



COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 30.4.2007  
COM(2007) 226 final

**GREEN PAPER**

**on Retail Financial Services in the Single Market**

(presented by the Commission)

# GREEN PAPER

## on Retail Financial Services in the Single Market

(Text with EEA relevance)

### SUMMARY

The Commission is currently reviewing the single market to ensure its policies are fit for the 21<sup>st</sup> century. The interim report to the Spring European Council outlines the new approach to using single market instruments, and focuses on enhancing consumer welfare<sup>1</sup>. The Commission will present its final report in autumn 2007, which will include concrete measures to benefit citizens. Retail financial services represent an important part of this review.

Retail financial services are an essential part of the everyday lives of EU citizens. Despite significant progress in delivering a single market for financial services in recent years, studies show that retail financial services integration appears not to have yet reached its potential and that competition seems insufficient in some areas.

Building on the Commission's White Paper on Financial Services 2005–2010<sup>2</sup>, the results of the Commission's sector inquiry into retail banking<sup>3</sup> and the interim report on business insurance<sup>4</sup>, the Green Paper seeks to strengthen and deepen our understanding of the problems faced by consumers and industry in the field of retail financial services and to establish the scope for and impediments to further initiatives in this area. The specific results of this consultation, including possible measures to improve the functioning of retail financial services markets, will be incorporated into the final report of the Single Market Review, to be published in the autumn.

The Green Paper sets out the overarching objectives of the Commission's policy in the area of retail financial services, presents in more detail the actions necessary to bring the benefits of integrated EU financial market to users, and requests feedback from stakeholders on the direction being taken.

The Commission believes that integration in EU retail financial services markets can be further developed by:

- bringing about concrete benefits for consumers by ensuring that properly regulated open markets and strong competition deliver products that meet consumers' needs, offering choice, value and quality;
- enhancing consumer confidence by ensuring that consumers are properly protected where appropriate, and that providers are financially sound and trustworthy;

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<sup>1</sup> COM(2007) 60, 22.2.2007.

<sup>2</sup> COM(2005) 629, 1.12.2005.

<sup>3</sup> COM(2007) 33, 31.1.2007 and SEC(2007) 106, 31.1.2007.

<sup>4</sup> "Interim Report on the Business Insurance Sector Inquiry", 24.1.2007.

- empowering consumers to make the right decisions for their financial circumstances. This is based on several elements, including financial literacy; clear, appropriate and timely information provision; high-quality advice; and a level playing field between products perceived as having similar characteristics. Empowered consumers may be more confident in seeking out the best deals to meet their needs, regardless of the location of the financial services provider.

While initiatives at the EU level are underway or imminent in some areas such as investment funds, payments, insurance, mortgage credit, bank accounts and credit intermediaries, in other areas, such as retirement savings and financial literacy, work is at a more preliminary stage.

The Commission considers that constant attention is needed to ensure that citizens reap the benefits of a single market. In pursuing its strategy, the Commission will adopt an open and inclusive approach to identify and address problems, consider the full range of policy tools and, where appropriate, will take targeted action.

**The Commission welcomes general comments and feedback from stakeholders on the contents of this paper and answers to the questions therein. Responses should be sent by 16 July 2007 to [markt-retail-consultation@ec.europa.eu](mailto:markt-retail-consultation@ec.europa.eu).** Responses will be placed on the Commission's website unless explicitly indicated otherwise.

## 1. INTRODUCTION

- (1) The Commission is currently reviewing the single market to ensure its policies are fit for the 21<sup>st</sup> century. The interim report to the Spring European Council outlines the new approach to using single market instruments, and focuses on enhancing consumer welfare<sup>5</sup>. The Commission will present its final report in autumn 2007, which will include concrete measures to benefit citizens. Retail financial services represent an important part of this review.
- (2) Building on the Commission's White Paper on Financial Services 2005–2010<sup>6</sup>, the results of the Commission's sector inquiry into retail banking<sup>7</sup> and the interim report on business insurance<sup>8</sup>, the Green Paper seeks to strengthen and deepen our understanding of the problems faced by consumers and industry in the field of retail financial services and to establish the scope for and impediments to further initiatives in this area. The results of this consultation will be incorporated into the Single Market Review, to be published in the autumn.
- (3) The Green Paper sets out the overarching objectives of the Commission's policy in the area of retail financial services, presents in more detail the actions necessary to bring the benefits of integrated EU financial market to users, and requests feedback from stakeholders on the direction being taken.

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<sup>5</sup> Cf. footnote 1.

<sup>6</sup> Cf. footnote 2.

<sup>7</sup> COM(2007) 33, 31.1.2007 and SEC(2007) 106, 31.1.2007.

<sup>8</sup> Cf. footnote 4.

