



Zurich Insurance Company Response to ESA Joint Consultation Paper 2014/05 on Guidelines for Cross-Selling Practices

The Zurich Insurance Company is pleased to have the opportunity to comment on the ESA paper. Before responding to the specific questions raised in the consultation paper, we have a number of comments as to the legal basis on the Guidelines and their general applicability. Zurich would argue that the legal basis for EIOPA's broad-based participation in this consultation appears doubtful. EIOPA cites to MiFID II as well as the "planned revision of Directive 2002/92/EC" (IMD2). MiFID II, of course, applies to insurance only to the extent of insurance-based investment products. Nevertheless, the Guidelines purport to apply broadly to insurance without such a limitation. Given that no political agreement has been reached on IMD2, we respectfully suggest that it would be appropriate to limit the scope of these Guidelines to insurance-based investment products until such time as EIOPA has a settled legal basis upon which to consider guidelines applicable to other insurance products. In fact, the regulation of "cross-selling" is one of the major elements of IMD2 and an area which, as we understand, political agreement is not yet reached. Accordingly, it would not appear appropriate for EIOPA to jump ahead of the resolution of the EU political process.

Moreover, EIOPA's decision to proceed with these guidelines as a joint consultation with the other ESAs appears grounded in the direction provided in MiFID. No such direction appears forthcoming in the context of IMD2. Accordingly, it is unclear what, if any, benefit customers of non-investment insurance products would realize from Guidelines that are designed for banking and other investment products. Indeed, the Guidelines themselves appear ill-fitted to the vast majority of insurance products available to European consumers.

For these reasons, we would urge EIOPA to limit the scope of this consultation to insurance-based investment products consistent with its authority under MiFID. We would further suggest that EIOPA separately contemplate appropriate (and relevant) guidance for other insurance products once the legislative process has produced authority on which EIOPA may do so.

Question 1: Do you agree with the general description of what constitutes the practice of cross-selling?

It is worth noting that the draft Guidelines do not appear to contain a definition of cross-selling. Rather, the Guidelines distinguish between a (a) bundled package; and (b) tied package. The Guidelines also utilize the defined term "component product" although it appears that the term



“product” and “component” are used separately within the Guidelines themselves which can be confusing. It also appears that the term “product” may sometimes be meant to include “services.”

It appears that the definition of “bundled package” is meant to describe the situation where a product and another product or a product and a service is offered together but the provider also makes the products or product and service available separately. If that is the case, a more clear formulation would be:

A package consisting of two or more component products or of a combination of products and financial services where the provider of the product(s) and service(s) also makes the component products and services available separately.

The definition of “tied package” would then be conformed to read:

A package consisting of two or more component products or of a combination of products and financial services where the provider of the product(s) and service(s) does not make the component products and services available separately.

The more significant concern is that the definitions in the Guidelines do not adequately define a “component product.” Without an adequate definition of “component product” there is a very real risk that the Guidelines may be misconstrued to impair the availability of time proven product configurations that consumers have come to expect from their insurers. While paragraph 4 of the guidelines and associated footnote 7 attempt to provide some parameters by way of exclusion, the base definition of “component product” remains impractical for use in the context of insurance products.

Question 2: Do you agree with the identified potential benefits of cross-selling practices?

Absent a useable definition of “component product,” it is difficult to discern the precise benefits or detriments that the consultation seeks to explore. Accordingly, the following discussion examines the benefits of sound insurance product configuration.

