

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

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1. Responding to the Consultation Paper

The European Insurance and Occupational Pensions Authority (hereinafter EIOPA) welcomes comments on the Consultation Paper on Technical Advice on possible delegated acts concerning the Insurance Distribution Directive.

This package includes:

- The Consultation Paper
- Template for comments.

EIOPA invites comments on any aspect of this paper and in particular on the specific questions summarised in Annex I. Comments are most helpful if they:

- respond to the question stated, where applicable;
- contain a clear rationale; and
- describe any alternatives EIOPA should consider.

Please send your comments to EIOPA in the provided Template for Comments, by email to CP-16-006@eiopa.europa.eu, by 18:00 CET on 3 October 2016.

Contributions not received in the provided template for comments, or sent to a different email address, or after deadline, will not be processed.

Publication of responses

Contributions received will be published on EIOPA's public website unless you request otherwise in the respective field in the template for comments. A standard confidentiality statement in an e-mail message will not be treated as a request for non-disclosure.

Please note that EIOPA is subject to Regulation (EC) No 1049/2001 regarding public access to documents and EIOPA's rules on public access to documents¹.

Contributions will be made available at the end of the public consultation period.

Data protection

Please note that personal contact details (such as name of individuals, email addresses and phone numbers) will not be published. They will only be used to request clarifications if necessary on the information supplied.

EIOPA, as a European Authority, will process any personal data in line with Regulation (EC) No 45/2001 on the protection of the individuals with regards to the processing of

¹ [https://eiopa.europa.eu/fileadmin/tx_dam/files/aboutceiops/Public-Access-\(EIOPA-MB-11-051\).pdf](https://eiopa.europa.eu/fileadmin/tx_dam/files/aboutceiops/Public-Access-(EIOPA-MB-11-051).pdf)

personal data by the Community institutions and bodies and on the free movement of such data. More information on data protection can be found at www.eiopa.europa.eu under the heading 'Legal notice'.

2. Underlying Strategic Objectives of EIOPA's policy proposals in this Consultation Paper

1. On 24 February 2016, EIOPA was asked with a formal "Request for Advice" by the European Commission to provide technical advice on possible delegated acts to further specify the following provisions of the Insurance Distribution Directive (IDD):
 - Product Oversight and Governance, Article 25 IDD;
 - Conflicts of Interest, Articles 27 and 28 IDD;
 - Inducements, Article 29(2) IDD; and
 - Assessment of suitability and appropriateness and reporting, Article 30 IDD.
2. EIOPA places consumer protection, both through prudential and conduct of business regulation, at the centre of its strategy. Misconduct by firms may not only harm individual consumers, but may also have a wider prudential impact, posing a threat to the stability of the financial sector. Notwithstanding the fact that the Commission requests advice of a technical nature from EIOPA, EIOPA sees this advice as also actively contributing to the completion of a single rulebook on consumer protection, namely through the implementation of the IDD.
3. EIOPA has developed its policy proposals in view of EIOPA's strategic objectives and priorities as outlined in EIOPA's annual work programme for 2016², in particular the objective *"to ensure transparency, simplicity, accessibility and fairness across the internal market for consumers"*.
4. In this respect, the focus is on the objectives, firstly, to *"provide a framework for better governance, suitability and accessibility of insurance products for consumers"* and, secondly to *"develop a framework for proper selling practices for direct sellers and intermediaries ensuring that advice to consumers is based on what best suits their needs and profiles"*.
5. The detailed policy proposals on product oversight and governance arrangements pursue the first objective to provide a framework for better governance of insurance products. They aim to ensure that the interests of the customers are taken into consideration throughout the life cycle of a product, namely the process of designing and manufacturing the product, bringing it to the market and monitoring the product once it has been distributed. The inclusion of the provisions in EIOPA's Product Oversight & Governance (POG) Preparatory Guidelines in the draft technical advice, is in line with EIOPA's objective of the Guidelines providing early guidance and supporting national authorities and market participants with the implementation of POG requirements in preparation for the formal requirements provided for in the IDD.
6. The policy proposals on conflicts of interest, inducements as well as suitability/appropriateness assessment pursue the second objective. They aim to ensure that distribution activities are carried out in accordance with the best interests of customers and that customers buy insurance products which are suitable and appropriate for the individual customer.

7. Taking into consideration that inducements have the potential to cause a conflict of interest between the interests of distributors and their customers, the policy proposals aim to ensure that any detrimental impact, stemming from the payment of inducements, on the quality of the service provided to the customers is excluded from the outset.
8. The policy proposals further specifying the suitability/appropriateness assessment, ensure that the insurance intermediary or insurance undertaking obtains all relevant information necessary to assess whether a specific insurance-based investment product is suitable or appropriate for a specific customer. This approach helps, for example, to ensure that insurance intermediaries or insurance undertakings do not request more information from the customer than needed to provide good quality advice to the customer or information requests are not duplicated. This will further enhance the quality of service provided to the customer, thereby strengthening the framework for proper selling practices.

3. Reasons for publication

1. On 30 June 2015, the European Parliament and the Council Presidency reached an agreement on a draft Directive establishing new improved rules on insurance distribution (the "Insurance Distribution Directive" – hereafter "IDD")³. Subsequent to this trilogue agreement being reached, the final legislative proposals of the IDD were approved by the European Parliament on 24 November 2015 and by the Council of the EU on 14 December 2015. Both were published on 2 February 2016 in the Official Journal of the European Union and entered into force on 23 February 2016.
2. The deadline for Member States transposing IDD is 23 February 2018. IDD effectively replaces the Insurance Mediation Directive (IMD)⁴ as the IMD is repealed from the date of transposition. In addition, the amendments made to the Insurance Mediation Directive (IMD) via Article 91 of Directive 2014/65/EC ("MiFID II") were also deleted from the IMD with effect from 23 February 2016.
3. The Insurance Distribution Directive (IDD) establishes new rules on insurance distribution and seeks to:
 - Improve regulation in the retail insurance market and create more opportunities for cross-border business;
 - Establish the conditions necessary for fair competition between distributors of insurance products, for example, through an extension of the Directive to direct sales; and
 - Strengthen consumer protection, in particular with regard to the distribution of insurance-based investment products (IBIPs).
4. Certain elements of the Directive need to be further specified in delegated acts to be adopted by the Commission. These include:
 - Product Oversight and Governance (Art. 25(2));
 - Conflicts of Interest (Art. 27 and 28(4));
 - Inducements (Art. 29(2)); and
 - Assessment of suitability and appropriateness and reporting to customers (Art. 30(5)).
5. EIOPA received a formal request ("Mandate")⁵ from the European Commission on 24 February 2016 to provide technical advice to the Commission by 1 February 2017 on the possible content of the delegated acts.

³ Directive 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution (recast): <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32016L0097&from=EN>

⁴ Directive 2002/92/EC of the European Parliament and of the Council of 9 December 2002 on insurance mediation

⁵ Request for EIOPA Technical Advice on possible delegated acts concerning the Insurance Distribution Directive: <https://eiopa.europa.eu/Publications/Requests%20for%20advice/I-EIOPA-2016-073%20COM%20Letter%20IDD%20%28GBE%29.pdf>

6. The Commission has invited EIOPA to build on the results of previous work that has already been carried out by EIOPA (e.g. EIOPA's previous technical advice on conflict of interests in direct and intermediated sales of insurance-based investment products ("IMD 1.5")⁶ and EIOPA's Preparatory Guidelines on Product Oversight & Governance arrangements by insurance undertakings and insurance distributors⁷).
7. In addition, EIOPA is invited under the Commission's mandate to achieve as much consistency as possible in the conduct of business standards for insurance-based investment products under IDD on the one hand and financial instruments under MiFID II on the other, where there is no fundamental difference in the wording of the provisions in the IDD and corresponding provisions in MiFID II.
8. As regards MiFID II, the following draft Delegated Acts are of relevance to the technical advice on the delegated acts on IDD and have been adopted by the Commission:
 - Draft Commission Delegated Directive supplementing Directive 2014/65/EU with regard to safeguarding of financial instruments and funds belonging to clients, product governance obligations and the rules applicable to the provision or reception of fees, commissions or any monetary or non-monetary benefits⁸;
 - Draft Commission Delegated Regulation supplementing Directive 2014/65/EU as regards organisational requirements and operating conditions for investment firms as defined terms of the purposes of that Directive⁹.
9. In order to provide stakeholders with an early orientation on issues that will need to be addressed in the technical advice to the Commission and to gather feedback from the market, EIOPA published an online survey in January 2016 (the results of which have also been published online)¹⁰.

Cost-benefit analysis

10. EIOPA has been requested by the Commission to support its Technical Advice to the Commission with data and evidence on the potential impacts of proposals identified, including an assessment of the relative impacts of different options where this is appropriate. Where impacts might be substantial, the Commission has requested, where feasible, that EIOPA provide quantitative data. The provision

⁶ [https://eiopa.europa.eu/Publications/Opinions/EIOPA-15-135_Technical%20Advice%20%20Impact%20Assessment_conflicts_of_interest_version%20for%20COM%20\(2\).pdf](https://eiopa.europa.eu/Publications/Opinions/EIOPA-15-135_Technical%20Advice%20%20Impact%20Assessment_conflicts_of_interest_version%20for%20COM%20(2).pdf)

⁷ Final Report on the Public Consultation on Preparatory Guidelines on product oversight and governance arrangements by insurance undertakings and distributors:

<https://eiopa.europa.eu/Publications/Reports/Final%20report%20on%20POG%20Guidelines.pdf>

⁸ COMMISSION DELEGATED DIRECTIVE (EU) .../... of 7.4.2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to safeguarding of financial instruments and funds belonging to clients, product governance obligations and the rules applicable to the provision or reception of fees, commissions or any monetary or non-monetary benefits

⁹ COMMISSION DELEGATED REGULATION (EU) .../... of 25.4.2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive

¹⁰ <https://eiopa.europa.eu/Pages/Consumer-Protection/Online-survey-Call-for-Advice-from-EC-IDD.aspx>

of such data and evidence will aid the Commission in preparing an Impact Assessment on the measures it shall adopt.

11. In order to gather feedback from market participants and interested parties, EIOPA has included a high-level assessment of possible impacts in Annex II. In developing this submission, EIOPA has also built upon the impact assessment work undertaken by the Commission for the revisions of the IMD and MiFID.
12. To further gather input from market participants and interested parties, EIOPA has also included specific questions in this Consultation Paper related to the assessment of impacts. EIOPA acknowledges that the impact of the proposals may differ significantly because of different market structures and already existing regulatory regimes in the different Member States of the European Union. In order to enable a thorough assessment, respondents are therefore invited to provide EIOPA with any data that they have related to the possible impacts of the proposals outlined.

Questions to stakeholders:

1. What would you estimate as the costs and benefits of the possible changes outlined in this Consultation?

Where possible, please provide estimates of one-off and ongoing costs of change, in euros and relative to your turnover as relevant. If you have evidence on potential benefits of the possible changes, please consider both the short and longer term. As far as possible, please link the costs and benefits you identify to the possible changes that would drive these.

Next Steps

13. EIOPA will consider the responses it receives to this CP, and will finalise the draft technical advice for submission to the Commission by 1 February 2017.
14. EIOPA will hold a public hearing on the published CP. The hearing will take place on 23 September 2016 in Frankfurt and registration for the hearing will be available in the relevant section of the EIOPA website in due course.
15. EIOPA will monitor the issues raised in this technical advice and assess, on the basis of sound evidence following the implementation of the Level 1 and Level 2 provisions in IDD in February 2018, the need for issuing guidance to further specify particular issues raised in this technical advice.

4. Product Oversight & Governance

Background/Mandate

Extract from the European Commission's request for advice

"EIOPA is invited to provide technical advice on detailed product oversight and governance arrangements for insurance undertakings and insurance intermediaries manufacturing and distributing insurance products in order to avoid and reduce, from an early stage, potential risk of detriment to customers' interest. The technical advice should identify when insurance undertakings and insurance intermediaries are acting as manufacturers, distributors, or both, and establish the level of responsibility of those actors. In addition, the technical advice should take into account the different types of distribution channels and differences in the size of the insurance undertaking or insurance intermediary concerned. EIOPA should also address the question of how the nature of the insurance product could be taken into consideration in terms of the practical application of the product oversight and governance arrangements.

With regard to product manufacturers, the technical advice should in particular deal with the arrangements of designing, approving and marketing insurance products, including the manufacturers' ongoing obligations as regards the life cycle of insurance products. In identifying the target market of customers, the technical advice should detail the level of granularity expected from manufacturers as regards the complexity of the insurance product and whether it is intended for mass market distribution. The technical advice should provide examples for activities that can be considered "manufacturing an insurance product for sale to customers".

With regard to insurance distributors, the technical advice should in particular deal with the arrangements for selecting insurance products for distribution to customers as well as for obtaining all the relevant information on the insurance product from the manufacturer in order to provide the distribution activities in accordance with the obligation to act in the best interest of the customer. EIOPA should assess whether distributors should be required to periodically inform the manufacturer about their experience with the product, or whether information on an incidental basis reflecting specific changes in the market would ensure sufficient protection of the customer's interest.

The technical advice should also specify the obligation for manufacturers and distributors of insurance products to regularly review their product governance policies as well as the products they manufacture, offer or recommend. The technical advice should refer to any appropriate actions to be taken by manufacturers and, where appropriate, distributors, to prevent and mitigate detriment to the interests of customers. Strengthening the role of management bodies and, where applicable, the compliance function, to ensure compliance with the arrangements should be duly considered."

1. The relevant provisions in the Insurance Distribution Directive are:

Recital 55:

"In order to ensure that insurance products meet the needs of the target market, insurance undertakings and, in the Member States where insurance intermediaries manufacture insurance products for sale to customers, insurance intermediaries should maintain, operate and review a process for the approval of each insurance product. Where an insurance distributor advises on, or proposes, insurance products which it does not manufacture, it should in any case be able to understand the characteristics and identified target market of those products. This Directive should not limit the variety and flexibility of the approaches which undertakings use to develop new products".

Article 25:

"1. Insurance undertakings, as well as intermediaries which manufacture any insurance product for sale to customers, shall maintain, operate and review a process for the approval of each insurance product, or significant adaptations of an existing insurance product, before it is marketed or distributed to customers.

The product approval process shall be proportionate and appropriate to the nature of the insurance product.

The product approval process shall specify an identified target market for each product, ensure that all relevant risks to such identified target market are assessed and that the intended distribution strategy is consistent with the identified target market, and take reasonable steps to ensure that the insurance product is distributed to the identified target market.

The insurance undertaking shall understand and regularly review the insurance products it offers or markets, taking into account any event that could materially affect the potential risk to the identified target market, to assess at least whether the product remains consistent with the needs of the identified target market and whether the intended distribution strategy remains appropriate.

Insurance undertakings, as well as intermediaries which manufacture insurance products, shall make available to distributors all appropriate information on the insurance product and the product approval process, including the identified target market of the insurance product.

Where an insurance distributor advises on, or proposes, insurance products which it does not manufacture, it shall have in place adequate arrangements to obtain the information referred to in the fifth subparagraph and to understand the characteristics and identified target market of each insurance product.

- 2. The Commission shall be empowered to adopt delegated acts in accordance with Article 38 to further specify the principles set out in this Article, taking into account in a proportionate way the activities performed, the nature of the insurance products sold and the nature of the distributor.*
- 3. The policies, processes and arrangements referred to in this Article should be without prejudice to all other requirements under this Directive including those relating to disclosure, suitability or appropriateness, identification and management of conflicts of interest, and inducements.*
- 4. This Article does not apply to insurance products which consist of the insurance of large risks."*

Policy work of ESMA and EBA

2. For the purpose of cross-sectoral consistency, EIOPA has also taken into account the initial policy work carried out in the Joint Committee of the ESAs on manufacturers' product oversight & governance processes¹¹ and policy work which ESMA and EBA developed with regard to product and oversight arrangements for credit institutions and investment firms, in particular ESMA's opinion on Structured Retail Products – Good Practices for product governance arrangements¹² and its technical advice to the Commission on MiFID II¹³ and EBA's Guidelines on product oversight and governance arrangements for retail banking products¹⁴.
3. As far as relevant, extracts of the policy work of ESMA and EBA are outlined in the respective parts below. Furthermore, it should be noted that the Commission recently published its proposal for a Delegated Directive specifying the product oversight and governance requirements which investment firms have to fulfil under MiFID II which was taken into consideration when drafting this Consultation Paper.¹⁵

Introduction

4. EIOPA has been invited by the Commission to provide technical advice on detailed product oversight and governance arrangements for insurance undertakings and insurance intermediaries manufacturing and distributing insurance products.
5. **EIOPA considers that product oversight and governance arrangements play a key role in customer protection by ensuring that insurance products meet the needs of the target market and thereby mitigate the potential for mis-selling.**
6. Product oversight and governance arrangements aim to ensure that the interests are taken into consideration throughout the life cycle of a product, namely the process of designing and manufacturing the product, bringing it to the market and monitoring the product once it has been distributed. They are an essential element of the new regulatory requirements under IDD. Because of their relevance in terms of customer protection, it is of utmost importance that the new requirements are further detailed and specified.
7. Product oversight and governance arrangements are complementary to the information requirements and conducts of business rules applicable at the point of sale disclosure when carrying out distribution activities towards the individual customers.

¹¹ https://eiopa.europa.eu/Publications/Administrative/JC-2013-77_POG_-_Joint_Position_.pdf

¹² https://www.esma.europa.eu/sites/default/files/library/2015/11/2014-332_esma_opinion_u_structured_retail_products_-_good_practices_for_product_governance_arrangements.pdf

¹³ https://www.esma.europa.eu/sites/default/files/library/2015/11/2014-549_-_consultation_paper_mifid_ii_-_mifir.pdf

¹⁴ <https://www.eba.europa.eu/documents/10180/1141044/EBA-GL-2015-18+Guidelines+on+product+oversight+and+governance.pdf>

¹⁵ COMMISSION DELEGATED DIRECTIVE (EU) .../...of 7.4.2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to safeguarding of financial instruments and funds belonging to clients, product governance obligations and the rules applicable to the provision or reception of fees, commissions or any monetary or non-monetary benefits: <https://ec.europa.eu/transparency/reqdoc/rep/3/2016/EN/3-2016-2031-EN-F1-1.PDF>

8. It should be noted that EIOPA has already thoroughly elaborated policy proposals in the context of drafting Preparatory Guidelines on product oversight and governance arrangements by insurance undertakings and insurance distributors¹⁶. In the course of this process, EIOPA conducted two public consultations in order to appropriately involve market participants and stakeholders in the development of policy proposals.¹⁷ This work has originally been initiated following the Joint Position of the European Supervisory Authorities on Manufacturers' Product Oversight and Governance Processes¹⁸. In its Request for Advice, the Commission has explicitly asked to "build on the results of previous work such as the Preparatory Guidelines".
9. After a thorough analysis of the legal requirements in Article 25, IDD and the request of the Commission for technical advice, EIOPA has come to the conclusion that the draft Preparatory Guidelines entail general principles which are consistent with the IDD and therefore can be used to further specify the product oversight and governance requirements in Article 25, IDD (**policy proposals based on EIOPA's policy work on preparatory Guidelines**). Following the analysis of the Commission request, EIOPA has identified several issues which have not yet been addressed by the Preparatory Guidelines so far. These issues and the corresponding policy proposals are outlined under **new policy proposals**.

¹⁶ Final Report on Public Consultation on Preparatory Guidelines G on product oversight and governance arrangements by insurance undertakings and insurance distributors:
<https://eiopa.europa.eu/Pages/Guidelines/Preparatory-Guidelines-on-product-oversight-and-governance-arrangements-by-insurance-undertakings-and-insurance-distributor.aspx>

¹⁷ First public consultation:
<https://eiopa.europa.eu/Pages/Consultations/CP-14150-Guidelines-on-product-oversight-and-governance-arrangements.aspx>

Second public consultation:
<https://eiopa.europa.eu/Pages/Consultations/EIOPA-CP-15-008-Consultation-Paper-on-POG-Guidelines-for-insurance-undertakings-and-insurance-distributors-.aspx>

¹⁸ [https://www.eba.europa.eu/documents/10180/15736/JC-2013-77+\(POG+-+Joint+Position\).pdf](https://www.eba.europa.eu/documents/10180/15736/JC-2013-77+(POG+-+Joint+Position).pdf)

4.1 Policy proposals based on EIOPA's policy work on Preparatory Guidelines

Analysis

10. The following policy proposals stem from EIOPA's policy work in the context of drafting Preparatory Guidelines on Product Oversight and Governance arrangements for insurance undertakings and insurance distributors. N.B. As these policy proposals are supplementary to the "New Policy Proposals" outlined below¹⁹, it should be noted that EIOPA's final technical advice will entail a consolidated and comprehensive set of policy principles to avoid any inappropriate duplication or overlap.
11. The policy proposals distinguish between:
 - (i) Policy proposals for insurance undertakings and insurance intermediaries which manufacture insurance products for sale to customers, and
 - (ii) Policy proposals for insurance distributors which distribute insurance products which they do not manufacture.
12. This is in line with the approach proposed by the Commission with regard to the draft Delegated Directive specifying the product oversight and governance requirements which investment firms have to fulfil under MiFID II.²⁰ For the purpose of developing a consistent set of rules for the insurance sector, it is worth noting that the Commission proposes implementing measures with a high level of detail for both manufacturers, as well as distributors which are based upon high-level principles or specific obligations in MiFID, similar to those required under IDD.
13. Article 25, IDD introduces general principles regarding the product oversight and governance requirements, for insurance undertakings and insurance intermediaries which manufacturer insurance products for sale to customers, and for insurance distributors which distribute insurance products which they do not manufacture.
14. **These policy proposals do not apply to services or products that are explicitly exempted from the scope of the IDD, such as certain activities on an ancillary basis as defined in Article 1(3) or to insurance products which consists of the insurance of large risks as stated in Article 25(4) thereof.**
15. EIOPA would like to point out that the product oversight and governance arrangements applicable to insurance undertakings that manufacture insurance products are closely linked to the requirements regarding the system of governance as laid down in Articles 40 and 41(1) of Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of insurance and reinsurance (hereinafter "Solvency II"). These Articles require insurance undertakings to have a sound and prudent management of the business under a risk-based approach including an appropriate risk management system.
16. In order to further specify the general principles on product oversight and governance arrangements which underlie Article 25, IDD, EIOPA considers it important to define in more detail, the arrangements regarding internal processes, functions and strategies for designing and bringing products to the

¹⁹ See page 17

²⁰ <https://ec.europa.eu/transparency/reqdoc/rep/3/2016/EN/3-2016-2031-EN-F1-1.PDF>

market, monitoring and reviewing them over their life cycle. The arrangements differ depending on the question whether the regulated entities are acting as a manufacturer and/or distributor of insurance products. In the case of manufacturers, these steps include:

- (i) identifying a target market for which the product is considered appropriate;
- (ii) identifying market segments for which the product is not considered appropriate;
- (iii) carrying out product analysis to assess the expected product performance in different stressed scenarios;
- (iv) carrying out product reviews to check if the product performance may lead to customer detriment and, in case this occurs, take actions to change its characteristics and minimise the detriment;
- (v) identifying the relevant distribution channels taking into account the characteristics of the target market and of the product;
- (vi) verifying that distribution channels act in compliance with the manufacturer's product oversight and governance arrangements; and
- (vii) the provision of appropriate information on the product and the product approval process to insurance distributors.