## 2. CONTEXT

- (4) In this paper, retail financial services are understood as services such as current accounts, payments, personal loans, mortgages, savings, pensions, investments and insurance products, when they are provided to individual customers, including retail investors. They are essential for the everyday lives of EU citizens by facilitating their full participation in the economy, enabling them to plan for the long term and protecting them in unforeseen circumstances. They involve major financial commitments. Home loans are the largest lifetime financial exposure for most EU citizens, with outstanding mortgage balances reaching almost 50% of EU GDP<sup>9</sup>. Investment funds in the different Member States account for between 4% and 23% of EU household financial assets<sup>10</sup>.
- (5) Retail financial services are important in macro-economic terms. Retail banking (over half of total banking activity) generates 2% of EU GDP annually in gross income<sup>11</sup>. An ageing population puts added pressure on public finances, increasing the potential need for more private and work-based retirement provisioning and health cover. This helps explain the growing economic importance of the pension, insurance and investment fund sectors. At the end of 2004, investments by primary insurers reached EUR 6 trillion and EU private pension funds managed EUR 2.5 trillion in assets<sup>12</sup>. UCITS funds are capitalised at over EUR 5.7 trillion, over 50% of EU GDP<sup>13</sup>. Life insurance premiums alone represent 5% of EU GDP<sup>14</sup>.
- (6) Significant progress has been made in delivering a single market for retail financial services. A framework is in place to ensure the financial soundness and integrity of Europe's retail financial services providers in the areas of banking, insurance and securities<sup>15</sup>. This framework is designed to achieve multiple policy goals, including prudential stability, competition and a high level of consumer and investor protection. In some areas, such as investment services and life assurance, comprehensive rules have been put in place to protect the interests of retail customers and investors<sup>16</sup>. Furthermore, the introduction of the euro, combined with the effects of the Financial Services Action Plan, has spurred greater competition in Europe's financial services markets, particularly wholesale markets.
- (7) Retail financial services integration appears not to have yet reached its potential and competition in some markets seems insufficient, particularly in areas like payments and retail banking<sup>17</sup>, which may leave EU consumers unable to take full advantage of the benefits of the single market. The following indicators illustrate this:

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<sup>9</sup> Hypostat 2005, European Mortgage Federation.

<sup>10</sup> SEC(2006) 1057, 26.7.2006.

<sup>11</sup> SEC(2007) 106, 31.1.2007, p. 7.

<sup>12</sup> Cf. footnote 10.

<sup>13</sup> EFAMA quarterly statistical release Q3 2006.

<sup>14</sup> Source: The European Insurance and Reinsurance Federation (CEA).

<sup>15</sup> E.g. Directives 2004/39/EC, 2006/48/EC and 2006/49/EC.

<sup>16</sup> E.g. Directives 2002/83/EC and 2004/39/EC.

<sup>17</sup> COM(2007) 33, 31.1.2007, p. 2 and p. 3.

- **Modest cross-border activity.** With the exception of UCITS, cross-border trade is limited and activity through cross-border establishment or mergers is lower than in most other sectors<sup>18</sup>. Commission surveys suggest that only 1% of EU consumers currently buy financial services cross-border at a distance, while 26% of consumers do so domestically, for instance over the phone or internet<sup>19</sup>. In insurance, consolidation of the industry has taken place through mergers and establishment rather than by opening branches and providing cross-border services. The volume of cross-border business is extremely small<sup>20</sup>, with domestic insurance companies accounting for more than 90% of total premium income in most markets. 50% of business is accounted for by the 20 largest European insurance groups, which in many cases have a wide European and even global presence<sup>21</sup>.
- **Wide variations in prices.** Although interest rate levels have converged to some extent in areas such as home loans, due largely to general macroeconomic convergence and the introduction of the euro<sup>22</sup>, substantial differences remain for payment services and products such as consumer credit and current accounts<sup>23</sup>. For example, euro credit transfers are free in some Member States and cost more than EUR 10 in others<sup>24</sup>. In other sectors, such as motor or home insurance, comparisons of the base price of an insurance product are more difficult as coverage and local risk conditions vary widely<sup>25</sup>. In 2008, the Commission will study the price variations in key retail financial services.
- **Restricted product diversity and choice.** In certain Member States long-term fixed rate mortgage products and some newer products, such as equity release mortgages, may be difficult to obtain, which may limit consumer demand and market growth. In four Member States, more than a quarter of all savings accounts have tax incentives, while such products are rare elsewhere in the EU<sup>26</sup>. Problems with tax deductibility have proved an obstacle to the cross-border sale of some life insurance and pension products.
- **Large variations in market performance.** The profitability of retail financial providers varies widely. For example, retail banking profitability in the Nordic countries, Spain and Ireland appears consistently above the EU average and much lower in Germany, Austria, the Netherlands and Belgium<sup>27</sup>.

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<sup>18</sup> SEC(2005) 927, 1.7.2005 and SEC(2006) 1057, 26.7. 2006.

<sup>19</sup> "Eurobarometer 230: Public Opinion in Europe on Financial Services", August 2005.

<sup>20</sup> According to data from Eurostat, intra-EU25 trade in insurance services fell by 14.6% between 2003 and 2005.

<sup>21</sup> Cf. footnote 14.

<sup>22</sup> SEC(2005) 927, 1.7.2005.

<sup>23</sup> COM(2007) 33, 31.1.2007, p. 3.

<sup>24</sup> SEC(2007) 106, 31.1.2007, p. 63.

<sup>25</sup> Risk profiles are different between national and even regional markets.

<sup>26</sup> SEC(2007) 106, 31.1.2007, p. 40.

<sup>27</sup> SEC(2007) 106, 31.1.2007, p. 22.

