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Making the digital market for retail financial services safer for consumers

Finance Watch's key recommendations for the fitness check of EU consumer law on digital fairness

A Finance Watch Position Paper

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Introduction

Finance Watch welcomes the European Commission's fitness check of EU consumer law on digital fairness. The digital transformation of the marketplace for consumer goods, including financial services, has brought with it new consumer protection issues which the current horizontal and sectorial EU consumer law instruments fail to adequately address. New technologies and data-driven practices have emerged which are used to influence consumers to make decisions that go against their interests and take advantage of consumer biases.

Targeted amendments are needed to the Unfair Commercial Practices Directive (UCPD) to address dark patterns, discriminatory price personalisation practices (also referred to as 'price optimisation practices'), influencer marketing, and unsolicited personalised advertising.

Key Takeaways

1. **Finfluencer promotions of retail investment and consumer credit products need to be banned**
   The increasing influencer marketing of investment products such as crypto assets poses huge financial risks to consumers and therefore needs to be banned. Given the riskiness of consumer credit, finfluencer promotions of these products should be banned as well.

2. **More robust measures are needed to prevent dark patterns**
   A list of prohibitions of the most commonly used dark patterns is needed in Annex I of the UCPD.

3. **Price optimisation practices should be banned**
   This practice is discriminatory, exploitative and detrimental for consumers. Any price personalisation should not be based on the optimum amount of margin firms can earn from an individual consumer but only on fair and objective criteria.

4. **Unsolicited personalised advertising should be prohibited**
   This practice takes advantage of consumers' unconscious biases and can incite them to make decisions that are not in their interests.

I. Finfluencer promotions of retail investment and consumer credit products need to be banned

Influencer marketing in the retail financial services sector is currently not sufficiently regulated in the Unfair Commercial Practices Directive (UCPD)[1] and therefore changes to the directive are urgently needed to protect consumers.

Influencer marketing in financial services has become widespread across Europe, and it's set to keep getting bigger. According to research by the International Organisation of Securities Commissions (IOSCO), the international standard setter for the regulation of the investment sector, 43% of European financial services firms plan to increase use of influencers as a marketing tool and this is the tool in which financial firms surveyed expect the highest growth going forward[2].

This trend has been accompanied by numerous cases of influencers encouraging consumers to purchase risky investment products such as crypto assets, with promotional messages which make crypto assets seem very lucrative while failing to point out the risks entailed in investing in these assets.[3] These influencers most often do not have the competence to speak about these products and are driven by conflicts of interest, i.e. remuneration by the product provider. Due to the fact that influencers often have huge amounts of followers, large numbers of consumers are exposed to these advertisements and in case of purchase, associated product risks.

Influencers are increasingly an important source of information for young people interested in investment solutions. For example, the UK's Financial Conduct Authority (FCA) found in 2021 that 54% of new investors aged 18–34 used social media as source material when researching investing, with 17% specifically using social media influencers.[4]

As a result, retail investors have lost huge amounts of money, sometimes their entire life savings. As indicated in a recent position paper on the topic by the consumer organisation BEUC, there are many documented examples of people suffering significant financial harm due to influencer promotions of crypto assets.[5] For example, in France, a consumer collective filed a complaint against about 100 influencers in January 2023 regarding promotions of investments in risky markets with promises of gains and the Dutch Financial Supervisory Authority (AFM) has received dozens of complaints from consumers who have lost a lot of money as a result of influencer tips.[6] Therefore, strong and binding regulation of social media influencer promotions for risky financial services, i.e. financial services where consumers can face serious financial detriment, is crucial.