17. The arrangements should be generally applied to all insurance undertakings and all insurance intermediaries manufacturing insurance products, including any natural or legal person pursuing the activity of insurance distribution, independent from the question whether these activities are pursued by an independent broker or by a tied agent, provided that they fall into the scope of the IDD. However, product oversight and governance arrangements need to be proportionate to the level of complexity and the risks related to the products as well as the nature, scale and complexity of the relevant business of the regulated entity.
18. Product oversight and governance arrangements are without prejudice to basic principles in insurance, in particular the principles of solidarity and mathematical methods. The interests of customers that need to be taken into account when designing products following the product oversight and governance arrangements, comprise individual and collective policyholder interests which need to be duly balanced.

a. Analysis for arrangements applicable to manufacturers.

18. The arrangements apply to all insurance undertakings and insurance intermediaries which manufacture any insurance product for the sale to customers.

Establishment of product oversight and governance arrangements

19. The manufacturer should establish, implement and review product oversight and governance arrangements that set out appropriate measures and procedures aimed at designing, monitoring, reviewing and distributing products for customers. The product oversight and governance arrangements should aim to prevent or mitigate customer detriment, support proper management of conflicts of interest and should ensure that the objectives, interests and characteristics are duly taken into account.

20. Good implementation of product oversight and governance arrangements should result in products that:
- Meet the needs of one or more identified target markets;
 - Deliver fair outcomes for customers; and
 - Are sold to customers in the target markets by appropriate distribution channels.
21. An application of product oversight and governance arrangements should also ensure that all relevant staff members have knowledge of these arrangements and monitor them for their respective area of activities. It also ensures that any changes to the arrangements are promptly communicated to them.

Role of Management

22. The administrative, management or supervisory body of the manufacturer or equivalent structure (in the case of two tier systems) is ultimately responsible for the establishment, subsequent reviews and continued compliance of the product oversight and governance arrangements. The manufacturer's administrative, management or supervisory body also ensures that the product oversight and governance arrangements are appropriately designed and implemented into the governing structures of the manufacturer.
23. The product oversight and governance arrangements, as well as any material changes to those arrangements, are subject to prior approval by the manufacturer's administrative, management or supervisory body or equivalent structure.

Target Market

24. The manufacturer should only design and bring to the market, products with features and identified distribution channels which are aligned with the interests, objectives and characteristics of the target market the manufacturer has identified.
25. When deciding whether a product is aligned with the interests, objectives and characteristics or not of a particular target market, the manufacturer should consider at least assessing the level of information available to the target market and the degree of financial capability and literacy of the target market.
26. The manufacturer should also identify groups of customers for whom the product is considered likely not to be aligned with their interests, objectives and characteristics.
27. To this extent, and taking into account the principle of proportionality, the manufacturer should define the target market with an appropriate level of granularity as further specified below.

Skills, knowledge and expertise involved in designing products

28. According to the general principle of good governance stated in Article 258(1)(e) of Commission Delegated Regulation (EU) No 2015/35 under Solvency II, insurance undertakings are required to *"employ personnel with the skills, knowledge and expertise necessary to carry out the responsibilities allocated to*

them properly". In that respect, the manufacturer should ensure that relevant personnel involved in designing products should possess the necessary skills, knowledge and expertise in order to properly understand the product's main features and characteristics as well as the interests, objectives and characteristics of the target market.

29. As necessary, the staff involved in designing products should receive, for instance, appropriate professional training to understand the characteristics and risks of the relevant products and the interests, objectives and characteristics of the target market.

Product Testing

30. Before a product is brought to the market, or if the target market is changed or changes to an existing product are introduced, the manufacturer should conduct appropriate testing of the product including, if relevant, scenario analyses in order to align the product with the interest of the target market. The range of scenario analysis needs to be proportionate to the complexity of the product, its risks and the relevance of external factors with respect to the product performance.
31. Keeping in mind the objectives of the defined target market, the assessment could imply considering the following questions:
- What if assumptions change, for instance if market conditions deteriorate?
 - Is the price of the policy in balance with the worth of the underlying? For instance, is it possible to conclude an all-risk policy for an old car?
 - What if certain circumstances during the lifetime of the product change? For instance, what happens with the premium of a Payment Protection Insurance (PPI) policy if a person becomes unemployed, disabled or experiences other life events? What are the consequences for the coverage of a PPI product when a married couple divorces?
 - What happens to the (guaranteed) coverage (insured amounts) of a fire and theft insurance when the income changes?
32. In addition to the question above, more specifically for insurance-based investment products, the assessment could imply considering also the following questions:
- What would happen to the risk and reward profile of the product following changes to the value and liquidity of underlying assets?
 - How is the risk/reward profile of the product balanced, taking into account the cost structure of the product?
 - When a product benefits from a certain tax environment or other condition; what happens if these conditions change?
 - What are the terms and conditions, and how do they affect the outcome of the product?
 - What will happen when the manufacturer faces financial difficulties?
 - What will happen if the customer terminates the contract early?

33. In addition to the questions above, more specifically for pure protection life insurance products, the assessment could imply considering also the following questions:
- What if the premises change, for instance, the mortality rate or the technical interest rate increases?
 - Does the benefit cover sufficiently future needs of beneficiary?
34. In the case of non-life insurance, the assessment could imply considering the following questions:
- What is the expected claims ratio and the claims payment policy? What if it is higher or lower than expected? Do the expected claims ratio and claims payment policy suggest that the product is of benefit to customers?
 - Does the coverage of one product potentially overlap with the coverage of another product?
 - Does the coverage meets sufficiently future needs of target market? How is the coverage updated in terms of reflecting future needs of target market?
 - Do customers understand the terms and limitations of the contract?
 - Would the manufacturer be able to cope with a large amount of customers? Is the amount of staff sufficient enough to deal with a large amount of requests from customers?
35. On the basis of the PRIIPs Regulation²¹, EIOPA considers that the manufacturer of an insurance-based investment product will be required to produce a Key Information Document (KID) containing information on the risk and reward profile of the product. Performance scenarios expected to be presented in the KID and the range of scenarios used for testing the product may present similarities; however, may not necessarily be identical. Performance scenarios are disclosed to customers whereas scenarios for testing the products cover a large range of factors that determine the performance of the product.

Product monitoring

36. The manufacturer should:
- a) Monitor on an on-going basis that the product continues to be aligned with the interests of the target market, taking into account, for example, the level of the claims ratio for the product as well as claims payment policy or causes of complaints in determining whether to revise the offering.
 - b) Identify, during the lifetime of a product, circumstances which are related to the product and give rise to the risk of customer detriment, and prevent the re-occurrence of detriment or take appropriate action to mitigate the situation.
37. Furthermore, the manufacturer needs to take appropriate action whenever he becomes aware that the product might cause detriment to customers. This might be the case during the regular product monitoring exercise, but also when he is, for instance, informed by the insurance distributor or through a complaint.

²¹ Regulation (EU) No 1286/2014 of the European Parliament and of the Council of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (PRIIPs)

38. The product lifetime is understood as capturing the entire life cycle of a product which begins at the moment when the product is being designed and only finishes once there is no product left on the market. It covers situations when the product is no longer being sold, but there are still customers who own the product. The end of the life cycle of the product is reached only when the last product has been withdrawn from the market.
39. For example, remedial action needs to be taken when the product no longer meets the general needs of the target market or when the product performance is significantly different (in terms of detriment to the customer) from what the manufacturer originally expected.
40. As a general principle, and, in accordance with national legal framework, the manufacturer can only make changes to the product that are consistent with the interests, objectives and characteristics of the already existing target market and these changes do not have an adverse impact on the customer to which the product has been sold already.
41. In order to prevent customer detriment efficiently, it might also be necessary that the manufacturer notifies the remedial action taken to the insurance intermediary involved and to the customers in case of direct sales. This might be the case where the risk profile of a product has changed due to market developments and the product is no longer in line with the interests, objectives and characteristics of the target market.

Distribution channels

42. The manufacturer needs to select insurance distributors that have the necessary knowledge, expertise and competence to understand the product features and the characteristics of the identified target market, correctly place the product in the market and give the appropriate information to customers.
43. If the manufacturer identifies problems with the selected distribution channels (i.e. when the insurance distributor is offering the product to customers for whom it is not compatible) they need to take appropriate action. In the case of independent insurance intermediaries, manufacturers might, for instance, need to consider ceasing making available the relevant products to the insurance intermediary not meeting the product oversight and governance objectives of the manufacturer.

Documentation

44. EIOPA considers it important that insurance intermediaries and insurance undertakings keep appropriate records about all relevant action taken in relation to the product oversight and governance arrangements and make available those records to the competent authorities upon request, if needed for supervisory purposes.

b. Analysis for arrangements applicable to insurance distributors

45. The arrangements apply to all insurance undertakings, insurance intermediaries and ancillary insurance intermediaries advising or proposing insurance products, which they do not manufacture.

Establishment of distribution arrangements

46. EIOPA considers that insurance distributors need to establish appropriate measures and procedures with regard to the insurance products they intend to distribute. Contrary to manufacturer's arrangements, insurance distributors are not required to design and subsequently to review the products, but to take the necessary steps in preparation of the distribution of the insurance products to the customers (such as obtaining all relevant information from the manufacturer and defining a distribution strategy).
47. The distribution arrangements should aim to prevent, or, if not, mitigate, customer detriment, support a proper management of conflicts of interests and should ensure that the objectives, interests and characteristics of customers are duly taken into account.
48. According to this approach, insurance distributors need to consider to which extent the product choice gives rise to the risk of conflicts of interest and if so, which measures should be taken in order to ensure that the distribution activities are carried out in accordance with the best interest of the customers. This might also imply that distributors abstain from distributing specific insurance products, for example, in cases where products do not offer any value to the customer, but only a high commission to the distributor.

Role of Management

49. EIOPA emphasises that the ultimate responsibility with regard to the product distribution arrangements lies with the insurance distributor's administrative, management or supervisory body or equivalent structure even though it is possible that the tasks are delegated either internally or even externally (e.g. in cases of outsourcing). In particular, the ultimate responsibility for the organisational measures and procedures lies with the management of the distributor which is registered and responsible for the distribution activities. For sole traders, it is evident that they bear the responsibility for their entire business.

Obtaining all necessary information from the manufacturer

50. An important prerequisite to setting up a distribution strategy is that the insurance distributor has detailed knowledge about the approval process of the manufacturer, in particular the target market of the individual insurance product, as well as about all other necessary information on the product from the manufacturer in order to fulfil its regulatory obligations towards the customer. This information helps the insurance distributor to select the insurance products the insurance distributor intends to distribute and to assess to which customers the insurance distributor may advertise and promote the individual insurance products.
51. According to this approach, the insurance distributor should establish appropriate arrangements to obtain from the manufacturer all relevant information on the product which is necessary to carry out its distribution activities.

Distribution strategy

52. Where the insurance distributor sets up or follows its own distribution strategy, this strategy needs to be consistent with the target market identified by the

manufacturer of the respective insurance product. In particular, this means that the distribution strategy generally does not allow insurance products to be distributed to customers which are not part of target market identified by the manufacturer. The distribution strategy may also outline circumstances under which the distribution of insurance products to customers outside of the target market is permitted exceptionally.

53. Without prejudice to any assessment of appropriateness or suitability to be subsequently carried out by the insurance distributor when providing services to the individual customer, if the insurance distributor can justify and demonstrate that the product is suitable for the relevant customer, the insurance distributor may exceptionally distribute insurance products to a customer, who is outside of the target market identified by the manufacturer.

Provision of sale information to the manufacturer

54. For the sake of customer protection, EIOPA considers it crucial to enhance the exchange of information between manufacturer and insurance distributor to facilitate market monitoring by the manufacturer. This does not mean that the insurance distributor needs to report every sale to the manufacturer or that the manufacturer needs to confirm that every transaction was made with respect to the correct target market, but the insurance distributor should communicate the relevant information such as the amount of sales made outside the target market, summary information on the customers or a summary of the complaints received with regard to a specific product.

Documentation

55. EIOPA considers it important that insurance distributors keep appropriate records about all relevant action taken in relation to the product oversight and governance arrangements and make available those records to the competent authorities upon request, if needed for supervisory purposes.

Draft Technical Advice

1. Policy proposals for insurance undertakings and insurance intermediaries which manufacture insurance products for sale to customers

Establishment of product oversight and governance arrangements

1. Insurance undertakings and insurance intermediaries which manufacture any insurance product for sale to customers (the "manufacturer") shall maintain, operate and review product oversight and governance arrangements that set out appropriate measures and procedures aimed at designing, monitoring, reviewing and distributing products for customers, as well as taking action in respect of products that may lead to detriment to customers (product oversight and governance arrangements).
2. The product oversight and governance arrangements need to be proportionate to the level of complexity and the risks related to the products as well as the nature, scale and complexity of the relevant business of the manufacturer.

3. The manufacturer shall set out the product oversight and governance arrangements in a written document ("product oversight and governance policy") and make it available to its relevant staff.

Objectives of the product oversight and governance arrangements

4. The product oversight and governance arrangements shall aim to prevent or mitigate customer detriment, support a proper management of conflicts of interests and shall ensure that the objectives, interests and characteristics of customers are duly taken into account.

Role of management

5. The manufacturer's administrative, management or supervisory body, or equivalent structure responsible for the manufacturing of insurance products, shall endorse, and be ultimately responsible for, the establishment, implementation, subsequent reviews and continued internal compliance with the product oversight and governance arrangements.

Review of product governance and oversight arrangements

6. The manufacturer shall regularly review the product oversight and governance arrangements to ensure that they are still valid and up to date and the manufacturer shall amend them, where appropriate.

Target market

7. The manufacturer shall include in its product oversight and governance arrangements, suitable steps in order to identify the relevant target market of a product.
8. The manufacturer shall only design and bring to the market, products with features, and through identified distribution channels, which are aligned with the interests, objectives and characteristics of the target market.
9. When deciding whether a product is aligned with the interests, objectives and characteristics or not of a particular target market, the manufacturer shall consider the level of information available to the target market and the degree of financial capability and literacy of the target market.
10. Where relevant, the manufacturer shall also identify groups of customers for whom the product is considered likely not to be aligned with their interests, objectives and characteristics.

Skills, knowledge and expertise of personnel involved in designing products

11. The manufacturer shall ensure that relevant personnel involved in designing products possess the necessary skills, knowledge and expertise in order to properly understand the product's main features and characteristics as well as the interests, objectives and characteristics of the target market.

Product testing

12. Before a product is brought to the market, or if the target market is changed, or changes to an existing product are introduced, the manufacturer shall conduct appropriate testing of the product including, if relevant, scenario analyses. The product testing shall assess if the product is in line with the objectives for the target market over the lifetime of the product.
13. The manufacturer shall not bring a product to the market if the results of the product testing show that the product is not aligned with the interests, objectives and characteristics of the target market.
14. The manufacturer shall carry out product testing in a qualitative and, where appropriate, in a quantifiable manner depending on the type and nature of the product and the related risk of detriment to customer.

Product monitoring

15. Once the product is distributed, the manufacturer shall monitor on an on-going basis that the product continues to be aligned with the interests, objectives and characteristics of the target market.

Remedial action

16. Should the manufacturer identify, during the lifetime of a product, circumstances which are related to the product and give rise to the risk of customer detriment, the manufacturer shall take appropriate action to mitigate the situation and prevent the re-occurrence of detriment.
17. If relevant, the manufacturer shall notify any relevant remedial action promptly to the distributors involved and to customers.

Distribution channels

18. The manufacturer shall select distribution channels that are appropriate for the target market considering the particular characteristics of the product.
19. The manufacturer shall select distributors with appropriate care.
20. The manufacturer shall provide information, including the details of the products to distributors, of an adequate standard, which is clear, precise and up-to-date.
21. The information given to distributors shall be sufficient to enable them to:
 - understand and place the product properly on the target market;
 - identify the target market for which the product is designed and also to identify the group of customers for whom the product is considered likely not to meet their interests, objectives and characteristics.
22. The manufacturer shall take all reasonable steps to monitor that distribution channels act in compliance with the objectives of the manufacturer's product oversight and governance arrangements.
23. The manufacturer shall examine, on a regular basis, whether the product is distributed to customers belonging to the relevant target market.

24. When the manufacturer considers that the distribution channel does not meet the objectives of the manufacturer's product oversight and governance arrangements, the manufacturer shall take remedial action towards the distribution channel.

Outsourcing of the product design

25. The manufacturer shall retain full responsibility for compliance with product oversight and governance arrangements as described in this Technical Advice when it designates a third party to design products on their behalf.

Documentation of product governance and oversight arrangements

26. Relevant actions taken by the manufacturer in relation to the product oversight and governance arrangements shall be duly documented, kept for audit purposes and made available to the competent authorities upon request.

2. Policy proposals for insurance distributors which advise on or propose insurance products which they do not manufacture

Establishment of product distribution arrangements

27. The insurance distributor shall establish and implement product distribution arrangements that set out appropriate measures and procedures for considering the range of products and services the insurance distributor intends to offer to its customers, for reviewing the product distribution arrangements and for obtaining all necessary information on the product(s) from the manufacturer(s).
28. The product distribution arrangements need to be proportionate to the level of complexity and the risks related to the products as well as the nature, scale and complexity of the relevant business of the insurance distributor.
29. The insurance distributor shall set out the product distribution arrangements in a written document and make it available to its relevant staff.

Objectives of the product distribution arrangements

30. The product distribution arrangements shall aim to prevent or mitigate customer detriment, support a proper management of conflicts of interests and shall ensure that the objectives, interests and characteristics of customers are duly taken into account.

Role of management

31. The insurance distributor's administrative, management or supervisory body, or equivalent structure responsible for insurance distribution, shall endorse and be ultimately responsible for the establishment, implementation, subsequent reviews and continued internal compliance with the product distribution arrangements.

Obtaining all necessary information on the target market from the manufacturer

32. The product distribution arrangements shall aim to ensure that the insurance distributor obtains all necessary information from the manufacturer on the insurance product, the product approval process, the target market in order to understand the customers for which the product is designed for, as well as the group(s) of customers for which the product is not designed for.

Obtaining all other necessary information on the product from the manufacturer

33. The product distribution arrangements shall aim to ensure that the insurance distributor obtains all other necessary information on the product from the manufacturer in order to fulfil its regulatory obligations towards the customers. This includes information on the main characteristics of the

products, its risks and costs as well as circumstances which may cause a conflict of interests at the detriment of the customer.

Distribution strategy

34. Where the insurance distributor sets up or follows a distribution strategy, it shall not contradict the distribution strategy and the target market identified by the manufacturer of the insurance product.

Regular review of product distribution arrangements

35. The insurance distributor shall regularly review the product distribution arrangements to ensure that they are still valid and up to date and shall amend them where appropriate, in particular the distribution strategy, if any.

Provision of sale information to the manufacturer

36. The insurance distributor shall inform the manufacturer without undue delay if he becomes aware that the product is not aligned with the interests, objectives and characteristics of the target market or if he becomes aware of other product related circumstances increasing the risk of customer detriment.

Documentation

37. Relevant actions taken by the insurance distributor in relation to the product distribution arrangements shall be duly documented, kept for audit purposes and made available to the competent authorities on request.

Questions to stakeholders:

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

3. Are there any further arrangements, except those outlined below, which you would consider necessary and important?

4. What costs will manufacturers and distributors face to meet these requirements? If possible, please estimate the costs through quantitative data.

4.2 New Policy Proposals

1. The following policy proposals have been developed in order to elaborate on issues which have not been addressed by EIOPA's previous policy work, but which EIOPA considers important in view of the Commission's mandate to provide technical advice on possible delegated acts to further specify the product oversight and governance arrangements under Article 25, IDD. As these proposals are supplementary to the principles outlined above, it should be noted that EIOPA's final technical advice will entail a consolidated and comprehensive set of policy principles to avoid any inappropriate duplication or overlap.

4.2.1. Acting as manufacturer

Background

Article 25(1), IDD provides:

"Insurance undertakings, as well as intermediaries which manufacture any insurance product for sale to customers, shall maintain, operate and review a process for the approval of each insurance product, or significant adaptations of an existing insurance product, before it is marketed or distributed to customers".

Article 9(1) of the draft Commission Delegated Directive under MiFID II covering product governance requirements, provides:

"Member States shall require investment firms to comply with this Article when manufacturing financial instruments, which encompasses the creation, development, issuance and/or design of financial instruments".

Analysis

2. Article 25(1), IDD acknowledges that, in certain circumstances, insurance intermediaries can be involved in the manufacturing of insurance products. As a consequence and in order to guarantee a level playing field, the IDD extends the product oversight and governance arrangements which apply for insurance undertakings manufacturing insurance products to insurance intermediaries which pursue such activities as well.
3. EIOPA considers it important to provide further guidance under which circumstances the activities of an insurance intermediary should be considered as manufacturing and further specifies what "manufacturing" means. Therefore, EIOPA considers it important to outline and specify under which conditions and based upon which criteria, an insurance intermediary can be considered as acting as a manufacturer.
4. Taking into account the principle of proportionality, it is clear that not all kinds of involvement or influence of an insurance intermediary in the design and manufacturing of an insurance product, should be considered as manufacturing.
5. Generally speaking, it can be expected that large brokers could more easily fall under the definition of "manufacturer" in comparison with tied agents – especially those who distribute products on behalf of a sole company. However, it is important to note that the IDD makes no distinction between brokers and tied

agents, adopting purely an activity-based definition of an “insurance intermediary”.

6. Taking into account the characteristics of the insurance distribution and the specific role of the insurance undertakings, it should be assumed that an intermediary can be considered a manufacturer only when it plays a key role in the design and development of insurance products.
7. This depends on the specific circumstances of the individual case and an overall analysis of the respective activities that the intermediary performs with regard to a specific product.
8. In particular, EIOPA considers that the following activities, taken on their own, cannot be considered significant and adequate in order to qualify an intermediary as a manufacturer:
 - 1) The mere call for tender for insurers to cover specific risks required by the insurance intermediary is not relevant when the insurance intermediary does not play any further role in the design of the product;
 - 2) The mere possibility to discount the commission or fee paid to the insurance intermediary;
 - 3) The activity of handling customer claims;
 - 4) The personalisation and adaptation of existing insurance products in the course of insurance distribution activities to the individual customer, in particular cases such as the mere opportunity to choose between different lines of products, contractual clauses and options, recommendation of asset, with regard to a product already designed by the insurance undertaking.
9. On the other hand, EIOPA is of the view that an incisive role of the insurance intermediary can be exercised through one of the following practices:
 - (i) Design of a new product: the following situations can be included in the notion of “design” if the insurance intermediary plays a key role:
 - a) The insurance intermediary takes the initiative to design and define the main elements of a specific insurance product in view of or not a customer request;
 - b) The insurance intermediary describes a certain kind of coverage not already existing in the market for a particular type of customer and asks the undertaking to provide it; or
 - c) The undertaking provides the coverage and establishes the premium under the mandate of the insurance intermediary.
 - (ii) A change of significant elements of an existing product: this condition occurs when the coverage, premium, costs, risks, target market or benefits of a type of contract are modified. In all these cases, as the undertaking still provides the coverage, any change should be made under the mandate/authorization of the undertaking and subject to its approval.
10. It should be noted that the mere opportunity to choose between different lines of products, contractual clauses and options, recommendation of asset, with regard to product already designed by the insurance undertaking, is not relevant in order to qualify an insurance intermediary as a manufacturer.
11. **It should be highlighted that the presence of one of these activities cannot be considered as an unquestionable evidence of the**

qualification of the insurance intermediary as a manufacturer, but this conclusion should be based upon an overall analysis of the specific activity of the intermediary which should be carried out by the intermediary on a case-by-case basis for each product designed. A relevant criterion which should be taken into consideration, is, furthermore, the question whether the product is sold under the brand name of the insurance intermediary and whether the insurance intermediary owns the intellectual property rights in the brand name of the product.