- (8) Without further efforts, European retail financial markets are likely to remain fragmented. Differing regulatory and consumer protection frameworks, taxation policies and fragmented infrastructures<sup>28</sup> create legal and economic barriers to market entry<sup>29</sup>. Legal barriers may prevent or complicate the offering of certain products or accessibility to market infrastructures, thus limiting competition and stifling innovation. Economic barriers such as the need to adapt products, business models and pricing strategies raise the costs of doing business in another Member State. These barriers deter market entrants, restrict consumer choice and push up prices for consumers. High switching costs can reduce consumers' potential to change providers for products such as bank accounts and investment funds. The inability to access information, or incomplete information, may mean that consumers are unable to choose the best deal.
- (9) Consumer behaviour and preferences may also limit market integration. Despite the increased mobility of the population and the growth of cross-border retail financial service provision (including through direct channels such as the Internet)<sup>30</sup>, most consumers still opt for products distributed locally through branches, subsidiaries, and intermediaries<sup>31</sup>.
- (10) Notwithstanding that most customers of retail financial services are likely to remain domestically focused and that consumers must remain free to choose a local product or service if that is their preference, the Commission considers that further reforms may be needed to make markets work better for consumers.

### **3. BETTER REGULATION AND RETAIL FINANCIAL SERVICES**

- (11) Improving the operation of Europe's retail financial services markets may require targeted and considered action, building on what has been achieved. Some of the stakeholders consulted in recent years have indicated that more regulation in this area is unlikely to bring significant benefits for consumers. However, according to other sources, a regulatory approach may be needed in some cases. Building a shared understanding of the policy challenges is indispensable in order to design policies that produce concrete benefits for consumers.
- (12) Initiatives should only be pursued where there is evidence of clear and concrete benefits for citizens and a strong economic rationale. Policies must be based on solid economic evidence and be subjected to thorough impact assessments. The assessment of appropriate solutions must be made on a case-by-case basis, depending on the specifics of the market and problems identified. The Commission will only undertake new regulatory initiatives in retail financial services if the economic case is made and if factors such as consumer confidence and cross-border activity can be improved. Once policies have had sufficient time to prove their efficiency, the Commission will

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<sup>28</sup> E.g. payment systems, clearing and settlement systems and credit registers.

<sup>29</sup> E.g. in insurance, the requirement in some Member States to appoint a fiscal representative in order to ensure the collection of premium taxes in the country of the risk makes it difficult to build up business profitably from a low base.

<sup>30</sup> A recent UK survey suggested that over 50% of internet users do their banking online (16.9 million people).

<sup>31</sup> Cf. footnote 19.

evaluate their impact, in particular whether they deliver genuine and concrete benefits for consumers. Where measures are not working, the Commission will not hesitate to propose their withdrawal.

- (13) In pursuing its strategy on retail financial services, the Commission will adopt an open and inclusive approach to identify and address problems, consider the full range of policy tools, binding or not, promoting where appropriate market-led initiatives or optional EU legal frameworks such as the so-called "28<sup>th</sup> regimes"<sup>32</sup>. Targeted actions will be undertaken where necessary.

#### **4. OBJECTIVES AND ACTIONS**

- (14) This section outlines the Commission's objectives in the field of retail financial services: bringing concrete benefits for consumers notably in terms of prices and choice; enhancing consumer confidence; and empowering consumers, and sets out how the Commission intends to achieve them.

##### **4.1. Lower prices and more choice for consumers**

- (15) The Commission is committed to removing barriers for retail financial services where this will lead to concrete benefits for consumers in the form of a wider choice of products which correspond to their needs and at more competitive prices.

##### ***Bringing down prices through increased competition***

- (16) The EU regulatory framework aims to create the conditions under which competition can thrive and market forces can push prices down while maintaining the quality of products provided. The Commission will take appropriate action, be it through enforcement of competition law or robust infringement policies, where there appears to be a practice of not applying or respecting Community legislation. It may also take other initiatives (including legislative ones, as justified following a full impact analysis) in order to ensure that markets are fair and give consumers better deals. Obstacles to the basic freedoms provided by the EC Treaty will be addressed to ensure that markets are open and competitive. The Commission's sector inquiry into retail banking suggests that better market access for financial institutions established in other Member States reduces prices for consumers<sup>33</sup>.
- (17) It is important that consumers wishing to change providers are not dissuaded or prevented in any manner from doing so. A market with well-informed and mobile consumers forces financial institutions to compete to attract and retain them.
- (18) Barriers to customer mobility, such as fees for terminating an account or policy, poor or complex information, product tying and the high administrative burden of changing providers, need to be addressed.

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<sup>32</sup> 28th regimes are legal frameworks of EU rules which do not replace national rules but are an optional alternative to them (e.g. European Company Statute).

<sup>33</sup> SEC(2007) 106, 31.1.2007, p. 32–33.

- (19) Lenders who are unable to access accurate credit information may charge higher prices or even refuse to provide credit to consumers. This makes it difficult for consumers to shop around for better offers, both nationally and on a cross-border basis.

#### **Ongoing and planned initiatives**

The Commission will tackle the barriers to competition identified by the sector inquiry into **retail banking**<sup>34</sup>. In relation to payment cards, the Commission will apply EC competition law where schemes artificially raise costs for consumers. An ongoing area of work refers to multilateral interchange fees, typically paid by the bank of the merchant to the bank of the cardholder<sup>35</sup>. Practices that weaken inter-network competition are likely to be subject to competition scrutiny<sup>36</sup>. Besides payment cards, the Commission's action will aim at ensuring that access to credit registers and to payment clearing and settlement systems is not unduly withheld.

The Commission will work together with the national competition authorities in the framework of the European Competition Network in deciding how to best deal with practices that restrict competition and reduce consumer welfare.

