It only enters the picture as a potential solution to the underlying problem: a lack of financial knowledge. This is why intermediaries play such a central role in financial markets.

In Europe, intermediaries are at the heart of financial markets. Beyond distributing financial products, they give many individuals guidance through choices, give investment recommendations, and often help with managing personal finances more broadly. For most individual investors, these intermediated channels are the main door to access the wide range of financial products available.

In this part, we will dive on the question of ***what*** financial advice is and ***how** it can be delivered*, and in what manner the law safeguards individual investors. In the following section, we will explain ***who can** give advice*.

Investment advice, in that regard, can be delivered in different ways[20]:

1. **Human advisor**, provided in person (face-to-face), over the phone or via video calls (e.g. Zoom or Skype);

[19] Demertzis, Mejino-Lopez, Lusardi and Léry-Moffat, '*The State of Financial Knowledge*', 2024.
[20] European Commission, *Report on Financial Advisors' Qualifications*, SWD (2022) 184 final.

- **Automated advice**, given through a website or application, using algorithms to make recommendations for individual products or portfolio management (e.g. robo advisors);

2. **Hybrid advice**, models which use a combination of 1. and 2., with some steps handled by algorithms and access to a human adviser when needed or agreed.

Naturally, the scope and type of financial advice, as well as advisers' qualifications and services differ across Member States and are highly influenced by national education systems and professional requirements.

According to the European financial services legislation relating to investment products, advisers can be categorised into:

- **Investment firms providing advice** (subject to Directive (EU) 2014/65 of 15 May 2014 on markets in financial instruments, "MiFID II[21]);
- **Firms providing advice under national rules** (exemption for national advice regimes under Article 3 of MiFID II[22]);
- **Insurance distributors** providing advice on insurance-based investment products (subject to Directive (EU) 2016/97 of 20 January 2016 on insurance distribution, "IDD"[23]).

Within the EU regulatory framework, two definitions of financial advice can be identified: one under MiFID and the other under IDD.

According to IDD, advice is defined as "*the provision of a personal recommendation to a customer, either upon request or at the initiative of the insurance distributors, in respect of one or more insurance contracts*[24]. In contrast, under MIFID II, investment advice means *"the provision of personal recommendations to a client, either upon its request or at the initiative of the investment firm, in respect of one or more transactions relating to financial instruments*[25].

According to Article 9 of MIFID II [26], in order to qualify as investment advice, a *recommendation* must be:

[21] Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (recast), *OJ L 173, 12.6.2014.*
[22] Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (recast), *OJ L 173, 12.6.2014.*
[23] Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution (recast)Text with EEA relevance *OJ L 26, 2.2.2016.*
[24] Article 2(1)(15) of IDD
[25] Article 4 (4) of MIFID II
[26] Commission Delegated Regulation (EU) 2017/565 of 25 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards

a) made to a person in his capacity as an investor or potential investor, or in his capacity as an agent for an investor or potential investor
b) presented as suitable for that person, or shall be based on a consideration of the circumstances of that person
and
c) be personal (i.e., nor issued to the general public)

IDD sets out a specific conduct of business framework for the distribution of insurance-based investment products, drawing inspiration on MIFID II. Both regimes pursue similar policy goals, in particular the prevention of mis-selling and the strengthening of consumer protection. This common objective explains the **close alignment** between the two frameworks in key areas such as disclosure requirements, suitability and appropriateness assessments, and the conditions under which advice or execution-only sales may be provided.

Nevertheless, the alignment is not complete. IDD does not distinguish between independent and non-independent advice and takes a less restrictive approach to inducements. In addition, the two regimes adopt different approaches to professional competence. MiFID II relies on a general obligation for firms to ensure that staff are sufficiently qualified, leaving implementation largely to Member States, whereas the IDD sets out minimum EU-level requirements for ongoing training and professional development. These differences show that, while the IDD borrows extensively from MiFID II, it also makes distinct regulatory choices to address the specific characteristics of insurance markets.

ESMA has introduced practical tools and convergence measures, including supervisory briefings[27], to support consistent supervisory approaches. Similar tools were[28]by EIOPA in the context of IDD, following up on the IDD Delegated Regulation[29] on the requirements related to insurance-based investment products[30].

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organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive.
[27] ESMA, *Supervisory Briefing on Understanding the Definition of Advice under MiFID II*, 11 July 2023.
[28] EIOPA, *Guidelines under the Insurance Distribution Directive on insurance-based investment products that incorporate a structure which makes it difficult for the customer to understand the risk involved*, EIOPA-BoS-18/xxx, adopted pursuant to Directive (EU) 2016/97 (IDD).

[30] Commission Delegated Regulation (EU) 2017/2359 of 21 September 2017 supplementing Directive (EU) 2016/97 of the European Parliament and of the Council with regard to information requirements and conduct of business rules applicable to the distribution of insurance-based investment products.

The following scheme illustrates five tests used to assess whether a firm's services amount to financial advice. According to MiFID II, **a service is classified as investment advice only if all five tests are met**.

For clarity, we will follow the sequence of ESMA's tests as numbered in Figure 1. For clarity, we will follow the sequence of ESMA's tests as numbered in Figure 1.

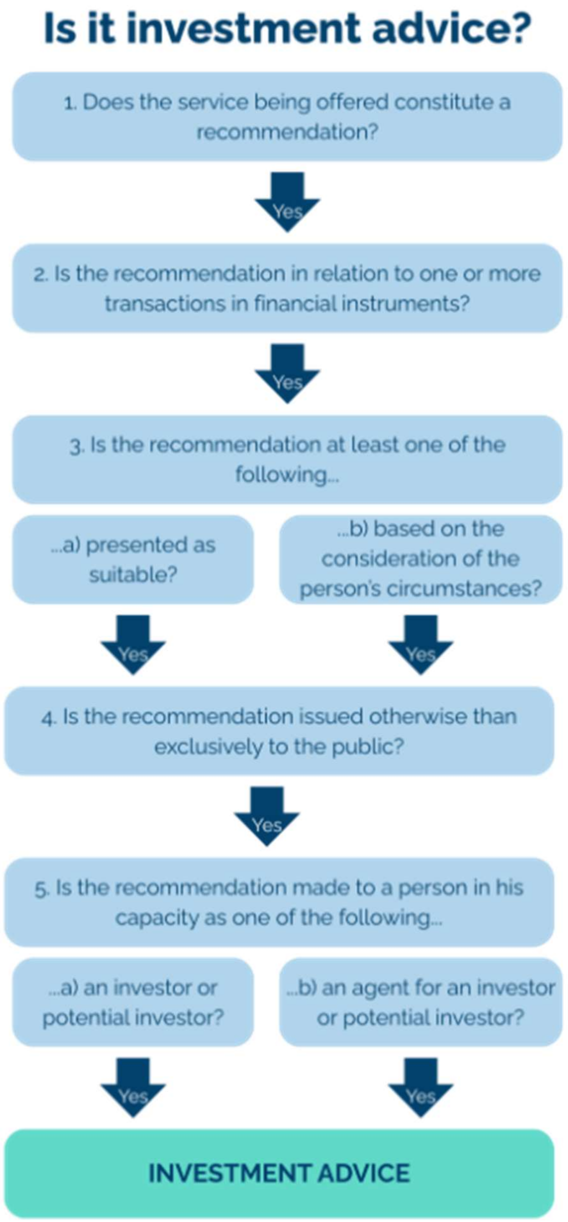

Figure 1 - ESMA, Supervisory Briefing on Understanding the Definition of Advice under MiFID II, 11 July 2023

Question 1. The Directive specifies that a service qualifies as investment advice only if it constitutes a personal recommendation, drawing a clear distinction between **giving advice and merely providing information**.

