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EIOPA
European Insurance and Occupational Pensions
Authority
Westhafen Tower, Westhafenplatz 1
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Germany

3 October 2016

Dear Sir, Madam,

EIOPA Consultation Paper on Technical Advice on possible delegated acts concerning the Insurance Distribution Directive

The Financial Services Consumer Panel is an independent statutory body, set up to represent the interests of consumers in the development of policy for the regulation of financial services in the UK.

The Panel welcomes this opportunity to comment on EIOPA's proposed Technical Advice on possible delegated acts concerning the Insurance Distribution Directive (IDD).

The Panel is broadly supportive of the proposed draft Technical Advice. The proposals are detailed and far-reaching and generally introduce enhanced rules for the protection of consumers, in line with the objectives of the IDD.

Sincerely,

Sue Lewis

Chair

Financial Services Consumer Panel

Consultation Questions

The Panel is responding to sections where it has substantive comments.

Product Oversight and Governance

2. Do you agree that the policy proposals above provide sufficient detail on product oversight and governance arrangements?

The Panel broadly agrees that the proposals provide a sufficient level of detail. However, as previously argued, we believe that EIOPA should consider urging companies to make their Product Oversight and Governance (POG) arrangements public to allow for greater scrutiny. In addition to increasing transparency, this would ensure rules put in place are more than a simple box-ticking exercise and it would encourage consumer confidence.

We remain concerned that EIOPA still appears content for the periodic review as currently foreseen to be conducted entirely internally within each firm. Reviewing POG arrangements independently could mean shortcomings are flagged up promptly. For example, the review could be covered by a firm's Audit Committee report, and thus be overseen by its auditors.

7. Do you agree with the proposed high level principle for the granularity of the target market? If not, please provide details on the level of detail you would prefer.

The draft Technical Advice on target market refers to the need to check compatibility of the product with certain types of customers and introduces a level of granularity in identifying a specific target market that we welcome. We agree it is essential that manufacturers are compelled to identify a target market in the development stage and to only add features that meet the needs of the target market. Too often, mis-selling of financial products is driven by the need to sell high volumes – irrespective of whether the product meets the individual clients' needs.

However, there is also an argument that some basic products can be appropriate for a large and diverse target market. The Panel has previously argued that more work needs to be done in establishing a test for whether a product can be deemed simple or not, as part of identifying the target market. Manufacturers and distributors should in particular consider the design and marketing of simple products that can be readily understood by all consumers.

We would like to reiterate the findings of the 2013 UK's Sergeant Review of Simple Financial Products¹, which found that many consumers need simple financial products because of "the challenge of making good choices in what seems to many to be an overwhelmingly complicated marketplace with a very wide range of products which are complex and difficult to understand".

The review also established a set of principles, which form the basis of an objective test to establish whether a product is simple or not. These include for example the use of standardised language, a transparent fee structure and straightforward and clear purchasing process.

1

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/191721/sergeant_review_simple_products_final_report.pdf

We would encourage EIOPA, in cooperation with the other ESAs, to conduct a similar exercise at EU-level to establish such operating principles for manufacturers. To ensure adequate consumer understanding of the types of products they are offered, it is also critical that a designation of a product as 'simple' is subject to oversight by a regulator or another independent body.

8. Do you agree with the proposed review obligations for manufacturers and distributors of insurance products? Would you consider it important to introduce a minimum frequency of reviews which should be undertaken by the product manufacturer e.g. every 3 years?

Whilst the Panel agrees with the proposed review obligations for both manufacturers and distributors we do believe that there should be a minimum frequency of reviews imposed by EIOPA. The Panel would like to propose that complex products such as insurance-based investment products have a review period of only one year and less complex non-life or pure life products, three years.

We were disappointed by the recommendation that if an event materially affecting the potential guarantees to the identified target market occurs, action will be decided upon on a case-by-case basis. We would have preferred EIOPA to stipulate the regulatory action/actions that could be taken in the case of an event occurring.

That said, we welcome the non-exhaustive list provided of possible actions that could be taken which manufacturers (and distributors if relevant) should find helpful.

