

Investor protection. IOSCO retail market conduct Task Force final report

April 2023

Following extensive engagement and work with IOSCO members, industry and other stakeholders, the Final Report of the Retail Market Conduct Task Force (RMCTF) has finally been approved by the Board of IOSCO. The report sets out a toolkit for regulators to use when addressing changing behaviours of retail investors and the evolving ways in which intermediaries engage with and sell to retail investors. The RMCTF has also identified a number of more detailed follow-up measures that will be addressed by the various standing committees of IOSCO. Following the outbreak of the COVID-19 pandemic and considering IOSCO's investor protection objective, the Board requested the RMCTF to focus its immediate attention on the emerging risks of misconduct to retail investors in the financial services industry due to pressures and turbulence caused by the pandemic. The RMCTF completed this work and published its Report in December 2020. The RMCTF subsequently turned its attention to its original mandate to take stock of regulatory approaches to conduct in retail markets. The RMCTF published a Consultation Report in March 2022. The final report, published on 30 March 2023, deepens into a broad spectrum of issues across retail investor environment, detailed below. Issues related to the conduct of the retail market are paramount. It also establishes a substantive analysis of the retail environment, market practices and related conduct implications. It should be noted that some of these trends are changing very quickly and attracting a lot of public and press attention (e.g. GameStop incident). Therefore, the Final Report provides "a global point-in-time view" on an evolving area with wide-reaching impact. It covers a wide range of topics and suggests an adaptive toolkit for regulators to consider when developing their respective supervisory and retail investor support approaches.

The report is based on an extensive stakeholder survey conducted through the Consultation Report, a previous survey responses, industry outreach and other information from IOSCO members. The report considers potential "magnifiers" of retail investor harm, including increasing retail trading and changing retail behaviour; the evolving frauds and scams landscape and the impact of technological elements, such as social media and digitisation, on retail trading. While the focus of the report is not on the impact of COVID-19 on retail investor trends and behaviour, influence on retail consumer behaviour and retail trading patterns stemming from responses to the COVID-19 pandemic has been observed (for example, government lockdowns, business closures, and economic support measures), as have broader trends such as an increase in fraudulent activity targeting retail investors. Misconduct and harmful practices affecting retail investors remain persistent global problems. Harmful practices cover a spectrum of behaviour. At one extreme, inadvertent or even legal practices can cause harm to retail investors; at the other are some egregious examples of deliberate and targeted misconduct. Bad actors in the financial landscape use a range of increasingly sophisticated tactics to build trust and exploit vulnerabilities and opportunities brought about by the pressures of the current economic environment and market conditions. These global inflationary pressures have led to more frequent offerings of risky and unsuitable products to the retail segment through technological means, resulting in significant losses to retail investors.

The RMCTF Final Report sets out a substantive analysis on the market environment, retail investor trends, related conduct implications, and a set of adaptive tools for regulators to consider in developing their respective approaches. Underlying these issues is the need for regulators to access resources, effective practices, tools and techniques to better fulfil their respective mandates.

The main thematic findings on recent retail investor trends and related behavioural challenges detailed in this Report (discussed in Chapters 2-6) focus on:

- The impact of technological advances, social media and changing market conditions on retail trading activity: the surge of self-directed online trading and more frequent offerings of riskier products, often highly leveraged, and with higher retail participation (particularly younger investors), along with the

emergence of crypto-assets, gamification of investment tools, and ubiquitous marketing by unlicensed firms and third parties. during and after periods of normal and stressed market conditions;

- Opportunities and challenges with the rise of digitalisation: opportunities may include increased retail accessibility to investments, increased competition and reduced costs; but the challenges include effectively monitoring, identifying and disrupting misconduct hidden behind the digital veil, and the growing influence of social media on retail investment decisions;
- Common financial consumer issues, such as amplified risk-taking, lack of understanding of complex products, information overload and asymmetries, behavioural problems, and social/psychological/financial pressures in times of uncertainty (for example , the COVID-19 pandemic), as well as situational vulnerabilities;
- The escalation in unlicensed activity, scams, fraudulent or harmful behaviour, and reported investor losses, ranging from egregious and deliberate acts targeting retail investors, to those that inadvertently break the law, largely assisted by more sophisticated veneers enabled by technology (for example, clone investment firms, crypto-asset scams, unregulated or illegal practices by 'Finfluencers', misselling, mislabelling and misleading disclosures);
- Increased risk of greenwashing in environmental investments, as well as in social and governance (ESG) investments, in general in all kinds of sustainable financial products. Greenwashing may take different forms and erode the necessary trust in disclosures regarding such investments, especially in the retail segment.

The toolkit of measures

Given the rapidly evolving retail landscape and mostly steered by technological developments, the regulatory toolkit (described in detail in Chapter 7) offers a set of measures for regulators to consider when developing their respective approaches to addressing emerging retail market conduct issues. Some measures derive from traditional regulatory approaches, while others may be considered novel. Some may not be appropriate in a particular jurisdiction. They are designed to be adaptable and broad enough to accommodate a variety of scenarios in the ongoing management of retail investor risks.