12. However, it should be noted that, even in cases where an insurance intermediary is considered as acting as a manufacturer, the insurance undertaking providing the coverage (i.e. insurance provider), remains fully responsible to the customer for the contractual obligations resulting from the insurance product.
13. Therefore, the insurance undertaking providing the coverage should always be considered a co-manufacturer for the purposes of the application of POG requirements, its role and contractual responsibilities with regard to the customer and its role in the approval process of the insurance product.
14. Co-manufacturing partnerships should necessarily be established in a written agreement, so that competent authorities are in a position to control collaboration arrangements.
15. In this case, through a necessary and proportionate collaboration between the two manufacturers (the insurance undertaking and the insurance intermediary/manufacturer *de facto*), all the arrangements and forms of collaboration necessary should be put in practice in order to comply with the product governance requirements for each product co-designed.

Draft technical advice

Acting as manufacturer

1. An insurance intermediary shall be considered as a manufacturer if the insurance intermediary plays a key role in designing and developing an insurance product for the market.
2. A key role shall be assumed, in particular, if the insurance intermediary is substantially involved in one of the following activities and provides substantial input into the following:
 - Defining the main elements of a new insurance product, such as the coverage, premium, costs, risks, target market or compensation and guarantee rights of the insurance product, or
 - Changing such elements of an existing product.
3. Activities which relate to the personalisation and adaptation of existing insurance products in the course of insurance distribution activities to the individual customer shall not be considered as activities of manufacturing, in particular cases such as the mere opportunity to choose between different lines of products, contractual clauses and options, individual premium discounts, recommendation of asset, with regard to a product already designed by the insurance undertaking.

4. Where an insurance intermediary is considered as a manufacturer, the insurance intermediary and insurance undertaking issuing the insurance product shall define their collaboration and their respective roles in a written agreement (e.g. the task to identify the target market). The insurance undertaking remains fully responsible to the customer for the coverage provided.

Questions to stakeholders:

5. Do you agree with the proposed high-level principle in order to assess whether activities of an insurance intermediary should be considered as manufacturing?

6. Do you consider that there is sufficient clarity regarding the collaboration between insurance undertakings and insurance intermediaries which are involved in the manufacturing of insurance products? If not, please provide details of how the collaboration should be established.

4.2.2. Granularity of the target market

Background

Article 25(1)(3), IDD provides:

"The product approval process shall specify an identified target market for each product, ensure that all relevant risks to such identified target market are assessed and that the intended distribution strategy is consistent with the identified target market, and take reasonable steps to ensure that the insurance product is distributed to the identified target market".

Articles 9(9), (11) and (12) of the draft Commission Delegated Directive under MiFID II, covering product governance requirements, provide:

"9. Member States shall require investment firms to identify at a sufficiently granular level the potential target market for each financial instrument and specify the type(s) of client for whose needs, characteristics and objectives the financial instrument is compatible. As part of this process, the firm shall identify any group(s) of clients for whose needs, characteristics and objectives the financial instrument is compatible. As part of this process, the firm shall identify any group(s) of clients for whose needs, characteristics and objectives the financial instrument is not compatible. Where investment firms collaborate to manufacture a financial instrument, only one target market needs to be identified.

Investment firms manufacturing financial instruments that are distributed through other investment firms shall determine the needs and characteristics of clients for whom the product is compatible based on their theoretical knowledge of and past experience with the financial instrument or similar financial instruments, the financial markets and the needs, characteristics and objectives of potential end clients.

11. Member States shall require investment firms to determine whether a financial instrument meets the identified needs, characteristics and objectives of the target market, including by examining the following elements:

(a) the financial instrument's risk/reward profile is consistent with the target market; and

(b) financial instrument design is driven by features that benefit the client and not by a business model that relies on poor client outcomes to be profitable".

Analysis

1. The IDD, the draft Delegated Directive under MiFID II and the Preparatory Guidelines developed by EIOPA on POG arrangements for insurance undertakings and insurance distributors, serve as a basis for the technical advice to be provided to the Commission.
2. EIOPA considers it important to take account of the principle of proportionality when considering the granularity of the target market. As stated above, insurance products are quite heterogeneous and their complexity varies. Some insurance products are obligatory for consumers and product choice would be limited. This is, for example, the case with motor insurance products. Some insurance products are complex such as many Insurance-Based Investment

Products (IBIPs). All products differ and, therefore, the granularity of the target markets can differ depending on the complexity and nature of the product and the risk of consumer detriment. There may be product limitations which are simple to understand, but would mean that the target market assessment would need to be more granular in detail.

3. At the same time, the IDD prescribes that any insurance product proposed should always be consistent with the customer's demands and needs²². EIOPA considers it important that products are manufactured and sold in line with the interests, characteristics and objectives of the customers belonging to the identified target market.
4. Insurance undertakings and insurance intermediaries which manufacture insurance products (hereafter "manufacturers") should therefore design products and bring them to the market only if they are aligned with these principles. Even with compulsory motor insurance products, for example, not all customers would need 'fully comprehensive' coverage meaning that a 'fully comprehensive' product would not be compatible for all customers. Therefore, specification of the target market should be more meaningful than simply describing it as 'mass market' suitable for any type of insurance product.
5. This approach is in line with the principles underlying other customer assessments in IDD, such as the "demands and needs" test and the suitability and appropriateness tests. The criteria used in these tests could also be relevant to define the target market since the target market is a description of the characteristics of a group of consumers and the assessments in IDD, test whether a product (or service) is appropriate for an individual consumer.
6. Examples of criteria which could be considered to determine the target market are detailed below. It should be noted that the examples are not exhaustive. If necessary, manufacturers should add additional categories based on the specific product and risk profile.
7. The criteria differ depending on the type of insurance product and the insurance coverage provided. Not all criteria which are relevant for one type of insurance product might be relevant for another type of insurance product as well. The level of detail will depend on the complexity of the product and some criteria may not be appropriate for less complex products.
8. Examples for all insurance products:
 - the level of the target market's knowledge and understanding of the complexity of the product,
 - the objectives, demands and needs of the customers belonging to the target market.
9. Examples, in particular, for IBIPs:
 - the age of the customers belonging to target market;
 - the occupational situation of the customers belonging the target market;
 - the level of risk tolerance of the customers belonging the target market;
 - the financial situation of the customers belonging the target market;
 - the financial and non-financial objectives and investment horizon of the customers belonging the target market.

²² Article 20(1)(2), IDD.

10. Examples, in particular, for health insurance:
 - The occupational situation of the customers belonging the target market;
 - The social security coverage of the customers belonging the target market;
11. Examples for other insurance products:
 - Risks, coverage, needs etc.
12. The level of knowledge and understanding of the product could also include experience of targeted consumers with similar products. The customer's financial situation could, for example, be relevant for the sale of Payment Protection Insurance (PPI). Is the product suitable for consumers with a temporary employment contract or is it only suitable for consumers with a fixed contract?
13. The policy proposal makes clear that identifying for whom the product may not be suitable, is helpful in order to obtain a clear picture of cases where it may be rather obvious for whom the product would not be suitable (e.g. a life insurance policy running for 30 years for a 97-year-old woman). If an insurance product is not compatible with the needs, characteristics, objectives and demands of a specific group of customers, the manufacturer shall also identify the target market to which the insurance product should not be distributed.
14. The level of granularity is a broad topic and in the insurance market there is a wide range of products which differ in characteristics and complexity. The features listed above may not be appropriate for all insurance products and should be applied using a risk-based approach.

Draft technical advice

Granularity of the target market

1. When manufacturing products, the manufacturer shall identify the target market for each product and specify the type(s) of customer for whose needs, characteristics, objectives and demands, the product is compatible.
2. When defining the target market it shall be considered whether an insurance product is compatible for a specified type of customer taking into account criteria such as the demands and needs, and, where relevant with regard to the complexity of the product, the knowledge and experience as well as the financial situation and objectives of that type of customer. As the target market describes a group of consumers at a broader and more abstract level, it differs from the individual assessment whether an insurance product corresponds with the demands and needs of a specific customer and where applicable whether the insurance product is suitable or appropriate for a specific customer.
3. The target market shall be identified at a sufficiently granular level depending on the characteristics, risk profile and complexity of the product, avoiding groups of customers/consumers for whose needs, characteristics, objectives and demands the product is generally not compatible.

4. Where relevant, the manufacturer shall identify any groups of customers for whose demand and needs, characteristics, objectives and demands the product is typically not compatible.

Questions to stakeholders:

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.

4.2.3. Review of the product governance arrangements and of the products

Background

Articles 9(7), (14) and (15) of the draft Commission Delegated Directive under MiFID II, provide the following:

Product governance obligations for investment firms manufacturing financial instruments

7. Investment firms shall ensure the compliance function monitors the development and periodic review of product governance arrangements in order to detect any risk of failure by the firm to comply with the obligations set out in this Article.

14. Member States shall require investment firms to review the financial instruments they manufacture on a regular basis, taking into account any event that could materially affect the potential risk to the identified target market. Investment firms shall consider if the financial instrument remains consistent with the needs, characteristics and objectives of the target market and if it is being distributed to the target market, or is reaching clients for whose needs, characteristics and objectives the financial instrument is not compatible.

15. Member States shall require investment firms to review financial instruments prior to any further issue or re-launch, if they are aware of any event that could materially affect the potential risk to investors and at regular intervals to assess whether the financial instruments function as intended. Investment firms shall determine how regularly to review their financial instruments based on relevant factors, including factors linked to the complexity or the innovative nature of the investment strategies pursued. Firms shall also identify crucial events that would affect the potential risk or return expectations of the financial instrument, such as:

- (a) the crossing of a threshold that will affect the return profile of the financial instrument; or*
- (b) the solvency of certain issuers whose securities or guarantees may impact the performance of the financial instrument.*

Member States shall ensure that, when such events occur, investment firms take appropriate action which may consist of:

- (a) the provision of any relevant information on the event and its consequences on the financial instrument to the clients or the distributors of the financial instrument if the investment firm does not offer or sell the financial instrument directly to the clients;*
- (b) changing the product approval process;*
- (c) stopping further issuance of the financial instrument;*
- (d) changing the financial instrument to avoid unfair contract terms;*
- (e) considering whether the sales channels through which the financial instruments are sold are appropriate where firms become aware that the financial instrument is not being sold as envisaged;*
- (f) contacting the distributor to discuss a modification of the distribution process;*

- (g) terminating the relationship with the distributor; or*
- (h) informing the relevant competent authority.*

Articles 10(4), (5) and (6) of the draft Commission Delegated Directive under MiFID II, provide the following:

Product governance obligations for distributors

4. Member States shall require investment firms to periodically review and update their product governance arrangements in order to ensure that they remain robust and fit for their purpose, and take appropriate actions where necessary.

5. Member States shall require investment firms to review the investment products they offer or recommend and the services they provide on a regular basis, taking into account any event that could materially affect the potential risk to the identified target market. Firms shall assess at least whether the product or service remains consistent with the needs, characteristics and objectives of the identified target market and whether the intended distribution strategy remains appropriate. Firms shall reconsider the target market and/or update the product governance arrangements if they become aware that they have wrongly identified the target market for a specific product or service or that the product or service no longer meets the circumstances of the identified target market, such as where the product becomes illiquid or very volatile due to market changes.

6. Member States shall require investment firms to ensure their compliance function oversee the development and periodic review of product governance arrangements in order to detect any risk of failure to comply with the obligations set out in this Article.

EBA's Guidelines on product oversight and governance arrangements provide the following:

Guideline 9.2: "The distributor should review and update the product oversight and governance arrangements on a regular basis."

Analysis

1. The Preparatory Guidelines developed by EIOPA on POG can serve as a basis for the advice to be provided to the European Commission. However several aspects are not covered by the EIOPA Preparatory Guidelines.
2. **The provisions related to review under the EIOPA Preparatory Guidelines only cover POG arrangements as a whole. However, the Commission's request for technical advice also asks manufacturers and distributors to review the products they manufacture or offer.** The review of products should therefore be added to the technical advice, in addition to the policy provisions in the EIOPA Preparatory Guidelines.

3. The Level 1 Directive requires insurance undertakings to regularly review the insurance products they offer or market. The issue of the frequency of the review was discussed in the impact assessment of the EIOPA Preparatory Guidelines and more specifically, whether the frequency of the review should be determined. The pros and cons of both options were discussed and EIOPA concluded that, given the wide range of products offered as well as the differences between the actors selling the products, that the frequency of the reviews should not be uniformly determined.
4. Instead, the decision with regards to the frequency of the review, should be left to the manufacturer (and the distributor, where appropriate). However, the manufacturer should be required to determine the frequency of review on his own, allowing him to take into consideration the product specificities. This option allows each manufacturer to adapt the correct frequency of the review process in line with the timing of the internal design product, also taking into account the size, scale and complexity of the insurance undertaking and of the different products it manufactures.
5. It is important that the manufacturer and the distributor coordinate their reviews and should aim to have similar frequencies of reviews. However, EIOPA considers the delegated acts should specify that the manufacturer should decide how regularly *their products* should be reviewed: This should be based on relevant factors such as the nature of the product and the target market or if they become aware of any event that could materially affect the potential risk to investors.
6. EIOPA considers manufacturers and distributors should take appropriate action when they become aware of an event that could materially affect the potential guarantees to the identified target market. However, given the wide range of products offered as well as the differences between the undertakings selling the products, EIOPA considers that there should be no determined action to be taken in all cases and that flexibility should be given to manufacturers and distributors to decide what steps they need to take based on the circumstances of the case.
7. Nevertheless, the manufacturers and distributors should make their best effort to identify events that would materially affect the potential guarantees expectations of the product and, when such an event occurs, they should take appropriate actions on a case-by-case basis. These actions could be the following (the list is not exhaustive):
 - The provision of any relevant information on the event and its consequences on the product to the customers, or the distributors of the product if the firm does not offer directly the product to the customer;
 - Changing the product approval process;
 - Changing the product;
 - Proposing a new product to the customer;
 - Changing the target market;
 - Stopping further issuance of the product;
 - Contacting the distributor to discuss a modification of the distribution process;
 - Terminating the relationship with the distributor;
 - Informing the relevant competent authority; or
 - Informing the customer.

8. EIOPA is of the opinion that the management body and/or, if delegated, the compliance function of the manufacturer should have a role in the oversight of the product governance process. This should in any case be in line with the role of the administrative, management or supervisory body (AMSB) under Solvency II.

Draft Technical Advice

Review obligations for insurance undertakings and insurance intermediaries which manufacture insurance products for sale to consumers

1. The manufacturer shall regularly review the product oversight and governance arrangements to ensure that they are still valid and up to date and the manufacturer should amend them where appropriate.
2. The manufacturer shall also review the product it manufactures on a regular basis and should take into account any event that could materially affect the risk coverage and guarantees offered to the identified target market. The manufacturer should determine the frequency for the regular review of its products taking into account the size, scale and complexity of the different products it manufactures. The manufacturer shall also consider the characteristics of the target market. The manufacturer and the distributor shall have appropriate written agreements in place in order to coordinate their reviews.
3. When reviewing existing products, the manufacturer shall consider if the product remains consistent with the needs, characteristics and objectives of the target market and consider if the product is being distributed to the target market, or is reaching customers outside of the target market.
4. On a continuous basis, the manufacturer shall identify crucial events that would affect the main features and coverage of the product, e.g. the potential risk or return expectations, when such an event occurs, it shall take appropriate action.
5. The manufacturer's compliance function or senior management in case of distributors which have not established a compliance function, shall oversee the development and the review of product governance arrangements in order to detect any risk of failure to comply with its obligations.

Review obligations for insurance distributors which advise on or propose insurance products which they do not manufacture

6. The distributor shall regularly review the product distribution arrangements to ensure that they are still valid and up to date. The manufacturer and the distributor shall have appropriate written agreements in place in order to coordinate their reviews.

7. If the distributor has independently set up a distribution strategy, he shall amend the distribution strategy in view of the outcome of the review, where appropriate.
8. If the distributor becomes aware of any problems regarding the target market for a specific product or service or that a given product or service no longer meets the circumstances of the identified target market, he shall promptly inform the manufacturer and, as appropriate, update the distribution strategy already put in place.
9. When reviewing distribution arrangements, the distributor shall consider if the product is being distributed to the identified target market, or is reaching customers outside of the target market.
10. The distributor shall determine how regularly to review the product distribution arrangements based on relevant factors and taking into account the size, scale and complexity of the different products it distributes.
11. Upon request, distributors shall provide the manufacturer with relevant sales information and, if necessary, information on the above reviews to support product reviews carried out by manufacturers.
12. The distributor's management shall oversee the development and the review of product governance arrangements in order to detect any risk of failure by distributors to comply with its obligations in this chapter.

Questions to stakeholders:

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?

4.2.4 Obtaining appropriate information on the product

Analysis

1. The new IDD rules on POG arrangements aim to strengthen the exchange of product-related information between the manufacturer and distributor.
2. According to Article 25(1)(5), IDD, insurance undertakings, as well as insurance intermediaries which manufacture insurance products, shall make available to distributors all appropriate information on the insurance product and the product approval process, including the identified target market of the insurance product.
3. Vice-versa, according to Article 25(1)(6), IDD, where the insurance distributor advises on or proposes insurance products which it does not manufacture, it shall have in place adequate arrangements to obtain the information (referred to above) and to understand the characteristics and identified target market of each insurance product.
4. The purpose of these requirements is to ensure that the distributor receives all necessary information on the product and the product approval process from the manufacturer which is considered as an important prerequisite in order to carry out the insurance distribution activities in accordance with the best interests of their customers.
5. The purpose of the requested exchange of information between manufacturers and distributors is laid down in Recital 55, IDD, stating that the distributor should *"in any case be able to understand the characteristics and identified target market of each insurance product"*.
6. The importance of having appropriate knowledge and competence is furthermore emphasised in the general rule of Article 10, IDD requiring insurance distributors and their employees carrying out insurance distribution activities, to possess appropriate knowledge and ability in order to complete their tasks and perform their duties adequately.
7. However, the obligation of the manufacturer to make available *"all appropriate information"* and the obligation of the distributor to obtain that information as laid down in Article 25 of IDD is generally abstract and high-level.
8. Besides the identified target market, the IDD neither specifies the information which the manufacturer is required to make available to the distributor nor specifies the consequences if the distributor does not receive all appropriate information. In view of the importance of this matter, EIOPA considers it important to further specify the information, which the distributor should obtain in order to be in a position to distribute the insurance products to its customers further.
9. In view of the variety of insurance products and product features, EIOPA does not consider it appropriate to propose an exhaustive list of information which the distributor should obtain. Instead, EIOPA proposes to introduce a high-level principle combined with specific information details, which should be understood as the bare minimum (see draft policy proposal below).
10. Taking into consideration the principle of proportionality, the level of information details should take into account the complexity and comprehensibility of the products, the risks of the product and the services provided with regard to the respective products (advice, non-advised sale, execution-only).

11. In order to ensure the information flow, EIOPA considers it important that the manufacturer and distributor specify their respective obligations to exchange the information in a written agreement.
12. With regard to the consequences in cases where the distributor fails to obtain all relevant information on the product from the manufacturer or from public sources, EIOPA notes that the legal text of the IDD does not specify what the consequence should be. From a customer protection point of view, however, EIOPA would consider it important that the distributor is pre-emptively prevented from recommending insurance products in order to avoid any detriment to customers' interests from the outset. This would be complementary to the empowerment of competent authorities to impose (*ex post*) sanctions for infringing the conduct of business requirements set out in Chapter V of IDD.

Draft Technical Advice

Information to obtain and written agreement

1. The manufacturer shall make available to the distributor all product-related information which is necessary to carry out insurance distribution activities in accordance with the best interests of its customers, including, but not limited to, information on the product structure and features and product risks, the product costs (including implicit costs), information to assess whether the product offers an added value to the customer, information on the target market and distribution strategy.
2. The manufacturer shall conclude written agreements with the distributor to specify the relevant information details as outlined in paragraph 1.

5. Conflicts of Interest

Background/mandate

Extract from the Commission's request for advice (mandate)

"EIOPA is invited to provide technical advice on:

- the different steps that insurance intermediaries and insurance undertakings distributing insurance-based investment products might reasonably be expected to take within an effective organisational and administrative arrangement designed to identify, prevent, manage and disclose conflicts of interest;*
- the circumstances and situations to take into account when determining which types of conflict of interest may damage the interests of the customers or potential customers of an insurance intermediary or insurance undertaking.*

The technical advice should specify the different steps to be taken within an effective organisational and administrative arrangement designed to identify, prevent, manage and disclose conflicts of interest. This should include, in particular, the requirements for periodical review of conflicts of interest policies and clarifications with respect to the last resort nature of disclosure which should not be over-relied on by insurance intermediaries and insurance undertakings nor used as a measure to manage conflicts of interest. Particular attention should be given to the practical implementation of the proportionality requirement.

In order to ensure regulatory consistency, the technical advice should build on existing conflict of interest rules, as laid down in Commission Directive 2006/73/EC, particularly with regard to establishing appropriate criteria for determining the types of conflict of interest whose existence may damage the interests of customers or potential customers. It should also be consistent with the line taken in the delegated acts expected to be adopted under Article 23(4) of MiFID II."

1. The relevant provisions in the Insurance Distribution Directive are:

Recital 39:

"The expanding range of activities that many insurance intermediaries and undertakings carry on simultaneously has increased potential for conflicts of interest between those different activities and the interests of their customers. It is therefore necessary to provide for rules to ensure that such conflicts of interest do not adversely affect the interests of the customer".

Recital 57:

"In order to ensure that any fee or commission or any non-monetary benefit in connection with the distribution of an insurance-based investment product paid to or paid by any party, except the customer or a person on behalf of the customer, does not have a detrimental impact on the quality of the relevant service to the customer, the insurance distributor should put in place appropriate and proportionate arrangements in order to avoid such detrimental impact. To that end, the insurance

distributor should develop, adopt and regularly review policies and procedures relating to conflicts of interest with the aim of avoiding any detrimental impact on the quality of the relevant service to the customer and of ensuring that the customer is adequately informed about fees, commissions or benefits”.

Article 27:

“Without prejudice to Article 17, an insurance intermediary or an insurance undertaking carrying on the distribution of insurance-based investment products shall maintain and operate effective organisational and administrative arrangements with a view to taking all reasonable steps designed to prevent conflicts of interest as determined under Article 28 from adversely affecting the interests of its customers. Those arrangements shall be proportionate to the activities performed, the insurance products sold and the type of the distributor.”