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[1] Directive 2005/29/EC concerning unfair business-to-consumer commercial practices in the internal market
[2] IOSCO, *FR12/22 Report on Retail Distribution and Digitalisation (iosco.org)*, page 17, Chart 6, 2022.
[3] Politico, *Got FOMO? Unregulated crypto firms have you just where they want you*, 2023.
[4]The Banker, *Regulators take aim at finfluencers*, 2023
[5]BEUC, *From Influence to Responsibility, Time to regulate influencer marketing*,2023
[6]https://www.capital.fr/economie-politique/un-collectif-porte-plainte-contre-des-influenceurs-qui-ont-recommande-des-placements-tres-risques-1458173 and https://www.afm.nl/en/nieuws/2021/december/verkenning-finfluencers

The UCPD, however, fails to provide these strong safeguards. Under the current legislation, any promotion of the products or services of a brand in a post that earns its influencer revenues or other types of benefits must be disclosed as an advertising activity. While this is helpful, it is not sufficient to adequately protect consumers from promotions of investment and consumer credit products where consumers risk losing considerable sums of money or becoming over-indebted. Even retail investment products with less complex risk profiles can in fact be risky if used by vulnerable consumers with a low capacity to understand and bear risks.

While disclosing that the social media post is advertising may help nudge consumers to question the content and accuracy of the post, additional protections are needed for retail investment products and consumer credit as these are products where consumers can face dire financial consequences if picking unsuitable products. Even with labels indicating that they are advertisements, there is a risk that consumers will misperceive influencer promotions of investments and consumer credit as a personal, non-commercial endorsement rather than an advertisement and underestimate the product's riskiness, especially if the influencer is someone they like and trust and if the consumer is not very financially literate.

Due to this, in several EU member states there is now a recognition that for investment products such as crypto assets, labeling alone is not enough. Belgium recently introduced new rules on virtual assets which mandate that influencer promotions for crypto assets must prominently disclose the risks associated with investing in these assets and include a prominent risk warning.[7] Spain recently issued very similar rules to Belgium[8] and France has banned influencer promotions of risky financial products (e.g. complex financial products and/or products with unknown risk or risk greater than the initial capital, crypto assets and Non fungible Tokens (NFT) unless approved).[9]

Therefore, Finance Watch calls on the European Commission to use the digital fairness check to ban influencer promotions of retail investment and consumer credit products in Annex 1 of the UCPD. Protecting consumers from the risk of mis-selling of retail investment products would also help foster trust in capital markets which is much needed to encourage retail investor participation in the capital markets and advance the Capital Markets Union (CMU) in the EU.

II.   More robust measures are needed to prevent dark patterns

Providers of consumer products and services, including financial services providers, are increasingly using techniques such as dark patterns that take advantage of behavioural biases of consumers. Dark patterns are deceptive online interface designs (e.g. colouring

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[7]FSMA, *Virtual currencies: the FSMA steps up its action to protect consumers*, 2023
[8] CNMV, https://cnmv.es/portal/Inversor/Publicidad-Criptoactivos.aspx?lang=en, 2022
[9]French Journal Officiel, Article 4, Loi n°2023-451 du 9 Juin 2023, https://www.legifrance.gouv.fr/download/pdf?id=LsFRbD6JvPkRailnsjmCz81EHFQ2DgWXsjxXY-a5RFQ=

of decision buttons) that are used to trick people into making decisions that are in the interests of the online business, but at the expense of the user. According to a mystery shopping exercise published by the European Commission in 2022, 97% of the most popular websites and apps used by EU consumers deploy at least one dark pattern.[10]

Therefore, Finance Watch very much welcomes that the recent review of the distance marketing of financial services rules (DMFS review)[11] made a first step in addressing this issue in the digital market for retail financial services. However, the final legislative text that was agreed by the co-legislators and is now in force unfortunately only obliges Member States to take measures to address one out of three possible types[12] of dark patterns. This is not sufficient to adequately protect consumers from dark patterns in the retail financial services sector.

For risky products such as financial services, dark patterns can lead to consumers taking out unsuitable retail investment products that can bring them enormous financial losses or taking out an unsuitable consumer credit product that can plunge the consumer into a situation of over-indebtedness.

Therefore, we believe that there is a need for the UCPD to be amended so that it introduces:

1. A horizontal ban on dark patterns
2. A list of prohibitions of the most commonly used dark patterns in Annex I of the Directive.