An **expert group on customer mobility** in relation to bank accounts was set up by the Commission in 2006. It will publish its recommendations in May 2007. Among the options considered by the group is the development of arrangements for switching bank accounts (at national or EU level) and of various measures aimed at increasing information transparency and comparability. These options will be carefully considered by the Commission, which will weigh their impact before making final decisions.

In recognition of the increasing possibilities of employees to work in other EU Member States, and the importance of preparing adequately for retirement, for example through work based pension schemes, the Commission has recently proposed a Directive to improve the **portability of supplementary pension rights**<sup>37</sup>.

The forthcoming White Paper on Mortgage Credit will outline initiatives to facilitate the transferability of consumers' credit histories and improve lenders' access to **credit information**. The Commission believes that, since this issue goes beyond mortgage credit, horizontal initiatives could be envisaged to improve access and transferability of credit data.

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<sup>34</sup> COM(2007) 33, 31.1.2007, p. 4–9.

<sup>35</sup> Cf. COMP/34.579 concerning MasterCard.

<sup>36</sup> Such as so-called blending (the acquiring banks' practice of charging businesses one global price for accepting cards of different types and/or issued by different networks) or the prohibition of surcharging, which avoids that merchants request additional fees for the use of the more expensive payment means.

<sup>37</sup> COM(2005) 507, 20.10.2005.

### *Increasing choice, quality and innovation*

- (20) Innovation creates new challenges such as ensuring that regulation of new products, providers or financial advisors is appropriate, that consumers are able to understand and compare new products, and that a level playing field between products is guaranteed. The Commission wishes to enhance consumer choice, provided that this benefits the consumer. Indeed, consumers often express the concern that a too wide choice of products may distract or confuse them, complicating their selection of the product best suited to their needs.
- (21) The Commission is determined to ensure that the removal of barriers to a single market in retail financial services improves or at least maintains the quality of products provided, and that consumers are in a position to make an informed choice. For example, the Payments Services Directive seeks to improve the quality of service provision to consumers by increasing the speed at which payments are made<sup>38</sup> and by facilitating the cross-border availability and use of certain payments products, such as direct debits. Another way to ensure the high-quality of the service provided to consumers might be accredited certification through international standards<sup>39</sup>. Indeed, accredited certification could provide a sound and transparent assessment of different aspects of performance, and serve as a quality indicator to consumers, especially in cases of cross-border activity.
- (22) A wide range of banking, insurance and savings products are available in the EU. However, a product offered to consumers in one market cannot, in many cases, be offered in another market without costly adaptation to local requirements. For example, certain products, such as the ability to execute direct debits on a cross-border basis, may not be available because of diverging legal regimes. These requirements may reflect local consumer customs and needs and be found in consumer protection rules, contract law, differing taxation and legal systems. Choice may also be unnecessarily limited by restrictions on the providers and channels through which consumers access retail financial services<sup>40</sup>. Such restrictions should only be maintained if objectively justified.

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<sup>38</sup> In some Member States, consumers enjoy “same day” payment whereas, in others, payments can take two or three days, even longer in cross-border cases.

<sup>39</sup> For further information about certification, please see:  
[http://ec.europa.eu/enterprise/regulation/index\\_en.htm](http://ec.europa.eu/enterprise/regulation/index_en.htm).

<sup>40</sup> E.g. new payment services providers such as supermarkets, money remitters or mobile phone operators cannot currently offer their services throughout the single market.

- (23) The insurance Directives allow insurers to advertise and sell their full range of insurance products throughout the EU, and have abolished the prior approval of tariffs and policy conditions. Insurance products are, however, required to respect national rules justified by the need to protect the 'general good'<sup>41</sup>. This may limit the choice of products available to consumers and impose further costs on insurers<sup>42</sup>. The insurance industry has expressed the view that retail business is local and requires a strong local presence. The Commission believes that action should concentrate on the elimination of market protectionism and on the reduction of unnecessary regulatory costs by, for example, removing unjustified general good rules and bureaucratic obstacles such as excessive reporting requirements. With the right regulatory regime, which provides a high standard of consumer protection, opportunities for direct cross-border trade will be exploited naturally, where and when this makes sense for companies and consumers.

#### **Ongoing and planned initiatives**

In **insurance**, the Commission will in 2007, together with the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS), – examine the national 'general good' rules taking into account the relevant case law principles.

The payments industry, on a self-regulatory basis, is drawing up the required technical and business rules to make the **Single Euro Payments Area (SEPA)** a reality by 2010 at the latest. The Commission is closely monitoring this process. In a Communication to be published before the end of 2007, the Commission will assess progress and consider further measures to guarantee the success of SEPA for the benefit of consumers.

The Commission will later this year publish a **White Paper on Mortgage Credit**, containing proposals to facilitate the creation of an integrated market for mortgage credit. Issues addressed will include early repayment, information requirements, annual percentage rate of charge, advice, property valuation, land registration and foreclosure procedures. In 2008, the Commission will review national regulatory frameworks under which **equity release** products are marketed, and the role of **non-banks** in mortgage markets, in order to assess whether appropriate EU intervention is needed.

In order to **develop the appropriate knowledge base** for future policy initiatives, the Commission will examine why consumers generally do not purchase financial services across borders and how they could be encouraged to seek the best deals to meet their needs regardless of the location of the financial services provider.

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<sup>41</sup> The general good concept is based on extensive and consistent case law of the Court of Justice. See for example the Commission's Interpretative Communication on the Freedom to provide services and the general good in the insurance sector, (OJ C 43 of 6 February 2000).