An insurance company will offer (and a consumer will often expect to purchase) what may be considered “component products” configured into a package because of the well-established benefits of:

- a. **Reduction in coverage gaps** – Purchasers of insurance tend to believe that a loss will not happen to them. Statistically, they are often correct. However, when a fortuitous



event does occur, the insurance customer often expects that the contract that he or she purchased provides a span of coverage that reflects the insurable exposures that the typical such consumer is likely to face. Over many decades, insurers have developed product configurations that have proven reasonably suited to address those expectations. For example, a homeowners policy will include coverage for a tree falling onto the insured's home – even if the insured never considered that possibility or, having done so, believed his or her trees to be unusually sturdy. Likewise, the typical renters policy will contain a coverage part insuring against a slip in fall on the entrance way rug, although the renter may have had no idea that liability – or the coverage itself – even existed. In short, an insurance consumer simply cannot understand and objectively assess his or her exposure to all foreseeable risks that he or she may face in life or business. The insurer relies on decades of experience and reams of data to generalize the customer's exposure to risk and provide product configurations that reasonably address those risks. One would hope that the guidelines are intended to protect and promote such product configurations, although it is difficult to see how they may do so.

- b. **Simplified Decision-Making** – The insurance consumer is often unable to consider all of the risks and exposures that he or she may face because of a lack of experience, data, analytical capabilities, interest and time. While many of us think of ourselves as special or unique, statistically as a group insurance customers of similar characteristics share a generally consistent exposure to a generally common set of insurable risks. Insurers have utilized their extensive experience, data, analytical capabilities, interest and time to develop product configurations for “average” consumers and those product configurations tend to suit them very well. If the intent of the guidelines is to decompose decades of proven product configuration building and refinement into dozens or hundreds of “menu options” for the consumer, the stated goal of the guidelines to “simply” customer decision-making will result in very much the opposite. It would be a terrible loss to consumers if they were to be forced to contemplate all exposures to which they may be exposed. For example, absent a meaningful boundary in the guidance it would be taken that the homeowner must be presented with detailed information about the coverages and pricing for ice dam, weight of snow, vandalism, civil commotion, falling objects, rolling objects, shifting of earth, vehicular collision, and on and on – and a tick list to pick and choose if the product is bundled rather than tied. It is hard to imagine any consumer has the capability or patience to go through such an exercise.



- c. **Reduced Intra-Insurer Disputes** – Insurers have also learned that certain coverage combinations are better left together in a single offering to prevent unnecessary disputes between insurance companies in the allocation of a loss that is indisputably covered but the precise component of the contract covering that loss is arguable. For example, if one insurer offered sewer backup coverage and another provided coverage for water damage, water damage resulting from the failure of a sump pump caused by a leaking pipe that shorts out the house’s electricity supply would undoubtedly be covered – but the common customer of the separate insurers may find himself or herself facing delays as the insurers worked out exactly which contract should pay (and as the insurers waste their own resources trying to sort it out). Where the coverages are provided by the same provided, such a question simply does not arise. It would appear that the guidance would seek to promote such efficiency and convenience for the consumer rather than regard it with suspicion.
- d. **Reduced Production and Distribution Costs** – Where products are configured together, the cost of production and distribution can be spread across both products. As a simple example, the insurer needs only one stamp to mail a single contract configured with multiple coverages. Similar and more meaningful efficiencies occur throughout the value chain resulting in a lower cost outcome for the consumer. It would appear to advance the stated objective of consumer protection to promote the spreading of costs across multiple “components” in order to deliver the lowest cost outcome for the consumer.
- e. **Product Innovation** – Flexibility in product configuration allows the insurer to quickly and less expensively bring new product features to market – especially where the new product feature would not alone generate sufficient premium to justify the cost of production and distribution. For example, some directors and officers policies now extend coverage to a financial institution’s Responsible Officer under FATCA. Because this extension of coverage is provided as part of a larger product it is often provided at very low (if any) cost. However, should an insurer provide Responsible Officer coverage as a stand-alone product separate from the directors and officers coverage the administrative costs associated with separate underwriting, risk analysis, actuarial justification, pricing structure and distribution would swallow the cost of the risk itself. In other words, the product would never find its way to market. It would appear that the guidelines should foster innovation and the expansion of coverages at the lowest possible costs, although it is not clear how the guidelines as configured would do so.