Article 28:

1. *“Member States shall ensure that insurance intermediaries and insurance undertakings take all appropriate steps to identify conflicts of interest between themselves, including their managers and employees, or any person directly or indirectly linked to them by control, and their customers or between one customer and another, that arise in the course of carrying out any insurance distribution activities.*
2. *Where organisational or administrative arrangements made by the insurance intermediary or insurance undertaking in accordance with Article 27 to manage conflicts of interest are not sufficient to ensure, with reasonable confidence, that risks of damage to customer interests will be prevented, the insurance intermediary or insurance undertaking shall clearly disclose to the customer the general nature or sources of the conflicts of interest, in good time before the conclusion of an insurance contract.*
3. *By way of derogation from Article 23(1), the disclosure referred to in paragraph 2 of this Article shall:*
 - (a) *be made on a durable medium; and*
 - (b) *include sufficient detail, taking into account the nature of the customer, to enable that customer to take an informed decision with respect to the insurance distribution activities in the context of which the conflict arises.*
4. *The Commission shall be empowered to adopt delegated acts in accordance with Article 38 in order to:*
 - (a) *define the steps that insurance intermediaries and insurance undertakings might reasonably be expected to take to identify, prevent, manage and disclose conflicts of interest when carrying out insurance distribution activities;*
 - (b) *establish appropriate criteria for determining the types of conflict of interest whose existence may damage the interests of the customers or potential customers of the insurance intermediary or insurance undertaking.”*

Analysis

2. EIOPA has been invited by the Commission to provide technical advice on organisational and administrative arrangements designed to identify, prevent, manage and disclose conflicts of interest that arise in the course of carrying out any insurance distribution activities.
3. In its Mandate, the Commission explicitly invites EIOPA to build on the results of previous work that has already been carried out by EIOPA, such as EIOPA's previous technical advice on conflicts of interests in direct and intermediated sales of insurance-based investment products²³. The latter was submitted to the Commission on 6 January 2015 and referred to the rules on conflicts of interest which were introduced under Article 91, MiFID II²⁴ and were originally supposed to amend the Insurance Mediation Directive (IMD)²⁵.
4. Taking into consideration that the new requirements on conflicts of interest as outlined in Articles 27 and 28, IDD, are almost identical with the requirements which have been originally introduced under MiFID II, EIOPA considers it appropriate to base its current technical advice on the previous policy recommendations. Some changes, in particular with regard to the disclosure of conflicts of interest, have been introduced for the sake of consistency with the wording of the Level 1 text and for the purpose of alignment with the draft Commission Delegated Regulation under MiFID II regarding organisational requirements and operating conditions for investment firms²⁶.
5. For this purpose, it has been clarified that the disclosure of conflict of interest should be understood as step of last resort to be used only in cases where the organisational and administrative measures are not sufficient to effectively prevent and manage conflicts of interest. Any overreliance on disclosure should be considered a deficiency in the conflicts of interest policy.
6. Instances where conflicts of interest typically arise and which need to be appropriately managed by the insurance undertakings or insurance intermediary include the following:
 - The insurer/intermediary has an own interest in selling products of its own group (e.g. funds contained in a unit linked product);
 - The insurer/intermediary is receiving sales commissions and/or follow-up commissions;
 - There is a horizontal conflict of interest between different customers, because there is higher demand for a specific life product than occasion for concluding of contracts/supply;
 - The insurer/intermediary is earning money in case of a change of funds during the lifetime of a unit-linked life insurance contract; or
 - The insurer/intermediary can have an interest to recommend or not to recommend a certain insurance-based investment product due to his own portfolio (own-account trading).
7. EIOPA also notes that the European legislator has put emphasis on the application of the principle of proportionality in stating in Article 27, IDD, that the "*arrangements shall be proportionate to the activities performed, the insurance*

²³ [https://eiopa.europa.eu/Publications/Opinions/EIOPA-15-135_Technical%20Advice%20%20Impact%20Assessment_conflicts_of_interest_version%20for%20COM%20\(2\).pdf](https://eiopa.europa.eu/Publications/Opinions/EIOPA-15-135_Technical%20Advice%20%20Impact%20Assessment_conflicts_of_interest_version%20for%20COM%20(2).pdf)

²⁴ <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32014L0065>

²⁵ <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32002L0092>. By virtue of Article 43, IDD, Chapter IIIA of the IMD is deleted with effect from 23 February 2016.

²⁶ <http://ec.europa.eu/transparency/regdoc/rep/3/2016/EN/3-2016-2398-EN-F1-1.PDF>

products sold and the type of distributor". EIOPA would like to point out that the policy proposals which were developed for the IMD explicitly refer to the principle of proportionality in stating that the procedures and measures should be "*appropriate to the size and activities of the insurance intermediaries or insurance undertaking ... and to the materiality of the risk of damage to the interests of the customers*". Against this backdrop, EIOPA would like to raise the question whether further specification and guidance in a separate policy instrument, on the principle of proportionality in the context of conflicts of interest, are seen as necessary from the view of market participants.

Draft Technical Advice

Identification of conflicts of interests

1. For the purpose of identifying the types of conflict of interest that arise in the course of carrying out any insurance distribution activities related to insurance-based investment products and which entail the risk of damage to the interests of a customer, insurance intermediaries and insurance undertakings shall assess whether they, including their managers, employees or any person directly or indirectly linked to them by control, have an interest related to the insurance distribution activities which is distinct from the customer's interest and which has the potential to influence the outcome of the services to the detriment of the customer. Insurance intermediaries and undertakings shall also identify conflicts of interest between one customer and another.
2. Conflicts of interests referred to above shall at least be assumed in situations including the following:
 - a. the insurance intermediary, insurance undertaking or linked person is likely to make a financial gain, or avoid a financial loss, at the expense of the customer;
 - b. the insurance intermediary, insurance undertaking or linked person has a financial or other incentive to favour the interest of another customer or group of customers over the interests of the customer;
 - c. the insurance intermediary, insurance undertaking or linked person receives or will receive from a person other than the customer a monetary or non-monetary benefit in relation to the insurance distribution activities provided to the customer;
 - d. the insurance intermediary, persons working in an insurance undertaking responsible for the distribution of insurance-based investment products or linked person are involved in the management or development of the insurance based-investment products.

Conflicts of interest policy

3. Insurance intermediaries and insurance undertakings shall establish, implement and maintain an effective conflicts of interest policy set out in writing and appropriate to their size and organisation and the nature, scale and complexity of their business. Where the insurance intermediary or insurance undertaking is a member of a group, the policy must also take into account any circumstances, of which the insurance intermediary or insurance undertaking is

or should be aware, which may give rise to a conflict of interest arising as a result of the structure and business activities of other members of the group.

4. The conflicts of interest policy established in accordance with paragraph 3 shall include the following content:
 - (a) it must identify, with reference to the specific insurance distribution activities carried out, the circumstances which constitute or may give rise to a conflict of interest entailing a risk of damage to the interests of one or more customers;
 - (b) it must specify procedures to be followed and measures to be adopted in order to manage and prevent such conflicts from damaging the interests of the customer of the insurance intermediary or insurance undertaking, appropriate to the size and activities of the insurance intermediaries or insurance undertaking and of the group to which they belong, and to the risk of damage to the interests of the customer.
5. For the purpose of paragraph 4(b), the procedures to be followed and measures to be adopted shall include, where appropriate, in order to ensure that the distribution activities are carried out in accordance with the best interest of the customer and are not biased by conflicting interests of the insurance undertaking, the insurance intermediary or another customer, the following:
 - (a) effective procedures to prevent or control the exchange of information between relevant persons engaged in activities involving a risk of a conflict of interest where the exchange of that information may damage the interests of one or more customers;
 - (b) the separate supervision of relevant persons whose principal functions involve carrying out activities on behalf of, or providing services to, customers whose interests may conflict, or who otherwise represent different interests that may conflict, including those of the insurance intermediary or insurance undertaking;
 - (c) the removal of any direct link between payments, including remuneration, to relevant persons principally engaged in one activity and payments, including remuneration to different relevant persons principally engaged in another activity, where a conflict of interest may arise in relation to those activities;
 - (d) measures to prevent or limit any person from exercising inappropriate influence over the way in which a relevant person carries out insurance distribution activities;
 - (e) measures to prevent or control the simultaneous or sequential involvement of a relevant person in insurance distribution activities where such involvement may impair the proper management of conflicts of interest.
6. If insurance intermediaries and insurance undertakings demonstrate that those measures and procedures are not appropriate to ensure that the distribution activities are carried out in accordance with the best interest of the customers and are not biased by conflicting interests of the insurance undertakings, the insurance intermediaries or another customer, insurance intermediaries and insurance undertakings must adopt adequate alternative measures and procedures for that purpose.
7. Insurance intermediaries and insurance undertakings shall avoid over reliance on disclosure and shall ensure that disclosure, pursuant to Article 28(2) of Directive 2016/97/EC, is a step of last resort that can be used only where the effective organisational and administrative measures established by insurance intermediaries and insurance undertakings to prevent or manage conflicts of

interests in accordance with Article 27 thereof are not sufficient to ensure, with reasonable confidence, that the risks of damage to the interests of the customer will be prevented.

8. Insurance intermediaries and insurance undertakings shall make that disclosure to customers, pursuant to Article 28(3) of Directive 2016/97/EC, in a durable medium. The disclosure shall:

- (a) include a specific description of the conflict of interest, including the general nature and sources of the conflict of interest, as well as the risks to the customer that arise as a result of the conflict of interest and the steps undertaken to mitigate these risks,
- (b) to clearly state that the organisational and administrative arrangements established by the insurance intermediary or insurance undertaking are not sufficient to ensure, with reasonable confidence, that the risks of damage to the interests to the customers will be prevented, in order to enable the customer to take an informed decision with respect to the insurance distribution activities in the context of which the conflict of interest arises.

9. Insurance intermediaries and insurance undertakings shall:

- (a) assess and periodically review – at least annually – the conflicts of interest policy established in accordance with this article and to take all appropriate measures to address any deficiencies, and
- (b) keep and regularly update a record of the situations in which a conflict of interest entailing a risk of damage to the interests of the one or more customers has arisen or, in the case of an ongoing service or activity, may arise.

10. Where established, senior management shall receive on a frequent basis, and at least annually, written reports on these situations.

Questions to stakeholders:

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.

10. Do you agree that the policy proposals do not need further specification of the principle of proportionality and allow sufficient flexibility to market participants to adapt the organisational arrangements to existing business models? If you do not agree, please explain how the principle of proportionality could be elaborated further from your point of view?

6. Inducements

Background/mandate

Extract from the Commission's request for advice (mandate)

"EIOPA is invited to provide technical advice on:

- the conditions under which payments and non-monetary benefits paid or received by insurance intermediaries or insurance undertakings in connection with the distribution of an insurance-based investment product may have a detrimental impact on the quality of the relevant service to the customer;*
- the circumstances and situations to take into account when determining whether an insurance distributor or an insurance undertaking paying or receiving inducements complies with its obligation to act honestly, fairly and professionally in accordance with the best interests of the customer.*

The technical advice should specify the methodology to be applied in determining a possible detrimental impact of inducements on the quality of the service and testing compliance with the insurance intermediaries' and insurance undertakings' duty to act in the best interests of its customers. Further clarification should be given with respect to the factual and legal elements and circumstances to take into account in determining whether the conditions set in Article 29(2) are met.

To achieve greater convergence in the application of the detrimental impact criteria, the technical advice should indicate examples of circumstances where a fee, commission or non-monetary benefit may generally be regarded as having a detrimental effect on the quality of the relevant service to the customer. This could be complemented by an exemplary enumeration of circumstances where third-party payments and benefits are generally considered acceptable. In the same way, it should identify circumstances indicating that an insurance intermediary or an insurance undertaking does not comply with the obligation to act honestly, fairly and in accordance with the best interests of the customer.

The technical advice should be consistent with the line taken in the delegated acts expected to be adopted under Article 24(13) of MiFID II, while recognising the difference in terminology between Article 29(2) (a) of the Directive and Article 24(9)(a) of MiFID II".

1. The relevant provisions in the Insurance Distribution Directive are:

Recital 57:

"In order to ensure that any fee or commission or any non-monetary benefit in connection with the distribution of an insurance-based investment product paid to or paid by any party, except the customer or a person on behalf of the customer, does not have a detrimental impact on the quality of the relevant service to the customer, the insurance distributor should put in place appropriate and proportionate arrangements in order to avoid such detrimental impact. To that end, the insurance distributor should develop, adopt and regularly review policies and procedures relating to conflicts of interest with the aim of avoiding any detrimental impact on the quality of the relevant service to the customer and of ensuring that the customer is adequately informed about fees, commissions or benefits".

Article 29(2):

"Without prejudice to points (d) and (e) of Article 19(1) and Article 22(3), Member States shall ensure that insurance intermediaries or insurance undertakings are regarded as fulfilling their obligations under Article 17(1), Article 27 or Article 28 where they pay or are paid any fee or commission, or provide or are provided with any non-monetary benefit in connection with the distribution of an insurance-based investment product or an ancillary service, to or by any party except the customer or a person on behalf of the customer only where the payment or benefit:

- (a) does not have a detrimental impact on the quality of the relevant service to the customer; and*
- (b) does not impair compliance with the insurance intermediary's or insurance undertaking's duty to act honestly, fairly and professionally in accordance with the best interests of its customers."*

Article 29(4):

"Without prejudice to paragraph 3 of this Article, the Commission shall be empowered to adopt delegated acts in accordance with Article 38 to specify:

- (a) the criteria for assessing whether inducements paid or receive by an insurance intermediary or an insurance undertaking have a detrimental impact on the quality of the relevant service to the customer;*
- (b) the criteria for assessing compliance of insurance intermediaries and insurance undertakings paying or receiving inducements with the obligation to act honestly, fairly and professionally in accordance with the best interests of the customer."*

Analysis

2. The Commission's request for advice refers to the *"payments and non-monetary benefits paid or received by insurance intermediaries or insurance undertakings in connections with the distribution of an insurance-based investment product"*.
3. Although IDD does not entail an explicit definition of an "inducement", Article 29(2), IDD clarifies that it refers to the payment of any fee or commission as well as the provision of any non-monetary benefit in connection with the distribution of an insurance-based investment product or an ancillary service, to or by any third party except the customer or a person on behalf of the customer. Unlike Article 17(3), IDD, Article 29(2) does not comprise internal payments from insurance distributors to their employees. In addition, the Commission's mandate makes explicit reference to "third party payments and benefits".
4. **Therefore, EIOPA's conclusion is that the Commission is seeking advice in relation to fees or commissions as well as non-monetary benefits paid by or to third parties only, but not in relation to internal payments (e.g. fees paid by the customer or internal payments to employees of insurance distributors).**
5. EIOPA understands the term, "inducement", as any fee, commission or non-monetary benefit which is paid or provided in connection with the distribution of an insurance-based investment product or an ancillary service to or by any party except the customer or a person on behalf of the customer.
6. In contrast, an "inducement scheme" is understood as set of rules that govern the payment of inducements and generally includes the obligations of the person paying the inducements and the person receiving the inducements. It normally outlines the criteria which the recipient of the inducements must achieve in order to earn an inducement and specifies the obligations to pay the inducements. It might elaborate on the amount of the inducement or how the inducement is calculated and any other governance measures in relation to the payment of the inducement. For example, an inducement scheme can be included as part of a contract of appointment between a distributor and a manufacturer.
7. The payment of inducements has been identified as a situation where a conflict of interest is likely to arise which can lead to a detrimental impact if it is not managed in accordance with a stringent conflicts of interest policy. Insurance intermediaries and insurance undertakings are expected to apply Articles 27 and 28, IDD to all situations where conflict of interests may arise, additional provisions exist in Article 29(2) in relation to inducements.
8. The Commission has asked EIOPA to provide technical advice on the conditions under which inducements may have a detrimental impact on the quality of the relevant service to the customer.
9. Although EIOPA has been asked by COM to ensure *"as much regulatory consistency as possible in the conduct of business standards for IBIPs and financial instruments under MiFID II"*, EIOPA notes that the IDD uses different terminology than the respective rules introduced by MiFID II which form the basis of ESMA's technical advice for MiFID II.
10. Whereas MiFID II requires that the inducement *"is designed to enhance the quality of the relevant service to the client"*²⁷, the IDD requires that the inducement does *"not have a detrimental impact on the quality of the relevant*

²⁷ Article 24(9)(a), MiFID II

*service to the customer*²⁸. From EIOPA's point of view, it is important to adequately consider these differences, which have been agreed upon by the European legislators, when establishing implementing measures for specifying the conditions under which inducements have a detrimental impact on the quality of the services.

11. In view of the cross-sectoral implications, EIOPA believes, however, that the approach for IDD should offer as much compatibility as possible to avoid any unnecessary burden for market participants and to further pursue the goal of a level playing field across the different financial sectors.
12. Against this background, EIOPA proposes to introduce a high-level principle stating the circumstances under which an inducement might have a "*detrimental impact on the relevant service to the customer*". For the sake of consistency, the high level principle mirrors the general requirement in Article 17(3), IDD requiring that any kind of remuneration does not "*incentivise a distributor to recommend a particular insurance product to a customer when the distributor could offer a different product which would better meet the customer's needs*".
13. For the sake of clarification, EIOPA would like to point out that, generally speaking, inducements which have a detrimental impact on the quality of the relevant service to the customer, also impair compliance with the insurance intermediary's or insurance undertaking's duty to act honestly, fairly and professionally in accordance with the best interests of its customers (Article 29 (2)(b) IDD). **For this reason, although the Commission's mandate mentions these two aspects separately, they have been analysed together for the purposes of this technical advice.**
14. Furthermore, EIOPA proposes to supplement the aforementioned high-level principle with a list of inducements to comply with the Commission's request for EIOPA to list "*examples of circumstances where a fee, commission or non-monetary benefit may generally be regarded as having a detrimental effect on the quality of the relevant service to the customer*".
15. EIOPA would like to clarify, however, that **this list is not supposed to introduce a legal assumption of detrimental impact, but to specify cases where "a high risk" of exposure to a detrimental impact exists. Therefore, EIOPA would like to emphasise that the objective of this list is not to introduce a *de facto* prohibition on the receipt/payment of inducements, but to provide guidance to market participants in assessing inducements and to point out specific circumstances where a detrimental impact is most likely to occur. The list builds upon supervisory work of national competent authorities²⁹** and entails payments

²⁸ Article 29(2)(a), IDD

²⁹ For example:

- The NL AFM reported in 2011 about **excessive commissions in the context of the distribution of payment protection insurance (PPI) products** where commissions of up to 86% of the single insurance premium were paid. It was also reported about the successful introduction of national legislation to eliminate "hit and run" practices which are initiated by revenue-related boni. Although referring to non-IBIPs products, this example shows the practical relevance of this issue: <https://www.rijksoverheid.nl/documenten/kamerstukken/2009/06/16/bijlage-provisies-voor-bemiddelaars-in-krediet-beschermers>
- UK FCA guidance on inducements published in January 2014 also provides a steer (<https://www.fca.org.uk/static/documents/finalised-guidance/fg14-01.pdf>). For example, paragraph 2.25 identifies examples of poor practice in relation to payments by providers for development by intermediaries of IT facilities. Similarly, paragraph 2.31 identifies generic examples of poor practices linked to **excessive payments by life insurers to advisory firms to attend their seminars and conferences**. Also para 2.36 refers to amounts of "**unreasonable value**" when providing gifts/prizes and hospitality.

such as contingent commissions³⁰, profit commissions, upfront commissions and excessive sales targets.

16. With regard to the request from the Commission to provide "an exemplary enumeration of circumstances where third-party payments and benefits are generally considered acceptable" EIOPA would like to emphasise that a "positive list" outlining circumstances generally be considered acceptable entails the high risk of creating loopholes for regulatory arbitrage. Therefore, EIOPA recommends not including such a positive list in the technical advice. However, EIOPA acknowledges that specific circumstances may be considered reducing the risk of detrimental impact on the quality of the relevant service to the customer and could be taken into consideration as part of an overall-assessment.
17. Without prejudice to additional requirements of IDD applicable to the insurance distribution, in particular Article 30 IDD, the possibility of Member States to impose stricter requirements as stated in Article 29(3), IDD and the outcome of a thorough overall-analysis of all relevant circumstances, the following practices may be considered to reduce the risk that inducements have a detrimental impact on the quality of the service to the customers, if they are appropriately taken into account:
 - The inducement scheme allows the insurance undertaking to claim back inducements in cases where the interests of a customer have been harmed while carrying out insurance distribution activities to the customer,
 - The inducement scheme provides for the prompt refunding of any inducements deducted from the customer's initial investment to the customer if the product lapses or is surrendered at an early stage,

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- In order to create a sounder market for advice on financial products, the Swedish Finansinspektionen (FI) has proposed **a ban on commissions in connection with investment advice and mediation of life insurance with elements of saving**. FI has specifically highlighted the problems with commissions paid out directly in connection with signing up for products or entering insurance agreements, known as **up-front commissions**. In 2014, the FI conducted a survey of commission income on the advisory market, covering around 200 insurance intermediaries, and firms authorised to conduct securities business. The survey showed that **"among both insurance intermediaries and investment firms, it is very common to have commissions that are paid out in direct connection with the customer purchasing the product, known as upfront commissions"....."Upfront commissions are particularly problematic because they also incentivise firms to recommend that consumers frequently switch investments, with the sole purpose of generating fresh commission income for the firm"**: http://www.fi.se/upload/90_English/20_Publications/10_Reports/2015/konsumentrapp_2015engNY.pdf
 - In **EIOPA's Third Annual Consumer Trends Report**, it was reported that DE, IE and NO carried out supervisory reviews of selling practices in response to mis-selling cases which found, for example, that sales incentive schemes might have components (**such as the use of thresholds/targets to unlock incentives, 100% variable remuneration**), which encouraged poor sales behaviour. The incentive schemes did not place sufficient emphasis on linking fair treatment of customers (or deterring/penalising poor treatment of customers) with the receipt of incentives: https://eiopa.europa.eu/Publications/Reports/EIOPA-BoS-14-207-Third_Consumer_Trends_Report.pdf
 - In **EIOPA's Fourth Annual Consumer Trends Report**, it was reported that "some NCAs also reviewed possible conflicts of interest arising from the selection of the underlying funds. If adequate governance and control frameworks are not in place, there is a risk that investments are made on the basis of those which provide the **highest commission from fund managers** and not in the best interests of the consumer": https://eiopa.europa.eu/Publications/Reports/EIOPA-BoS-15-233%20-%20EIOPA_Fourth_Consumer_Trends_Report.pdf

³⁰ Contingent commissions and profit commissions were also identified by the Commission, as sources of conflict of interest, in the context of its Sector Inquiry on business insurance in 2007 (notwithstanding that this inquiry was primarily focussed on non-life products in the non-retail sector): "Conflicts of interest that could jeopardise the role of brokers and multiple agents in stimulating competition in the insurance marketplace can also arise from a number of sources, linked to their remuneration, including contingent commissions and fees from services rendered to insurers". http://ec.europa.eu/competition/sectors/financial_services/inquiries/final_report_annex.pdf

- The inducement is solely or predominantly based on qualitative criteria, reflecting compliance with the applicable regulations, fair treatment of customers and the quality of services provided to customers, or
 - The inducements serve to finance adequate training on a specific insurance product, the regulatory and ethical standards as well as the fair treatment of customers.
18. This list is non-exhaustive and is not intended to create a legal "safe harbour" and should be understood as criteria to be applied in an overall analysis, only. They are deemed to promote more customer-centric behaviour by distributors. **It should be noted that insurance undertakings and insurance intermediaries are in any case not relieved from a thorough assessment whether an inducement has a detrimental impact and that these practices cannot be used to legitimate practices which are detrimental from the outset (e.g. combination with inducements listed in paragraph 4 of the draft Technical Advice below).**
 19. Furthermore, EIOPA considers it important that specific organisational measures are introduced to support and ensure that the substantive requirements are fulfilled by the regulated entities on an ongoing basis. EIOPA considers that the responsibility and the types of organisational measures will be different for those who pay inducements and those who receive them.
 20. Insurance undertakings and insurance intermediaries who pay inducements should have organisational measures in place to assess the design and structure of any inducement scheme which they pay to insurance distributors to ensure it is compliant with Article 29(2).
 21. Insurance intermediaries and insurance undertakings who receive inducements need to consider the inducement schemes which they are party to, both individually and collectively, and ensure that there are organisational measures in place to ensure that inducements do not lead to detriment for customers or hinder their ability to act honestly, fairly and in accordance with the best interests of consumers.
 22. Against this backdrop, EIOPA would like to raise the question whether further specification and guidance in a separate policy instrument, on amending the list of inducements which have a high risk of leading to a detrimental impact, is seen as necessary from the view of market participants.

