Thematic review on reporting the costs of investment services and products to the clients

Content

Writers

Merja Junnonen/merja.junnonen(at)finanssivalvonta.fi

Esa Pitkänen/esa.pitkanen(at)finanssivalvonta.fi

Riitta Seppä/riitta.seppä(at)finanssivalvonta.fi

1 Background, objectives and conclusion of the thematic review

1.1 Background of the thematic review

In 2022, the Financial Supervisory Authority (FIN-FSA) conducted a thematic review on the reporting of the costs of investment services and products to clients. The thematic review is part of a Common Supervisory Action (CSA) coordinated by the European Securities and Markets Authority (ESMA).

1.2 Objectives and method of implementation of the thematic review

The objective of the thematic review was to assess whether credit institutions providing investment services and investment firms (hereinafter “firms”) comply with disclosure obligations concerning costs and charges as well as inducements (so-called ex-post disclosure of costs). The objective of regulation concerning cost reporting is to ensure that clients receive adequate and clear information from firms on costs related to investment services and financial instruments on an annual basis. The thematic review focused on cost reporting provided to non-professional clients with an at least annual frequency.

In addition to the part on cost reporting, the FIN-FSA assessed the firms’ additional services or higher-level services involving inducements.

The thematic review was conducted through a written survey of selected firms which submitted, in addition to their responses, a sample consisting of five clients’ cost reports (anonymised) for assessment by the FIN-FSA, as well as their related internal guidelines. Some discrepancies were found between the responses and sample reports submitted by the firms to the FIN-FSA. Thematic reviews at the FIN-FSA are primarily conducted in writing without engaging in closer discussion with the firms.

Firms responding to the thematic review will be provided firm-specific findings of the review, which enable them to evaluate the need for any remedial actions and to submit their feedback to the FIN-FSA for a final assessment. The FIN-FSA recommends that also other firms take into consideration findings and FIN-FSA's views and take necessary actions.

In addition, ESMA usually publishes the main findings of supervisory actions coordinated by it, based on thematic reviews conducted in various EU member states, as well as any follow-up actions.

1.3 Summary of the key findings of the thematic review

Time and method of submission of cost report to the clients:

- Two out of eight firms had reported their 2021 costs in the first quarter of 2022.
- Furthermore, three out of eight firms had reported their 2021 costs to the clients by 22 June 2022 (due date of the request for information).
- The majority of the firms submitted cost reports to some of their clients in an online service and to some clients by letter.

Presentation of cost information:

- All but one of the firms reported the cost information as required by regulation, broken down into costs related to investment services and those arising from financial instruments.
- Five out of eight firms categorised the costs using a more granular breakdown required by regulation (one-off charges, ongoing charges, all costs related to the transactions, and costs related to ancillary services).
- The majority of the firms had room for development in how they disclose the effect of costs on return.
- One of the firms provided product-specific cost information in the cost report, while almost all other firms provide product-specific cost information to the client at request.

Cost items to be reported and their calculation:

- The firms identify and report costs and charges related to financial instruments used in services provided by them. However, based on the firms' internal guidelines, the FIN-FSA was unable to ascertain whether they disclose all costs to the clients.

Firms' internal guidelines:

- Only half of the firms submitted their internal guidelines on cost reporting to the FIN-FSA.
- Not all guidelines submitted to the FIN-FSA indicated clearly which costs are reported to the client and how the firm monitors the quality of cost reporting.

Inducements and additional services:

- All but one of the firms disclosed inducements received by them in the cost report.
- Some of the firms could define additional services in more detail. Two firms could be more specific in their guidance on inducements, while three firms lacked relevant guidelines altogether.

1.4 Regulatory background

Since 2019, firms providing investment services have been required to report costs and charges incurred by their clients on investment products and services and at the client's request.

The obligation is based on the MiFID II Regulation[1], which entered into force in 2018. One of the objectives of the Regulation is to ensure that clients receive information on all costs related to investment services and financial instruments both before acquiring a service and during the client relationship. The information must be provided on a client-specific basis so that the client may understand the costs applicable to the investments being offered or acquired and to the relevant investment amount and can compare different services and financial instruments based on this information.

1.5 Background information on the firms responding to the survey

Based on the criteria established by ESMA, the FIN-FSA selected eight firms (investment firms and credit institutions providing investment services) to respond to a thematic review survey and submit a sample consisting of five of their clients' cost reports for review by the FIN-FSA. In addition to ESMA's criteria, the sample selection reflected information from transaction reporting on the extent and nature of dealing by each firm, as well as the FIN-FSA's recent supervisory actions targeted to them.