The list of prohibited commonly used dark patterns should include: • Giving more prominence to certain choices when asking the consumers who are recipients of their service for a decision;

• Repeatedly requesting that consumers who are recipients of the product/service make a choice where that choice has already been made, especially by presenting pop-ups that interfere with the user experience;

• Making the procedure for terminating a product/service more difficult than subscribing to it;

• Using pre-selected or default options;

• Hiding important information about the product (such as its risks and all or some of its cost components), including the practice of pushing consumers to continue or finalise a purchase before accessing all relevant information (e.g. costs) on that purchase.

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[10]European Commission, *Behavioural study on unfair commercial practices in the digital environment*, 2022
[11] https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32023L2673
[12]Practices: (a) giving more prominence to certain choices when asking the consumers who are recipients of their service for a decision; (b) repeatedly requesting that consumers who are recipients of the service make a choice where that choice has already been made, especially by presenting pop-ups that interfere with the user experience; or (c) making the procedure for terminating a service more difficult than subscribing to it.

• Creating a false sense of urgency to pressure consumers into purchasing a product by falsely informing them that a product is only available for a limited period of time or in limited quantities.

III.   Price optimisation practices should be banned

Price optimisation practices are practices where, with the help of algorithmic tools, firms assess consumers' behavioural data such as their shopping habits, values or individual tolerance for price changes to determine a consumer's price sensitivity when setting a personalised price for a product offered to a consumer.

A number of studies, such as one by the European Parliament's IMCO Committee from November 2022[13], confirm that price optimisation practices need to be urgently addressed. In financial services this can mean, for example, assessing whether consumers tend to switch general insurance products, such as home or motor insurance at renewal, or tend to hold them for long periods of time and are therefore unlikely to react to price rises and shop around. This information can, in turn, be misused by firms to charge consumers higher premiums.

Data from EIOPA, for example, shows that firms are increasingly using price optimisation practices for popular insurance products, including accident, health, household and motor insurance.[14] Vulnerable consumers, e.g. elderly people, people with limited access to digital channels or other sources of information are more likely to be affected by this practice as they are more likely to lack knowledge about these practices, or lack access to IT tools and the time to compare or switch products due to a particular life circumstance.[15]

Price optimisation practices are discriminatory, exploitative and detrimental for consumers and therefore should be banned in Annex 1 of the UCPD as an unfair commercial practice. Any price personalisation should not be based on the optimum amount of margin firms can earn from an individual consumer but only on fair and objective criteria such as, for example, an individual consumer's risk and/or cost when taking out an insurance product.

IV.   Unsolicited personalised advertising should be prohibited

Unsolicited personalised advertising is a practice where with the help of AI tools assessing personal data of the consumer collected online, mostly without consumers' knowledge or express consent, firms generate and deliver individualized advertisements to current or prospective consumers without their prior consent. This practice should be banned as well as there are serious consumer protection problems associated with this kind of advertising

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[13]European Parliament, IMCO Committee, _Personalised pricing_ or BEUC, _The use of big data and artificial intelligence in insurance_, 2020.
[14]EIOPA, _Consumer Trends Report 2023_, 2023
[15] EIOPA, _Supervisory statement on differential pricing practices in non-life insurance lines of business_, 2023

activity. Not only are these advertisements generated without the consumer's consent but they also take advantage of consumers' unconscious biases.

For instance, algorithms are used to identify a consumer's propensity for compulsive buying and, on the basis of this, generate a personalised ad for consumer credit, nudging the consumer to take out a consumer credit even though this would incite the consumer to spend beyond their financial means and end up over-indebted.

Malpractices in targeted advertising are likely to increase due to the digital transformation as it is becoming increasingly easier for financial services providers to obtain information about consumers and their behaviours online and therefore it is urgent to tackle this now.

Conclusion

The rapid digitalisation of the online consumer marketplace brings with it benefits but also considerable challenges and risks for consumers that need to be urgently tackled. These new risks are either not sufficiently or not at all addressed in the current EU consumer protection law framework. Therefore, the digital fairness check launched by the European Commission should be utilised to amend the Unfair Commercial Practices Directive (UCPD) to address these risks. Key risks that need to be tackled are dark patterns, influencer marketing, price optimisation practices and unsolicited personalised advertising.

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