Inducement and Inducement Scheme

1. An inducement is any fee, commission or non-monetary benefit which is paid or provided in connection with the distribution of an insurance-based investment product or an ancillary service to or by any party except the customer or a person on behalf of the customer.
2. An inducement scheme is a set of rules that govern the payment of inducements. It generally includes the criteria under which inducements are paid.

Detrimental Impact

3. Detrimental impact occurs when an inducement or structure of an inducement scheme provides an incentive to carry out the insurance distribution activities in a way which is not in accordance with the best interests of the customer.
4. The following types of inducements are considered to have a high risk of leading to a detrimental impact on the quality of the relevant service to the customer:
 - a) the inducement encourages the insurance intermediary or insurance undertaking carrying out distribution activities to offer or recommend a product or service to a customer when from the outset a different product or service exists which would better meet the customer's needs;
 - b) the inducement is solely or predominantly based on quantitative commercial criteria and does not take into account appropriate qualitative criteria, reflecting compliance with the applicable regulations, fair treatment of customers and the quality of services provided to customers;
 - c) the value of the inducement is disproportionate or excessive when considered against the value of the product and the services provided in relation to the product;
 - d) the inducement is entirely or mainly paid upfront when the product is sold;
 - e) the inducement scheme does not provide for the refunding of any inducements deducted from the customer's initial investment to the customer if the product lapses or is surrendered at an early stage;
 - f) if the inducement scheme entails any form of variable or contingent threshold or any other kind of value accelerator which is unlocked by attaining a sales target based on volume or value of sales.
5. The list of instances as laid down in paragraph 4 is non-exhaustive.

Organisational requirements

6. Insurance undertakings and insurance intermediaries shall maintain and operate appropriate organisational arrangements and procedures in order to assess at the outset and ensure that inducements and the structure of inducement schemes which they pay to or receive from a third party:
 - a. do not lead to a detrimental impact on the quality of the service provided to customers; and
 - b. do not prevent the insurance intermediary or insurance undertaking from complying with their obligation to act honestly, fairly and in accordance with the best interests of their customers.
7. Insurance undertakings and insurance intermediaries as referred to in paragraph 6 shall ensure that any inducement scheme is approved by the insurance undertaking or insurance intermediary's senior management.
8. Insurance intermediaries and insurance undertakings as referred to in paragraph 6 shall document the assessment of each inducement in a durable medium.
9. As part of the conflicts of interest policy (as outlined under ...) insurance intermediaries and insurance undertakings should set up a gifts and benefits policy that stipulates what benefits are acceptable and what should happen where limits are breached.

Questions to stakeholders:

- 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?**
- 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?**
- 13. To which extent are inducements which are considered bearing a high risk of detrimental impact part of existing business and distribution models? Please specify your answer and describe the potential impact of these proposals (if possible, with quantitative data).**
- 14. Are there any further organisational measures or procedural arrangements which you would consider important to monitor whether and to ensure that inducements have no detrimental impact on the relevant service to the customer and do not prevent the professional from complying with their obligation to act honestly, fairly and in accordance with the best interests of their customers?**

7. Assessment of suitability and appropriateness and reporting to customers

7.1 Assessing the suitability or appropriateness of insurance-based investment products

Extract from the Commission's request for advice (mandate)

"EIOPA is invited to provide technical advice on the information to obtain when assessing the suitability or appropriateness of insurance-based investment products for their customers, whereby a distinction has to be made between the situation when advice is provided and the situation when no advice is provided".

1. The following provisions in the Insurance Distribution Directive are relevant to this topic:

Recital 10:

Current and recent financial turbulence has underlined the importance of ensuring effective consumer protection across all financial sectors. It is appropriate, therefore, to strengthen the confidence of customers and to make regulatory treatment of the distribution of insurance products more uniform in order to ensure an adequate level of customer protection across the Union. The level of consumer protection should be raised in relation to Directive 2002/92/EC in order to reduce the need for varying national measures. It is important to take into consideration the specific nature of insurance contracts in comparison to investment products regulated under Directive 2014/65/EU of the European Parliament and of the Council (1). The distribution of insurance contracts, including insurance-based investment products, should therefore be regulated under this Directive and be aligned with Directive 2014/65/EU. The minimum standards should be raised with regard to distribution rules and a level playing field should be created in respect of all insurance-based investment products.

Recital 56:

Insurance-based investment products are often made available to customers as potential alternatives or substitutes to investment products subject to Directive 2014/65/EU. To deliver consistent investor protection and avoid the risk of regulatory arbitrage, it is important that insurance-based investment products are subject, in addition to the conduct of business standards defined for all insurance products, to specific standards aimed at addressing the investment element embedded in those products. Such specific standards should include provision of appropriate information and requirements for advice to be suitable...

Article 20(1):

Prior to the conclusion of an insurance contract, the insurance distributor shall specify, on the basis of information obtained from the customer, the demands and the needs of that customer and shall provide the customer with objective information about the insurance product in a comprehensible form to allow that customer to make an informed decision.

Any contract proposed shall be consistent with the customer's insurance demands and needs.

Where advice is provided prior to the conclusion of any specific contract, the insurance distributor shall provide the customer with a personalised recommendation explaining why a particular product would best meet the customer's demands and needs.

Article 30(1):

Without prejudice to Article 20(1), when providing advice on an insurance-based investment product, the insurance intermediary or insurance undertaking shall also obtain the necessary information regarding the customer's or potential customer's knowledge and experience in the investment field relevant to the specific type of product or service, that person's financial situation including that person's ability to bear losses, and that person's investment objectives, including that person's risk tolerance, so as to enable the insurance intermediary or the insurance undertaking to recommend to the customer or potential customer the insurance-based investment products that are suitable for that person and that, in particular, are in accordance with that person's risk tolerance and ability to bear losses.

Member States shall ensure that where an insurance intermediary or insurance undertaking provides investment advice recommending a package of services or products pursuant to Article 24, the overall bundled package is suitable.

Article 30(2):

Without prejudice to Article 20(1), Member States shall ensure that an insurance intermediary or insurance undertaking, when carrying out insurance distribution activities other than those referred to in paragraph 1 of this Article, in relation to sales where no advice is given, asks the customer or potential customer to provide information regarding that person's knowledge and experience in the investment field relevant to the specific type of product or service offered or demanded so as to enable the insurance intermediary or the insurance undertaking to assess whether the insurance service or product envisaged is appropriate for the customer. Where a bundle of services or products is envisaged pursuant to Article 24, the assessment shall consider whether the overall bundled package is appropriate.

Where the insurance intermediary or insurance undertaking considers, on the basis of the information received under the first subparagraph, that the product is not appropriate for the customer or potential customer, the insurance intermediary or insurance undertaking shall warn the customer or potential customer to that effect. That warning may be provided in a standardised format.

Where customers or potential customers do not provide the information referred to in the first subparagraph, or where they provide insufficient information regarding their knowledge and experience, the insurance intermediary or insurance undertaking shall warn them that it is not in a position to determine whether the product envisaged is appropriate for them. That warning may be provided in a standardised format.

Article 30(6):

The Commission shall be empowered to adopt delegated acts in accordance with Article 38 to further specify how insurance intermediaries and insurance undertakings are to comply with the principles set out in this Article when carrying out insurance distribution activities with their customers, including with regard to the information to be obtained when assessing the suitability and appropriateness of insurance-based investment products for their customers..... Those delegated acts shall take into account:

- (a) the nature of the services offered or provided to the customer or potential customer, taking into account the type, object, size and frequency of the transactions;*
- (b) the nature of the products being offered or considered including different types of insurance-based investment products;*
- (c) the retail or professional nature of the customer or potential customer.*

2. The following provisions in Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU ("MiFID II") are relevant to this topic:

Article 25(2)(3):

2. When providing investment advice or portfolio management the investment firm shall obtain the necessary information regarding the client's or potential client's knowledge and experience in the investment field relevant to the specific type of product or service, that person's financial situation including his ability to bear losses, and his investment objectives including his risk tolerance so as to enable the investment firm to recommend to the client or potential client the investment services and financial instruments that are suitable for him and, in particular, are in accordance with his risk tolerance and ability to bear losses.

Member States shall ensure that where an investment firm provides investment advice recommending a package of services or products bundled pursuant to Article 24(11), the overall bundled package is suitable.

3. Member States shall ensure that investment firms, when providing investment services other than those referred to in paragraph 2, ask the client or potential client to provide information regarding that person's knowledge and experience in the investment field relevant to the specific type of product or service offered or demanded so as to enable the investment firm to assess whether the investment service or product envisaged is appropriate for the client. Where a bundle of services or products is envisaged pursuant to Article 24(11), the assessment shall consider whether the overall bundled package is appropriate.

Where the investment firm considers, on the basis of the information received under the first subparagraph, that the product or service is not appropriate to the client or potential client, the investment firm shall warn the client or potential client. That warning may be provided in a standardized format.

Where clients or potential clients do not provide the information referred to under the first subparagraph, or where they provide insufficient information regarding their knowledge and experience, the investment firm shall warn them that the investment firm is not in a position to determine whether the service or product envisaged is appropriate for them. That warning may be provided in a standardized format.

3. The following provisions in the draft Commission Delegated Regulation under MiFID II are relevant for this topic:

Article 54 - Assessment of suitability and suitability reports (Article 25(2) of Directive 2014/65/EU):

1. Investment firms shall not create any ambiguity or confusion about their responsibilities in the process when assessing the suitability of investment services or financial instruments in accordance with Article 25(2) of Directive 2014/65/EU. When

undertaking the suitability assessment, the firm shall inform clients or potential clients, clearly and simply, that the reason for assessing suitability is to enable the firm to act in the client's best interest.

Where investment advice or portfolio management services are provided in whole or in part through an automated or semi-automated system, the responsibility to undertake the suitability assessment shall lie with the investment firm providing the service and shall not be reduced by the use of an electronic system in making the personal recommendation or decision to trade.

2. Investment firms shall determine the extent of the information to be collected from clients in light of all the features of the investment advice or portfolio management services to be provided to those clients. Investment firms shall obtain from clients or potential clients such information as is necessary for the firm to understand the essential facts about the client and to have a reasonable basis for determining, giving due consideration to the nature and extent of the service provided, that the specific transaction to be recommended, or entered into in the course of providing a portfolio management service, satisfies the following criteria:

(a) it meets the investment objectives of the client in question, including client's risk tolerance;

(b) it is such that the client is able financially to bear any related investment risks consistent with his investment objectives;

(c) it is such that the client has the necessary experience and knowledge in order to understand the risks involved in the transaction or in the management of his portfolio.

3. Where an investment firm provides an investment service to a professional client it shall be entitled to assume that in relation to the products, transactions and services for which it is so classified, the client has the necessary level of experience and knowledge for the purposes of point (c) of paragraph 2.

Where that investment service consists in the provision of investment advice to a professional client covered by Section 1 of Annex II to Directive 2014/65/EU, the investment firm shall be entitled to assume for the purposes of point (b) of paragraph 2 that the client is able financially to bear any related investment risks consistent with the investment objectives of that client.

4. The information regarding the financial situation of the client or potential client shall include, where relevant, information on the source and extent of his regular income, his assets, including liquid assets, investments and real property, and his regular financial commitments.

5. The information regarding the investment objectives of the client or potential client shall include, where relevant, information on the length of time for which the client wishes to hold the investment, his preferences regarding risk taking, his risk profile, and the purposes of the investment.

6. Where a client is a legal person or a group of two or more natural persons or where one or more natural persons are represented by another natural person, the investment firm shall establish and implement policy as to who should be subject to the suitability assessment and how this assessment will be done in practice, including from whom information about knowledge and experience, financial situation and investment objectives should be collected. The investment firm shall record this policy.

Where a natural person is represented by another natural person or where a legal person having requested treatment as professional client in accordance with Section 2 of Annex II of Directive 2014/65/EU is to be considered for the suitability assessment,

the financial situation and investment objectives shall be those of the legal person or, in relation to the natural person, the underlying client rather than of the representative. The knowledge and experience shall be that of the representative of the natural person or the person authorised to carry out transactions on behalf of the underlying client.

7. Investment firms shall take reasonable steps to ensure that the information collected about their clients or potential clients is reliable. This shall include, but shall not be limited to, the following:

(a) ensuring clients are aware of the importance of providing accurate and up-to-date information;

(b) ensuring all tools, such as risk assessment profiling tools or tools to assess a client's knowledge and experience, employed in the suitability assessment process are fit-for-purpose and are appropriately designed for use with their clients, with any limitations identified and actively mitigated through the suitability assessment process;

(c) ensuring questions used in the process are likely to be understood by clients, capture an accurate reflection of the client's objectives and needs, and the information necessary to undertake the suitability assessment; and

(d) taking steps, as appropriate, to ensure the consistency of client information, such as by considering whether there are obvious inaccuracies in the information provided by clients.

Investment firms having an on-going relationship with the client, such as by providing an ongoing advice or portfolio management service, shall have, and be able to demonstrate, appropriate policies and procedures to maintain adequate and up-to-date information about clients to the extent necessary to fulfil the requirements under paragraph 2.

8. Where, when providing the investment service of investment advice or portfolio management, an investment firm does not obtain the information required under Article 25(2) of Directive 2014/65/EU, the firm shall not recommend investment services or financial instruments to the client or potential client.

9. Investment firms shall have, and be able to demonstrate, adequate policies and procedures in place to ensure that they understand the nature, features, including costs and risks of investment services and financial instruments selected for their clients and that they assess, while taking into account cost and complexity, whether equivalent investment services or financial instruments can meet their client's profile.

10. When providing the investment service of investment advice or portfolio management, an investment firm shall not recommend or decide to trade where none of the services or instruments are suitable for the client.

11. When providing investment advice or portfolio management services that involve switching investments, either by selling an instrument and buying another or by exercising a right to make a change in regard to an existing instrument, investment firms shall collect the necessary information on the client's existing investments and the recommended new investments and shall undertake an analysis of the costs and benefits of the switch, such that they are reasonably able to demonstrate that the benefits of switching are greater than the costs.

Article 55 Provisions common to the assessment of suitability or appropriateness (Article 25(2) and 25(3) of Directive 2014/65/EU)

1. Investment firms shall ensure that the information regarding a client's or potential client's knowledge and experience in the investment field includes the following, to the extent appropriate to the nature of the client, the nature and extent of the service to be provided and the type of product or transaction envisaged, including their complexity and the risks involved:

(a) the types of service, transaction and financial instrument with which the client is familiar;

(b) the nature, volume, and frequency of the client's transactions in financial instruments and the period over which they have been carried out;

(c) the level of education, and profession or relevant former profession of the client or potential client.

2. An investment firm shall not discourage a client or potential client from providing information required for the purposes of Article 25(2) and (3) of Directive 2014/65/EU.

3. An investment firm shall be entitled to rely on the information provided by its clients or potential clients unless it is aware or ought to be aware that the information is manifestly out of date, inaccurate or incomplete.

Article 56 Assessment of appropriateness and related record-keeping obligations (Article 25(3) and 25(5) of Directive 2014/65/EU)

1. Investment firms, shall determine whether that client has the necessary experience and knowledge in order to understand the risks involved in relation to the product or investment service offered or demanded when assessing whether an investment service as referred to in Article 25(3) of Directive 2014/65/EU is appropriate for a client.

An investment firm shall be entitled to assume that a professional client has the necessary experience and knowledge in order to understand the risks involved in relation to those particular investment services or transactions, or types of transaction or product, for which the client is classified as a professional client.

7.1.1 Information to obtain when assessing the suitability and appropriateness of insurance-based investment products

Analysis

4. The assessment of suitability is one of the most relevant obligations for consumer protection. In accordance with this obligation, distributors providing advice have to provide suitable personal recommendations regarding insurance-based investment products to their customers or potential customers. Suitability has to be assessed against customers' knowledge and experience, financial situation and investment objectives.
5. The assessment of suitability and appropriateness is, according to Article 30, IDD, without prejudice to the "demands and needs" test of Article 20(1), IDD. (This point is also explicitly recognised in the draft technical advice below). Before concluding an insurance contract and irrespective of whether this contract is concluded on an advised or non-advised basis, the distributor has to specify the **demands and the needs** of a customer and has to provide the customer with objective information about the insurance product in a comprehensible form to allow that customer to make an informed decision. For that reason, not just insurance-based investment products, but any insurance contract proposed has to be consistent with the customer's insurance demands and needs. Where advice is provided prior to the conclusion of an insurance contract, the distributor should inform the customer why a particular product would best meet the customer's demands and needs.
8. Advice is defined as *"the provision of a personal recommendation to a customer, either upon their request or at the initiative of the insurance distributor, in respect of one or more insurance contracts"*³¹. Therefore, advice is not limited just to the point of sale, but can be provided at any time during the customer relationship. Every personal recommendation given to the customer has to be suitable, which includes, for example, whether or not to switch embedded investment elements or to hold or sell an insurance-based investment product. While Article 30(2), IDD, refers to distribution activities "in relation to sales", paragraph 1 of Article 30 IDD has no such reference to a certain point of time in the customer relationship.
9. The customer's knowledge and experience is a common criterion when assessing suitability or appropriateness. Therefore, assessing the customer's knowledge and experience is relevant to the assessment of suitability and appropriateness equally.
10. The draft Technical Advice below sets out requirements with regard to the information to obtain for the assessment of suitability and appropriateness and has been adjusted to take into account, specificities arising from the insurance sector:
 - a) Where concepts/terminology contained in MiFID II (e.g. execution of orders, portfolio management) do not exist in the insurance sector;
 - b) Where the MiFID framework allows for assumptions with regard to the assessment of suitability and appropriateness of professional clients, as there is no specific client classification provided for in IDD (other than an exemption in certain cases for "large risks"³²).

³¹ Article 2(1)(15), IDD

³² Article 22(1), IDD. N.B. "Large risks" only cover certain non-life products in Annex I of the Solvency II Directive.

9. In addition, in the case of Article 54(9)³³ of the draft MiFID II Delegated Regulation, there is perceived to be an overlap with the envisaged Level 2 provisions on product oversight and governance. For this reason, Article 54(9) has not been replicated in the draft technical advice below. Copying across Article 54(9), could, in EIOPA's view, create some confusion and legal uncertainty with the POG provisions in the envisaged Delegated Act under IDD on POG.
10. Furthermore, EIOPA also sees the following difference between the equivalent Level 1 provisions of MiFID II and IDD: There is no comparable provision in Article 25, IDD, to Article 24(2)(2), MiFID II which states that an "investment firm shall understand the financial instruments they offer or recommend.....". There is an equivalent provision in Article 25(1)(4), IDD of Article 16(3)(4), MiFID II, which refers to the fact that the "insurance undertaking shall understand and regularly review the insurance products it offers or markets". The IDD text does not go as far as referring to a "recommendation". A "recommendation" would provide an obvious link to the suitability assessment under Article 30(1), IDD. Furthermore, the provision in Article 25(1)(4), IDD only applies to insurance undertakings and not insurance intermediaries, whereas Article 30(1), IDD covers both insurance intermediaries and insurance undertakings.
11. EIOPA acknowledges that insurance distributors will need to obtain further information from customers to comply with other rules, such as anti-money laundering (AML) regulation. AML and other requirements are equally not part of the Commission's Request for Advice and are, therefore, not included in the technical advice.
12. EIOPA does not consider it appropriate to develop rules on the demands and needs test in the context of distribution of insurance-based investment products. It is EIOPA's understanding that, due to the fact that the Commission's empowerment for delegated acts on this issue under Article 30(6), IDD is limited to the "information to obtain under the suitability/appropriateness assessment" (and not the "demands and needs" test) and the fact that this is also reflected in the Commission's Request for Advice, its technical advice should be limited to the information to obtain under the suitability/appropriateness assessment only. This is also in line with the request by the Commission to EIOPA to ensure regulatory consistency with the line taken in the draft Commission Delegated Regulation under MiFID II.
13. EIOPA appreciates, however, that there is a close relationship between the "demands and needs" test in Article 20(1), IDD and the suitability/appropriateness assessment under Article 30, IDD. Against this backdrop, EIOPA would like to raise the question whether further specification and guidance in a separate policy instrument on the relationship between the "demands and needs" test and the suitability/appropriateness assessment, are seen as necessary from the view of market participants.

³³ "Investment firms shall have, and be able to demonstrate, adequate policies and procedures in place to ensure that they understand the nature, features, including costs and risks of investment services and financial instruments selected for t³³ Article 2(1)(15), IDD

³³ "Investment firms shall have, and be able to demonstrate, adequate policies and procedures in place to ensure that they understand the nature, features, including costs and risks of investment services and financial instruments selected their clients and that they assess, while taking into account cost and complexity, whether equivalent investment services or financial instruments can meet their client's profile".

Assessment of suitability

1. The insurance intermediary or insurance undertaking shall determine the extent of the information to be collected from customers in light of all the features of the advice to be provided to those customers.
2. Without prejudice to the fact that any contract of insurance proposed shall be consistent with the customer's insurance demands and needs under Article 20(1), IDD, an insurance intermediary or insurance undertaking shall obtain from customers or potential customers such information as is necessary for the insurance intermediary or the insurance undertaking to understand the essential facts about the customer and to have a reasonable basis for determining that the personal recommendation satisfies the following criteria:
 - (a) it meets the customer's investment objectives, including that person's risk tolerance;
 - (b) it meets the customer's financial situation, including that person's ability to bear losses;
 - (c) it is such that the customer has the necessary knowledge and experience in the investment field relevant to the specific type of product or service.
3. It can be the case that the information to obtain for the suitability assessment is covered already by other requirements of Chapter V of Directive 2016/97/EU.
4. The insurance intermediary or the insurance undertaking shall not create any ambiguity or confusion about their responsibilities in the process when assessing the suitability in accordance with Article 30(1) of Directive 2016/97/EU. The insurance intermediary or insurance undertaking shall inform customers, clearly and simply, that the reason for assessing suitability is to enable them to act in the customer's best interest.
5. When advice on insurance-based investment products is provided in whole or in part through an automated or semi-automated system, the responsibility to undertake the suitability assessment shall lie with the insurance intermediary or insurance undertaking providing the service and shall not be reduced by the use of an electronic system in making the personal recommendation.
6. The necessary information regarding the customer's or potential customer's financial situation including that person's ability to bear losses, includes, where relevant, the following to the extent appropriate to the specific type of product or service information on the source and extent of his regular income, his assets, including liquid assets, investments and real property, and his regular financial commitments.
7. The necessary information regarding the customer's or potential customer's investment objectives, including that person's risk tolerance, includes, where relevant, the following to the extent appropriate to the specific type of product or service information on the length of time for which the customer wishes to hold the investment, his preferences regarding risk taking, his risk profile, and the purposes of the investment.
8. With reference to collective contracts where more than one person is insured or participating as contractual party, the insurance intermediary or insurance

undertaking shall establish and implement policy as to who shall be subject to the suitability assessment and how this assessment will be done in practice, including from whom the information about knowledge and experience, financial situation and investment objectives shall be collected. The insurance intermediary or the insurance undertaking shall record this policy.