The thematic review comprised an assessment of cost reports submitted by banks and investment firms on costs and charges for 2021 relating to the provision of investment service or the transmission of orders on behalf of non-professional clients. The thematic review did not address for example costs reported to asset management clients.

The product range of the firms selected to the thematic review varied from a wide range to a very narrow one. In the thematic review, information was requested on costs and charges concerning the following financial instruments: Finnish UCITS and non-UCITS funds, foreign UCITS, shares subject to public trading, plain vanilla bonds, structured products, and financial instruments denominated in other currencies than the euro.

2 Time and method of submission of the cost report

2.1 Criterion

Information on all costs and charges shall be provided to the client on a regular basis, at least annually, during the life of the investment.[2]

The provision of investment service and ancillary services shall be carried out honestly, fairly and professionally, in accordance with the best interests of the client.[3]

---

[1] Act on Investment Services 747/2012 (hereinafter '"Investment Services Act"'; chapter 10, sections 5 and 6, MiFID II Delegated Regulation 2017/565 (hereinafter "MiFID II Delegated Regulation") recitals 78–79 and Articles 50(2), 50(3) 50(4) 50(9) and 50(10), Annex II and ESMA Q&A on MiFID II and MiFIR investor protection and intermediaries (ESMA35-43-349) Q&A; hereinafter "ESMA Q&A") chapters 9 and 12.8 and PRIIPs Delegated Regulation 2017/653 (hereinafter PRIIPs Delegated Regulation, Annex VI).

[2] Chapter 10, section 5(4) of the Investment Services Act.

[3] Chapter 10, section 2(1) of the Investment Services Act.

2.2 Findings

By 22 June 2022, the due date for responses to the thematic review, five firms had reported the costs charged in 2021 to all clients; two firms had reporting in progress, and one had not yet started it at all. Table 1 indicates the closing date of cost reporting for 2020 and 2021 or the anticipated closing date of reporting for 2021.

All eight firms had reported the cost information for 2020 to their clients.

None of the firms submits a cost report more often than once a year.

The majority of the firms submits the information to some of its clients in the online service and to some clients by letter. Most of the firms do not send a separate notification to the client on a report provided in the online service (Table 2).

Table 1. Submission of cost reporting (closing date)

Quarter (Q) in which cost information was or is expected to be reported	Number of firms	
	2020 costs	2021 costs
Q1	2	2
Q2	2	3 + 2*
Q3	2	0
Q4	2	1

*The firm has commenced reporting but not completed it by 22 June 2022.

Table 2. Method of communication

Method of communication	Number of firms (several choices allowed)
Online service, notification to the client	2
Online service, no notification to the client	5
E-mail	1
Letter	6

2.3 FIN-FSA's view

The Investment Services Act requires the provision of information to the client at least on an annual basis. Regulation does not determine in more detail the time of submission of the cost report relative to the reporting reference period. Where the ex-post reporting of realised costs is concerned, firms may be required to submit cost reports as soon as possible after the end of the reporting period. The FIN-FSA considers it a good practice to complete reporting within three months of the end of the reporting period.

If cost information is provided in the firm's web service, it should be found easily by the client.

3 Presentation of the cost report

3.1 Assessment of the clarity and understandability of the cost report

3.1.1 Criterion

Information on costs and charges related to investment services and products shall be provided to the client in an aggregated form on a regular basis, at least annually.[4] The cost information may be presented either as a standalone document or within another document, provided that the information can be found easily by the client and is presented prominently.[5]

3.1.2 Findings

All firms reported they provide the cost report as a standalone document. All firms reported they also provide the client with instructions on how to read the report. One firm's cost report provided explanations related to costs as footnotes instead of separate reading instructions. All respondents submitted to the FIN-FSA a sample consisting of five of their clients' cost reports.

Six firms self-assessed their cost reports as clear and understandable, but two firms considered their cost reports partly clear and understandable. The reasons cited were challenges faced by some clients with the interpretation of regulation and difficult terminology, which had given rise to questions from the clients about the cost reports.

According to the FIN-FSA's assessment, the cost reports were in most respects adequately clear and understandable, despite certain identified shortcomings. Regulation does not determine any unambiguous reporting template; the room for interpretation allowed by regulation was shown as very diverse ways of implementation. Clarity and understandability are also somewhat subjective concepts, making the implementation options prone to divide opinions.