A recommendation requires an explicit or implicit suggestion from the adviser and generally involves proposing a course of action in the client's interest. By contrast, information is factual and objective and, on its own, does not constitute a recommendation. However, information can become a recommendation depending on how it is presented or the context in which it is given. Implicit recommendations may arise if information is framed subjectively, emphasises one product over others, or references products chosen by similar clients.

Context is crucial: the same information may or may not be a recommendation depending on circumstances. General share prices, company news, product terms, broad comparisons, league tables, alerts, and directors' dealings are examples of information that typically *does not* qualify as a recommendation. But these can become recommendations if linked to prior advice or used to guide client decisions.

A service is unlikely to be considered a personal recommendation if it only helps the client choose products based on features they value. For example, price comparison websites that let clients filter products without guiding their choices generally do not provide investment advice.

Question 2. Under MiFID II, a recommendation can be related to transactions in specific financial instruments, when it touches upon buying, selling, subscribing, redeeming, holding, or exercising rights attached to the instrument. Any advice concerning one or more financial instruments, even if no transaction occurs, may constitute investment advice, including recommendations covering several alternatives. Personal recommendations require consideration of the client's circumstances, whereas generic advice addresses types of instruments or asset classes without tailoring to an individual. General recommendations are typically not investment advice.

Advice does not occur simply by suggesting a client become a customer of a firm; it must relate to specific instruments. Similarly, advice on asset classes alone is considered generic, but pointing to particular instruments within those classes qualifies as investment advice. Finally, portfolio management advice, such as recommending the terms of a mandate, may fall under MiFID II requirements for assessing suitability, even if it is not strictly a personal recommendation.

Question 3 a). A financial instrument can be presented as suitable either explicitly or implicitly, and both forms may constitute investment advice if other tests are met. Implicit recommendations occur when a firm highlights a product over others in a way that influences the client's choice, even without stating it is suitable. A product can be presented as suitable even if it is not actually appropriate for the client; the firm must still collect sufficient information about the client's knowledge, experience, financial situation, risk tolerance, and investment objectives to comply with suitability rules. Disclaimers alone cannot prevent a communication from being considered investment advice. Even if a firm states that no advice is given, if the service meets the criteria for a recommendation, it will still qualify as investment advice. Firms must also ensure internal systems, controls, and staff training reflect the nature of the service they provide to avoid inadvertently presenting products as suitable.

Question 3 b). What is under-evaluated here is a person's "circumstances": factual information (e.g., income, address, marital status) and subjective information (e.g., risk appetite, investment objectives, sustainability preferences, or protection needs). A firm is considered to base a recommendation on a person's circumstances if it collects relevant information and reasonably uses it to guide a recommendation. This is often the case when there is an ongoing relationship and a consistent contact point, so the firm is expected to consider previously provided information.

A firm cannot avoid being seen as providing a personal recommendation simply by failing to use relevant client information if it is reasonable that the information should have been considered. Similarly, disclaimers stating that client information will not be used do not prevent a service from qualifying as investment advice if the client could reasonably expect the recommendation to be based on their circumstances.

Question 4. A recommendation is not considered a personal recommendation if it is issued exclusively to the public, such as via newspapers, magazines, TV, radio, or public posters. However, recommendations delivered through digital channels like websites, apps, social media, or private messages can be personal recommendations if they are directed at specific individuals or groups, or presented as suitable for them. Publishing general "best products" lists or aggregated recommendations for the public does not normally constitute investment advice, but if targeted to particular clients, it could. Similarly, messages sent to multiple clients may be personal recommendations depending on the target audience, message content, and language used – particularly if the message implies suitability for specific clients. Financial training or courses can also constitute advice if the firm collects client information and uses it to provide or suggest suitable recommendations. Investment research intended for the public is not personal advice, but discussing research directly with clients in a way that guides them toward specific products can constitute investment advice. Finally, responding to a professional client's precise product request is not advice unless the firm expresses an opinion on the product's suitability for the client.

Question 5. A) A personal recommendation under MiFID II is given to someone acting as an investor or as their agent. Payment or intention does not change this. Corporate finance advice is different: it focuses on strategy, capital structure, or mergers, not financial return, and does not require MiFID authorisation. Investment advice is provided when the primary purpose is financial – earning returns or managing risk. If both financial and strategic goals exist, advice may overlap. Firms must assess the client's objectives, clearly define services, and ensure staff and processes match the type of advice offered.

Question 5b) A recommendation to a person acting as an agent for an investor applies when the agent makes decisions on behalf of someone else, such as under a power of attorney. Typically, the agency relationship is clear, but in some cases – like a portfolio manager commissioning advice – the firm must ensure it knows the circumstances of the ultimate client. Suitability and consideration of circumstances apply to the client represented by the agent, not the agent personally.

Having explored the nuances and grey areas of what constitutes financial advice, we can now appreciate the careful scrutiny embedded in the EU framework. When a recommendation is made to a client – whether at their request or proactively by the investment firm – regarding one or more transactions in financial instruments, it crosses the threshold into advice. This distinction is critical and the legislator's intent is clear: to shield investors from guidance that is unfiltered, biased, or lacking objectivity, ensuring that any advice given genuinely serves the client's best interest.

A key point is that anyone, whether based inside or outside the EU, who disseminates information recommending investments in EU financial instruments (such as stocks or bonds) may fall under Market Abuse rules[31]. These rules require full identification of the person making the recommendation, presentation of advice in an objective manner, and disclosure of any relationships or circumstances that could compromise impartiality. This highlights the importance of a clear definition of financial advice, both for regulatory purposes and for consumer protection. Such provisions are essential not only to help clients make informed decisions but also to guide advisers in understanding legal obligations and mitigating the risk of misconduct. From here, the discussion naturally turns to the question of *who is authorised* to *give* financial advice.

Regulatory Framework & Consumer Protection Mechanisms

The question of ***who*** can give financial advice is linked to the qualifications needed to do so, which are governed mainly by MiFID II, and, where applicable, IDD. The European Commission made clear its intention to increase the professional qualification threshold: Action 8 of the Capital Markets Union Plan (adopted 24 September 2020[32]) envisaged improving professional qualifications for financial advisers across the EU and assessing the feasibility of a pan-EU label for such advisers[33].

Since then, important legal developments have followed. In March 2024, the EU adopted amendments to MiFID II and MiFIR in the "MiFID /MiFIR Review" package

[31] Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse (market abuse regulation) and repealing Directive 2003/6/EC of the European Parliament and of the Council and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC.
[32] Communication from the Commission, *A Capital Markets Union for people and businesses – New Action Plan*, COM(2020) 590 final, 24 September 2020, available at https://eur-lex.europa.eu/resource.html?uri=cellar:61042990-fe46-11ea-b44f-01aa75ed71a1.0001.02/DOC_1&format=PDF
[33] European Commission, *Report on the current framework for qualification of financial advisors*, SWD (2022) 184 final.

– Directive 2024/790[34] and Regulation 2024/791[35] – which entered into force on 28 March 2024. While many of these focus on transparency, market data, consolidated tapes, the ban on payments for order flow, and trading obligations, they form part of the broader regulatory context in which advice is given. Many of those amendments must be transposed by Member States by 29 September 2025, so the actual requirements in each country are still in transition.