9. The insurance intermediary or insurance undertaking shall take reasonable steps to ensure that the information collected about the customer is reliable. This shall include, but shall not be limited to, the following:
 - (a) ensuring customers are aware of the importance of providing accurate and up-to-date information;
 - (b) ensuring all tools, such as risk assessment profiling tools or tools to assess a customer's knowledge and experience, employed in the suitability assessment process are fit-for-purpose and appropriately designed for use with their customers, with any limitations identified and actively mitigated through the suitability assessment process;
 - (c) ensuring questions used in the process are likely to be understood by the customer, capture an accurate reflection of the customer's objectives and needs, and the information necessary to undertake the suitability assessment; and
 - (d) taking steps, as appropriate, to ensure the consistency of customer information, such as considering whether there are obvious inaccuracies in the information provided by the customer.
10. Where, when providing the advice, the insurance intermediary or insurance undertaking does not obtain the information required under Article 30(1) of Directive 2016/97/EU, the insurance intermediary or the insurance undertaking shall not recommend insurance-based investment products to the customer or potential customer.
11. When providing the advice, an insurance intermediary or the insurance undertaking shall not recommend where none of the products are suitable for the customer.
12. When providing advice that involves switching embedded investments, either by selling an embedded element and buying another or by exercising a right to make a change in regard to an existing embedded element, the insurance intermediary or insurance undertaking shall collect the necessary information on the customer's existing investments and the recommended new investments and shall undertake an analysis of the costs and benefits of the switch, such that they are reasonably able to demonstrate that the benefits of switching are greater than the costs.

Provisions common to the assessment of suitability or appropriateness

13. The necessary information regarding the customer's or potential customer's knowledge and experience in the investment field, includes, where relevant the following to the extent appropriate to the specific type of product or service:
 - (a) the types of service, transaction, insurance-based investment product or financial instrument with which the customer is familiar;

- (b) the nature, volume, and frequency of the customer's transactions in insurance-based investment products or financial instruments and the period over which they have been carried out;
 - (c) the level of education, and profession or relevant former profession of the customer or potential customer.
14. An insurance intermediary or the insurance undertaking shall not discourage a customer or potential customer from providing information required for the purposes of Article 30(1) and (2) of Directive 2016/97/EU.
15. An insurance intermediary or the insurance undertaking shall be entitled to rely on the information provided by its customers or potential customers unless it is aware or ought to be aware that the information is manifestly out of date, inaccurate or incomplete.

Assessment of appropriateness

16. Without prejudice to the fact that any contract of insurance proposed shall be consistent with the customer's insurance demands and needs under Article 20(1), IDD, the insurance intermediary or insurance undertaking shall determine whether that customer has the necessary experience and knowledge in order to understand the risks involved in relation to the product proposed when carrying out insurance distribution activities other than those referred to in Article 30(1) of Directive 2016/97/EU, in relation to assessing the appropriateness of sales where no advice is given.

Questions to stakeholders:

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?

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?

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

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?

7.2 Criteria to assess non-complex insurance-based investment products for the purposes of point (ii) of point (a) of paragraph 3 of Article 30

Extract from the Commission's request for advice (mandate)

"EIOPA is invited to provide technical advice on the criteria to assess non-complex insurance-based investment products for the purposes of point (ii) of point (a) of paragraph 3 of Article 30".

1. The following provisions in the Insurance Distribution Directive are relevant to this topic:

Article 30(3)(a):

"3. Without prejudice to Article 20(1), where no advice is given in relation to insurance-based investment products, Member States may derogate from the obligations referred to in paragraph 2 of this Article, allowing insurance intermediaries or insurance undertakings to carry out insurance distribution activities within their territories without the need to obtain the information or make the determination provided for in paragraph 2 of this Article where all the following conditions are met: (a) the activities refer to either of the following insurance-based investment products (i) contracts which only provide investment exposure to the financial instruments deemed non-complex under Directive 2014/65/EU and do not incorporate a structure which makes it difficult for the customer to understand the risks involved; or (ii) other non-complex insurance-based investments for the purpose of this paragraph;..."

Article 30(6), IDD:

"The Commission shall be empowered to adopt delegated acts in accordance with Article 38 to further specify how insurance intermediaries and insurance undertakings are to comply with the principles set out in this Article when carrying out insurance distribution activities with their customers, including with regard to..... the criteria to assess non-complex insurance-based investment products for the purposes of point (ii) of point (a) of paragraph 3 of this Article..... Those delegated acts shall take into account:

- (a) the nature of the services offered or provided to the customer or potential customer, taking into account the type, object, size and frequency of the transactions;*
- (b) the nature of the products being offered or considered including different types of insurance-based investment products;*
- (c) the retail or professional nature of the customer or potential customer".*

2. The following provision in the draft Commission Delegated Regulation under MiFID II are relevant for this topic:

Article 57 - Provision of services in non-complex instruments (Article 25(4) of Directive 2014/65/EU)

"A financial instrument which is not explicitly specified in Article 25(4)(a) of Directive 2014/65/EU shall be considered as non-complex for the purposes of Article 25(4)(a)(vi) of Directive 2014/65/EU if it satisfies the following criteria:

(a) it does not fall within Article 4(1)(44)(c) of, or points (4) to (11) of Section C of Annex I to Directive 2014/65/EU;

(b) there are frequent opportunities to dispose of, redeem, or otherwise realise that instrument at prices that are publicly available to market participants and that are either market prices or prices made available, or validated, by valuation systems independent of the issuer;

(c) it does not involve any actual or potential liability for the client that exceeds the cost of acquiring the instrument;

(d) it does not incorporate a clause, condition or trigger that could fundamentally alter the nature or risk of the investment or pay out profile, such as investments that incorporate a right to convert the instrument into a different investment;

(e) it does not include any explicit or implicit exit charges that have the effect of making the investment illiquid even though there are technically frequent opportunities to dispose of, redeem or otherwise realise it;

(f) adequately comprehensive information on its characteristics is publicly available and is likely to be readily understood so as to enable the average retail client to make an informed judgment as to whether to enter into a transaction in that instrument."

3. Regarding the provisions in MiFID II, it seems reasonable to expect that any exposure to a complex product as defined by MiFID would make the corresponding product complex under IDD. The list of specifically "non-complex" products in the MiFID II is quite short – so this would restrict exposure to products such as vanilla shares, bonds and derivatives, and non-structured UCITS if an insurance-based investment product was to be classified "non-complex". As IDD links through to MiFID non-complex financial instruments, some of the criteria that ESMA proposed in their recent final guidelines on complex debt securities and structured deposits in relation to some of the inherent features of a product – having unusual or unfamiliar underlyings, the use of leverage, a lack of redemption or maturity date etc. – may also be considered for insurance-based investment products as factors that would make it difficult for the client to understand the risks involved, taking into account that in any case the insurance products can be considered non-complex if they do not incorporate a structure which makes it difficult for the customer to understand the risks involved.
4. EIOPA has also noted the draft Commission Delegated Regulation under MIFID II regarding suggested criteria for non-complex products and incorporated these as relevant in the draft technical advice below.

Analysis

5. The results of EIOPA's evidence-gathering on suitability and appropriateness with regard to Art 30(3)(a)(ii) indicate that there are a limited number of insurance-based investment product types which offer complex investments but have a suitably non-complex structure to enable client understanding of the risks involved. They may only relate to insurance products which have a unit-linked investment element (as opposed to more overtly equity backed and/or pooled investments such as with-profits).
6. It appears that very few (if any) types of non-complex products would be appropriate to be sold by means of execution-only transactions but some

Member States have advocated retention of some discretion over this at local level.

7. Balanced against this, however, several Member States allow for the sale of non-complex products on a non-advised basis, for example, via rule regimes relating to appropriateness of the product having regard to the customer's knowledge and experience. In such examples, non-complex insurance-based investment products may be capable of being sold (if they are not already) and to restrict them now may be seen as anti-competitive.
8. Examples of the type of insurance-based investment products which may already be sold on this basis include whole of life insurance with attached additional benefits (for example waiver of premium or contribution or separate pay-out for critical illness diagnosis), an Over 50's Life plan with a guaranteed pay-out within the first year of premiums, and unit-linked single premium Life insurance-linked short term investment bonds.
9. The draft technical advice below contains a provision to exclude cases where the insurance-based investment product incorporates a structure which makes it difficult for the customer to understand the risk involved. This criterion mirrors an element which is found in point (i) of point (a) of paragraph 3 of Article 30. Adding it in the draft technical advice below is important to achieve symmetry within point (a) of paragraph 3.
10. Insurance contracts which incorporate contractual features that allow changing material consequences with regard to benefits and gains, as the pay-out profile, of the insurance contract can indicate a complex insurance contract. In those cases, a policyholder might not easily understand the ramifications of such changes and more information is essential to avoid consumer detriment. EIOPA assumes that a beneficiary clause that cannot be modified during the duration of the contract, is one example of a non-complex insurance contract.
11. The beneficiary clause in some policies may be personalised, but in these cases a structure which makes it difficult for the customer to understand the risk involved should be assumed. This is to exclude, for example, policies where the lump sum payable on death of the insured may be paid to a named beneficiary but this is capable of being altered to another under the terms of the policy; also for example joint life policies where there is an option to pay the lump sum on the first death or (again potentially to another named beneficiary) on the second death. The use of non-standard beneficiary clauses in such cases are potentially complex and therefore outside the definition of other non-complex products.
12. Under Art 30 (3)(a)(i), insurance-based investment products can be considered non-complex when they provide investment exposure to the financial instruments deemed non-complex under Directive 2014/65/EU:
 - (a) shares admitted to trading on a regulated market or an equivalent third country market (that is, one which is included in the list which is published by the European Commission and updated periodically) or on a MTF, where those are shares in companies, and excluding shares in non-UCITS collective investment undertakings and shares that embed a derivative (Article 25(4)(a)(i) of Directive 2014/65/EU); or
 - (b) bonds or other forms of securitised debt admitted to trading on a regulated market or on an equivalent third country market or on a MTF, excluding those that embed a derivative or incorporate a structure which makes it difficult for the client to understand the risk involved (Article 25(4)(a)(ii) of Directive 2014/65/EU); or

(c) money-market instruments, excluding those that embed a derivative or incorporate a structure which makes it difficult for the client to understand the risk involved (Article 25(4)(a)(iii) of Directive 2014/65/EU);

(d) shares or units in UCITS, excluding structured UCITS as referred to in the second subparagraph of Article 36(1) of Regulation (EU) No 583/2010 (Article 25(4)(a)(iv) of Directive 2014/65/EU); or

(e) structured deposits, excluding those that incorporate a structure which makes it difficult for the client to understand the risk of return or the cost of exiting the product before term (Article 25(4)(a)(v) of Directive 2014/65/EU); or

(f) other non-complex financial instruments (Article 25(4)(a)(vi) of Directive 2014/65/EU); and

(g) do not incorporate a structure which makes it difficult for the customer to understand the risk involved (Article 25(10) of Directive 2014/65/EU).

13. Therefore in order to define other non-complex insurance-based investment products for the purposes of Art 30(3) more generally, this will need to be done using suitable high-level criteria capable of general application by Member States having regard to their specific statutory regimes.

Draft Technical Advice

1. An insurance-based investment product with investments embedded that are not explicitly specified in Article 25(4)(a) of Directive 2014/65/EU shall be considered as non-complex for the purposes of Article 30(3)(a)(ii) of Directive 2014/65/EU if it satisfies the following criteria:
 - (a) the contract does not provide investment exposure (whether directly or via underlying investment) to a derivative or other security giving the right to acquire or sell a transferable security or giving rise to a cash settlement determined by reference to transferable securities, currencies, interest rates or yields, commodities or other indices or measures;
 - (b) there are frequent opportunities to dispose of, redeem, or otherwise realise the insurance-based investment product at prices that are publicly available to the market participants and that are either market prices or prices made available, or validated, by valuation systems independent of the issuer, that do not imply excessive burdens for the policyholder;
 - (c) it does not involve any additional actual or potential liability for the customer to incur that exceeds the cost of acquiring the insurance-based investment product;
 - (d) adequately comprehensive information on the characteristics of the contract is available to the customer and is likely to be readily understood so as to enable the average retail customer to make an informed judgment as to whether to enter into a transaction in that insurance-based investment product;
 - (e) it does not incorporate a clause condition or trigger that could fundamentally alter the nature or risk of the investment or pay out profile, such as switch clauses;
 - (f) it does not include any explicit or implicit exit charges that have the effect of making the investment illiquid even though technically frequent opportunities to dispose or redeem it may be possible, and which may cause detriment to customers;
 - (g) it does not in any other way incorporate a structure which makes it difficult for the customer to understand the risk involved;
 - (h) it does not incorporate contractual features that allow alteration of material consequences with regard to benefits and gains in relation to the pay-out profile of the insurance contract. Such features can be assumed to exist in the case of a modification or personalisation of contractual provisions with regard to the person receiving benefits at the end of the contractual relationship (the "beneficiary clause").

Questions to stakeholders:

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?

20. Are there any further high level criteria which you would consider necessary and important, and why? In particular, how could insurance specificities be taken into account?

21. While point (i) of point (a) of paragraph 3 of Article 30 is intended to capture the majority of non-complex products, the above listed criteria should capture equally non-complex products falling outside of point (i). Are there any gaps?

7.3 Retention of records

Extract from the Commission's request for advice (mandate)

"EIOPA is invited to provide technical advice on the content and format of records and agreements for the provision of services to customers".

1. The following provisions in the Insurance Distribution Directive are relevant to this topic:

Article 30(4):

The insurance intermediary or insurance undertaking shall establish a record that includes the document or documents agreed between the insurance intermediary or insurance undertaking and the customer that set out the rights and obligations of the parties, and the other terms on which the insurance intermediary or insurance undertaking will provide services to the customer. The rights and duties of the parties to the contract may be incorporated by reference to other documents or legal texts.

Article 30(6), IDD:

The Commission shall be empowered to adopt delegated acts in accordance with Article 38 to further specify how insurance intermediaries and insurance undertakings are to comply with the principles set out in this Article when carrying out insurance distribution activities with their customers, including with regard to.....the content and format of records and agreements for the provision of services to customers. Those delegated acts shall take into account:

- (a) the nature of the services offered or provided to the customer or potential customer, taking into account the type, object, size and frequency of the transactions;*
- (b) the nature of the products being offered or considered including different types of insurance-based investment products;*
- (c) the retail or professional nature of the customer or potential customer.*

Article 2(1)(18):

'durable medium' means any instrument which:

- (a) enables a customer to store information addressed personally to that customer in a way accessible for future reference and for a period of time adequate for the purposes of the information; and*
- (b) allows the unchanged reproduction of the information stored.*

Article 23(1):

All information to be provided in accordance with Articles 18, 19, 20 and 29 shall be communicated to the customer:

- (a) on paper;*
- (b) in a clear and accurate manner, comprehensible to the customer;*
- (c) in an official language of the Member State in which the risk is situated or of the Member State of the commitment or in any other language agreed upon by the parties; and*

(d) free of charge.

2. The following provisions of the MiFID II Directive and the MiFID II Draft Commission Delegated Regulation are relevant for this topic:

MiFID II

Art. 25(5), MIFID II:

5. The investment firm shall establish a record that includes the document or documents agreed between the investment firm and the client that set out the rights and obligations of the parties, and the other terms on which the investment firm will provide services to the client. The rights and duties of the parties to the contract may be incorporated by reference to other documents or legal texts.

MiFID II Level 2 – Draft COM Delegated Regulation C(2016) 2398

Article 56, Assessment of appropriateness and related record-keeping obligations (Article 25(3) and 25(5) of Directive 2014/65/EU)

2. Investment firms shall maintain records of the appropriateness assessments undertaken which shall include the following:

(a) the result of the appropriateness assessment;

(b) any warning given to the client where the investment service or product purchase was assessed as potentially inappropriate for the client, whether the client asked to proceed with the transaction despite the warning and, where applicable, whether the firm accepted the client's request to proceed with the transaction;

(c) any warning given to the client where the client did not provide sufficient information to enable the firm to undertake an appropriateness assessment, whether the client asked to proceed with the transaction despite this warning and, where applicable, whether the firm accepted the client's request to proceed with the transaction.

Article 73, Record keeping of rights and obligations of the investment firm and the client (Article 25(5) of Directive 2014/65/EU)

Records which set out the respective rights and obligations of the investment firm and the client under an agreement to provide services, or the terms on which the firm provides services to the client, shall be retained for at least the duration of the relationship with the client.

Analysis

Introduction

3. The technical advice developed by ESMA on MIFID 2 and the draft Delegated Regulation under MiFID II adopted by the European Commission on 25 April 2016 have served as a basis for this part of the draft technical advice. The results of EIOPA's online survey in early 2016 showed a general support for alignment with MIFID II requirements. At the same time, respondents agreed that insurance specificities should be taken into account in the technical advice.
4. EIOPA acknowledges that the draft MiFID II Delegated Regulation covers record-keeping in an appropriateness scenario only, and does not introduce specific rules for the content of records for the suitability assessment. Furthermore, the draft MiFID II Delegated Regulation does not provide more information about the format for records. EIOPA has taken note of ESMA's Guidelines on certain aspects of the MiFID suitability requirements³⁴, where certain expectations with regard to record-keeping of the assessment of suitability were set.
5. With particular reference to the content of the agreements for the provision of services to customer, the draft MiFID II Delegated Regulation does not reflect specificities of the insurance sector. In particular, it refers to the written basic agreement between the investment firm and the retail client, which the Member State shall require the investment firm to enter into with the latter, as provided by Article 58, draft MiFID II Delegated Regulation. Taking into account that the same written basic agreement is not foreseen by IDD, the reference to "*the agreements for the provision of services to customers*" mentioned by the Commission's request for advice seems to be not applicable in the IDD context. IDD mentions the documents agreed between the parties only, but does not introduce the concept of a written basic agreement.
6. Therefore, the reference to the written basic agreements for the provision of services to the customers could be interpreted as a reference to the contractual terms and conditions in which the essential rights and obligations of the parties are regulated. Member States might want to introduce this concept at their own discretion or have done so in the past.
7. In fact, although from a formal point of view, IDD does not introduce the concept and the requirements of the written basic agreement (but only mentions the documents agreed between the insurance intermediary or insurance undertaking and the customer), the content of the written basic agreement does not appear inconsistent with the IDD framework, except for those features specifically referred to the investment sector and not suitable to the specificities of the insurance market (e.g. the reference to portfolio management, custody services and financing transactions).

Retention of records

8. As regards the Commission's request for advice about the content of the agreements for the provision of services to customers, it was also pointed out by many respondents to EIOPA's online survey that the fact that the content of insurance contracts is already regulated at national level, should be also taken into account. Therefore, the definition of the information to be included into the contract at EU level could interfere with national civil law. For this reason, with reference to the documents agreed between the insurance intermediary or insurance undertaking and the customer setting out the rights and obligation of

³⁴ Section V.IX on Record-keeping: https://www.esma.europa.eu/sites/default/files/library/2015/11/2012-387_en.pdf

the parties which the insurance intermediary or insurance undertaking is obliged to record, the rules on retention of records remains high level.

9. As regards the content of records, many respondents agreed that the requirement for the insurance intermediary or insurance undertaking to keep a record of documents on services provided (including the insurance contract, the suitability statements and the periodic reports) would be sufficient to ensure effective consumer protection and that a request to record any additional information could overload the consumer and create administrative burdens for the insurance intermediary or the insurance undertaking.

Format of the documents agreed between the parties

10. In relation to the Commission's request for advice about the format of records and agreements for the provision of services to customers, Article 30(5), IDD already refers to "durable medium" in relation to periodic reports to customers on the services provided and to the suitability statements to be provided to the customer.
11. EIOPA has taken note that the draft MiFID II Delegated Regulation has a number of provisions on the format, such as Articles 46 and Article 58. Accordingly, the draft technical advice specifies the format for record-keeping and reporting purposes to make Article 30, IDD, more practical and allow national competent authorities to supervise market practice.
12. Therefore, it would be sufficient to make a reference to the notion of durable medium as defined by Article 2(1)(18) IDD, which states the following:
"durable medium" means any instrument which:
 - (a) enables a customer to store information addressed personally to that customer in a way accessible for future reference and for a period of time adequate for the purposes of the information; and*
 - (b) allows the unchanged reproduction of the information stored".*
13. EIOPA acknowledges the challenges for distributors with regard to providing documents in the most suitable format. EIOPA believes it is useful to:
 - Further clarify which kind of instruments could be considered as "durable medium": CD-ROMs, DVDs and hard drives of personal computers on which electronic mail is stored, excluding Internet sites, unless such sites meet the criteria specified by Article 2(1)(18) IDD; and
 - Make a reference to the general provisions on the disclosure rules laid down by Article 23 IDD (as regards the use of paper or another durable medium and the use of the official language of the Member State in which the risk is situated or of the Member State of the commitment or in any other language agreed upon by the parties).
14. Article 23, IDD introduced certain criteria when deviating from the default paper-based format. These criteria should be understood in a pragmatic way, that is in accordance with the best interests of the customer.

Retention of records

15. The insurance intermediary or insurance undertaking shall keep orderly records of its business and internal organisation including all services provided by it. These records may be expected to include the customer information obtained where the insurance intermediary or the insurance undertaking is required to produce a suitability statement or the customer information obtained to assess appropriateness.

Record-keeping obligations for the assessment of suitability

16. The insurance intermediary or the insurance undertaking shall at least:

- (a) maintain adequate recording and retention arrangements to ensure orderly and transparent record-keeping regarding the suitability assessment, including any advice provided, the result of the suitability assessment and all changes to investments embedded in the insurance-based investment product made;
- (b) ensure that record-keeping arrangements are designed to enable the detection of failures regarding the suitability assessment (such as mis-selling);
- (c) ensure that records kept are accessible for the relevant persons within the insurance intermediary or insurance undertaking, and for competent authorities;
- (d) have adequate processes to mitigate any shortcomings or limitations of the record-keeping arrangements.

17. The insurance intermediary or the insurance undertaking shall record all relevant information about the suitability assessment, such as information about the customer, and information about insurance-based investment products recommended to the customer or purchased on the customer's behalf. Those records shall include:

- (a) any changes made by the insurance intermediary or the insurance undertaking regarding the suitability assessment, in particular any change to the customer's investment risk profile;
- (b) the types of insurance-based investment product that fit that profile and the rationale for such an assessment, as well as any changes and the reasons for them.

Record-keeping obligations for the assessment of appropriateness

18. Insurance intermediary or insurance undertaking shall maintain records of the appropriateness assessments undertaken which shall include the following:

- (a) the result of the appropriateness assessment
- (b) any warning given to the customer where the product was assessed as potentially inappropriate for the customer, whether the customer asked to proceed with concluding the contract despite the warning and, where applicable, whether the insurance undertaking or the insurance intermediary accepted the customer's request to proceed with concluding the contract;
- (c) any warning given to the customer where the customer did not provide sufficient information to enable the insurance undertaking or the insurance intermediary to undertake an appropriateness assessment, whether the

customer asked to proceed with concluding the contract despite this warning and, where applicable, whether the insurance undertaking or the insurance intermediary accepted the customer's request to proceed with concluding the contract.

Format

19. With reference to the format, the document or documents agreed between the insurance intermediary or insurance undertaking and the customer that set out the rights and obligations of the parties, shall be kept and provided:
- a) in an official language of the Member State in which the risk is situated or of the Member State of the commitment or in any other language agreed upon by the parties;
 - b) in a clear and accurate manner, comprehensible to the customer;
 - c) in the format as defined by Article 2(1)(18) of Directive 2016/97/EU.