3.1.3 FIN-FSA's view

The cost report must be clear and easily understandable, and it may not be misleading due to the complexity or manner of presentation of the information.

The FIN-FSA recommends that the cost report includes clear reading instructions and consistent terminology. In the reading instructions and specific explanations, attention must be paid to the clarity and understandability of the cost report as a whole. The presentation of costs must also reflect the nature of the investment services and the degree of complexity of the cost structure of the products. The more complex cost structure is involved, the clearer and more comprehensive reading instructions are necessary.

---

[4] Chapter 10, section 2(2) and chapter 10, section 5(4) of the Investment Services Act.
[5] ESMA Q&A 9.33.

3.2 Breakdown of information presented in the cost report

3.2.1 Criterion

The cost report submitted to the client shall present costs and charges broken down into costs related to investment services and costs related to financial instruments. In addition, the report shall provide an itemised breakdown of payments received from a third party (inducements). The costs and charges shall be expressed both as cash amounts and percentages.[6]

3.2.2 Findings

All firms reported they break down cost information into investment services (incl. ancillary services) and financial instruments in accordance with regulation. Based on the sample reports submitted, however, one of the firms did not break the information down in this manner.

The firms were requested to specify the most detailed level at which they report the information on overall costs. The firms responded they report the costs as follows:

- five firms report the costs of all investments on an aggregated basis
- one reports costs by financial instrument category (for example all structured products)
- two firms report costs using another grouping: one by financial instrument and the other by client portfolio

None of the firms responded they disclose cost information on every financial instrument (by ISIN code).

Based on the sample reports submitted, one firm presents costs on a product-specific basis for almost all financial instruments. The majority of the other firms disclose cost information in the cost report as an aggregated sum of the costs of all investments.

Six firms responded they report the information both as cash amounts and percentages. One firm responded it reports only some of the costs as a percentage. One firm does not report the percentages.

3.2.3 FIN-FSA's view

The starting point of regulation is the aggregation of realised costs and charges using a certain breakdown and reporting them to the client. Regulation does not determine the more detailed reporting level within each cost item that should be applied to a given investment service or financial instrument. However, the client is entitled to request a more detailed itemised breakdown of these costs and charges (see section 4 More detailed itemised breakdown of the cost information).

The FIN-FSA considers there is no reason not to report more detailed cost information in addition to the summary in the actual cost report, which would eliminate the need for the client to request a more detailed itemised breakdown.[1] A more detailed cost report than an itemised breakdown and a summary of aggregated costs required by regulation is more informative, but in this case, particular attention should be paid to the clarity and understandability of presentation. Based on the sample reports

---

[6] *Article 50(2) of the MiFID II Delegated Regulation and ESMA Q&A 9.13.*

submitted, product-specific (financial instrument-specific) reporting of costs seems clear while enabling a comparison of the costs of different products.

3.3 Illustration of the cumulative effect of costs on return

3.3.1 Criteria

Firms shall provide their clients with an illustration showing the cumulative effect of costs on return when providing investment services. Such an illustration shall be provided both on an ex-ante and ex-post basis. Hence, the cost report must include the following illustrations:

a) cumulative effect of overall costs on return;
b) any cost spikes (fluctuations); and
c) narrative description of the illustration.[7]

3.3.2 Findings

The FIN-FSA has assessed the fulfilment of the requirements based on the responses and sample reports. Where there were discrepancies in the material provided, the finding is based on the sample reports.

<u>Illustration of the cumulative effect of overall costs on return</u>

Five firms illustrate the effect of overall costs on return in their cost report. Three of these firms presented the cumulative effect of costs on return only as a monetary sum (itemised) or as a percentage of returns. One firm described the effect on the return also with respect to future costs, based on the service and assumed holding period of the investments.

Three firms failed to meet the regulatory requirement to present the overall costs as a proportion of return.

<u>Presentation of spikes and fluctuations in costs</u>

Two firms illustrated fluctuations in costs as a graph, and one of them also presented a monthly table. One firm’s cost report shows the fluctuation in costs on a quarterly basis.

Five firms do not illustrate fluctuations in costs in a manner required by regulation.

<u>Narrative description of the effect of costs on return.</u>

Seven firms’ sample reports included a narrative description of the effect of overall costs on return. One firms’ cost reports do not meet the regulatory requirement to include a narrative description of the effect of the overall costs on the return of the investments.