Taken together, these political commitments and ongoing reviews set the stage for a higher, harmonised standard of professional qualification for financial advice in the EU. As of mid-2025, full harmonisation has not yet been achieved, and many details (which levels of education, training, certification, supervision, etc.) remain to the Member State's discretion.

Member State approaches differ notably in the following areas:

a) <u>QUALIFICATION REQUIREMENTS ESTABLISHED BY NATIONAL COMPETENT AUTHORITIES (NCAS)</u>

Under Article 25(1) of MiFID II[36], investment firms must be able to demonstrate to competent authorities that staff providing investment advice or information have the *necessary knowledge and competence*. Under Article 25(9) of MIFID II, ESMA is tasked with defining what counts as sufficient knowledge and competence for advisers working in investment services, but ultimately **Member States retain discretion to set and publish the specific assessment criteria**.

ESMA issued Guidelines on Knowledge and Assessment[37] in 2017, emphasising that competence should be based on **'appropriate qualification'** and **'appropriate experience'**, to fulfil the obligation under Articles 24 and 25 of MIFID II.

> 'Appropriate qualification' means a qualification or other test or training course that meets the criteria set out in the guidelines[38].
>
> 'Appropriate experience' means that a member of staff has successfully demonstrated the ability to perform the relevant services through previous work. This work must have been performed, on a full-time equivalent basis, for a minimum period of 6 months[39].

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[34] Directive (EU) 2024/790 of the European Parliament and of the Council of 13 March 2024 amending Directive 2014/65/EU on markets in financial instruments. *OJ L, 2024*.
[35] Regulation (EU) 2024/791 of the European Parliament and of the Council of 13 March 2024 amending Regulation (EU) No 600/2014 on markets in financial instruments. *OJ L, 2024*.
[36] Article 25(1) of MiFID II: "*Member States shall require investment firms to ensure and demonstrate to competent authorities on request that natural persons giving investment advice or information about financial instruments, investment services or ancillary services to clients on behalf of the investment firm possess the necessary knowledge and competence to fulfil their obligations under Article 24 and this Article. Member States shall publish the criteria to be used for assessing such knowledge and competence*"
[37] ESMA, *Guidelines for the assessment of knowledge and competence*, 3 January 2017, ESMA71-1154262120-153 EN (rev).
[38] ESMA, *Guidelines on knowledge and competence*, 2017
[39] ESMA, *Guidelines on knowledge and competence*, 2017

However, since qualification systems are not harmonised across the EU, each national authority must say which qualifications count or at least describe the features a valid qualification should have. Most countries have published such lists or descriptions, though a few rely only on ESMA's broad principles. Whichever they choose, NCAs should also publish:

1. The period of professional experience required (at least six months full-time, subject to national choice)
2. The maximum time unqualified staff may work under supervision, and
3. Whether periodic reviews of staff qualifications are carried out internally by firms or externally by another body.

The result is a patchwork: in some countries, firms can decide internally whether staff are qualified, while in others, advisers must pass an exam or earn a recognised diploma. Across the EU, the qualifications range from university or professional degrees to specialised certification schemes, with different emphases on skills, training requirements and testing.

On the other hand, knowledge and competence requirements in the **IDD** scope are set directly in the Directive ITSELF (Level 1 of Lamfalussy), being IDD a minimum harmonization directive. Therefore, Member States have issued transposition rules including those requirements, but retain discretion to go beyond these minimum standards.

According to the EIOPA Report on the application of the IDD[40], and the EFPA Policy Proposal[41], most of Member States have included criteria on knowledge and competence in their insurance laws (e.g., Czech Republic, France, Germany, Luxembourg). Some of them have merely included IDD general criteria and Annex I of IDD in their own legislation (e.g., Austria, Poland). Other Member States (e.g., Ireland, Spain) issued a list of qualifications, apart from including the relevant criteria in their legislation.

b) FORMAL EDUCATION REQUIRED

While the **ESMA Guidelines** do not explicitly require a minimum formal education, the **European Commission** reports that almost all National Competent Authorities (NCAs) in practice impose at least a basic entry requirement, typically secondary education. Several Member States explicitly include this prerequisite as a condition for meeting further qualification requirements, including the Czech Republic, Hungary, Ireland, and Italy. For example, in the Czech Republic, candidates must demonstrate minimum general knowledge through a secondary or higher education diploma, a requirement that also applies under the IDD.

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[40] EIOPA, *Report on the application of the Insurance Distribution Directive (IDD)*, Annexes I-VIII, EIOPA-BoS-21/582, 6 January 2022.
[41] Zunzunegui F et al.., *Improving Qualifications for Financial Advisors in the EU: Policy Proposals*, 2023.

Under the IDD, almost all Member States require individuals providing advice on insurance-based investment products to hold specific qualifications and/or relevant experience. In most cases, this includes at least advanced secondary education (e.g. Czech Republic, Italy, Portugal, Poland, Slovakia), while some Member States require higher education depending on the role (e.g. France, Hungary, Luxembourg). In a limited number of cases, no additional requirements apply beyond general insurance distribution rules (e.g. Bulgaria)[42].

c) PROFESSIONAL EXPERIENCE

Nevertheless, there is greater consistency on the **professional experience needed**: most countries follow ESMA's six-month full-time practice as a minimum, though some require longer where the advice concerns complex products[43]. The rules differ more, however, on how long unqualified staff can work under supervision[44], leaving another layer of divergence across Member States. In this line, with regard to training experience, Member States apply different minimum hour requirements for providing advice and for giving information. For example, Spain and Portugal require significantly more training hours for advice than for information, while Luxembourg sets a minimum of 60 hours of external training without distinguishing between the two activities.

IDD does not include any provision regarding a period required to gain appropriate experience and a maximum period to work under supervision. For this reason, most IDD transposition rules do not include provisions of this kind; apart from Ireland, where the same knowledge and competence regulation is applicable both to MiFID II and IDD scope[45].

d) CONTINUOUS TRAINING

Disparities are also visible in **continuing professional development (CPD) requirements**. ESMA stipulates that firms need to review staff competence annually, monitor regulatory changes, and ensure advisers maintain and update their knowledge through ongoing training or professional development, including specific preparation before introducing new investment products. National practices diverge hugely in this regard, with in some countries firms must test staff

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[42] Zunzunegui F et al.., *Improving Qualifications for Financial Advisors in the EU: Policy Proposals*, 2023.
[43] ESMA, *Guidelines on knowledge and competence*, 2017
[44] 'Under supervision' means providing the relevant services to clients under the responsibility of a staff member who has both an appropriate qualification and appropriate experience. According to the ESMA *Guidelines on knowledge and competence, 2017* (paragraph 20(d)), where a member of staff has not acquired the appropriate qualification and/or the appropriate experience to provide the relevant services, s/he can only provide the relevant services under supervision. The staff member can work under supervision for a maximum period of 4 years except where a shorter period is determined by the NCA (ESMA *Guidelines on knowledge and competence*, 2017, paragraph 4(j)).
[45] Zunzunegui F et al.., *Improving Qualifications for Financial Advisors in the EU: Policy Proposals*, 2023.

every year (e.g., Netherlands), in other advisers must commit to CPD training hours per year (e.g., 15 hours per year in Austria and Ireland) , and elsewhere firms simply verify that diplomas remain current (e.g., Czech Republic)[46].