- f. **Ensuing Adequate Insurance** – While the guidelines imply that the purchase of an insurance package is an activity to be regarded with suspicion, we respectfully submit that adequate insurance is what keeps families and businesses financially sound in times of tragedy and loss. Any effort to discourage the purchase of appropriate insurance in the name of improved customer choice is unlikely a prudent long-term outcome for either the customer or for society. For example, the State of California has effectively cleaved off earthquake insurance from homeowners insurance which results in a clearly separable policyholder decision. Only 12% of policyholders purchase this separate coverage. That is, 88% of California homeowners “go bare” on earthquake insurance which is unlikely a positive outcome for the economic resiliency of the State or its inhabitants despite the exceptionally high utilization of consumer choice.
- g. **Continuity of Traditional Coverage Compositions** – Current insurance configurations are well tested and have come to be expected as presently offered. For example, a life insurance contract may contain a waiver of premium coverage in the event that the policyholder sustains a disability which, absent clear definition, could be mistaken as a packaging of a life and disability coverage potentially resulting in the separation or withdrawal of the limited disability component at considerable cost and inconvenience to the consumer. The present ease with which logical coverage combinations are presently offered and accepted is of significant benefit to consumers.

Question 3: Do you agree with the identified potential detriment associated with cross-selling practices?

The consultation lists a series of potential detriments. The detriments identified appear rather specific to certain types of products while the guidance purports to apply generally to insurance. For example, it is difficult to understand how motor vehicle insurance, homeowners insurance or business owners insurance impede mobility (yet these would be the vast majority of insurance contracts that would be subject to these guidelines). In fact, policyholders can (and do) quickly and without significant (if any) penalty terminate those contracts.

The detriments list also appears to assume that the consumer is able to make objective and well-informed judgments about the specific mortality, disability, property and casualty risks that the consumer faces. It seems highly unlikely that an insurance customer would consult a mortality table, windstorm model or crash safety ratings before deciding whether it is prudent to insure against those risks. Even a highly sophisticated customer would appear unlikely equipped to make such a



judgment. While there may be certain products where an overconsumption risk may arise, the guidance has not endeavored to describe where that risk, in EIOPA's view, may occur. Absent such a safeguard, there is real risk that the guidelines could overshoot especially outside of the investment product space.

The consultant's list of detriments lead one to the conclusion that, in fact, the drafters have only insurance-based investment products in mind when considering the propriety of these guidelines. If that is the case, then the guidelines should be limited to that scope. If not, then considerable more should be invested in exploring the intended and unintended consequences of applying these guidelines more broadly.

Question 11: Please provide any specific evidence or data that would further inform the analysis of the likely cost and benefit impacts of the guidelines.

The guidelines would require the distributor to provide the price of both the package and its component parts in the case of either a bundled package (where the component parts are available separately) or a tied package (where they are not). It appears logically inconsistent to mandate the provision of a separate price for a component part that is not – by definition – separately available. Setting aside the cost of developing and providing this information, there appears no use to which the consumer could put this information.

In fact, the series of guidelines make no distinction between "tied" and "bundled" product offerings other than with respect to the last two paragraphs of Guideline 7 (relating to optionality). It seems implausible that tied and bundled insurance products should be regulated in exactly the same manner other than with respect to the presentation of the fact of optionality.

This series of guidelines makes it abundantly obvious that the concepts of "bundled", "tied," "packaged," and "component" must be clearly demarcated – and done so in the context of insurance. The current lack of practical insurance-based definitions is certain to create confusion, inconsistency and diminution of the chance that these guidelines may serve their stated objectives.

In conclusion, we respectfully submit that the joint consultation is not an appropriate vehicle for EIOPA to pursue outside of insurance-based investment products because (a) there is no legal authority for such a broad consultation; and (b) insufficient consideration has been given to the risks that the guidelines proposed in this consultation present to non-life insurance products and pure protection life insurance products.