Questions to stakeholders:

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

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

7.4 Reports to customers on the services provided

Extract from the Commission's request for advice (mandate)

"EIOPA is invited to provide technical advice on the content and format of periodic reports to customers on the services provided."

1. The following provisions in the Insurance Distribution Directive are relevant to this topic:

Article 29 - Information to customers

1. Without prejudice to Article 18 and Article 19(1) and (2), appropriate information shall be provided in good time, prior to the conclusion of a contract, to customers or potential customers with regard to the distribution of insurance-based investment products, and with regard to all costs and related charges. That information shall include at least the following:

(a) when advice is provided, whether the insurance intermediary or insurance undertaking will provide the customer with a periodic assessment of the suitability of the insurance-based investment products recommended to that customer, referred to in Article 30.

Article 30 - Assessment of suitability and appropriateness and reporting to customers

5. The insurance intermediary or insurance undertaking shall provide the customer with adequate reports on the service provided on a durable medium. Those reports shall include periodic communications to customers, taking into account the type and the complexity of insurance-based investment products involved and the nature of the service provided to the customer and shall include, where applicable, the costs associated with the transactions and services undertaken on behalf of the customer.

When providing advice on an insurance-based investment product, the insurance intermediary or the insurance undertaking shall, prior to the conclusion of the contract, provide the customer with a suitability statement on a durable medium specifying the advice given and how that advice meets the preferences, objectives and other characteristics of the customer. The conditions set out in Article 23(1) to (4) shall apply.

Where the contract is concluded using a means of distance communication which prevents the prior delivery of the suitability statement, the insurance intermediary or the insurance undertaking may provide the suitability statement on a durable medium immediately after the customer is bound by any contract, provided both of the following conditions are met:

(a) the customer has consented to receiving the suitability statement without undue delay after the conclusion of the contract; and

(b) the insurance intermediary or insurance undertaking has given the customer the option of delaying the conclusion of the contract in order to receive the suitability statement in advance of such conclusion.

Where an insurance intermediary or an insurance undertaking has informed the customer that it will carry out a periodic assessment of suitability, the periodic report shall contain an updated statement of how the insurance-based investment product meets the customer's preferences, objectives and other characteristics of the customer.

2. The following provision in MiFID II is relevant to this topic:

Art. 25(6):

6. The investment firm shall provide the client with adequate reports on the service provided in a durable medium. Those reports shall include periodic communications to clients, taking into account the type and the complexity of financial instruments involved and the nature of the service provided to the client and shall include, where applicable, the costs associated with the transactions and services undertaken on behalf of the client.

When providing investment advice, the investment firm shall, before the transaction is made, provide the client with a statement on suitability in a durable medium specifying the advice given and how that advice meets the preferences, objectives and other characteristics of the retail client.

Where the agreement to buy or sell a financial instrument is concluded using a means of distance communication which prevents the prior delivery of the suitability statement, the investment firm may provide the written statement on suitability in a durable medium immediately after the client is bound by any agreement, provided both the following conditions are met:

(a) the client has consented to receiving the suitability statement without undue delay after the conclusion of the transaction; and

(b) the investment firm has given the client the option of delaying the transaction in order to receive the statement on suitability in advance.

Where an investment firm provides portfolio management or has informed the client that it will carry out a periodic assessment of suitability, the periodic report shall contain an updated statement of how the investment meets the client's preferences, objectives and other characteristics of the retail client.

3. The following provisions in the draft MiFID II Commission Delegated Regulation are relevant to this topic:

Article 54 Assessment of suitability and suitability reports (Article 25(2) of Directive 2014/65/EU)

12. When providing investment advice, investment firms shall provide a report to the retail client that includes an outline of the advice given and how the recommendation provided is suitable for the retail client, including how it meets the client's objectives and personal circumstances with reference to the investment term required, client's knowledge and experience and client's attitude to risk and capacity for loss.

Investment firms shall draw clients' attention to and shall include in the suitability report information on whether the recommended services or instruments are likely to require the retail client to seek a periodic review of their arrangements.

Where an investment firm provides a service that involves periodic suitability assessments and reports, the subsequent reports after the initial service is established

may only cover changes in the services or instruments involved and/or the circumstances of the client and may not need to repeat all the details of the first report.

13. Investment firms providing a periodic suitability assessment shall review, in order to enhance the service, the suitability of the recommendations given at least annually. The frequency of this assessment shall be increased depending on the risk profile of the client and the type of financial instruments recommended.

Article 52 Information about investment advice (Article 24(4) of Directive 2014/65/EU)

1. Investment firms shall explain in a clear and concise way whether and why investment advice qualifies as independent or non-independent and the type and nature of the restrictions that apply, including, when providing investment advice on an independent basis, the prohibition to receive and retain inducements.

5. Investment firms providing a periodic assessment of the suitability of the recommendations provided pursuant to Article 54(12) shall disclose all of the following:

- (a) the frequency and extent of the periodic suitability assessment and where relevant, the conditions that trigger that assessment;
- (b) the extent to which the information previously collected will be subject to reassessment; and
- (c) the way in which an updated recommendation will be communicated to the client.

Article 60 Reporting obligations in respect of portfolio management (Article 25(6) of Directive 2014/65/EU)

1. Investment firms which provide the service of portfolio management to clients shall provide each such client with a periodic statement in a durable medium of the portfolio management activities carried out on behalf of that client unless such a statement is provided by another person.

2. The periodic statement required under paragraph 1 shall provide a fair and balanced review of the activities undertaken and of the performance of the portfolio during the reporting period and shall include, where relevant, the following information:

- (a) the name of the investment firm;
- (b) the name or other designation of the client's account;
- (c) a statement of the contents and the valuation of the portfolio, including details of each financial instrument held, its market value, or fair value if market value is unavailable and the cash balance at the beginning and at the end of the reporting period, and the performance of the portfolio during the reporting period;
- (d) the total amount of fees and charges incurred during the reporting period, itemising at least total management fees and total costs associated with execution, and including, where relevant, a statement that a more detailed breakdown will be provided on request;
- (e) a comparison of performance during the period covered by the statement with the investment performance benchmark (if any) agreed between the investment firm and the client;
- (f) the total amount of dividends, interest and other payments received during the reporting period in relation to the client's portfolio;

(g) information about other corporate actions giving rights in relation to financial instruments held in the portfolio;

(h) for each transaction executed during the period, the information referred to in Article 59(4)(c) to (l) where relevant, unless the client elects to receive information about executed transactions on a transaction-by-transaction basis, in which case paragraph 4 of this Article shall apply.

3. The periodic statement referred to in paragraph 1 shall be provided once every three months, except in the following cases:

(a) where the investment firm provides its clients with access to an online system, which qualifies as a durable medium, where up-to-date valuations of the client's portfolio can be accessed and where the client can easily access the information required by Article 63(2) and the firm has evidence that the client has accessed a valuation of their portfolio at least once during the relevant quarter;

(b) in cases where paragraph 4 applies, the periodic statement must be provided at least once every 12 months;

(c) where the agreement between an investment firm and a client for a portfolio management service authorises a leveraged portfolio, the periodic statement must be provided at least once a month.

The exception provided for in point (b) shall not apply in the case of transactions in financial instruments covered by Article 4(1)(44)(c) of, or any of points 4 to 11 of Section C in Annex I to Directive 2014/65/EU.

4. The following provisions in Directive 2009/138/CE (Solvency II) are relevant to this topic:

Article 185

2. The following information about the life insurance undertaking shall be communicated:

(a) the name of the undertaking and its legal form;

(b) the name of the Member State in which the head office and, where appropriate, the branch concluding the contract is situated;

(c) the address of the head office and, where appropriate, of the branch concluding the contract;

(d) a concrete reference to the report on the solvency and financial condition as laid down in Article 51, allowing the policy holder easy access to this information.

3. The following information relating to the commitment shall be communicated:

(a) the definition of each benefit and each option;

(b) the term of the contract;

(c) the means of terminating the contract;

(d) the means of payment of premiums and duration of payments;

(e) the means of calculation and distribution of bonuses;

(f) an indication of surrender and paid-up values and the extent to which they are guaranteed;

(g) information on the premiums for each benefit, both main benefits and supplementary benefits, where appropriate;

- (h) for unit-linked policies, the definition of the units to which the benefits are linked;*
- (i) an indication of the nature of the underlying assets for unit-linked policies;*
- (j) arrangements for application of the cooling-off period;*
- (k) general information on the tax arrangements applicable to the type of policy;*
- (l) the arrangements for handling complaints concerning contracts by policy holders, lives assured or beneficiaries under contracts including, where appropriate, the existence of a complaints body, without prejudice to the right to take legal proceedings;*
- (m) the law applicable to the contract where the parties do not have a free choice or, where the parties are free to choose the law applicable, the law the life insurance undertaking proposes to choose.*

4. In addition, specific information shall be supplied in order to provide a proper understanding of the risks underlying the contract which are assumed by the policy holder.

5. The policy holder shall be kept informed throughout the term of the contract of any change concerning the following information:

- (a) the policy conditions, both general and special;*
- (b) the name of the life insurance undertaking, its legal form or the address of its head office and, where appropriate, of the branch which concluded the contract;*
- (c) all the information listed in points (d) to (j) of paragraph 3 in the event of a change in the policy conditions or amendment of the law applicable to the contract;*
- (d) annually, information on the state of bonuses.*

Where, in connection with an offer for or conclusion of a life insurance contract, the insurer provides figures relating to the amount of potential payments above and beyond the contractually agreed payments, the insurer shall provide the policy holder with a specimen calculation whereby the potential maturity payment is set out applying the basis for the premium calculation using three different rates of interest. This shall not apply to term insurances and contracts. The insurer shall inform the policy holder in a clear and comprehensible manner that the specimen calculation is only a model of computation based on notional assumptions, and that the policy holder shall not derive any contractual claims from the specimen calculation.

In the case of insurances with profit participation, the insurer shall inform the policy holder annually in writing of the status of the claims of the policy holder, incorporating the profit participation. Furthermore, where the insurer has provided figures about the potential future development of the profit participation, the insurer shall inform the policy holder of differences between the actual development and the initial data.

Analysis

5. EIOPA has been asked to provide advice on periodic reports to customers on the services provided. Notwithstanding that the suitability statement is a one-off document; EIOPA has included the suitability statement in this part of the analysis and advice. EIOPA is of the view that providing the one-off statement and a periodic suitability assessment should be dealt with together.
6. Reporting obligations should include a fair and balanced review of the activities undertaken and of the performance during the relevant period. The reports on the services provided, should be provided in a durable medium.

Suitability statement

7. EIOPA acknowledges that distributors, when providing advice, will usually take into account all information available. IDD introduced in Chapter V, the demands and needs test, applicable to all insurance contracts. According to Article 20(1) IDD, prior to the conclusion of an insurance contract, the insurance distributor shall specify, on the basis of information obtained from the customer, the demands and the needs of that customer. EIOPA expects that the suitability statement will focus on the elements of the suitability assessment and does not intend to introduce with its technical advice any form of mandatory "demands and needs statement".
8. When an advice is provided to the customer regarding insurance-based investment products, the suitability statement has to provide feedback on the customer-specific information, which has been gathered and analysed in order to make the recommendation of a suitable contract, transparent.
9. The suitability statement should therefore contain at least:
 - An outline of the advice given; and
 - How the recommendation provided is suitable for the customer.

Periodic Suitability report:

10. EIOPA considers the periodic suitability report referred to in Article 30(5), IDD to be an on-going and regular revision of the initial suitability assessment with the aim of determining whether the product is still in accordance with the best interests of their customers.
11. EIOPA considers it proportionate that a periodic suitability report covers in certain circumstances only changes in the services or investments embedded in the insurance-based investment product and/or the circumstances of the customer and may not need to repeat all the details of the first report.
12. However, if the assessment shows that the product is not in accordance with the best interests of the customer anymore, the customer should be informed without undue delay after the assessment.
13. If the assessment shows that the product is still suitable, EIOPA considers it sufficient to refer to the periodic assessment in the periodic communications to the customer. This would also be proportionate and would not overwhelm the customer with too much information.

Periodic communications to customers

14. EIOPA understands that adequate reports on the service provided are mandatory according to Article 30(5), IDD. In practice, they might not be separable from

other customer communication and could be delivered together with other documents or even electronically.

15. EIOPA refers in its draft technical advice to services provided to and transactions undertaken on behalf of customers. This is due to the fact that IDD specifies that *"reports shall include periodic communications to customers, taking into account the type and the complexity of insurance-based investment products involved and the nature of the service provided to the customer and shall include, where applicable, the costs associated with the transactions and services undertaken on behalf of the customer"*. EIOPA expects the periodic communication to disclose to the customer the costs that are incurred by transactions, which is understood with regard to insurance-based investment products covering changes to the embedded investment elements.
16. The recommended frequency of adequate reports on the service provided should be yearly. EIOPA acknowledges that reporting under MiFID II in the case of portfolio management, foresees quarterly reporting. However, substantial differences exist in EIOPA's view between reporting with regard to portfolio management and periodic communications with regard to insurance-based investment products. Mainly, in the case of insurance-based investment products, the recommended holding period is generally several years, whereas portfolio management can encompass all sorts of financial instruments to report on.
17. At the same time, EIOPA recognises the similarities of portfolio management and periodic communications with regard to insurance-based investment products. Therefore, EIOPA considers it important to report on relevant information. The non-exhaustive list takes into account the type and the complexity of insurance-based investment products and the nature of the service provided to the customer and suggests including, where applicable, the costs associated with the transactions and services undertaken on behalf of the customer.

Draft Technical Advice

Suitability statement

1. When providing advice, the insurance intermediary or insurance undertaking shall provide a statement to the customer that includes an outline of the advice given and how the recommendation provided is suitable for the customer, including how it meets the customer's investment objectives, including that person's risk tolerance; the customer's financial situation, including that person's ability to bear losses; and the customer's knowledge and experience.
2. The insurance intermediary or insurance undertaking shall draw the customer's attention to, and shall include in the suitability statement, information on whether the recommendation is likely to require the customer to seek a periodic review of their arrangements.
3. Where an insurance intermediary or insurance undertaking has informed the customer that it will carry out a periodic assessment of suitability, the subsequent reports after the initial service is established, may only cover changes in the services or investments embedded in the insurance-based

investment product and/or the circumstances of the customer and may not need to repeat all the details of the first report.

4. Insurance intermediary or insurance undertaking providing a periodic suitability assessment shall review, in accordance with the best interests of their customers, the suitability of the recommendations given at least annually.
5. The frequency of this assessment shall be increased depending on the characteristics of the customer, such as the risk profile of the customer, and the insurance-based investment product recommended.
6. The insurance intermediary or insurance undertaking providing a periodic suitability assessment pursuant to paragraph 1, shall disclose all of the following:
 - (a) the frequency and extent of the periodic suitability assessment and where relevant, the conditions that trigger that assessment;
 - (b) the extent to which the information previously collected will be subject to reassessment; and
 - (c) the way in which an updated recommendation will be communicated to the customer.

Periodic communications to customers

7. The insurance intermediary or insurance undertaking shall provide the customer with a periodic statement in a durable medium of the services provided to and transactions undertaken on behalf of that customer.
8. The periodic statement required under paragraph 7, shall provide a fair and balanced review of the services provided to and transactions undertaken on behalf of that customer and shall include, where relevant, the following information:
 - (a) Amount of the premium during the reporting period;
 - (b) Other cost associated with the services provided to and transactions undertaken on behalf of the customer during the reporting period;
 - (c) Any potential reduction to the contract during the reporting period;
 - (d) Guaranteed return;
 - (e) Surrender value;
 - (f) Information on the state of bonuses;
 - (g) Amount of profit participation;
 - (h) Annual rate of return on the asset value;
 - (i) Amount of guaranteed investment;
 - (j) Value of each investment element embedded in the insurance-based investment product, global trend since subscription and significant changes affecting the investments embedded in the insurance-based investment product;
 - (k) Information on surrender, transfer, and reduction practicalities;
 - (l) Date of maturity.

9. The periodic statement referred to in paragraph 7 shall be provided annually, except where the insurance intermediary or insurance undertaking provides its customers with access to an online system, which qualifies as a durable medium, where up-to-date information can be accessed and the insurance intermediary or the insurance undertaking has evidence that the customer has accessed the information at least once during the relevant reporting period.

Questions to stakeholders:

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?

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

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?

8. **Annex I: Summary of Questions to Stakeholders**

1. What would you estimate as the costs and benefits of the possible changes outlined in this Consultation? Where possible, please provide estimates of one-off and ongoing costs of change, in Euros and relative to your turnover as relevant. If you have evidence on potential benefits of the possible changes, please consider both the short and longer term. As far as possible, please link the costs and benefits you identify to the possible changes that would drive these.
2. Do you agree that the policy proposals above provide sufficient detail on product oversight and governance arrangements?
3. Are there any further arrangements, except those outlined below, which you would consider necessary and important?
4. What costs will manufacturers and distributors face to meet these requirements? If possible, please estimate the costs through quantitative data.
5. Do you agree with the proposed high-level principle in order to assess whether activities of an insurance intermediary should be considered as manufacturing?
6. Do you consider that there is sufficient clarity regarding the collaboration between insurance undertakings and insurance intermediaries which are involved in the manufacturing of insurance products? If not, please provide details of how the collaboration should be established.
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.
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?
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.
10. Do you agree that the policy proposals do not need further specification of the principle of proportionality and allow sufficient flexibility to market participants to adapt the organisational arrangements to existing business models? If you do not agree, please explain how the principle of proportionality could be elaborated further from your point of view?
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?

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?
13. To which extent are inducements which are considered bearing a high risk of detrimental impact part of existing business and distribution models? Please specify your answer and describe the potential impact of these proposals (if possible with quantitative data).
14. Are there any further organisational measures or procedural arrangements which you would consider important to monitor whether and to ensure that inducements have no detrimental impact on the relevant service to the customer and do not prevent the professional from complying with their obligation to act honestly, fairly and in accordance with the best interests of their customers?
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?
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?
17. In practice, what information do you expect to collect for the assessment of suitability and appropriateness in addition to the demands and needs?
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?
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?
20. Are there any further high level criteria which you would consider necessary and important, and why? In particular, how could insurance specificities be taken into account?
21. While point (i) of point (a) of paragraph 3 of Article 30 is intended to capture the majority of non-complex products, the above listed criteria should capture equally non-complex products falling outside of point (i). Are there any gaps?

22. On retention of records, do you agree with the high level criteria used? Are there any you would exclude, and why?
23. When EIOPA is reflecting insurance specificities in the policy proposals, do you agree with them?
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?
25. When EIOPA is reflecting insurance specificities in the policy proposals, do you agree with them?
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?

9. Annex II: Impact Assessment

1. Procedural issues and consultation of interested parties

The Commission has requested EIOPA to provide technical advice on possible delegated acts concerning Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution (hereinafter "IDD"). In particular, the Commission seeks EIOPA's technical advice regarding the following issues:

- Product oversight and governance,
- Conflicts of interest,
- Inducements and
- Assessment of suitability and appropriateness and reporting to customers.

According to the Commission's request, EIOPA should justify its advice by identifying, where relevant, a range of technical options and undertaking a qualitative, and as far as possible, quantitative assessment of the costs and benefits of each. Where administrative burdens and compliance costs on the side of the industry could be significant, EIOPA should where possible quantify these costs.

The analysis of costs and benefits is undertaken according to an Impact Assessment methodology.

The draft technical advice and its impact assessment are envisaged to be subject to public consultation. Stakeholders' responses to the public consultation will be duly analysed and will serve as a valuable input for the revision of the draft technical advice and its impact assessment.

2. **Product Oversight & Governance**

With respect to the technical advice on product oversight and governance, EIOPA will also take into account all the relevant input provided by stakeholders during the policy development process of EIOPA Preparatory Guidelines on product oversight and governance arrangements by insurance undertakings and insurance distributors³⁵. A first public consultation of the draft Guidelines and their impact assessment took place between 27 October 2014 and 23 January 2015 and a second public consultation between 30 October 2015 and 29 January 2016. Additionally, in accordance with Article 16, EIOPA Regulation, the Insurance and Reinsurance Stakeholder Group was consulted and provided a formal Opinion.

³⁵ <https://eiopa.europa.eu/Publications/Reports/Final%20report%20on%20POG%20Guidelines.pdf>

3. Problem definition

Article 25, IDD introduces product oversight and governance requirements for insurance manufacturers and distributors, to mitigate the risk of customer detriment from unsuitable and/or poorly designed products.

As this matter is being addressed by ESMA and EBA³⁶, there is also potential for the coexistence of different regulatory/supervisory approaches in the three financial sectors.

Baseline scenario

A baseline scenario is used to compare policy options as part of the impact assessment methodology. This helps to identify the incremental impact of each policy option. The aim of the baseline scenario is to explain how the current situation would evolve without additional regulatory intervention.

EIOPA has applied as a baseline scenario to assess the potential costs and benefits from the provisions in the technical advice, the IDD requirements and the EIOPA Preparatory Guidelines on product oversight and governance arrangements for insurance undertakings and insurance distributors.

4. Objective pursued

The objectives of the technical advice are:

Objective 1: to specify the product oversight and governance principles and ensure that manufacturers and distributors of insurance products comply.

Objective 2: to identify product manufacturer and distributor responsibilities in a proportionate manner, taking into account the nature of the product and service provided.

Objective 3: to enhance cross-sectoral consistency with product oversight and governance arrangements for credit institutions and investment firms.

These objectives are consistent with the IDD aim of providing general policyholder protection.

5. Policy options

With the intention to meet the objectives set out in the previous section, EIOPA has analysed different policy options throughout the policy development process.

Taking into account that the technical advice contains several proposals based on the policy work developed by EIOPA for the development of the Preparatory Guidelines, part of the policy issues identified during the drafting process of the guidelines are deemed to be relevant for this impact assessment. Those policy issues are:

- principle of proportionality;

³⁶ Regarding the work done in respect of the other sectors of the market:

- Directive 2014/65/EU (MIFID II) includes product oversight and governance requirements for investment firms. On 25th April 2016 the Commission has adopted a delegated regulation supplementing MiFID II, which includes product governance provisions.

- On 22nd March 2016, the EBA approved product oversight and governance guidelines for retail banking products.

- product testing;
- frequency of the review process for the product oversight and governance arrangements;
- outsourcing of product design;
- exchange of information between manufacturers and distributors; and
- documentation of product oversight and governance arrangements.

For the sake of completeness and transparency, the analysis of the different options considered for those policy issues has also been included in this impact assessment.

During the drafting process of the technical advice the following policy issues were identified:

- definition of insurance intermediary acting as manufacturer;
- relationship between and respective responsibilities of the insurance undertaking and the intermediary when acting as a manufacturer;
- identification of the target market; and
- frequency of the review process for products.

Policy issue 1: Principle of proportionality

The impact of POG requirements will differ depending on the size (level of the undertaking), on their type of business (product level) and also depending on the risks inherent in the product. Insurance products are quite heterogeneous, in particular their complexity varies (example: general liability insurance vs. with-profit life insurance). Thus the question arose whether regulation should be more prescriptive and differentiate between insurance business classes or whether it would be sufficient to apply the principle of proportionality more generally.

A further option would be to further develop and complement the approach above by some guidance regarding what the applicability of the principle of proportionality could mean in relation to insurance business classes. The following options were considered:

- **Option 1.1** – specific requirements by line of business: to differentiate between insurance business classes within the product oversight and governance provisions.
- **Option 1.2** – general application of the principle: not to differentiate between insurance business classes, but to take account of the applicability of the principle of proportionality in general.
- **Option 1.3** – specific guidance on application of the principle: not to differentiate between insurance business classes but to give supervisors and insurance undertakings some guidance on details of applicability of the principle of proportionality for product and governance processes.