---

[7] *Article 50(10) of the MiFID II Delegated Regulation and ESMA Q&A 9.3.*

Based on the responses and cost reports submitted to the FIN-FSA, two out of the eight firms present the cumulative effect of costs on return in compliance with regulation, also presenting fluctuations in costs and a narrative description of the effect of costs on return.

3.3.3 FIN-FSA's view

Firms should provide the client with information on realised costs in relation to the return and a narrative description of the effect of costs on the return. Fluctuation in costs and cost spikes may be shown in various ways (for example as a table or graphically)[8] and using various frequencies (for example quarterly or monthly).

3.4 Disclosure of inducements in the cost report

3.4.1 Criterion

The prerequisites for receiving inducements and related code of conduct are provided in the Investment Services Act.[9]

The amount of inducements received by the firm from a third party in connection with the provision of investment service shall be disclosed in the cost report either as a separate item or a sub-item under service costs.[10]

If the firm transfers inducements received by it to its clients, the client shall be informed how the inducements are transferred.[11] Inducements transferred to the client may be disclosed in the cost report or another report issued on a regular basis.[12]

3.2.4 Findings

Seven firms responded they receive inducements, while one does not do so. The firms receiving inducements responded they disclose inducements as separate items in the cost reports. However, based on the sample reports submitted, the amount of inducements was not shown in the cost report of one of the firms.

Two out of the firms receiving inducements reported they also pay inducements forward to their clients. One of these firms responded it reports transferred inducements in the cost report and the other professed to do so in other client reporting.

[8] ESMA Q&A 9.2 and 9.3.
[9] Chapter 10, section 6 of the Investment Services Act.
[10] Chapter 10, section 6(3) of the Investment Services Act, Article 50(2) of the MiFID II Delegated Regulation, ESMA Q&A 9.7 and 9.13.
[11] Chapter 10, section 6(3) of the Investment Services Act.
[12] FIN-FSA Regulations and guidelines 7/2018, paragraph 6.2(5).

4 More detailed breakdown of cost information

4.1 Criterion

The firm shall provide an itemised breakdown of costs and charges at the client's request.[13]

The cost items to be disclosed are presented in a table in Annex II of the MiFID II Delegated Regulation (the table is appended to this report). Cost information on both investment and ancillary services as well as financial instruments should be presented as an itemised breakdown including at least the following categories:

- one-off costs
- ongoing costs
- all costs related to the transactions
- any charges that are related to ancillary services and
- incidental costs.[14]

In case a given cost item has not been charged to the client, that item should not be removed from the itemised breakdown, but it should be reported as zero.[15]

The aggregated figures in terms of cash amounts and percentages provided in the cost report shall be consistent and reconcilable with the corresponding cash amounts and percentages reported in the itemised breakdown. Any discrepancies should be explained and justified.[16]

4.2 Findings

Three firms stated they provide the more detailed itemised breakdown information already in the actual cost report. Two firms informed their clients in the cost report of the possibility to request a more detailed itemised breakdown, while three firms did not communicate this possibility.

Five firms that stated they provide the itemised breakdown information in a document separate from the cost report reported having given 1–10 breakdowns of cost information for 2020. The number of breakdowns of cost information for 2021 was not asked separately.

All firms responded they itemise costs in accordance with Annex II of the MiFID II Delegated Regulation (one-off charges, ongoing charges, transaction-related costs, ancillary service costs and incidental costs). Based on the cost reports submitted, seven firms itemise costs in the cost report in accordance with the Annex of the Regulation. However, in providing product-specific information, two firms did not apply the breakdown provided in Annex II.

The manner of presentation of the breakdown information is not determined in regulation, and therefore there was variation in the presentation. However, where a given cost specified in the Annex of the Regulation (such as ongoing costs) had not been charged to the client, this cost item was reported in the itemised breakdowns as zero, with the exception of one firm.

[13] Chapter 10, section 5(4) of the Investment Services Act.
[14] ESMA Q&A 9.13.
[15] Article 50(2) of the MiFID II Delegated Regulation and ESMA Q&A 9.20.
[16] ESMA Q&A 9.33.

One out of the eight firms reported its clients receive more detailed cost information than required in Annex II from the firm's online service, but this claim could not be verified based on the material submitted to the FIN-FSA.