With regard to continuing professional development under the **IDD**, most Member States require advisers to complete at least 15 hours of CPD per year, in line with the Directive (e.g. Austria, Czech Republic, Hungary, Luxembourg). Some Member States apply higher requirements for advice activities, such as Spain, where 25 hours per year are required for providing advice. CPD may be delivered by a wide range of bodies, including accredited professional or educational institutions, trade associations, universities, insurance undertakings, or private providers, depending on the Member State. In some cases, CPD is subject to certification (e.g. Czech Republic), while other approaches include exams or flexible provider arrangements[47].

These uneven approaches further complicate cross-border activity. While many jurisdictions accept qualifications from other Member States, some impose additional conditions, such as extra exams, before recognising them. Only a few qualifications are automatically accepted in multiple countries, leaving significant barriers not just for advisers but also for consumers.

For retail investors, this means it is harder to know whether an adviser in another Member State is held to the same standards, or whether their qualification is considered sufficient to provide advice. The lack of consistency makes it less clear for clients what level of expertise they can expect, especially when seeking advice across borders.

When the very notion of a "qualified" adviser is inconsistent across jurisdictions, how can the EU ensure that retail investors are not exposed to weaker regimes of protection?

Financial services remain a two-sided market: advisers provide, and consumers choose. But it is in the moment of advice – where the two sides meet – that the law must guarantee trust and fairness. MiFID II recognises that retail clients, with limited knowledge and experience of investment than professionals, deserve the highest standard of protection to ensure advice serves their interests.

MiFID II sets out a series of obligations that firms must uphold at all times in their operations, with several requirements designed specifically to protect the interests of retail clients. These rules cover every stage of the investment process: from the moment a client considers a product, through the provision of advice or

[46] Zunzunegui F et al.., *Improving Qualifications for Financial Advisors in the EU: Policy Proposals*, 2023.
[47] Zunzunegui F et al.., *Improving Qualifications for Financial Advisors in the EU: Policy Proposals*, 2023.

portfolio management, to the execution of orders and ongoing reporting. Their intended goal is to ensure that clients receive clear, accurate, and timely information, that investments are suitable for their objectives and risk profile, and that transactions are executed in a way that achieves the best possible outcome. By establishing these standards, MiFID II places the client's interests at the centre of the financial services market.

The first step is knowing, **before the investment,** whether the *retail* client is / could ask to be considered as a *professional investor*[48][49]. To qualify as a professional client, an investor must meet at least two of the following three criteria:

- Regularly carry out regular transactions
- Have a large portfolio
- Have worked in investment services

  Professional clients are assumed to be capable of making their own investment decisions and evaluating associated risks, which is why they have access to a broader range of products than retail clients and lesser degree of protection.

The following stage has to do with the type of service asked for. MIFID offers a different level of protection to each. There are **3 different types of service** for which a firm may be called:

1. *The client wants to buy or sell a financial product without asking for investment advice*
   In this case, there are two possibilities: if the product is considered non-complex under MiFID, the firm may provide the service on an execution-only basis without performing an assessment; if the product is considered complex, an appropriateness check is required.

   - **Appropriateness test [50]**
     This is a moderate protection mechanism to protect those investors who may not understand or may not be conscious of the level of risk of a transaction, in particular when products are "complex"[51], or when the investors haven't themselves taken the initiative to carry out the transaction.

[48] See Directive 2014/65/EU (MiFID II), Annex II, Section II, which provides that a retail client may be treated as a professional client only upon explicit request and following an assessment by the firm, and that such treatment does not preclude subsequent reclassification.
[49] FSMA, *MiFID II Directive: More protection for investors*, Brussels, 2023.
[50] Directive (EU) 2014/65/EU (MiFID II), Arts 25(4) and 25(5); Commission Delegated Regulation (EU) 2017/565, Arts 35–38.
[51] Under Article 25(4)(a) of MiFID II, non-complex financial products include instruments such as shares or bonds admitted to trading on a regulated stock exchange. Complex financial products include options, futures, swaps, other derivatives, convertible bonds, and warrants.

In this test, the firm must assess the client's investment knowledge and experience, typically using a standard questionnaire. Based on the responses, the firm determines whether the client understands the risks involved.
If the client does, the transaction may proceed. If not, or if the client failed to provide sufficient information to allow it to form an opinion, the firm will issue a warning – either highlighting that the transaction may be inappropriate or noting that it cannot form a reliable opinion. If the client insists, the transaction will be carried on, with the client assuming the associated risks.

- **Execution-only**[52]
  For certain transactions that do not involve advice, the appropriateness test is not mandatory. These are qualified as 'execution only' services. It applies only when the transaction involves a 'non-complex' product (within MIFID II) and is initiated by the client (and not as a response to a proposal by the firm).
  In such a case, no questions will be asked about knowledge and experience in investment of the client, on its financial situation and investment objectives. The firm will just execute the order.

2. *The client wants to buy or sell a financial product and get investment advice about this transaction*

Suitability test[53]

When a client requests investment advice, their reliance on the firm is greater. The firm must understand the client's individual needs and personal situation to recommend suitable products and/or transactions. MiFID II requires the firm to perform a **suitability test**, whereby the firm makes a recommendation based on information it collects about the client's:

- Investment objectives: risk profile, preferred investments, goals, and whether capital protection is required.
- Financial situation: income, assets, commitments, and ability to bear losses
- Knowledge and experience: familiarity with products, past transactions, transaction volume and frequency, and level of education.

If the firm cannot obtain sufficient information, it cannot provide recommendations. The client's responses determine both the suitability of products and the scope of service the firm may offer.

[52] Directive (EU) 2014/65/EU (MiFID II), Arts 25(4); Commission Delegated Regulation (EU) 2017/565, Arts 35–36.
[53] Directive (EU) 2014/65/EU (MiFID II), Arts 24(1) and 25(2)(3); Commission Delegated Regulation (EU) 2017/565, Arts 25–27.

3. *The client wants the firm to manage their investment portfolio (portfolio management)*

   Suitability test

   If a client entrusts a firm with portfolio management, they rely entirely on the firm's decisions. Since the firm is not required to inform the client of every transaction, it must first gather sufficient information to provide the service appropriately. As with investment advice, a **suitability test** is required, even though the output is not a recommendation for a specific product but for a mandate from the client to the firm. Without the necessary information from the client, the firm cannot provide portfolio management services.

Every investment firm must have a policy explaining who takes the appropriateness or suitability test and how it is done. When investments involve a couple or someone acting as a legal representative, the firm decides whether to test each person individually or a designated representative. The test evaluates the representative's knowledge and experience, while considering the financial situation and investment objectives of the people represented[54].

Before any investment is made, MiFID and IDD require firms to provide clients with key information: details about the firm and its services, the nature of investment advice or portfolio management, and the associated risks. All costs, fees, and commissions, [55], must be fully disclosed, showing their cumulative impact on expected returns [56]. New retail clients must receive a contract, and when advice is given, a suitability report explaining how recommendations align with the client's objectives, financial situation, and risk profile. Clients must also be informed about complaint procedures and investor compensation schemes against the firm, should they need to [57]. Importantly, this information is required to be provided in "good time" before the client is bound by any contract; however, the absence of a precise definition in EU legislation has led to divergent practices, with disclosure often occurring at the point of sale rather than sufficiently in advance to meaningfully inform client decisions.