We also welcome the proposal that the senior management body and/or the compliance function of the manufacturer or distributor should have responsibility for the oversight of the product governance process as this clearly states where the responsibility for good governance lies.

Conflicts of interest

9. Are there any other elements which you would consider appropriate in order to specify the regulatory requirements on conflicts of interest as laid down on Article 27 and Article 28, IDD? If possible, please specify in detail.

The Panel strongly believes that the emphasis should be on the avoidance and elimination of conflicts, rather than their 'management' and therefore welcome EIOPA's recommendation that manufacturers and distributors put in place a robust conflict of interest policy which is regularly reviewed. We agree that disclosure of conflict of interests, whilst essential if such a conflict should occur, should be a step of last resort and that overreliance on disclosure should be considered a deficiency in the conflicts of interest policy.

Conflicts of interest are a crucial factor in many instances of mis-selling, and manufacturers and distributors should be called on to eliminate them wherever possible.

We also welcome the inclusion of examples of situations where conflicts of interest shall be assumed until otherwise eliminated.

Inducements

11. Do you agree with the proposed high level principle to determine whether an inducement has a detrimental impact on the relevant service to the customer?

The Panel strongly agrees with this high level principle. Unfair and excessive inducements have proved to be the reason for mis-selling and a cause of great detriment for consumers.

We also welcome the inclusion of a non-exhaustive list of examples where an inducement may generally be regarded as having a detrimental effect on the quality of the service to the customer. Examples can aid with clarity if manufacturers or distributors are unclear.

12. Are there any further inducements which entail the high risk of leading to a detrimental impact and should be added to the list in paragraph 4 of the draft technical advice above?

The Panel would support the inclusion of internal remuneration packages. The Panel would urge EIOPA to consider a review of internal remuneration packages as excessive bonus payments or a requirement to produce high volume sales in order to meet minimum salary payments is also a cause of mis-selling.

The Panel would also like to point out the need for clarification on the definition of inducements as presently outlined in the consultation document. In its Draft Technical Advice EIOPA has interpreted the term "*inducement*" to mean "(...) any fee, commission or non-monetary benefit (...) paid to or by any party except the customer or a person on behalf of the customer". However, in the preceding analysis, it considers an inducement to be "in relation to fees or commissions as well as non-monetary benefits paid by or to third parties only" which would exclude those payments which do not originate from a third party (rather than only excluding just those originating from the customer as per the former).

Assessment of suitability and appropriateness

Insurance based investment products

15. Do you agree with the high level criteria used to specify the assessment of suitability and appropriateness? Are there any criteria you would exclude, and why?

The Panel agrees with the high level criteria used. There is no criteria we would suggest excluding.

16. When EIOPA is reflecting insurance specificities in the policy proposals above, do you agree with them? In particular, with regard to insurance specificities related to the protection elements within an insurance-based investment product (e.g. biometric risk cover), are there aspects regarding the information to obtain (such as the 'risk profile') for the assessment of suitability and appropriateness that would necessitate further and/or more explicit insurance specificities?

The Panel agrees that insurance specificities should be reflected in the policy proposals. However, we note that Policy Option 2 (Preferred Option) whilst offering a reasonable 'middle ground' may not capture all the elements required to assess whether an

insurance-based investment is a suitable product for a consumer.

Investments which also have an insurance element will have additional costs which will affect the performance of the investment (as any cost or charge applied against a product must). Insurance-based investment products (IBIPs) serve two needs: one for protection and one for investment. Bundling these two very different requirements together may not always be the most efficient or cost effective method of providing either. Therefore it is essential that the manufacturer or the distributor fully reflects why an IBIP is the most suitable product for both the investment and protection needs and why this cannot be replicated elsewhere through two separate products.

Policy Option 3 on the other hand has a requirement for substantially different types of information to be obtained from the customer in order to fully take into account the customer's "basic needs" and certain insurance-specific elements of an IBIP (such as biometric risk cover).

Given that the costs and charges associated with IBIPs are higher and that the need for both investment and protection is likely to be less prevalent with many consumers, the Panel favours Option 3.

17. In practice, what information do you expect to collect for the assessment of suitability and appropriateness in addition to the demands and needs?