1. Heightening regulators' digital presence and online strategy to proactively and expeditiously address retail investor harm

The first measure aims to help regulators to be proactive, agile and vigilant regarding misconduct in the digital environment, taking into account the pace and volume of information, the constantly changing environment and the lack of visibility (anonymity) and reliability that may exist in online offerings. The main recommendations of the report in this area are:

- Targeting fraudsters directly when misconduct occurs
- Monitoring and assessing online marketing and distribution trends to interrupt harmful marketing channels, such as detrimental Finfluencer activity
- Issuing public alerts and warnings and monitor consumer sentiment
- Enhancing engagement with online service providers, where possible, for early prevention and disruption of misconduct
- Tailoring messaging to retail investors for different websites and social media forums

2. Refine approaches to better identify and mitigate misconduct

The second measure describes preventative means to help early detection and/or mitigation of misconduct, as well as identification of the actors behind the misconduct. Since the behaviour of retail investors can be strongly influenced by various psychological factors and external influences (as highlighted in Chapter 2), a practical, and technology-based regulatory approach against retail market misconduct, which considers behavioural aspects, may support better results. The main recommendations of the report in this area are:

- Enhance internal capabilities and/or use external providers to streamline regulatory surveillance and supervision efforts
- Develop technological tools and use advanced data analytics to better facilitate early intervention and identification of bad actors

- Use behavioural science to analyse retail behaviour and design consumer protection initiatives
- Allow easier access to whistleblowing and an intake system for triaging tips, referrals and complaints

3. Enhancing cross-border and domestic frameworks for supervisory cooperation, both bilaterally and multilaterally

The third measure reiterates the fundamental notion of cooperation, a cornerstone of effective national and international regulation, and the continued need for strong cooperation frameworks to support effective supervisory and compliance capacities, and the mitigation of emerging threats and harms in the midst of a changing environment. IOSCO's Multilateral Memorandum of Understanding (MMoU) and Enhanced MMoU (EMMoU), for example, represent the global gold standard for multilateral cross-border compliance cooperation. The IOSCO MMoU completed twenty years of use in 2022. The interchange of supervisory information and best practices also play a crucial role in dealing with the ever fluid and complex nature of global financial ecosystems, crypto-assets being the most multi-jurisdictional example featured in this report. The main recommendations of the report in this area are:

- Facilitate greater cooperation and collaboration, minimising regulatory arbitrage, where possible
- Work with other national and international bodies where appropriate, to address common problems of misconduct, identify individuals and groups involved in misconduct, and promote early intervention and disruption of misconduct.

4. Addressing retail investors harms that stem from crypto-assets

The fourth measure provides tools for regulators, particularly to counter harm related to crypto-assets, considering the significant growth in investor interest in crypto-assets and the commensurate increase in crypto-asset related scams. The main recommendations of the report in this area are:

- To the extent not already covered by an existing regulatory framework, determine whether there are any regulatory powers that can be used to provide better KYC and trade reporting databases for crypto-asset transactions.
- Employ applicable regulatory intervention powers to address cross-border crypto-asset fraud and theft targeting retail investors

5. Implementating new regulatory approaches against retail market misconduct

The fifth measure presents a variety of tools that can be considered together to address the constantly changing misconduct issues in today's retail landscape. The main recommendations of the report in this area are:

- Rules relating to the marketing of high-risk products
- Consumer help lines and anti-scam campaigns
- Use of mystery shopping to supervise the point of sale
- Regulatory sandbox approach
- Use of intrusive supervision and law enforcement techniques
- Use of tools to better identify firms' compliance with climate disclosure standards and to better detect greenwashing

While this report primarily serves as a guide for regulators, the findings and observations are useful to all stakeholders in creating greater awareness and commitment to retail conduct issues given their significance across industries and presence in both emerging markets as well as developed ones. This report is also designed to complement various works promoted by IOSCO Committees and Task Forces such as those on digitisation, crypto-assets, decentralised finance (DeFi), sustainable finance and investor education, which may present more specific tools to address scenarios related to particular retail markets. The recently published reports by IOSCO on retail distribution and digitisation and decentralised finance are examples of this. Financial education is a key instrument in the fight against misconduct in retail markets, but the traditional approach is a starting point that the supervisor should use within his range of supervisory tools, as it can be a constant source of early information to the supervisor in detecting of bad practices. In addition, the supervisor should explore new ways of enhancing the capabilities of retail investors by promoting the development of skills rather than knowledge. Financial education

should take particular account of retail investors' conduct and provide tools to manage impacts on them. Gamification can help improve the knowledge and skills of retailers. All these measures must be adapted to the different groups of retail investors and their more specific needs.

Useful links:

Retail Market Conduct Task Force Consultation Report. March 2022
<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD698.pdf>

Retail Market Conduct Task Force Final Report. March 2023.
<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD730.pdf>