

5 February 2018

Ms. Verena Ross
Executive Director
European Securities and Markets Association (ESMA)
CS 60747, 103 rue de Grenelle
75345 Paris Cedex 07 France

Via Response Form Re: Call for Evidence on Potential Intervention Measures for Contracts for Differences / Binary Options to Retail Clients

Dear Ms. Ross:

Financial Planning Standards Board Ltd.'s (FPSB¹) European member organizations (collectively, FPSB Europe) are pleased to respond to ESMA's call for evidence on potential product intervention measures on contracts for differences and binary options for retail clients (ESMa35-43-904). FPSB Europe consists of eight nonprofit professional financial planning bodies, including:

- 1) Österreichischer Verband Financial Planners (Austria)
- 2) Association Francaise des Conseils en Gestion de Patrimoine Certifies (France)
- 3) Financial Planning Standards Board Deutschland (Germany)
- 4) Financial Planning Standards Board Ireland
- 5) Federatie Financieel Planners (The Netherlands)
- 6) Swiss Financial Planners Organization (Switzerland)
- 7) Finansal Planlama Derneği (Turkey)
- 8) Chartered Institute for Securities & Investment (United Kingdom)

Established in 2004, FPSB's mission is to benefit the public by establishing, upholding and promoting worldwide professional standards in financial planning. Working through our member organizations, represented in Europe by the organizations above, FPSB and its member organizations develop, promote and enforce internationally consistent, locally relevant standards so that:

- The public can identify qualified, competent and ethical financial planners;
- Practitioners can distinguish themselves as qualified, competent and ethical financial planning professionals; and
- Consumers, regulators and other key stakeholders can have confidence in the financial planning profession and in financial planning professionals, and recognize the benefits financial planning offers to individuals and society.

¹ FPSB manages, develops and operates certification, education and related programs for financial planning organizations to benefit the global community by establishing, upholding and promoting worldwide professional standards in financial planning. FPSB demonstrates its commitment to excellence with the marks of professional distinction – CFP, CERTIFIED FINANCIAL PLANNER and CFP Logo Mark. FPSB has a nonprofit member organization in the following 26 territories: Australia, Austria, Brazil, Canada, Chinese Taipei, Colombia, France, Germany, Hong Kong, India, Indonesia, Ireland, Israel, Japan, Malaysia, New Zealand, the Netherlands, the People's Republic of China, the Republic of Korea, Singapore, South Africa, Switzerland, Thailand, Turkey, the United Kingdom and the United States. For more, visit fpsb.org.

FPSB owns the international CERTIFIED FINANCIAL PLANNER certification program outside the United States, and has licensed the member bodies of FPSB Europe to oversee the administration, promotion and enforcement of CERTIFIED FINANCIAL PLANNER certification in Europe.

CERTIFIED FINANCIAL PLANNER professionals meet rigorous competency, ethics and practice standards, qualifying them to develop financial planning strategies that assist clients in achieving their financial and life goals. CERTIFIED FINANCIAL PLANNER professionals are part of a growing global community of financial services practitioners who place clients' interests first as part of their commitment to financial planning professionalism, and who embrace FPSB's Code of Ethics and Professional Responsibility and Financial Planning Practice Standards.

As of 31 December 2017, there were over 175,500 CFP professionals in 26 countries and territories worldwide, with over 9,000 CERTIFIED FINANCIAL PLANNER professionals certified by the members of FPSB Europe.

About FPSB's Standards

FPSB's standards are based on a global framework that includes empirical research of the abilities, professional skills and knowledge needed to practice financial planning. FPSB and its member organizations have developed initial education, assessment, experience and ethics requirements, as well as continuing professional development standards for financial planning professionals globally. FPSB Europe's member bodies have localized these global standards and certification requirements for applicability in each of their territories, and maintain the relevancy of these standards through regular analyses of the practice of financial planning in Europe.

What is Financial Planning?

FPSB and its member organizations define financial planning as the process of developing strategies to assist clients in managing their financial affairs to meet life goals. The process of financial planning involves reviewing all relevant aspects of a client's situation across a large breadth of financial planning activities, including interrelationships among often conflicting objectives. At the end of the financial planning process, a financial planner may or may not recommend products to a client.

Although financial planning is gaining prominence as a professional practice globally, people who call themselves financial planners often do so with little or no training or oversight. FPSB seeks to position financial planning oversight and models of professionalism within, or adjacent to, existing or proposed regulatory frameworks, whereby regulators and professional financial planning bodies work together to protect and benefit consumers.