<sup>42</sup> Requirements imposed on retail insurance products in the interest of the general good may only be justified if they are necessary to protect consumers, if they are proportionate and if they do not duplicate home country requirements.

Ageing populations and increasing pressure on public finances present clear challenges for consumers and investors, and are a new market for the financial industry. The EU framework needs to lay strong foundations for enabling a competitive, open and effective market for **long-term savings, retirement and pension** solutions that meet consumers' needs. The Commission has commissioned external research that will report at the end of 2007 on the current state and development of the market for retail long-term savings vehicles to help identify the range of products currently available, the main distribution channels and the influences on consumer choices. Building on this, the Commission will examine developments affecting the marketing of savings and retirement products together with arrangements governing their sale and recommendation. Due to the nature of long-term savings and pension plans, particular care is needed to ensure that consumers are being offered products that are really adapted to their needs and marketed appropriately. These are major, once in a lifetime, financial decisions for consumers. Therefore, consumers must be in a position to make their choices in full knowledge of the product, correctly assessing their circumstances and needs.

The Commission considers that there could be benefits for both consumers and financial services providers, if optional simplified, standardised financial services, such as **basic bank accounts** could be offered. These would be less complex than other products and would meet a European standard of consumer protection, for instance in respect of information requirements. They could therefore be offered cross-border without the need to be modified to meet local regulations. Banks would not be obliged to offer them, and would only do so where there was a business case. Consumers would have a wider choice of easier to understand products. Further work could be undertaken to assess the need for, feasibility and usefulness of such optional standardised products.

#### 4.2. Enhancing consumer confidence

- (24) European consumers need confidence to make the right choices. However, surveys show that European consumers remain concerned about the risks of cross-border activity and lack confidence in the available legal protection<sup>43</sup>. Further efforts may therefore be required to ensure that consumers are confident that they will enjoy the same rights, regardless of the location of the financial institution and of the selling mode chosen. Four main issues arise in this respect: protecting consumers' interests, providing legal certainty, ensuring access to adequate redress and promoting sound and safe retail financial institutions.

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<sup>43</sup> Cf. footnote 19.

### *Protecting consumers' interests*

- (25) An equivalent level of protection throughout the EU gives consumers the confidence to choose from a range of providers wherever they are in Europe. This protection ensures a level playing field for both consumers and service providers.
- (26) Traditionally, EU legislation in the field of retail financial services has sought to establish minimum rules for protecting consumers in all Member States. For example, the Life Assurance Directive requires a minimum cooling-off period of 14 days<sup>44</sup>. This approach is not without difficulties: in many cases, Member States have gone beyond the minimum requirements, thereby limiting the extent of the level playing field and creating diverging levels of protection amongst European consumers.
- (27) The modified proposal for a revised Consumer Credit Directive<sup>45</sup>, whose scope is narrower than in the original 2002 proposal, seeks to promote the emergence of a genuine single market in consumer credit while ensuring a high level of consumer protection. Consumers should be able to have access to a wider range of consumer credit products at more competitive prices. Providers should be in the position to market their consumer credit products in all Member States without having to adapt the essential features to different national legislations. So far, it has proven very difficult to find a consensus between Member States on the content and the level of harmonisation.
- (28) Financial services are increasingly sold or marketed over the internet or by telephone. The Directive on the distance marketing of financial services<sup>46</sup> was adopted in 2002 in order to boost consumer confidence in using these technologies in the area of financial services cross-border and to ensure a smooth functioning of the single market. Key elements of the Directive are pre-contractual information requirements and the right of withdrawal.
- (29) The Markets in Financial Instruments Directive (MiFID)<sup>47</sup> introduces a harmonised comprehensive set of operating conditions applicable to both investment firms and credit institutions that regulates the relationship between them and their clients when they offer investment services. This framework consists in a set of conduct of business, best execution and client order handling rules as well as inducements and conflicts of interest provisions. Specific attention is granted to retail clients for which a specific regime has been established, which entails reinforced fiduciary duties upon the firm. The purpose of this approach is to protect consumers by enhancing responsible behaviour by firms<sup>48</sup>.

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<sup>44</sup> See Article 35 of Directive 2002/83/EC.

<sup>45</sup> COM(2005) 483, 7.10.2005.

<sup>46</sup> Directive 2002/65/EC.

<sup>47</sup> Directive 2004/39/EC and its implementing measures, Regulation (EC) No 1287/2006 and Directive 2006/73/EC.

<sup>48</sup> To avoid that additional rules affect the creation of a level playing field and, at the same time introduce barriers to market entry without enhancing investor protection, the MiFID introduces a flexibility clause, allowing Member States to add rules at national level – but only in strictly exceptional circumstances – in order to enhance investor protection.

- (30) Consumers are also indirectly protected through professional indemnity insurance that ensures that, in the event of financial loss owing to negligent advice or other professional misconduct by insurance and investment intermediaries, damages or settlements may be claimed<sup>49</sup>. A recent report concluded that the requirements to have professional indemnity insurance remain valid but that further monitoring will be required as the legislation is not yet fully implemented in Member States<sup>50</sup>.