During and after the investment, disclosure requirements are essential. MiFID established the **principle of best execution for the client**. It means that during the sale or purchase of financial products, the firm must execute the client's orders in such a way as to constantly obtain the best possible result for him. *How*? By providing information that is accurate, clear, and not misleading, prioritizing the

[54] Directive (EU) 2014/65/EU (MiFID II), Arts 25(1) & (2)(b); Commission Delegated Regulation (EU) 2017/565, Arts 25(2) & Recital 45.
[55] Directive (EU) 2014/65/EU (MiFID II), Article 24(4)(c)
[56] Directive (EU) 2014/65/EU (MiFID II), Arts 24(4) & (5), and 50; Commission Delegated Regulation (EU) 2017/565, Arts 27–29.
[57]

most important details for the client's decision-making. This includes ongoing updates on the performance of investments, any changes in risks, and the impact of costs and fees. Clients must also be informed of material events affecting their portfolio, the execution of their orders, and any inducements received by the firm. Regular reporting ensures that clients can monitor their investments and make informed decisions throughout the life of the product[58].

Firms executing orders must provide information about the steps taken to achieve **best execution**. This includes:

- How the firm determines the relative importance of best-execution factors[59].
- The execution venues that have been selected.
- The factors considered when choosing these venues.
- A warning that if the client provides specific instructions, the firm may not be able to fully apply its execution policy for those aspects[60].
- A summary of the selection process for execution platforms, the strategies used, procedures for monitoring execution quality, and how the firm verifies that the best possible results are achieved[61].

Finally, the last stage safeguarded by MiFID II happens after the transaction is executed. After a transaction, the firm must provide a clear **confirmation** detailing the product, date, execution venue, price, and total fees. For ongoing investment advice, clients receive **regular updates** showing how recommendations align with their goals, preferences, and financial profile. In portfolio management, **comprehensive reports** track portfolio value, performance, and fees, with additional alerts if the total value drops by 10%. For leveraged or contingent instruments, the firm must notify the client each time the value falls by 10%. Clients are advised to retain all documents received from the firm.

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[58] Directive (EU) 2014/65/EU (MiFID II), Arts 21, 24(4)–(5), 25(1), 50–51; Commission Delegated Regulation (EU) 2017/565, Arts 27–30, 67–70.
[59] Directive (EU) 2014/65/EU (MiFID II), Arts 27–28; Commission Delegated Regulation (EU) 2017/565, Arts 65-66.
[60] Directive (EU) 2014/65/EU (MiFID II), Article 27.
[61] Directive (EU) 2014/65/EU (MiFID II), Arts 50-51; Commission Delegated Regulation (EU) 2017/565, Arts 73-74.

Challenges in the current EU Framework

Even with MiFID II's extensive safeguards covering disclosures, suitability tests, best execution, and ongoing reporting, individual investors still face significant challenges. Many of the rules, including the ESMA Guidelines, rely on broad principles rather than concrete prescriptions, creating room for inconsistent implementation and leaving gaps in protection. On top of this, conflicts of interest, robo-advisors and digital platforms, inducements, and payment-for-order-flow arrangements introduce further complexities that the framework does not fully address.

The following section explores these areas, highlighting where investors remain exposed despite the regulatory safeguards intended to protect them.

One clear area where investor protection may be uneven concerns the so-called **"local advisers"** under Article 3 of MiFID II. Article 3 of MiFID II lets Member States exempt certain people from the full MiFID regime. These "local advisers" may give investment advice if conditions are met[62]. When using this exemption, Member

Note: The fact that an "independent" advisor does not charge the client does not mean the advice service is not paid for.

The essential distinction between "independent" and "non-independent" advice relies on who is directly paying the adviser:

- if the client pays for receiving the advice, the advice is considered "independent;"
- If it is a third-party (such as investment product manufacturers) that pays the adviser, the advice is considered "non-independent;" however, in most cases, the client still ultimately bears the cost of advice, which is bundled in the total cost figures of the investment product.

Figure 2 – BETTER FINANCE, Evidence Paper on Inducements (2022)

States must set national regimes with rules similar to MiFID II. But the knowledge and competence requirement in Article 25 **is not included.** This leaves qualification standards for local advisers entirely to national discretion.

ESMA found that more than half of Member States use this option[63]. The impact varies: in Lithuania, only three local advisers exist, while in Germany, there are almost 38,000. About a third of Member States set no specific qualification requirements for local advisers. Where requirements exist, they differ and do not always match MiFID II standards. For example, according to the data of the EC Report[64], in many cases (e.g. Hungary, Italy, Portugal), NCAs have published the

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[62] Directive (EU) 2014/65/EU (MiFID II), Article 3 (1): Local advisors require national authorization and are subject to national regulation. Key features include they cannot hold client funds or securities, and they may only provide limited services – specifically, the reception and transmission of orders of non-complex financial products.

[63] European Commission, *Report on the current framework for qualification of financial advisors*, SWD (2022) 184 final.

[64] European Commission, *Report on the current framework for qualification of financial advisors*, SWD (2022) 184 final, Annex II

criteria that qualifications must meet, while only a few (e.g. Luxembourg, Spain) have issued lists of specific recognised qualifications. Other Member States (e.g. Poland, Estonia) have limited their approach to publishing translations of the ESMA Guidelines, leaving interpretation and implementation largely to investment firms, which has contributed to uneven application in practice. By contrast, countries with pre-existing competency frameworks, such as Ireland [65], have integrated the ESMA and IDD requirements into established national regimes, relying on recognised qualifications, experience, and continuing professional development rather than issuing new lists.

Another critical area for investor protection lies in the management of **conflicts of interest**. Firms must act in the best interests of their clients and take effective measures to prevent conflicts of interest from adversely affecting them. Conflicts can arise, for example, when a firm stands to gain financially or avoid a loss at a client's expense, or when incentives encourage prioritising other clients' interests[66].

Under MiFID II, firms are required to disclose the main measures they have implemented to identify and manage such conflicts. If these measures are insufficient, the firm must clearly inform clients of the nature and source of the conflict, as well as the steps taken to mitigate its impact, before providing any investment service [67].

In investment advice, the distinction between **independent** and **non-independent** services is central. Independent advisers are paid directly by the client, without receiving any remuneration from third parties. Non-independent advisers, by contrast, may be compensated by product manufacturers or other service providers through **inducements** (commonly known as commissions,

[65] Zunzunegui F., Corbal P., Szymańska M., Braga M.D., Levaldaur P. and Carluccio E.M., *Improving Qualifications for Financial Advisors in the EU: Policy Proposals*, EFPA, 2023, available at: https://ssrn.com/abstract=4466821

[66] de Bruin et al., *Demand for Financial Advice*, 7/2024.

[67] Directive (EU) 2014/65/EU (MiFID II), Article 23: "1. *Member States shall require investment firms to take all appropriate steps to identify and to prevent or manage conflicts of interest between themselves, including their managers, employees and tied agents, or any person directly or indirectly linked to them by control and their clients or between one client and another that arise in the course of providing any investment and ancillary services, or combinations thereof, including those caused by the receipt of inducements from third parties or by the investment firm's own remuneration and other incentive structures.*
2. Where organisational or administrative arrangements made by the investment firm in accordance with Article 16(3) to prevent conflicts of interest from adversely affecting the interest of its client are not sufficient to ensure, with reasonable confidence, that risks of damage to client interests will be prevented, the investment firm shall clearly disclose to the client the general nature and/or sources of conflicts of interest and the steps taken to mitigate those risks before undertaking business on its behalf."

retrocessions, or kickbacks)[68]. We recall the definitions set out in an earlier BETTER FINANCE research project[69].