Seven firms reported they itemise charges unrelated to any single transaction as follows (one firm did not answer the question on account of providing the itemised information in the cost report):

- three firms itemise ***custody-related charges***
- five firms itemise charges related to ***investment advice and asset management***
- two firms itemise charges incurred in the ***preparation of separate certificates and reports***
- three firms itemise ***other ongoing charges*** (such as funds' management fees and account servicing fees)

Based on the submitted sample reports and their itemised breakdowns:

- two out of eight firms itemise custodian fees
- charges related to investment advice were not itemised in the sample reports
- none of the sample reports included an itemisation of charges related to certificates and the preparation of reports
- other ongoing charges were itemised in one firm's report.

However, not all of the firms had necessarily reported a zero in the report and the itemised breakdown on the rows for costs which had not been charged. Therefore, it is possible that more firms than those mentioned above actually itemise charges unrelated to any individual transaction.

Seven out of the eight firms considered their itemisation consistent and comparable with the information contained in the cost report. However, the amounts of the aggregated information in one firm's sample report did not match the amounts shown in the itemised breakdowns. The reason for this discrepancy was not given.

Two firms' product-specific breakdowns submitted to the FIN-FSA disclosed costs as a percentage of total portfolio costs.

4.3 FIN-FSA's view

The FIN-FSA considers it good practice to mention in the cost report the client's possibility to receive more detailed breakdown information. If the cost information is provided in an online service, the client could be provided access to the breakdown information as conveniently as possible, for example via hyperlinks[17].

The FIN-FSA finds it informative and clear that the information is presented on a product-specific basis in the itemised breakdown. It would be consistent to apply the categorisation of cost information under Annex II of the Regulation also in the product-specific breakdowns. Furthermore, it would be informative to itemise payments unrelated to any individual transaction.

[17] *ESMA Q&A 9.13.*

5 Producing cost information

5.1 Criterion

In producing cost information, the firm may utilise investment funds' KIIDs and PRIIPs' KIDs. [18] If the firm is unable to obtain the necessary cost information from the abovementioned documents or product manufacturers, it shall assess itself whether it is able to generate an adequately accurate estimate of the cost information for reporting purposes, applying the methodology under the PRIIPs Delegated Regulation.[19]

5.2 Findings

All firms obtained cost information from product manufacturers, and most of them also obtained information from public sources and third parties. Table 3 below shows the reported sources of cost information.

Table 3. Source of cost information	
Source	**Number of firms**
Public sources	5
Direct contact with product manufacturers	8
Third parties	6
Other, what?	0

Four firms reported they had not received relevant cost information from all product manufacturers and not received the information in a timely manner. Several firms cited challenges concerning cost information on ETFs and foreign investment funds. One firm had decided not to report performance-based fees due to data gaps.

5.3 FIN-FSA's view

Cost reporting is regular reporting that recurs at least annually. The FIN-FSA notes that firms should therefore consider and anticipate how to generate the cost information on financial instruments provided by them as efficiently as possible after the reporting period. For example, the descriptions and distribution agreements for new products and services should cover access to information for cost reporting.

[18] Articles 50(4) and 51 of the MiFID II Delegated Regulation and ESMA Q&A 9.9.
[19] ESMA Q&A 9.11.

6 Cost items to be reported

6.1 Criterion

The firm shall disclose to the client all information on costs and charges, including such costs and charges arising in connection with an investment service and a financial instrument that are not caused by the occurrence of underlying market risk.[20] All cost included in the price of the product shall also be disclosed to the client. The background of the principle is that the difference between the price of the position for the firm and the price for the client shall be reported as a cost.[21] Annex II of the MiFID II Delegated Regulation includes a table of costs to be disclosed in respect of investment services (so-called service costs) and a table of costs to be disclosed in respect of financial instruments (so-called product costs).

As regards UCITS funds and PRIIPs, firms shall also disclose other related costs which may not have been included in the KIID/KID as well as costs and charges related to investment services provided by them in connection with said financial instruments.[22] Firms shall request any necessary information from product manufacturers, or if the information is unavailable, estimate UCITS funds' transaction costs until a Key Investor Document (KID) under PRIIPs regulation is prepared for the funds, which includes transaction costs.[23]

6.2 Findings

In the thematic review, the firms were inquired on a financial instrument-specific basis what transaction costs they report to clients in order to ascertain whether all costs, including any implicit ones, are reported to the client.

In their responses, the firms classified costs into explicit and implicit costs in diverse ways. This may reflect the fact that MiFID regulation does not acknowledge this classification[24] and that the firms apply different operating models; for example, some of the firms operate as product manufacturers, while some only act as distributors. Some of the firms deal in financial instruments on own account and some do not. The majority of the firms also highlighted in their response the costs reported on products.