### *Providing legal certainty for consumers*

- (31) The law applicable to contractual obligations is currently regulated by the Rome Convention of 1980. On the basis of this Convention, a consumer who concludes a contract for the supply of goods or services is faced with a complex situation: the law applicable to the contract is, in principle, the one chosen by the parties, which often means in practice the law chosen by the provider in the standard terms and conditions. However, a consumer will, under certain conditions, benefit from the protection given by the mandatory provisions of the law of the country where he resides<sup>51</sup>. The proposal for a Regulation on the law applicable to contractual obligations<sup>52</sup> will modify somewhat the rules on the law applicable to contractual obligations in contracts with consumers. One of the most important changes is the establishment of the principle that the law of the country where the consumer resides habitually will apply to the contract if the provider pursues his commercial activities in the country where the consumer has his habitual residence<sup>53</sup>. This will provide more legal certainty – and thus, confidence – for the consumer who will know that the rules he knows best will apply to the contract. The proposal for a Regulation is currently discussed in the Council and the European Parliament with a view, in particular, to finding an adequate balance between consumer and industry legitimate interests.

### *Ensuring access to adequate redress*

- (32) To have confidence in buying financial services cross-border, consumers need to know that they would have easy access to redress in the event of a dispute. Consumers have two main options: bringing their dispute to court, or to an out-of-court alternative dispute resolution (ADR) scheme, such as ombudsman or consumer complaints board. ADRs do not replace the possibility of court action, but offer an easier, cheaper and quicker alternative. ADR schemes may be either public or private initiatives. Partly because of this diversity, the status of the ADR decisions may vary.

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<sup>49</sup> See provisions included in Directives 2002/92/EC and 2006/49/EC.

<sup>50</sup> COM(2007) 178, 11.4.2007.

<sup>51</sup> Article 5 of the Convention.

<sup>52</sup> COM(2005) 650, 15.12.2005.

<sup>53</sup> Some areas remain excluded from the application of the proposed rule: life and non-life insurance Directives provide for specific laws of conflict and therefore these special rules will take precedence on the general regime. DK, IE and UK are not part of the Convention and will not be covered by the Regulation (although UK and IE have an opt-in clause).

- (33) Normally, an ADR scheme in the country of a financial services provider is competent to deal with consumers' complaints. This may prove complicated for consumers involved in cross-border disputes, since they need to be aware of the existence and details of foreign ADR schemes. In 2001, the Commission launched a network of EU ADR schemes, FIN-NET<sup>54</sup>, in which members cooperate under common rules, thereby facilitating the out-of-court resolution of cross-border consumer disputes in financial services. Cooperation between FIN-NET members means that consumers shall only contact ADR schemes in their own country. Member schemes assist consumers in transferring complaints to the competent ADR scheme in the country of the financial services provider.
- (34) Despite these efforts, the handling of consumer complaints may still be particularly problematic in a cross-border context.

### *Promoting sound and safe retail financial institutions*

- (35) A robust prudential framework is of paramount importance. Indeed, consumers need to be confident in the soundness of financial institutions, wherever they are located in the Union. The current EU prudential framework should be kept under constant review and adapted to market and financial developments. The next step in this respect will be the modernisation of the insurance prudential framework, with the forthcoming "Solvency 2" proposal.
- (36) Specific Directives in the field of investment services<sup>55</sup> and banking<sup>56</sup> ensure that consumers throughout the EU enjoy a high standard of protection, should the establishment with which they have deposited or invested fail. Following a review of the framework for deposit guarantee schemes, the Commission will seek to ensure that consumers are well informed about the coverage of their deposits; that all deposits are covered even for newer financial products and that the length of time that it takes for consumer to be reimbursed is limited<sup>57</sup>.

#### **Ongoing and Planned Initiatives**

Negotiations in the Council on the modified proposal for a new **Consumer Credit Directive** are being pursued with the aim of a rapid adoption.

The objective of increasing consumers' cross-border activities in financial services at a distance has not yet been achieved<sup>58</sup>. The Commission has begun a review of the **Directive on the distance marketing of financial services**<sup>59</sup> and launched two studies in order to assess the legal and economic impact of the Directive. A Commission report is scheduled for 2008. It will examine if the Directive has achieved its goals and, if not, why it has not. If necessary, the Commission will propose amendments to the Directive.

<sup>54</sup> FIN-NET currently has 48 members from 21 EEA countries.

<sup>55</sup> Directive 97/9/EC.

<sup>56</sup> Directive 94/19/EC.

<sup>57</sup> COM(2006) 729, 27.11.2006.

<sup>58</sup> Cf. footnote 19.

<sup>59</sup> Directive 2002/65/EC.

The Commission will follow closely the work announced by CEIOPS for 2007 to examine **co-operation between supervisors** on issues directly influencing insurance policyholder protection such as the treatment of cross-border complaints.

The Commission will monitor existing recommendations<sup>60</sup> which establish a number of minimum guarantees for **ADR schemes**. The proposal for a directive on certain aspects of mediation in civil and commercial matters<sup>61</sup>, when adopted, will complete the recommendations by ensuring a sound relationship between the mediation process and judicial proceedings.

The Commission is aware that not all national ADR schemes are members of FIN-NET and that not all EU Member States have ADR schemes for financial services. The Commission will contact competent national authorities later this year to collect information on the existing national ADR schemes that are not members of FIN-NET and identify gaps. It will then assess how the gaps in FIN-NET membership and at national level could be filled.

### 4.3. Empowering consumers

- (37) Consumers are able to make the most of the single market if they have the financial literacy to make decisions for themselves, are well-informed, receive independent high-quality advice and can move freely between providers. By empowering consumers in this way, they may be more confident in seeking out the best deals to meet their needs regardless of the location of the financial services provider. This in turn can stimulate competition and make financial services markets work better.