It should be noted, however, that neither MiFID nor IDD do formally define categories of "independent" or "non-independent" advisers. Instead, it regulates whether advice is given *on an independent basis* in a specific instance, allowing (at least in theory) the same firm to provide independent advice in one case and non-independent advice in another.

The system of inducement is a critical source of conflicts of interest. The very term of inducement, in itself, is opaque and misleading for most retail investors. These payments are in reality sales rewards, yet the financial jargon obscures their true nature. As former EIOPA Chair Gabriel Bernardino noted, calling them "kickbacks" would clarify it for many savers[70][71]. In practice, inducements fundamentally skew incentives: intermediaries are naturally driven to sell the products that pay them most, rather than those that best serve clients' needs. It not only prevents retail investors from accessing truly unbiased advice, but also undermines the goal of the SIU, which depends on strengthening trust and encouraging households to channel more of their savings into capital markets.

Moreover, MiFID II itself adds to the confusion by blurring the line between "advice" and "sales." In reality, inducements never remunerate advice: they remunerate the sale of products. Distributors are paid by providers regardless of whether a transaction was done "execution-only" or upon receiving advice; and, while the "inducements" are supposed to compensate advisers for the cost of providing advice, the amount and frequency of payments are usually disconnected from the actual quantity of advice provided to the client. In most cases, a distributor will continue to receive trailing commissions for as long as the product is held, even if they have met the client only once and never provided any further advice. The notion of "investment advice" in EU rules is therefore misleading, as most inducements are sales commissions in disguise. From BETTER FINANCE's perspective, this legal ambiguity perpetuates conflicts of interest and prevents savers from clearly understanding what they are paying for. That is why inducements should ultimately be banned across the board – not only for MiFID-covered products, but also for insurance-based investments, pensions, and execution-only transactions. The emergence of "clean share classes"[72] shows that a

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[68] BETTER FINANCE, *Evidence Paper on the Detrimental Effects of Inducements*, 3 February 2022, available at: https://betterfinance.eu/wp-content/uploads/BETTER-FINANCE-Evidence-Paper-on-Detrimental-Effects-of-Inducements-03022022.pdf
[69] BETTER FINANCE, *Evidence Paper on Inducements* (2022).
[70] BETTER FINANCE, *Evidence Paper on Inducements* (2022).
[71] BETTER FINANCE, *Evidence Paper on Inducements* (2022).
[72] Clean share classes are mutual fund units that exclude embedded distribution fees or commissions paid to financial intermediaries, thereby separating product costs from advisory remuneration. They were introduced following regulatory reforms aimed at reducing conflicts of interest, notably the Retail Distribution Review (RDR) in the United Kingdom.

market without inducements is possible, and clear labelling of non-independent advisers would finally give retail investors the transparency they deserve.

Conflicts are also embedded in execution practices. Payment for order flow ("PFOFs") occurs when brokers are paid by execution venues to direct client orders their way, a model often tied to "zero-fee" trading platforms[73]. This practice has been criticised for obscuring costs and clashing with the principle of best execution, which obliges firms to secure the best possible outcome for their clients. Reflecting this concern, the revised Regulation on Markets in financial instruments ('MiFIR')[74] introduced a new Article 39a[75], which prohibits firms acting on behalf of retail clients or "opt-in" professional clients from receiving payments, fees, or non-monetary benefits tied to routing orders to a particular execution venue. The rule clarifies that execution choices should be based solely on best execution, not on financial incentives.

The scope of the ban of PFOFs is broad: it applies to investment firms when executing or forwarding client orders and covers both retail and opt-in professional clients. Exemptions exist, such as rebates or fee discounts from trading venues that exclusively benefit the client. A grandfathering clause allows Member States to delay full implementation until 30 June 2026, provided firms were already engaged in PFOF before March 2024. Germany has opted for this transitional period, while countries such as France, Spain, Italy, and the Netherlands are applying the ban immediately[76]. The fragmented uptake of the exemption raises concerns about a potential uneven playing field in cross-border brokerage services.

Finally, the broader debate on remuneration models remains unresolved when it comes to **commission-based system,** where firms are paid indirectly by product providers, versus a **fee-based system**, which relies on direct payments by clients, typically upfront. Both systems are prevalent in various markets and have prompted a range of research.

Over the past decade, research has consistently shown that advisers often act in ways that increase costs for clients [77] and tend to recommend portfolio designs

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[73] BETTER FINANCE, *Evidence Paper on Inducements* (2022).
[74] Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012
[75] The new article reads: "*Investment firms acting on behalf of retail clients, as defined in Article 4(1), point (11), of Directive 2014/65/EU, or professional clients as referred to in Section II of Annex II to that Directive shall not receive any fee, commission or non-monetary benefit from any third party for executing orders from those clients on a particular execution venue or for forwarding orders of those clients to any third party for their execution on a particular execution venue ('payment for order flow'*)."
[76] Hogan Lovells, Communication: EU: MiFIR Amendments prohibiting Payment for Order Flow (PFOF) entered into force on 28 March 2024, 17 April 2024, available at: https://www.hoganlovells.com/en/publications/eu-mifir-amendments-prohibiting-payment-for-order-flow-pfof-entered-into-force-on-28-march-2024 .
[77] A. Hackethal, M. Haliassos, T. Jappelli, *Financial advisors: a case of babysitters?* Journal of Banking and Finance, vol. 36 no.2) (2012), pp. 509-524, 10.1016/j.jbankfin.2011.08.008.

that are in the sole financial interest of the adviser [78]. Studies from 2017 onwards found that advisers frequently recommend products that are not optimal for clients to maximise their own income [79] and tend to push investments that generate the highest commissions [80]. Evidence also indicates that advisers favour bonds or transactions that bring the most profit to their firms, even when these options underperform[81][82], and rarely tailor their recommendations to individual clients, instead relying on a generic, one-size-fits-all approach [83].

Academic literature suggests that commission-based models improve access but compromise independence, while fee-based models reduce conflicts but risk excluding smaller investors. Some studies have been put forth on the effects of switching from a commission-based remuneration system to a fee-based compensation, ultimately showing that greater transparency leads costumers [84] twice about whether they really want to pay for financial advice [85].

BETTER FINANCE has consistently expressed its position on both remuneration models in the past, and our stance remains firm: professionals providing independent advice, execution-only services (particularly reception and transmission of orders) and portfolio management, regardless of the type of EU retail investment product concerned, should not be allowed to receive and retain commissions[86] [87].