FPSB Europe's Point of View

FPSB Europe's response to ESMA's call for evidence is provided through the rubric of financial planning – a client-centric, process-driven professional practice that can help (re)build trust and restore the public's confidence in the marketplace and financial intermediaries. If you have any questions on our submission, or would like additional information, please feel free to contact us at +31-06-30-024-862 or marc.van.poeteren@ffp.nl or +1-720-407-1902 or nmaye@fpsb.org. We appreciate the opportunity to participate in ESMA's comment process.

Respectfully submitted,



Marc Van Poeteren
Chairperson
FPSB Europe



Noel Maye, CAE
Chief Executive Officer
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cc: Otto Lucius, Director, Österreichischer Verband Financial Planners
Raymond Leban, Chairman, Association Francaise des Conseils en Gestion de Patrimoine Certifies
Rolf Tilmes, Chairman, Financial Planning Standards Board Deutschland
Paul Grimes, CEO, Financial Planning Standards Board Ireland
Sjaak de Graaf and Rob van den Aker, acting managing directors, Federatie Financieel Planners
Markus Streule, Director, Swiss Financial Planners Organization
Murat Ergin, Director, Finansal Planlama Derneği
Jacqueline Lockie, Head of Financial Planning, Chartered Institute for Securities & Investment

ESMA Call for Evidence on Contracts for Differences (CFDs) / Binary Options (BOs) to Retail Clients

Financial Planning Standards Board Ltd.'s European member organizations (collectively, FPSB Europe) will respond to ESMA's Call for Evidence in our capacity as organisations representing the public interest. Consequently, we will focus our feedback on **Question I: What impact do you consider that the envisaged measures would have on retail investors?**

General Statement

A European study² recognized that while limited financial literacy or asymmetric information may contribute to a customer's inability to make sound decisions about increasingly complex retail financial products, other factors, such as limited time to fully understand the products, processes of persuasion, personal interaction and trust play a role in decision-making. The report asserts that belief formation can be subject to framing effects or biases, such as overconfidence.

A September 2017 Bloomberg article³, Ronaldo Is Hawking One of the World's Riskiest Derivatives, described how CFD investors in Spain lose money 82% of the time. According to a Comision Nacional Del Mercado de Valores study, 31,000 investors in Spain lost 142 million euros over a 21-month period ended in September 2016, including transaction costs. In 2014, the French Autorité des Marchés Financiers highlighted findings showing that nine out of 10 French investors in retail CFD products lost money, with average losses over four years of nearly €11,000.⁴ ESMA's call for evidence document itself cites studies showing that between 74 and 89% of clients trading in CFDs/BOs lose money.

CFDs are a valid investment tool, and some collective investments or investment trusts (such as closed-end investment companies) use them in portfolios that are sold to retail investors. A key issue is with how retail investors use CFDs or more appropriately, how retail investors are enticed to use them, and then (in the majority of cases) lose from them.

FPSB Europe is concerned that the aggressive marketing and incentives offered during distribution of these products fail to adequately describe, in a way understandable to retail investors, the inherent risk of rapid, large and unexpected losses (amplified by leverage) that can result from investing in CFDs/BOs. How these products are marketed and sold in Europe at present appears to mask the fact that the vast majority of retail clients trading in CFDs/BOs lose money.

² Chater, Huck and Inderst. Consumer Decision-Making in Retail Investment Services: A Behavioural Economics Perspective. November 2010.

³ "Ronaldo Is Hawking One of the World's Riskiest Derivatives," 20 September 2017, www.bloomberg.com/news/articles/2017-09-21/ronaldo-touts-500-1-leverage-derivatives-that-regulators-loathe

⁴ 2014 Autorité des Marchés Financiers Study of Investment Performance of Individuals Trading in CFDs and Forex in France, www.amf-france.org/en_US/Actualites/Communiqués-de-presse/AMF/annee_2014.html?docId=workspace%3A%2F%2FSpacesStore%2F96c52a14-3900-464f-8fff-7d4700ff37e3

FPSB Europe is concerned that many European retail investors are making investment decisions absent a sufficient duty of care from intermediaries, absent specialist advice in the nature and risks inherent in retail CFDs, and absent a defined goals-based approach to investing. All investment advisors, financial advisors and financial planners who provide investment products or guide investing decisions should properly assess the suitability of a given investment in the context of each client's goals, needs and objectives, and provide products and services in their clients' best interest (ideally with a fiduciary level of care).

FPSB Europe recommends that ESMA's intervention measures for CFDs/BOs expand on the best execution obligations contained in Article 21 of the MiFID Implementing Directive (that investment firms take all reasonable steps to obtain, when executing orders, the best possible result for their clients) to ensure that retail CFD providers and advisors are suitably qualified to guide investors on investment decisions and to address the fiduciary duty an investment firm owes its clients. FPSB Europe supports the notion that an investment firm or investment advisor should place the interest of the client first, at all times acting honestly, with the utmost good faith, and in a manner the advisor reasonably believes to be in the best interest of the client. This would involve being able to reconcile the concentration of risk and potential for loss inherent in CFDs/BOs with a client's current financial position and overall financial objectives.