#### *Developing consumers' financial literacy*

- (38) Developing consumers' literacy in financial matters is becoming increasingly important, particularly as individuals take an increasing role in making decisions affecting their financial security and as capital markets become more accessible to consumers. Numerous international surveys have demonstrated a low level of understanding of financial matters on the part of consumers<sup>62</sup>. There is also a strong correlation between low levels of functional literacy and the ability to make appropriate financial decisions. Consumers with poor financial literacy find it hard to understand and make use of the information they receive when they purchase financial services, since information is generally prepared having average consumers in mind rather than those with lower levels of financial literacy.

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<sup>60</sup> Recommendation on the principles applicable to the bodies responsible for out-of-court settlement of consumer disputes, 30.3.1998, and Recommendation on the principles for out-of-court bodies involved in the consensual resolution of consumer disputes, 4 April 2001.

<sup>61</sup> COM(2004) 718, 22.10.2004.

<sup>62</sup> See for example, "Financial Capability in the UK: Establishing a Baseline", UK Financial Services Authority, March 2006; research by the Irish National Adult Literacy Agency, August 2006 (see <http://www.nala.ie/press/pressreleases/20060914161103.html>); results of research published by a working group of the Autorité des Marchés Financiers (France), June 2005 (see [http://www.amf-france.org/documents/general/6080\\_1.pdf](http://www.amf-france.org/documents/general/6080_1.pdf)).

### **Ongoing and Planned Initiatives**

While financial education is primarily a matter for Member States, the Commission has already funded some **financial literacy** initiatives, in the context of its work on consumer protection and on combating social exclusion<sup>63</sup>, and believes that more could be done to encourage the provision of high-quality financial education. The role of the Commission could be, for instance, in developing guidelines, collecting and promoting best practices, or indicating new innovative approaches. In developing its policies towards financial literacy, the Commission will draw on the feedback from participants to its Conference on financial capability held on 28 March 2007 and on the findings of a study on financial literacy schemes in the EU which it has commissioned and which will be available at the end of 2007.

### ***Providing the right information at the right time***

- (39) Selecting an inappropriate product can have adverse consequences for retail consumers and investors and the best safeguard against this is good disclosure and sound information. Good information helps consumers to understand the key features of a financial product, including the risks, potential returns and costs. However, evidence<sup>64</sup> suggests that the information provided is often inadequate or too complex, making it difficult to compare prices, products and providers and to take an informed financial decision. Financial products are subject to different information requirements and therefore offer different degrees of protection. The Commission believes that information needs to be complete, correct, clear, proportionate, understandable and presented in a timely manner. Information requirements also need to be consistent.

### **Ongoing and Planned Initiatives**

The Commission has ongoing **initiatives to improve the quality of information provided** to consumers in areas such as consumer credit, mortgage credit, investment funds (UCITS) and payment services.

**Consumer testing** will be undertaken to evaluate the relevance and usefulness of **pre-contractual information** in certain areas, such as credit.

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<sup>63</sup> For instance, in 2005–2006, the European Commission funded the development of the DOLCETA programme, an online training tool designed for use by adult education providers. In 2006, the European Commission funded a study of financial education initiatives across the EU to develop and exchange best practice models and new strategies to improve the access to financial services for people experiencing poverty and social exclusion – and especially over indebted people, which has been carried out by a consortium of debt-management agencies. This work has facilitated information sharing between the organisations involved.

<sup>64</sup> SEC(2007) 106, 31.1.2007, p. 67 and "Eurobarometer 230: Public Opinion in Europe on Financial Services", August 2005.

In the area of **long-term savings and investments**, but also possibly in other areas, a sector approach to legislation has created a situation where, despite certain products being perceived as having similar characteristics by investors, they are subject to different requirements, notably regarding information disclosure both at the point of sale and on an ongoing basis. In moving to ensure that information requirements in EU financial services legislation are appropriate and consistent, the Commission will launch a **cross-sector study** in 2008. This will build on the work of the three Level 3 committees on conduct of business (including disclosure) rules across comparable investment products.

### *Advising consumers*

- (40) Providing advice is distinct from providing information. Whilst information merely describes a product or service, advice implies a recommendation to a given consumer to opt for a specific product. When advice is given, it should be objective, based on the profile of the customer, and commensurate with the complexity of the products and the risks involved. This is already required by MiFID for the provision of investment advice (i.e. recommendations to clients must be suitable to their personal circumstances). For products such as home loans and retirement savings, which have a considerable impact on the financial situation of the consumer, consumers in some countries rely on independent high-quality advice to make appropriate decisions.
- (41) The Commission is giving increased attention to the role of financial intermediaries. The market infrastructure for sales and distribution is not always optimal to assist consumers in selecting sound and suitable financial products. For instance, intermediation for pensions currently differs on a product-by-product basis and according to "pension pillar"<sup>65</sup> classification, although some of the services provided share similar characteristics.

### **Ongoing and Planned Initiatives**

The Commission will shortly launch a study on **credit intermediaries** in order to analyse the EU credit intermediation market, to review the framework in which intermediaries operate and to examine any possible consumer detriments. On the basis of this study, the Commission will examine whether it is necessary to propose an appropriate European legal framework.

The **Insurance Mediation Directive**<sup>66</sup> will be reviewed to make sure it is achieving its objectives of protecting consumers while promoting the single insurance market. As a first step, the Commission has asked CEIOPS to look into the way the Directive has been implemented. This report will be used as a basis for a possible revision of the Directive in 2008-2009.