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[78] S. Mullainathan, M. Noeth, A. Schoar, *The Market For Financial Advice: An Audit Study* (No. w17929) National Bureau of Economic Research (2012) https://www.nber.org/papers/w17929

[79] S. Anagol, S. Cole, S. Sarkar, *Understanding the advice of commissions-motivated agents: evidence from the Indian life insurance market*, Review of Economics and Statistics, vol. 99, no. 1 (2017) pp. 1-15, 10.1162/REST_a_00625

[80] J. Chalmers, J. Reuter, *Is conflicted investment advice better than no advice*? Journal of Financial Economics, vol. 138, no. 2 (2020), pp. 366-387, https://doi.org/10.1016/j.jfineco.2020.05.005

[81] M. Egan, *Brokers versus retail investors: conflicting interests and dominated products,* Journal of Finance, vol. 74, no. 3 (2019), pp. 1217-1260, https://doi.org/10.1111/jofi.12763

[82] D. Hoechle, S. Ruenzi, N. Schaub, M. Schmid, *Financial advice and bank profits*, *Review of Financial Studies*, vol. 31, no. 11 (2018), pp. 4447-4492, https://doi.org/10.1093/rfs/hhy046

[83] S. Foerster, J.T. Linnainmaa, B.T. Melzer, A. Previtero, Retail financial advice: does one size fit all?, *Journal of Finance*, vol. 72, no. 4 (2017), pp. 1441-1482, https://doi.org/10.1111/jofi.12514

[84] Lars Frölich, Dr Jörg Schneider, *'Inducements - Ban with an exception: tighter rules for commissions and other benefits'* (24 September 2018) BaFin – Consumer protection topics, available at: https://www.bafin.de/SharedDocs/Veroeffentlichungen/EN/Fachartikel/2018/fa_bj_1808_Zuwendungen_en.html;jsessionid=49A3A525C96A362CF6EF14035E65EAE5.1_cid501?nn=8813520 and KPMG, *The Future of Advice: A comparison of fee-based and commission-based advice from the perspective of retail clients* – Whitepaper (November 2021), available at: https://die-dk.de/themen/pressemitteilungen/kpmg-studie-provisionsverbot-wurde-breite-bevolkerungskreise-von-finanzberatung-ausschliessen/

[85] de Bruin et al., *Demand for Financial Advice*, 7/2024.

[86] BETTER FINANCE, *BETTER FINANCE's Key Positions on the Retail Investment Strategy proposals* (2023).

[87] BETTER FINANCE, *Evidence Paper on Inducements* (2022).

As financial advice increasingly moves online, robo-advisors[88] have emerged as a growing alternative to traditional intermediaries[89]. BETTER FINANCE noted that while robo-advisors are generally less prone to conflicts of interest due to their fee-based models and the absence of incentives in the underlying funds, they still face challenges such as limited customisation and reliance on basic questionnaires rather than sophisticated artificial intelligence. These factors can impact the quality of advice provided to clients.[90]

One of the EU key legislations for financial intermediaries and investor protection is MiFID II. The Directive adopts a technology-neutral approach, meaning its rules also apply to robo-advisors, although practical implementation can be unclear at times. Under MiFID II, firms operating robo-advisors can provide both investment advice and portfolio management, while algorithmic trading falls under Article 17 requiring firms to implement additional safeguards to ensure system safety and operational reliability[91],. What matters is that as robo-advisory services expand, regulation must evolve to ensure these tools truly strengthen, rather than weaken, investor protection.

A growing area of interest in investor protection is advisory services for small and medium-sized enterprises (SMEs) [92]. While not the core focus of this paper, SME advice is increasingly relevant, particularly because where there is evidence that financial advice is beneficial to SMEs, the main findings on the value of advice (and some of the known risks) can also be applied to them. The raison d'être of financial advisers lies in their ability to "*improve SME's financial situation, increase efficiency, reduce the information gap and or reduce complexity for the client*"[93]. Moreover, sustainable challenges are poised to have a major impact on SMEs' future. The scale and complexity of these issues create financial uncertainty, and advisers are ideally positioned to help reduce this uncertainty, guiding SMEs toward a financially healthy and responsible future for both society and the environment[94]. BETTER FINANCE has contributed to best practices for sustainable

[88] A robo-advisor is a software that is operated by a financial intermediary. It is based on an algorithm and provided to customers online. European Parliament, Robo-advisors How do they fit in the existing EU regulatory framework, in particular with regard to investor protection? Policy Department for Economic, Scientific and Quality of Life Policies Directorate-General for Internal Policies, June 2021 , available at http://www.europarl.europa.eu/supporting-analyses

[89] See BETTER FINANCE's latest edition of the Robo-Advice Report, available here https://betterfinance.eu/publication/Robo-advice-2022-Report-Breaking-Barriers-of-Traditional-Advice

[90] BETTER FINANCE, *Evidence Paper on Inducements* (2022).

[91] Policy Department for Economic, Scientific and Quality of Life Policies Directorate-General for Internal Policies, June 2021 , available at http://www.europarl.europa.eu/supporting-analyses

[92] de Jong and Wagensveld, '*Sustainable Financial Advice for SMEs*'

[93] de Jong and Wagensveld, '*Sustainable Financial Advice for SMEs*'

[94] de Jong and Wagensveld, '*Sustainable Financial Advice for SMEs*'

investment through its report on shareholder engagement and transition of capital flows [95].

In summary, while EU frameworks like MiFID II provide robust safeguards for retail investors, gaps remain. Inconsistent adviser qualifications, conflicts of interest from commissions and inducements, payment-for-order-flow practices, and the rise of digital and robo-advisory platforms all create vulnerabilities. These challenges highlight areas where investor protection is still imperfect and call for continued regulatory attention.

High Quality Financial Advice

Against this backdrop, the question is no longer only whether appropriate rules exist, but whether they are sufficient to ensure that retail investors actually receive high-quality financial advice in practice. Regulatory safeguards can mitigate risks, but they do not, on their own, define what good advice looks like or guarantee that it serves the client's best interests in real-world interactions. This invites a closer examination of the essential features of high-quality financial advice and the conditions under which it can be consistently delivered.

First, any assessment of what constitutes high-quality financial advice must take into account the financial reality of European households. Evidence from the joint study conducted by the European Financial Planning Association (EFPA) and BETTER FINANCE[96] underscores the scale of this challenge. The report shows that many European citizens lack long-term financial planning strategies, emergency reserves, and structured investment habits. Approximately one-third of European adults have not defined any long-term financial goals, while among those who do, only around 15% effectively follow through.

These weaknesses are mirrored in low participation in capital markets. The majority of Europeans do not invest in long-term financial instruments, with 51% holding their savings primarily in bank accounts and only 22% investing in mutual funds, shares, or exchange-traded funds. This pattern highlights both a behavioural and structural gap in household financial decision-making, reinforcing the need for financial advice that effectively supports long-term planning, informed investment choices, and sustained engagement.

MiFID II and IDD do not define what constitutes high-quality financial advice. While both frameworks set out detailed rules intended to improve the quality of advice, such as requirements on suitability, disclosures, and the management of conflicts of interest, they do not provide a clear benchmark or definition that

[95] BETTER FINANCE, *Shareholder Engagement and Transition of Capital Flows*, February 2025, available at https://betterfinance.eu/publication/shareholder-engagement-transition-capital-flows-report/

[96] European Financial Planning Association (EFPA) and BETTER FINANCE, *The Financial Health of Europeans*, Joint Report, Brussels,2025.

captures what high-quality financial advice actually is. **What should high-quality financial advice look like in the European context?**

High-quality advice exists where:

- **Recommendations are not influenced by remuneration schemes**
  Professionals providing independent advice, execution-only services (particularly reception and transmission of orders) and portfolio management, regardless of the type of EU retail investment product concerned, should not be allowed to receive and retain commissions. There should be a mandatory disclosure of adviser status and fees.

a) **It is given on the best interest of the client**
This test requires advisers to base recommendations on a sufficiently broad range of products, to recommend the most cost-efficient financial products, and to offer at least one product without unnecessary features and costs.

b) **It is provided by qualified registered advisers**
Higher qualifying education and competence standards should be mandatory for retail investment advice. These standards should include appropriate initial training, demonstrated knowledge of financial products, risks, and costs, as well as an understanding of client needs and behavioural factors.

c) **It supports informed and sustainable financial decision-making**
High-quality advice should enable clients to understand the recommendations provided, their risks and costs, and how they align with the client's profile, long-term objectives and financial situation.