Retail clients deserve to have the highest level of protections in place regarding duty of care, required disclosures and management of conflicts when it comes to complex investment products. The over 9,000 CERTIFIED FINANCIAL PLANNER professionals conducting business in eight European and neighboring countries (i.e., Austria, France, Germany, Ireland, the Netherlands, Switzerland, Turkey and the U.K.) meet knowledge, skills and abilities requirements based on the FPSB Financial Planner Competency Profile, along with ethical and professional conduct obligations to put the client's interest first.

FPSB welcomes ESMA's desire to have increased attention by supervisors in the areas of Contracts for Differences (CFDs) and binary options (BOs), and urges ESMA, under Article 40 of Regulation (EU) 600/2014 (MiFIR), to extend its product intervention powers for CFDs/BOs as follows:

i. Prohibition or Restriction of CFDs for Retail Investors

FPSB supports ESMA's desire to protect consumers by restricting how CFDs are marketed and sold to retail investors in Europe. While FPSB Europe supports the principle that investors be empowered and able to make their own investment choices, the outcomes for investors in retail CFDs to date demonstrates a mismatch of intent by the investors and the CFD providers. In the interest of strong consumer protection, FPSB Europe recommends that in addition to the restrictions that ESMA is proposing on the provision of CFDs to retail investors in Europe, ESMA consider adding restrictions on the qualifications of those providing or advising on retail CFDs. Additionally, FPSB Europe recommends that ESMA adopt an approach similar to the U.K. Financial

Conduct Authority proposal⁵ to introduce conduct standards for best execution that require CFD manufacturers/distributors to assess a target market for retail CFD products, and to take steps to ensure these CFD products are distributed appropriately, reviewing distribution and product performance to ensure it remains appropriate for the retail investor segment being targeted.

While FPSB Europe understands that ESMA is likely to omit “professional clients” from any such restrictions due to (as yet) a lack of evidence of harm to this type of client, classifying an investor as “retail” or “professional” based on characteristics such as net worth, investment experience or previous exposure to complex CFD products, may be misleading. A client’s wealth level is not a direct correlation to financial sophistication, nor is a client’s sophistication level necessarily fixed or equivalent across all complex products.

Restriction of “Non-Cryptocurrency” CFDs: Leverage Limits

If we start with the premise that the vast majority (70-90%) of retail investors lose money on CFD investments, and don’t understand (or are not adequately informed of) the risk of loss involved, then as Quinn Perrott, Owner, TRAction FinTech, assessed in his blog⁶, one could argue that lowering leverage may not save investors from losing money, it may simply take investors longer to lose the money. As previously stated, FPSB Europe recommends that restrictions on the provision of CFDs to retail investors in Europe include stricter leverage limits as proposed by ESMA. FPSB Europe also proposes adding restrictions on the qualifications of those providing or advising on retail CFDs, introducing a fiduciary (client first) level of care to clients and requiring CFD manufacturers and distributors to assess a target market for their retail CFD products and to take steps to ensure these CFD products are distributed appropriately, reviewing distribution and product performance to ensure it remains appropriate for the retail investor segment being targeted.

Restriction of “Cryptocurrency” CFDs: Leverage Limits

Using leveraged derivatives such as CFDs to trade unregulated and ultravolatile cryptocurrencies compounds the level of risk and the speculative nature of CFD investments for retail investors. Given the immature and largely unregulated nature of the cryptocurrency CFD market in Europe, and the potential for substantial offshore trading activity, FPSB Europe recommends that ESMA prohibit Cryptocurrency CFDs for retail investors, while adopting an approach similar to the U.S. Securities and Exchange Commission (SEC).

“The SEC has urged the securities industry to address ‘significant investor protection issues’ before offering cryptocurrency-related products, cryptocurrency ETFs (exchange-traded funds) in particular, to retail investors (citing, among other things, the risk of potential market manipulation of the

⁵ Financial Conduct Authority Consultation Paper, Enhancing Conduct of Business Rules for Firms Providing Contract for Difference Products to Retail Clients,” www.fca.org.uk/publication/consultation/cp16-40.pdf

