

Studies in Focus: Mis-selling of Financial Products

Background

Consumers of financial services in the European Union (EU) have been affected by numerous mis-selling cases in recent years, in particular in the aftermath of the financial crisis. Mis-selling may be defined as a practice of misleading the customer while selling a financial product, eventually resulting in consumer detriment. Such unlawful practices carried out by financial institutions have been widespread in the sense that they simultaneously affected a large number of consumers and occurred in a variety of financial products. This has led not only to great losses for retail investors and borrowers, but also to a deterioration of trust in financial institutions and supervisory bodies.

In recent years, EU legislation in this area has made great strides to better protect consumers, particularly with the adoption of the Markets in Financial Instruments Directive and Regulation (MiFID II/MiFIR), applicable since 3 January 2018. Nevertheless, challenges remain both in preventing the recurrence of mis-selling but also in finding adequate ways for consumers to seek compensation for past cases.

Since the years of the financial crisis, the European Parliament has received a number of petitions and complaints regarding alleged cases of mis-selling of financial products.

Focus of the studies

Against this background, the European Parliament's Committee on Economic and Monetary Affairs (ECON) has requested five studies to gain a better understanding of recent cases and remedies associated with selected questions of mis-selling of financial products in the EU.

The overarching objective is to analyse the causes of complaints and petitions made in the view of the existing EU regulation of the conduct of business of financial institutions when they offer financial products to retail investors. The studies also provide an assessment of the most imminent problems, and explain how and to which degree EU standards in this area were implemented. The five studies cover the following thematic areas:

- **Subordinated debt** and other junior liabilities, including the issue of self-placement;
- **Mortgage credit** and related products, including 'floor rate' clauses and cross-currency loans;
- **Marketing, distribution and sale of financial products** regulated under MiFID, UCITS, or AIMFD as well as endowment insurance products, including the respect of the 'best interest' principle, 'closet indexing' practices and the obligation to publish benchmarks laid down in MiFID;
- **Consumer credit** products (apart from mortgage credit);
- **Belgium case study**: compensation of investors subject to mis-selling.

Key findings

Subordinated debt and self-placement (Pierre-Henri Conac, University of Luxembourg)

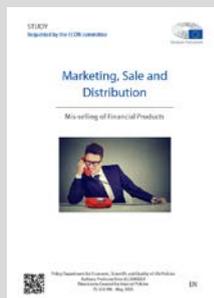


The focus of this document is mis-selling of subordinated debt and other junior liabilities and weaknesses of MiFID. This report concludes that the mis-selling, essentially through self-placement, was due to violations of MiFID rules rather than weaknesses of the legislative scheme. The report includes proposals to strengthen the legislation and to provide compensation for retail investors.



Mortgage credit (Fernando Zunzunegui, Universidad Carlos III de Madrid)

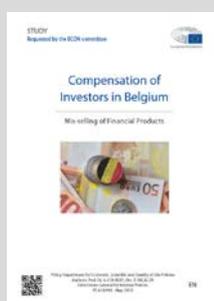
The mis-selling of mortgage loans that include floor clauses, foreign currencies (forex) clauses and related products is the subject of this research. The paper analyses the context, the handling of the problem in the most affected Member States (Croatia, Hungary, Poland, Romania and Spain) and its compatibility with EU law. It concludes with recommendations.

Marketing, distribution and sale of financial products (Kern Alexander, University of Zurich)

The study reviews the EU legislative and regulatory framework for the marketing, sale and distribution of financial products to assess whether post-crisis EU regulatory reforms have met their objectives and, if not, what are the gaps and weaknesses in the current EU regulatory approach. The EU follows a sectoral approach to regulating the marketing and sale of financial products, which results in segmentation and arbitrage risks. The paper argues that the European Supervisory Authorities should adopt more harmonised regulatory and technical standards to reduce these risks and ensure more effective enforcement by Member State authorities.

Consumer credit (Olha Cherednychenko and Jesse Meinderstma, University of Groningen)

Retail financial markets across the EU have been upset by large-scale mis-selling of financial products to consumers. As part of a series of five studies on this topic, this paper examines the problem of mis-selling with a particular focus on consumer credit. It identifies the most problematic products and practices in consumer credit markets that may cause consumer detriment and shows some important limitations of the current EU regulatory framework for consumer credit in providing adequate consumer protection.

Belgium case study: compensation of investors (Veerle Colaert and Thomas Incalza, KU Leuven University)

The paper analyses three important and highly publicised cases of mis-selling of investment products to retail clients, featuring interesting legal particularities: the Citibank case, the Dexia case and the Fortis case. On the basis of this analysis, the paper draws a number of conclusions on the national and EU regulatory framework in respect of investor compensation.

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