Findings on the reporting of transaction costs by financial instrument category:

- As regards **investment funds**, many respondents stated they report subscription and redemption fees as well as management fees. Based on the sample reports submitted, all firms report the transaction costs incurred by the investment funds, or at least estimated transaction costs. One firm responded it itemises, as an implicit cost, the difference between the price of the firm's position and the price for the client (spread cost) as part of transaction costs.

- As regards **shares subject to public trading**, the firms responded they report mainly brokerage fees and settlement charges. One firm treats foreign exchange costs as implicit costs.

[20] *Chapter 10, section 5(4) of the Investment Services Act, ESMA Q&A 9.12, recital 79 of the MiFID II Delegated Regulation.*
[21] *Recital 79 of the MiFID II Delegated Regulation and MiFID Q&A 9.16 and 9.17.*
[22] *Articles 50(4) and 51 of the MiFID II Delegated Regulation.*
[23] *ESMA Q&A 9.10 and 9.11. The transitional period allowed for UCITS funds in PRIIPs regulation ended on 1 January 2023.*
[24] *In PRIIPs regulation, implicit costs refer to costs embedded in the price of the product, which are not charged separately to the client.*

- As regards **plain vanilla bonds**, some of the firms responded they report the spread and some responded they report transaction fees, brokerage fees or settlement charges.

- As regards **structured products**, all firms stated they report the structuring cost. Five firms also labelled subscription fees as costs in their response. As regards dealing in secondary markets, the firms named the transaction cost, secondary market fee or settlement fees as costs to be reported. With some firms, the content of costs related to secondary markets remained unclear.

Based on the responses and sample reports submitted by the firms, the firms identify and report costs and charges associated with financial instruments used in their services. The firms' responses revealed that half of the respondents did not report foreign exchange costs in the cost report.

About half of the firms did not submit to the FIN-FSA their internal guidelines indicating which costs they report and how they calculate these costs. Therefore, the FIN-FSA was unable to ascertain whether the firms report all costs to the clients.

6.3 FIN-FSA's view

A firm must ensure that all costs required by regulation, including any implicit costs, are reported consistently to the client. PRIIPs regulation defines the cost calculation methods used in the products of its scope. The firms can use these methods also when calculating costs of other products.[25]

The firm must have clear internal guidelines for cost reporting, determining for each financial instrument category the costs to be reported as well as the methods applied to calculating them.

7 Calculation of the cost percentage

7.1 Criterion

In cost reporting, costs and charges shall be reported both as cash amounts and percentages.[26] Regulation does not determine in more specific terms how the value of the investment portfolio or an individual financial instrument should be accounted for in calculating the percentage share of realised costs for reporting purposes.

7.2 Findings

In the thematic review, the firms were asked whether they, in calculating the percentage share of realised costs, they define the value of a financial instrument as an average of daily closing values or monthly closing values or by some other method.

---

[25] *Q&A 9.6, 9.8 and 9.12.*
[26] *Article 50(2) of the MiFID II Delegated Regulation.*

The responses received are presented in the table below.

Table 4.	Number of firms				
Financial instrument category	**Day**	**Week**	**Month**	**Other method**	**Not offered**
Finnish UCITS and non-UCITS funds	4	0	0	3	1
Foreign UCITS	4	0	0	2	2
Publicly traded equities	4	0	0	2	2
Plain vanilla bonds	2	0	0	3	3.
Structured products	3	1	0	3	1

Three firms calculated the value of all financial instruments provided by them by reference to the daily closing values. Other firms reported they apply either another method or the daily value to certain products.

In the “other method” field, firms mentioned for example transaction value and repurchase price. One firm does not, for the time being, report percentages, and therefore it checked the “other method” field.

Four firms’ internal guidelines described the valuation method at least partly. Another four firms’ internal guidelines did not allow for the verification of this kind.

7.3 FIN-FSA’s view

In the absence of more a detailed definition based on regulation, there is no single correct way to determine value for the purposes of calculating the percentage share. The FIN-FSA finds it would be preferable to explain in the report at least what the reported percentage is based on and how it has been calculated. For the sake of consistency and comparability, this matter would call for more specific regulation or additional guidance, for example by ESMA. It is possible that ESMA will provide additional guidance on the matter.