BETTER FINANCE believes that regulatory initiatives such as the Retail Investment Strategy (RIS) help move the discussion closer to the core of this definition. These efforts can only be effective if they are applied in a harmonised manner across the European Union. Without a common European approach, similar investors may receive materially different levels of advice quality depending on their Member State, undermining trust in financial markets and the internal market for retail financial services.

The United Kingdom provides a useful example of how clear adviser classifications and harmonised professional standards can affect retail investor confidence and market participation. The current framework for Independent Financial Advisers (IFAs) was consolidated through the Retail Distribution Review (RDR)[97], implemented in 2013 by the Financial Conduct Authority following policy

[97] Financial Conduct Authority (FCA), *Retail Distribution Review (RDR)*, United Kingdom, regulatory reform implemented from 2012, aimed at improving the quality of financial advice and reducing conflicts of interest by banning commission-based remuneration for

initiatives led by HM Treasury. This reform introduced three core changes: a clear distinction between independent and restricted financial advice; mandatory disclosure of adviser status and fees; and higher, qualifying education and competence standards for retail investment advisers.

A comprehensive FCA evaluation of the impact of the RDR, published in 2020, shows several concrete shifts in the market[98]:

- Professional qualification levels increased: nearly all advisers held valid professional standing under the new regime, with 97.9% meeting the required standard in 2019, up slightly from 97.5% in 2017.
- Consumer satisfaction and trust in advisers have risen: the proportion of advised consumers rating advice quality as high increased over time, and a larger share reported trusting that advisers act in their best interests (66% in 2020 compared to 58% in 2017)
- Market participation indicators suggest broader engagement: data showed that a notable share of UK adults with investible assets reported receiving regulated financial advice, with 17% of adults with over £10,000 in investible assets receiving advice in the previous year.
- Complaints against advisers declined: complaints handled by the Financial Ombudsman Service related to advice fell from 2,197 in 2016/17 to 1,635 in 2019/20.
- Advice supply remained resilient: after initial concerns that higher qualification requirements would shrink the adviser population, FCA data show that adviser numbers increased slightly from about 35,000 in 2012 to approximately 36,400 by the end of 2019; the proportion of firms offering independent advice also grew.

Although the UK is an example of proven success, significant work remains to be done at the European Union level to achieve the broader objective of a competitive and innovative market that genuinely serves the long-term interests of retail investors.

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independent financial advice, available at: https://publications.parliament.uk/pa/cm201012/cmselect/cmtreasy/857/857.pdf

[98] Financial Conduct Authority (FCA), *Evaluation of the impact of the Retail Distribution Review and the Financial Advice Market Review*, December 2020, available at: https://www.fca.org.uk/publication/corporate/evaluation-of-the-impact-of-the-rdr-and-famr.pdf

Conclusion

The Final Report of the High-Level Forum on the Capital Markets Union[99] underlined a widespread perception in the EU that financial services are not serving citizens well enough and that it is mainly wealthy individuals who benefit from capital markets.

Building on this observation, financial advice plays a vital role in European financial markets, helping to reduce transaction costs, bridge information gaps, and guide clients through increasingly complex investment decisions. The demand for advice does not arise merely from insufficient financial literacy, but from the practical reality that retail investors cannot devote the time and expertise required to manage investments effectively. Consequently, intermediaries are central to addressing this gap, yet their effectiveness depends on a framework that ensures competence, transparency, and alignment of interests.

In this context, MiFID II and IDD have established comprehensive safeguards, covering suitability tests, disclosure obligations, and ongoing reporting. These regulatory measures are designed to protect retail clients by ensuring that recommendations are tailored to individual circumstances, transactions are executed in the client's best interest, and potential conflicts of interest are disclosed. Despite these protections, implementation remains uneven across Member States. Variations in qualifications, continuing education requirements, and national exemptions for "local advisers" leave retail investors exposed to inconsistent standards and potential gaps in protection.

Conflicts of interest remain a persistent concern. Commission-based remuneration and inducements, disguised as advisory fees, continue to skew adviser incentives toward the highest-paying products rather than those best suited for clients. While the ban on payment-for-order-flow arrangements under the revised MiFIR marks progress, fragmented adoption across Member States risks creating uneven protections.

The emergence of robo-advisors and hybrid advisory models introduces both opportunities and challenges. Their fee-based structures generally reduce conflicts of interest, but limitations in customisation and reliance on simplistic algorithms may compromise advice quality. Regulatory oversight must adapt to ensure that technology genuinely strengthens investor protection rather than introducing new vulnerabilities.

Advisory services for SMEs are an emerging but critical area of attention. Evidence suggests that financial advice can materially improve SMEs' financial outcomes, efficiency, and decision-making while helping navigate the growing

[99] High Level Forum on the Capital Markets Union, a New vision for Europe's Capital Markets. Final Report, 10 June 2020, https://finance.ec.europa.eu/document/download/e3689370-b1ba-49fd-8829-646592d9464f_en?filename=200610-cmu-high-level-forum-final-report_en.pdf .

financial uncertainty posed by sustainability challenges. Advisers, therefore, have a potential role in guiding SMEs toward responsible and resilient financial futures.

Beyond structural and regulatory challenges, the persistent low financial literacy of EU consumers amplifies investor vulnerability to low-quality investment advice. On average, only one in two people in the EU correctly answer three out of five financial literacy questions, and over one-third do not understand inflation – a basic concept affecting everyday purchasing power[100]. Without sufficient understanding of fundamental financial principles, consumers are at higher risk of making poor investment decisions. Regulation can mitigate certain pitfalls, but it cannot replace the need for knowledge.

In this context, BETTER FINANCE believes that regulatory initiatives such as the Retail Investment Strategy (RIS) help move the discussion closer to the core of the definition of high-quality financial advice developed in this paper.

Financial literacy is, therefore, a necessary complement to regulation, enabling investors to make informed decisions and participate effectively in the financial markets. Moreover, advancing literacy is crucial to the EU's broader agenda, supporting responsible investment and greater household participation in capital markets.

In conclusion, EU regulatory frameworks provide strong foundations for investor protection, yet gaps remain. Conflicts of interest, inconsistent qualifications, digitalisation, and fragmented national regimes all create vulnerabilities. To truly empower retail investors, regulations must not only harmonise adviser standards across borders but also adapt to technological innovations and emerging markets, such as SMEs and sustainable finance. Only by addressing these challenges can financial advice fully deliver on its promise: to inform, protect, and support investors in achieving financially sound and responsible outcomes.

[100] Demertzis et al., 'The State of Financial Knowledge in the European Union', Policy Brief 04/2024.

BETTER FINANCE is the European federation representing individual savers, investors, and financial services users. It protects the interests of individual savers and investors, promotes sustainable finance, and helps restore confidence in capital markets and financial intermediaries. As a bridge between EU institutions, policymakers, and regulators on the one hand, and its national member associations on the other – each directly connected to millions of individual investors and users of financial services – BETTER FINANCE ensures that the voices and real experiences of Europe's citizens are heard at the heart of EU financial policymaking.

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