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<sup>65</sup> The pensions framework in the EU is commonly characterised by a three pillar structure which is also often used during debates and discussions at European level: Pillar 1: statutory social security systems; Pillar 2: occupational pension schemes; Pillar 3: voluntary individual pension savings. The three pillar typology generally reflects the different legal characteristics of the three pillars, although Community texts covering pensions do not refer formally to the pillars.

<sup>66</sup> Directive 2002/92/EC.

The **White Paper on Mortgage Credit** will address the question of ensuring high-quality independent advice for consumers.

## 5. CONCLUSION

- (42) This Green Paper seeks to strengthen and deepen our understanding of the problems faced by consumers and industry in the field of retail financial services, as well as to establish the scope for and impediments to further initiatives in this area. The consultation is open until 16 July 2007. Unless indicated otherwise, all responses to the consultation will be published on the Commission website at [http://ec.europa.eu/internal\\_market/finservices-retail/policy\\_en.htm](http://ec.europa.eu/internal_market/finservices-retail/policy_en.htm).
- (43) The Commission will organise a hearing on 19 September 2007 to draw the conclusions of the consultation launched by this Green Paper and discuss with all stakeholders which initiatives are needed to bring about a more efficient internal market for retail financial services.
- (44) The results of this extensive consultation process will be incorporated into the Single Market Review report to be published in the autumn.

- (1) Do you agree with the objectives and priorities set out in this paper?
- (2) Are there issues that are not covered in this Green Paper, which are important for the integration of retail financial markets and to which the Commission's attention should be drawn? For example, are consumers in their everyday life confronted with requirements or limitations from either financial services providers or other stakeholders (employers, social security, administrations, businesses, etc.) which restrict their ability to use cross border financial services (such as an obligation to have a bank account or insurance policy in one specific country, etc.).
- (3) The Commission has undertaken several initiatives to improve consultation with consumers and to secure their input into its policy making. Should further steps be taken and, if so, what steps?
- (4) Is consumer choice unnecessarily limited by restrictions on the providers and channels through which they access retail financial services. What are, in your experience, these restrictions?

- (45) This paper presents the actions currently being undertaken to bring the benefits of integrated EU financial market to users, and requests feedback from stakeholders on the direction being taken. However, building on work to date, the Commission believes that there is scope for more action to ensure that European retail financial services markets reach their potential and to ensure that citizens reap the benefits of a single market. The Commission wishes in particular to receive feedback on the following specific issues.

- (5) Despite efforts, in particular the creation of FIN-NET, the handling of **cross-border consumer complaints** in the field of financial services still remains problematic. The Commission would welcome input as to the ways to improve the current situation. For example, should Member States be obliged to ensure that alternative dispute resolution (ADR) schemes are in place? Should providers be obliged to adhere to an ADR scheme? Should they be contractually obliged to offer ADR mechanisms to their clients?
- (6) The creation of the **Single Euro Payments Area (SEPA)** offers challenges and opportunities for businesses and consumers alike. What do stakeholders think of SEPA's impact on consumers? Should consumers be more involved in the governance and the preparation of SEPA?
- (7) With view to the launch of its study on **credit intermediaries**, later this year, the Commission would like to know whether stakeholders believe the current legislative framework to be sufficient and if consumers face any particular problems in dealing with credit intermediaries, particularly on a cross-border basis.
- (8) The Commission believes that it has an important role to play in developing a competitive, open and effective market for **long-term savings, retirement and pension** schemes that meet consumers' needs. Do stakeholders agree and how could the Commission contribute? Could an optional legal EU-wide regime ("28th regime") for savings and/or 3rd pillar pension products be envisaged?
- (9) Do you think that there could be benefits for both banks and consumers, if banks would have the opportunity to offer an **optional simplified standardised product**, which would have a good level of consumer protection, would be easy to understand, and could be offered across borders without the need to be modified to fit local rules?
- (10) The Commission believes that more could be done to improve **consumers' financial literacy and capability**. Possible measures include developing guidelines or promoting best practices. The Commission would welcome input on how this policy should be further developed at the European level.
- (11) Do you think that, as they stand, the provisions on **consumer information** contained in financial services directives are adequate and consistent with one another? Were it not the case, how could the Commission ensure that information requirements are set at the right level, ensuring proper information but without creating any overload? Do you think that informing consumers is sufficient or that **advice** should also be provided? If yes, should that be compulsory or on request?

- (12) Measures to improve lenders' access to **credit data** will be discussed in the context of the forthcoming White Paper on Mortgage Credit. The Commission believes that more could be done to promote the accessibility of credit data, in particular on a cross-border basis. Who should be able to access consumer credit data? How could the cross-border transferability of consumer credit data be improved, ensuring in particular that mobile credit data follows increasingly mobile consumers? Could a memorandum of understanding, ensuring smooth data circulation between credit bureaus, be a workable solution?
- (13) Fragmentation of **retail insurance markets**, for example in the field of motor insurance, does not allow consumers to reap full benefits of EU integration in this area. Do you think that more should be done at EU level to address this fragmentation?
- (14) **Customer mobility** and competition are closely associated. The Commission would welcome input as to how customer mobility could be enhanced. In particular, in the field of bank accounts, and as a follow-up to the Expert Group's work, would stakeholders see merits in, for example, having EU wide account switching arrangements? Will SEPA have an impact on customer mobility?