8 Control measures concerning cost reporting

8.1 Criterion

The cost report is a statutory report, and therefore firms are required to have determined adequate internal control measures to comply with the obligations. The measures shall be described at an adequately detailed level in the firm's policies.[27]

8.2 Findings

All firms reported they ascertain, at least by spot checks, that cost reports provided to clients include all information required by regulation and that the information is accurate. Five firms highlighted control measures geared to ensure that the true amount of inducements is disclosed to the clients.

Only four of the firms had defined these control measures in their internal guidelines, while the other firms did not have such measures in place.

8.3 FIN-FSA's view

Firms must specify adequate control measures to ensure the accuracy and timeliness of the reporting of cost information. This requires the firms to have up-to-date guidance on cost reporting and related procedures, also indicating how regulatory compliance is ensured; for example, what actions are considered necessary to ensure the quality of reporting.

9 Additional and higher-level services involving inducements

9.1 Criterion

A firm may pay and receive payments and benefits (inducements) from another person than a client in connection with the provision of investment or ancillary service if the payment or benefit is designed to enhance the quality of the service provided to the client and does not impair compliance with the obligation of the investment firm to act honestly, fairly and professionally in the best interest of the client. However, when providing asset management or investment advice on an independent basis, an investment firm may not receive and retain inducements.[28]

The enhancement of service provided to the client is assessed based on the following three criteria:
1) the service is an additional or higher-level service;
2) the service is specifically focused on the relevant client or client group; and
3) the service is proportional to the level of inducements received by the firm.

FIN-FSA regulations and guidelines 7/2018[29] and ESMA Q&A[30] include examples of services that are acceptable as additional or higher-level services.

---

[27] Chapter 7, section 2(2–4) of the Investment Services Act.
[28] Chapter 10, section 6 of the Investment Services Act.
[29] FIN-FSA regulations and guidelines 7/2018, paragraph 6.3 (10).
[30] ESMA Q&A 12.8.

Firms must maintain an internal list of all inducements received from a third party in connection with the provision of investment and ancillary service and record how the inducements received or paid enhance the quality of service provided to the relevant client. In addition, they must determine what actions they have taken to ensure they are able to act honestly, fairly and professionally accordance with the best interest of the client.[31]

9.2 Findings

In connection with the thematic review, the firms were inquired about additional and higher-level services provided to the client, associated with inducements. Seven firms reported they receive broker fees, commissions, or non-monetary benefits capable of enhancing the quality of service provided to the client.

For example, the firms listed the following as additional services:

- *A wide range of financial instruments* was reported as an additional service. However, being brief, the responses did not indicate in more detail how extensive the offered range is or how actively it is being offered.
- Some of the firms reported they provide investment advice through a *personal investment advisor* or asset manager. Some of the firms offered *investment advice combined* with an annual offer to assess whether the client's previous investments are still suitable.
- It was also common among the firms to report that they provide *regular additional reporting* to the clients to support decision making and monitoring of their investments.
- Some of the firms offer their client various *regular market reviews*, events and seminars, which may be considered to enhance their investment knowledge.
- Some of the firms reported *an extensive branch network, telephone and mobile services and digital investment advice service* as additional services.

In some of the firms, client categorisation was based on the client's amount of assets under management or the service level provided. In some firms, additional service was focused on clients whose investment objectives required a wider range of investment products provided by third parties. One of the firms targeted additional services only to institutional and professional clients, and one firm only at private banking clients.

Two firms had partly deficient internal guidelines on inducements, and three firms lacked relevant guidelines altogether. Some of the firms' guidance concerning inducements listed the kind of inducements received by the firm, but the guidance was not updated in some respects reflecting the additional services reported in the thematic review. The principles of the regulatory criteria were described in the guidance, but the description of the definition of the relevant client or client group was in many cases incomplete. While the assessment and relevant considerations concerning the proportionality of an inducement received and a service were described in the guidance, the description was often limited to a theoretical level.

[31] *FIN-FSA regulations and guidelines 7/2018, paragraph 6.3 (13).*

9.3 FIN-FSA's view

In providing an additional or higher-level service, a firm should consider what services are included in the investment service provided by the firm and what services are provided on top of the normal service and enhance the service for the client. The provision of financial instruments also involves many statutory obligations that cannot be considered additional services. The provision of investment advice in itself is not an additional service, nor does the use of different service channels in the distribution make it an additional service. However, a designated personal investment advisor may make it a higher-level service. Furthermore, the firm's commonly available online or telephone services or branch network cannot be considered additional services since none of the firm's services could be provided without them.