The consultation document provides good guidance on the information that would be required in order for suitability and appropriateness to be fully assessed. Specifically, the following information should be included in addition to demands and needs:

- Details of the customer's current income and expenditure and any expectations of future changes;
- Breakdown of customer's assets and other financial products, including protection products and employment benefits, if applicable;
- Family circumstances, including any dependencies;
- The customer's risk profile. Their appetite for risk, but more importantly their capacity for loss. So how much can they realistically afford to lose?
- The customer's knowledge and experience of investing in this type of product;
- The customer's savings and investment objectives, including how long the investment will be held and their retirement plans.

18. Do you think that it could be useful for EIOPA to provide any specification and/or guidance on the relationship between the demands and needs test and the suitability/appropriateness assessment, in a separate policy instrument, given that this point is not addressed in this technical advice?

The Panel believes this would be useful. It is essential that crucial information is collected so that suitability and appropriateness can be adequately assessed and then applied against the established demands and needs of the customer. However, there is likely to be overlap in the collection of information and data to comply with these two statutory requirements.

Some manufacturers/distributors may be better equipped than others to collect this data in a streamlined fashion which won't over burden the customer. Others may be over compliant, concerned only with the regulatory consequences of 'getting it wrong'. Nor should the collection of data be reduced to a tick-box exercise. Therefore, we feel guidance and some prescription is needed here to help intermediaries and firms get this right.

The process for collecting data to satisfy both the suitability and appropriateness requirements and the demands and needs test should be personal and on a one-to-one basis with the customer. It is essential that the customer understands why these questions are being asked and the importance of answering them fully and honestly – and the consequences should they provide inadequate answers or ‘guessing’.

We feel that EIOPA could provide valuable guidance which all manufacturers and distributors could follow when collecting information from customers to meet both of these statutory requirements. More importantly, this would ensure that the necessary data is being collected in order for a full suitability assessment to be made against the customer’s demands and needs.

Criteria to assess non- complex insurance based investment products

19. Do you agree with the high level and cumulative list of criteria used to define other non-complex products? Are there any you would make optional or exclude, and why?

The Panel broadly agrees with the high level and cumulative list of criteria used to define other non-complex products. There is no criteria we would suggest making optional or any we would exclude.

However, we do have concerns that the perception of what is, in truth, a non-complex product or a complex product, depends very much on the knowledge and experience of the purchaser. Our concern is that even relatively simple investment-based products might appear complex to the inexperienced investor, but if sold without advice, there may be no requirement to establish suitability or appropriateness.

22. On retention of records, do you agree with the high level criteria used? Are there any you would exclude, and why?

We agree with the high level criteria used. There are no criteria we would exclude.

23. When EIOPA is reflecting insurance specificities in the policy proposals, do you agree with them?

Yes.

24. Do you agree with the high level criteria used with regard to the suitability statement and the periodic communications to customers? Are there any criteria you would exclude, and why?

The Panel agrees with the high level criteria used with regard to the suitability statement and periodic communications to customers. There are no criteria we would wish to see excluded.

However, the Panel believes the suitability statement should highlight any needs identified that are not met by the recommended product. Many consumers may not, unprompted, identify all their needs but during the data collection phase further needs may be uncovered that the customer does not wish to have addressed at that time. We believe these should be noted and the suitability statement is a good document to use for this purpose.

If it is decided that a periodic review shall take place, the fact that needs not met by the original recommendation are contained in the suitability statement will act as a prompt for both the customer and the intermediary during the review.

25. When EIOPA is reflecting insurance specificities in the policy proposals, do you agree with them?

Yes.

26. Should EIOPA specify further criteria with regard to the periodic communication to customers, such as the division of responsibility or more details on the online system?

See response to Question 24 concerning any needs not met by the original recommendation. It would also be useful if the periodic communication could highlight if a more suitable product or solution has been introduced since the first recommendation was made.

In addition, it would be helpful if the total cost paid into the policy could be published alongside the current surrender value, so the customer can easily identify the actual performance of the investment to date. Often only premiums paid during the last year are shown which does not provide a complete picture.