⁶ <https://financefeeds.com/fca-rulings-cfds-lambasted-lowering-leverage-wont-save-clients-losses-says-regulatory-technology-expert-quinn-perrott/>

assets).” The SEC’s director of the Division of Investment Management went on to say, “Until the questions identified can be addressed satisfactorily, we do not believe that it is appropriate for fund sponsors to initiate registration of funds that intend to invest substantially in cryptocurrency and related products, and we have asked sponsors that have registration statements filed for such products to withdraw them.”⁷

ii. Margin Close-Out Rule on a Position-by-Position Basis

iii. Negative Balance Protection

Retail investors are attracted to CFDs because investors tend to focus almost exclusively on the upside of leverage – for a low initial capital input (sometimes as little as 1%), the return can be outstanding (100%). Sadly, the reverse is equally true and apparently more relevant – without sufficient protection on the downside, CFD investors (potentially nine out of every 10) experience the double-edged sword of leverage, and get wiped out by ending up owing more than they invested in the product. FPSB Europe recommends that the provision of CFDs to retail investors be restricted in Europe.

Margin Close-Out: FPSB Europe appreciates, and is supportive of, ESMA’s proposal to have a margin close-out rule on a position-by-position basis to protect retail investors from losing more than what they have invested, and to make it easier for retail investors to understand their exposure to each individual CFD. However, as indicated by the G20/OECD INFE Report on Adult Financial Literacy in G20 Countries⁸, “the way in which people are choosing financial products is a particular concern with only 15% of respondents in G20 countries choosing a product with the help of independent advice or information.” The OECD report goes on to say that, “Policy makers and product providers need to: ... strengthen efforts to ensure that the provider-specific information especially for complex products is timely, clear, not misleading and tested with consumers; make it easier for people to access to high-quality independent information and access impartial product comparison tools (possibly using digital tools); and support the development of appropriate financial advice especially for complex products ...”⁹ FPSB Europe recommends that ESMA stipulate that retail investors accessing complex products such as CFDs have input from competent, ethical financial advisors or financial planners, who will put the client’s interests first.

Negative Balance Protection: FPSB Europe believes that ESMA’s rationale to support negative balance protection on a “per account” basis rather than a “per position” basis “so as not to increase the impact on firms and on the ongoing prices offered to clients” falls short of an appropriate level of consumer protection for retail investors investing in CFDs. By offering the protection on a “per position basis,” investors with positions in multiple CFDs could be alerted to the failure rate of each position at the earliest opportunity, and have the ability to

⁷ <https://cryptovest.com/news/allay-investor-fears-before-launching-crypto-etfs-sec-tells-securities-industry/>

⁸ www.oecd.org/daf/fin/financial-education/G20-OECD-INFE-report-adult-financial-literacy-in-G20-countries.pdf

⁹ Page 53, Ibid.

shut down remaining CFD positions, rather than finding that the overall account of CFDs was valued at zero, with no ability to salvage some of the investments.

iv. Restriction on Incentivisation of Trading

FPSB Europe is not sure what ESMA is proposing – if the recommendation is to restrict payments or non-monetary benefits during marketing, sale or distribution of CFDs, what is the proposed restriction? FPSB Europe recommends that CFD providers be prohibited from providing retail clients payments or non-monetary benefits as enticements to invest in these high-risk, complex products.

v. Standardized Risk Warning

FPSB Europe supports a requirement that CFD providers be required to provide standardized warnings in any communication to retail investors (and would add to “professional investors” too). Rather than ESMA’s proposal to have a more abbreviated risk warning for media other than durable media or webpages, FPSB Europe proposes a risk warning for retail (and professional) investors that is short, comprehensible and unambiguous for all media. If investors are fully aware of the failure rate of investments in retail CFDs, and continue to invest in them (after possibly experiencing one large investment return), the content of warnings and disclosures for retail CFDS may need to align with research into the cognitive biases that enable gamblers to understand the low probabilities of winning, yet to believe that they may still have a chance to win.

Research suggests that effectively communicated knowledge does not modify irrational beliefs or erroneous estimations of the chances of winning.¹⁰ Rather than a firm-centric message of “the percentage of client accounts that were loss-making and profit-making based on the firm’s data from previous quarters,” ESMA might consider developing “self-appraisal messages, which are particularly relevant for gambling as research shows that having accurate knowledge of gambling probabilities and understanding games does not influence gambling behaviour. ... Messages encouraging self-appraisal (e.g., “Have you spent more than you intended?”) had a significantly greater reported effect on thoughts and behaviours than informative messages.”¹¹

In Relation to BOs

FPSB Europe supports the prohibition on the marketing, distribution or sale of binary options (BOs) to retail clients.

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¹⁰ Journal of Business Research Optimal Content for Warning Messages to Enhance Consumer Decision Making and Reduce Problem Gambling, www.sciencedirect.com/science/article/pii/S0148296315001216

¹¹ Ibid.