In identifying additional or higher-level services, one should also consider that the service is a genuine additional service, actively targeted to the relevant client. Where a service is limited to a firm's theoretical internal information and has not been brought to the client's attention, it has not been targeted to the relevant client in an adequate manner. The service cannot be considered as an active service if it is offered less frequently than on an annual basis and this kind of service will not necessarily bring sufficient added value to the relevant client. Various digital tools may also meet the criteria of an additional service if they help clients monitor their investments and make related decisions. On the other hand, this kind of services may not necessarily be relevant for clients who prefer to be served by a personal investment advisor. Additional services may also be targeted to a segment of clients defined by the firm if all additional services provided to it may be considered relevant for all clients belonging to this segment.[32]

The provision of non-independent investment advice is based on a more limited number and selection of financial instruments and often to the firm's own products or those of a service provider closely linked with the firm (for example, financial instruments provided by a group company). If this kind of investment advice is provided with an extensive selection of financial instruments suitable for the client, and access to these financial instruments is enabled, this could be considered an additional service. An extensive selection must also include an appropriate number of third-party product providers that do not have close links with the firm. An extensive selection may also be considered an additional service in circumstances where it is offered actively to the client in combination with various value-added tools that help the client take investment decisions or adjust the selection of financial instruments they have invested in.[33]

The firm's guidance should define in more detail how a list of inducements received is maintained, to which clients/client groups additional services are being provided and how they enhance the quality of service provided to such clients. In addition, the firm must conduct a review on a regular basis to ensure regulatory compliance.

[32] *ESMA Q&A 12.8.*
[33] *FIN-FSA Regulations and guidelines 7/2018, paragraph 6.3 (10).*

Appendix: Tables of Annex II of the MiFID II Delegated Regulation

Identified costs that should form part of the costs to be disclosed to the clients[34]

Table 1 — All costs and associated charges charged for the investment service(s) and/or ancillary services provided to the client that should form part of the amount to be disclosed

Cost items to be disclosed		Examples:
One-off charges related to the provision of an investment service	All costs and charges paid to the investment firm at the beginning or at the end of the provided investment service(s).	Deposit fees, termination fees and switching costs[35] .
Ongoing charges related to the provision of an investment service	All ongoing costs and charges paid to investment firms for their services provided to the client.	Management fees, advisory fees, custodian fees.
All costs related to transactions initiated in the course of the provision of an investment service	All costs and charges that are related to transactions performed by the investment firm or other parties.	Broker commissions[36], entry- and exit-charges paid to the fund manager, platform fees, mark ups (embedded in the transaction price), stamp duty, transactions tax and foreign exchange costs.
Any charges that are related to ancillary services	Any costs and charges that are related to ancillary services that are not included in the costs mentioned above.	Research costs Custody costs
Incidental costs		Performance related fees

[34] It should be noted that certain cost items appear in both tables but are not duplicative since they respectively refer to costs of the product and costs of the service. Examples are the management fees (in Table 1, this refers to management fees charged by an investment firm providing the service of portfolio management to its clients while in Table 2 it refers to management fees charged by an investment fund manager to its investor) and broker commissions (in Table 1, they refer to commissions incurred by the investment firm when trading on behalf of its clients while in Table 2 they refer to commissions paid by investment funds when trading on behalf of the fund).

[35] *Switching costs should be understood as costs (if any) that are incurred by investors by switching from one investment firm to another investment firm.*

[36] *Broker commissions should be understood as costs that are charged by investment firms for the execution of orders.*

Table 2 – All costs and associated charges related to the financial instrument that should form part of the amount to be disclosed

Cost items to be disclosed		Examples:
One-off charges	All costs and charges (included in the price or in addition to the price of the financial instrument) paid to product suppliers at the beginning or at the end of the investment in the financial instrument.	Front-loaded management fee, structuring fee[37], distribution fee.
Ongoing charges	All ongoing costs and charges related to the management of the financial product that are deducted from the value of the financial instrument during the investment in the financial instrument.	Management fees, service costs, swap fees, securities lending costs and taxes, financing costs.
All costs related to the transactions	All costs and charges that incurred as a result of the acquisition and disposal of investments.	Broker commissions, entry- and exit-charges paid by the fund, mark ups embedded in the transaction price, stamp duty, transactions tax and foreign exchange costs.
Incidental costs		Performance related fees

[37] *Structuring fees should be understood as fees charged by manufacturers of structured investment products for structuring the products. They may cover a broader range of services provided by the manufacturer.*