Policy issue 2: Need for including requirements for product testing

Product governance requirements stipulate that manufacturers should define a target market and make sure that the product is aligned with the interests, objectives and characteristics of the target market.

In order to comply with this requirement, it is important that the manufacturer tests the product thoroughly before they are brought to the target market. The conditions and methods applied for product testing including scenario analysis where relevant are in the responsibility of the manufacturer. It can be argued that these conditions and methods differ depending on the type of product that will be manufactured or reviewed and on the risks that the product bears for customers. Product testing may include qualitative and, where appropriate, quantitative testing or scenario analyses in order to properly assess whether the product is in line with the interests, objectives and characteristics of the target market.

Various options were examined:

- **Option 2.1** - no requirement: not to require product testing for any insurance product.
- **Option 2.2** - requirement for life: to only require product testing for life insurance products.
- **Option 2.3** - requirement for all products: to require product testing for life and non-life insurance products.

Policy issue 3: Need for a specific provision on outsourcing of product design

The manufacturer may outsource different tasks and processes – in particular, the design of products - to third parties. This organisational choice does not mean that the manufacturer can outsource his responsibility for the outcome or for applying the relevant requirements for the outsourced process. The following options were considered:

- **Option 3.1** - specific provision: provision meaning that when product design is being outsourced the administrative, management or supervisory body (AMSB) of the manufacturer stays ultimately responsible regardless of the outsourcing
- **Option 3.2** – do nothing: meaning that the responsibility for applying the requirements is not especially described in case of outsourcing.

Policy issue 4: Need to strengthen the exchange of information between manufacturers and distributors of insurance products

The increasing complexity and variety of insurance products pose new challenges to insurance distributors selling insurance products manufactured by third parties. To a large extent, distributors rely on the product information provided by the manufacturers of insurance products. However, the supervisory practice has proven that distributors do not always get all relevant information which is necessary to fully

understand the product characteristics and the group of customers for which the products are designed for. In order to address this issue, the following options were considered:

- **Option 4.1** – do nothing: not to specify the general requirement that the manufacturer provides all appropriate information on the product to the distributor.
- **Option 4.2** - list of information to be exchanged: to specify the information on the product and on the distribution of the product which the manufacturer and distributor should exchange.

Policy issue 5: Documentation of product oversight and governance arrangements

From an internal governance and supervisory point of view, it is important that all relevant actions taken by manufacturers and distributors in relation to the product oversight and governance arrangements are duly documented. The following policy options were considered in this regard:

- **Option 5.1** - for manufacturers and distributors: to require manufacturers and distributors to document all relevant actions in relation to the product oversight and governance arrangements and product distribution arrangements, respectively.
- **Option 5.2** – for manufactures: to require manufacturers only to document all relevant actions in relation to the product oversight and governance arrangements, but not distributors.
- **Option 5.3** – do nothing: not to require manufacturers and distributors to document all relevant actions in relation to the product oversight and governance arrangements and product distribution arrangements.

Policy issue 6: Insurance intermediary acting as a manufacturer of insurance products

Article 25(1), IDD applies certain product governance requirements to "*insurance undertakings, as well intermediaries which manufacture any insurance product for sale to customers*". The IDD is silent on when insurance intermediaries should be considered "manufacturers" and there is no definition of "manufacturing". It is therefore useful to consider circumstances where an intermediary may also be acting as a manufacturer.

The following options were considered:

- **Option 6.1** – Cumulative conditions: identification of a cumulative list of conditions where an insurance intermediary could also be considered a manufacturer.
- **Option 6.2** – General criteria: identification of general criteria where an insurance intermediary could be considered a manufacturer and circumstances where an intermediary would be less likely to be considered a manufacturer.

Policy issue 7: Target market

Product oversight and governance requirements set out systems and controls firms must put in place to design, approve, market and manage products throughout their lifecycle to ensure they meet the needs, objectives and characteristics of a defined target market. These processes help to mitigate mis-selling. The identification of the target market is an important component of the Product Oversight and Governance (POG) arrangements.

Insurance products are varied in nature, ranging, for example, from simple, but compulsory motor insurance through to complex insurance based investment products (IBIPs). The policy issue centres on identifying how best to address the question of target market granularity level while maintaining firm responsibility and discretion over product manufacturing.

The following options were considered:

- **Option 7.1** - No principles to identify the target market: One option would be to introduce no principles to identify the target market for products and allow manufacturing and distribution on a broader, more generic basis.
- **Option 7.2** - High-level principles to identify the target market: Another possibility would be to adopt high-level principles to identify the target market. This means it would be possible to emphasise that the target market can differ depending on the type of product being developed.
- **Option 7.3** - Detailed requirements to identify the target market: Another possibility would be to enforce detailed requirements and describe requirements per category of products. A mandatory target market could be based on specified criteria e.g. financial situation, age, experience etc.

Policy Issue 8: Frequency of review process

Any internal process should be reviewed periodically in order to assess the permanence of the attitude and capability to reach the objectives. In light of this, the product and arrangements established by manufacturers on product oversight and governance should both be reviewed to ensure that they are still valid and up to date and amended where appropriate. Furthermore, the distributor's distribution arrangements should also be reviewed and amended where appropriate.

Regarding the frequency of the review process three options were examined:

- **Option 8.1** - Annual review: Article 41, Solvency II Directive requires insurance undertakings to review written policies on an annual basis. An annual review of product governance arrangements would be in line with this.
- **Option 8.2** - At least, review every three years.
- **Option 8.3** - No pre-determined frequency of review.

6. Analysis of impacts

Policy issue 1: Proportionality principle and differentiation between insurance classes of business

Summary of options considered:

Option 1.1: to differentiate between insurance business classes within the POG requirements.

Benefits:

- For customers: minimized risk of mis-selling due to detailed rules considering all eventualities (incl. specificities of insurance business classes).

Costs:

- For NCAs and industry: among the three options considered, the highest implementation costs due to most detailed requirements. Too prescriptive provisions could also become an obstacle for product innovation.

Option 1.2: not to differentiate between insurance business classes within the POG requirements, taking account of the applicability of the principle of proportionality in general.

Benefits:

- For customers: minimum risk of mis-selling due to clear rules on product oversight and governance.

Costs:

- For NCAs and industry: implementation costs; considered the lowest among the three options compared.

Option 1.3: not to differentiate between insurance business classes within the POG requirements but to give supervisors and insurance undertakings some guidance on details of applicability of the principle of proportionality for product and governance processes.

Benefits:

- For customers: minimized risk of mis-selling due to detailed rules considering all eventualities (incl. specificities of insurance business classes).
- For NCAs: compared to Option 1, higher level of flexibility.

Costs:

- For NCAs and industry: among the three options compared; the second highest implementation costs.

- For EIOPA: potential for the evolution of diverging supervisory practices.

Policy issue 2: Need for including requirements for product testing

Various options were examined:

Option 2.1: Not to require product testing for any insurance product.

Benefits:

- For industry: out of the options compared, the lowest or no implementation costs.
- For customers: potentially more options/product variants to choose from.

Costs:

- For industry: there is a risk that the product will not at all times fulfil the identified needs of the target market. This may harm the trust customers have in the insurance undertaking or insurance intermediary.
- For customers: out of all options compared, the highest risk of detriment occurs, as the product's design may not be entirely suitable for the customer. At a certain moment in time, the product can be the right choice, yet the customer does not know what will happen when the circumstances change.

Option 2.2: to only require product testing for life insurance products.

Benefits:

- For industry and customers: more certainty that the life insurance product fulfil the identified need of the target market at all times. The maintenance/ rebuild of trust in undertakings and their products will benefit both undertakings and the customers.

Costs:

- For customers: risk of potential detriment in the case of non-life products.
- For industry: higher implementation costs than under Option 4.1. Product testing may also hinder innovation as it can prove to be time consuming and may delay the development and issuance of new insurance products.

Option 2.3: to require product testing for both life and non-life insurance products.

Benefits:

- For industry and customers: out of all options compared, the highest certainty that any insurance product (incl. non-life) will fulfil the identified need of the target market at all times. The maintenance/rebuilding of trust in financial institutions and their products will benefit both financial

institutions and their customers.

Costs:

- In general, more requirements lead to higher costs. Product testing may also hinder innovation as it can prove to be time consuming and may delay the development and issuance of new insurance products.

Policy issue 3: Need for a specific provision on outsourcing of product design

The following options were considered:

Option 3.1: specific provision when product design is being outsourced; meaning that the administrative, management or supervisory body (AMSB) of the manufacturer remains ultimately responsible, regardless of the outsourcing.

Benefits:

- For customers: Customer protection is ultimately assured, regardless of the governmental structure and the internal decisions taken by the manufacturer on how to organise the designing of its products.
- For industry: The manufacturer faces no reputational risk in the case that the product design is being outsourced and that the arrangements on POG are not applied at the third party service provider level. The manufacturer keeps the ultimate responsibility, meaning he has the right to continuously monitor and therefore can ensure that the products offered comply with all arrangements requested. The manufacturer has the possibility to request in its contract with the third party service provider that the POG requirements are part of their contract.
- For national competent authorities (NCAs): When supervising the manufacturer, the supervisory authority concerned has one point of contact, the AMSB of the manufacturer and not unknown third parties like the service provider. It is assumed that the supervisor is engaging in several dialogues with the insurance undertaking, i.e. due to Solvency II requirements, and therefore already has a good understanding of the manufacturer and its governmental structures.
- For EIOPA: The Solvency II requirements in the system of governance require the ultimate responsibility of the AMSB for any outsourced important function. To provide technical advice with the same underlying principle assures a better and consistent approach of customer protection throughout different areas.

Costs:

- For customers: Customers may face higher costs for insurance products. The risks are that the manufacturer who is going to outsource product design may face higher product costs himself. Those costs may be passed onto the buyer of the product, namely the customer.
- For industry: As described above, the manufacturer may face higher costs when outsourcing its product design. Secondly, the possibility could be that not all service providers want to apply the POG requirements or are not familiar with them which may lead to lower availability of possible service providers.

Option 3.2: no specific provision; meaning that the responsibility for applying the requirements is not specifically described in case of outsourcing.

Benefits:

- No particular benefits in comparison to Option 3.1 were identified, as the manufacturer remains responsible for any outsourced activities.

Costs:

- For customers: The customer could face insufficient customer protection when buying an insurance product which has not been designed by the manufacturer himself, but by a service provider. In many, if not all, cases, the customer has no knowledge of how the product has been designed. Therefore, insufficient information is provided, which does not allow the customer to make a clear choice.
- For NCAs: Outsourcing may hinder the competent authority's ability to take supervisory action if needed and deemed necessary in order to request that customers' interest are addressed by the third party service provider in the development phase of the product. Supervisory powers would be limited and the objective of enhanced customer protection could not be realised.
- For EIOPA: The system of governance under Solvency II includes requirements on outsourcing. In case of a different approach under POG regulation, no consistent approach would be ensured. This could result in an unlevel playing field from the perspective of risk-based supervision.

Policy issue 4: Need to strengthen the exchange of information between manufacturers and distributors of insurance products

Option 4.1: not to specify the general requirement that the manufacturer provides all appropriate information on the product to the distributor.

Benefits:

- For industry: allows for flexibility and discretion regarding the information which is exchanged between manufacturer and distributor.

Costs:

- For industry: if regulation does not specify the relevant information which manufacturers and distributors should exchange, the exchange of information depends highly on the willingness of the manufacturer and distributor to exchange information; this can have a negative impact on the exchange of information which is relevant for both in order to fulfil their regulatory requirements with regard to the product and customers.
- For NCAs: a possible need to specify the information to be exchanged through guidance at a later point in time.

Option 4.2: to specify the information on the product and on the distribution of the product which the manufacturer and distributor should exchange.

Benefits:

- For industry: strengthens the position of the distributor and manufacturer to ask for and get the information necessary to fulfil the distributor's duties towards the customers.
- For NCAs: no need to specify the information to be exchanged through further guidance at a later point of time.

Costs:

- For industry: cost of implementation and ongoing costs related to the increase of information to be exchanged between distributor and manufacturer.

Policy issue 5: Documentation of product oversight and governance arrangements

Option 5.1: to require manufacturers and distributors to document all relevant actions in relation to the product oversight and governance arrangements and product distribution arrangements, respectively.

Benefits:

- For industry: facilitates the internal monitoring and review of processes

and measures taken in relation to the product oversight and governance arrangements.

- For NCAs: facilitates the supervision and the assessment of how the provisions are implemented by the undertakings.

Costs:

- For industry: additional costs following from the requirement to document all relevant actions in relation to the product oversight and governance arrangements.

Option 5.2: to require manufacturers only to document all relevant actions in relation to the product oversight and governance arrangements, but not distributors.

Benefits:

- For industry: distributors would not bear additional costs to document all relevant actions in relation to the product oversight and governance arrangements; this would be for the benefit of small distributors which would potentially suffer more than large undertakings.

Costs:

- In general: would create unlevelled playing field and regulatory arbitrage between distributors and manufacturers.

Option 5.3: not to require manufacturers and distributors to document all relevant actions in relation to the product oversight and governance arrangements and product distribution arrangements.

Benefits:

- For industry: no additional costs to document all relevant actions in relation to the product oversight and governance arrangements.

Costs:

- For industry: will make it more difficult for undertakings to monitor and review actions taken in relation to the product oversight and governance arrangements.
- For NCAs: will make it more difficult for NCAs to supervise and assess the implementation of the provisions by the undertakings.

Policy issue 6: Intermediary acting as manufacturer of insurance products

Option 6.1: - Cumulative conditions

Benefits:

- For industry: industry would be provided with specific circumstances

when they may or may not be considered to be manufacturers. This could also, however, restrict innovation.

Costs:

- For customers: a restrictive approach could result in circumstances where an intermediary is involved in the manufacturing process, but this is not captured in the list. This could mean the intermediary does not put in place, product governance arrangements they would otherwise have put in place, had they been considered the product manufacturer.

Option 6.2: - General criteria

Benefits:

- For customers: general criteria to identify a manufacturing function could allow for local conditions to be taken into account
- For industry: Since the general criteria are complemented with the identification of activities which should not be considered as activities of manufacturing, uncertainty for insurance intermediaries is limited.

Policy issue 7: Target market

Option 7.1: - No principles to identify the target market

Benefits:

- For industry and customers: Greater scope for product innovation due to wider market provisions.
- For industry: Manufacturers have full discretion and responsibility over product manufacturing.

Costs

- For industry: when there are no principles to identify the target market, this could lead to legal uncertainty for manufacturers. They may not know if they meet the IDD requirements to identify a target market.
- For customers and in general: Greater risk of miss-selling. Could undermine the aim of the product governance requirements which are intended to ensure products meet the needs and characteristics of the target market. If these are not the relevant characteristics in a particular context then it is unlikely they will be helpful and could even drive the development of product which runs counter to customer interest and limits innovation.
- For NCAs: If there are no principles to identify the target market, it could be difficult and costly to supervise the IDD requirements.

Option 7.2: – High level principles to identify the target market

Benefits

- For customers, industry and in general: high-level principles may help

industry to identify the needs and characteristics of the target market more clearly and manufacture products which are in line with the specifications of the target market. This would likely lead to a reduction in mis-selling and provide industry with discretion to innovate when manufacturing insurance products.

- For NCAs: High level principles would provide NCAs with the legal basis to act if products run counter to customer interest.

Costs

- For customer and industry: High level principles could potentially lead to more implementation costs than no principles at all. This could result in increased product costs for the customer.

Option 7.3: – Detailed requirements to identify the target market

Benefits

- For industry: Detailed regulation will provide (legal) certainty to manufacturers.

Costs

- For industry and customers: Detailed regulation would likely result in higher implementation costs which may be passed on to the customer through higher product prices. Furthermore, prescriptive regulation would reduce manufacturer discretion and responsibility. It could also limit product innovation and the manufacturer's ability to respond to changing circumstances that could benefit customers.
- It might also be disadvantageous for smaller firms because they would be less likely to absorb the costs.
- For NCAs: Prescriptive legislation could reduce NCAs' ability to act if detailed requirements are fulfilled but the product produced is not in line with the interest of customers. It would also reduce NCA options to organise their assessments more efficiently and effectively. This could lead to higher supervision costs.

Policy issue 8: Frequency of the review

Option 8.1: - At least annual review

Benefits:

- For customers: Alignment with Solvency II review requirements would deliver a consistent approach for customers.
- For industry: Alignment with the Solvency II review provisions could enable firms to develop efficiencies and consistency of approach.

Costs:

- For industry: Annual reviews of POG arrangements may be costly for smaller manufacturers or distributors which also play a role in

manufacturing where the product offering does not change on a yearly basis.

Option 8.2: - At least, review every three years

Benefits:

- For industry and in general: Certainty about the minimum frequency of the review without imposing an annual review, which may be too costly (in particular for small manufacturers).
- For customers: Reduce the risk of customer detriment by avoiding that a review would not take place as often as necessarily.

Costs:

- For industry and general: Not alignment with the annual review of written policies in Solvency II.

Option 8.3: – No uniform pre-determined frequency

Benefits:

- For customers: Manufacturers could undertake POG reviews more frequently if no specific timeframe is imposed. This could be appropriate for new products introduced throughout the year.
- For industry: The manufacturer would have discretion over the most relevant and appropriate timing based on the product offering and risk profile.

Costs:

For industry and in general: POG reviews which are not aligned to the Solvency II annual governance review requirement could result in an inconsistent approach which could potentially lead to additional costs for the firm.

7. Comparing the options

Policy issue 1: Proportionality principle and differentiation between insurance classes of business

When comparing the costs and benefits of the different options, it became apparent that the anticipated benefits would be largely similar in all cases. Based on the assessment of costs, Option 1.2 seemed preferable. Besides, the criteria for the proportionality principle as well as for its application are being referred to in the IDD³⁷ and the Solvency II Directive³⁸.

Taking this into consideration, **option 1.2** (not to differentiate between insurance business classes, taking account of the applicability of the principle of proportionality in general) **was chosen**. It points out that the principle of proportionality does not mean only to ensure a proportionate application of the requirements in order to limit burden on small size manufacturers/distributors but also to avoid too burdensome processes for insurance business classes with lower risk and/or complexity.

An explicit reference has been inserted in the proposed technical advice to clarify that product oversight and governance arrangements and product distribution arrangements need to be proportionate to the level of complexity and the risks related to the products as well as the nature, scale and complexity of the relevant business of the insurance distributor.

Policy issue 2: Need for including requirements for product testing

A quantitative test can be run in order to see whether risk and return are well balanced under different scenarios for unit-linked investments. For non-life insurance, the coverage of the product can be looked at, for instance, to see under what conditions, or in which "scenarios", an overlap with other products occur. Based on this analysis, the manufacturer can align the coverage of the product with the other products he offers in order to prevent or reduce overlap in coverage.

Scenario analysis should therefore be seen in a broader context, and should be considered as a useful method in order to make sure that the product is aligned with the interests, objectives and characteristics of the target market during the life cycle of the product. Due to the fact that the technical advice capture all types of insurance products, it was decided that **option 2.3** (to require product testing for life and non-life insurance products) **is the most appropriate level of requirement**.

³⁷ Article 25 (1) IDD: "The product approval process shall be proportionate and appropriate to the nature of the product."

³⁸ Article 29 (3) Solvency II: "Member States shall ensure that the requirements laid down in this Directive are applied in a manner which is proportionate to the nature, scale and complexity of the risks inherent in the business of an insurance or reinsurance undertaking."

Policy issue 3: Need for a specific provision on outsourcing of product design

In the system of governance requirements under Solvency II, the insurance undertaking remains ultimately responsible when outsourcing important tasks or key functions. EIOPA deems this principle to be one of the most important for good governance. Cases in the market where this rule has not been applied can serve as examples of failures not only in governance and therefore as failures for the insurance undertaking, but even serve as examples of very poor customer protection.

It was concluded that in order to ensure that the product design complies with and serves the overall objective of this technical advice to enhance customer protection - even in those cases where the manufacturer has chosen to outsource this tasks -, a specific provision in the draft technical advice was needed. Hence **option 3.1** (specific provision when product design is being outsourced) **is the preferred option**. This option does not prevent the manufacturer from organising his internal processes to best fit his business and to avoid customer detriment at the same time.

Policy issue 4: Need to strengthen the exchange of information between manufacturers and distributors of insurance products

As outlined in the presentation of policy issue 4, the supervisory practice has shown that distributors do not always receive all relevant information, which is necessary to fully understand the products they intend to distribute. Deficits in information may impede the proper assessment and thorough understanding of insurance products, as well as negatively affect the quality of services provided to the customer, eventually leading to poor quality of services and raising the risk of customer detriment.

Strengthening the exchange of information on the product between manufacturer and distributor seems the appropriate way of overcoming this risk. Against this background, **option 4.2** (to specify the information on the product and on the distribution of the product which the manufacturer and distributor should exchange) **is the preferred option**.

Policy issue 5: Documentation of product oversight and governance arrangements and product distribution arrangements

As outlined in the presentation of policy issue 5, it is important from an internal governance and supervisory point of view, to duly document all relevant actions in relation to the product oversight and governance arrangements. For insurance distributors, an appropriate documentation facilitates the compliance, internal monitoring and review of processes and measures taken in relation to product oversight and governance arrangements.

For national competent authorities, a proper documentation facilitates the supervision of implementation. This does not only apply with regard to manufacturers, but also for distributors. Therefore, a distinction between manufacturers on one side and

distributors on the other side does not seem appropriate. Against this background **option 5.1** (to require manufacturers and distributors to document all relevant actions in relation to the product oversight and governance arrangements and product distribution arrangements, respectively) **is the preferred option**. In order to limit this requirement, it has been specified that the documentation should be kept for a minimum period of five years (which is in line with the approach taken by MiFID I and MiFID II).

Policy issue 6: Intermediary acting as product manufacturer

Intermediaries should be considered manufacturers where they have a role in product design and development. Distribution strategies across Member States vary, which means it can be challenging to identify specific circumstances where the intermediary is involved in product manufacturing.

According to this, **option 6.2** (general criteria) **was followed**. Non-exhaustive criteria can be used to determine the intermediary's role as manufacturer on a case-by-case basis. This should be based on an overall analysis of the specific activities of the insurance intermediary in the product design.

Policy issue 7: Target market

EIOPA's preferred policy option is option 7.2 (high-level principles to identify the target market). High level principles support the aim of the POG arrangements to produce insurance products which are in line with the interest and characteristics of the target market. It will give more legal certainty for the industry, but will also leave discretion and responsibility with the manufacturer. Furthermore, it will give NCAs a legal basis to challenge products, which do not meet customer interests.

Policy issue 8: Frequency of the review

The benefit of option 8.1 (annual review) is that it provides consistency with Solvency II, which requires insurance firms to annually review governance arrangements. EIOPA considered an annual review to be too costly particularly for small undertakings or to those that do not frequently design new products. On the other hand, an annual review could be seen as not sufficiently effective for larger insurance undertakings or for those that frequently design new product lines.

Bearing these concerns in mind, **option 8.2** (no frequency requirements) **was followed**. The technical advice does not specify the frequency of the process, leaving such decisions to the manufacturer. This option allows each manufacturer to adapt the frequency of the review process in line with the timing of the internal design product, also taking into account the size, scale and complexity of the insurance undertaking and of the different products that it manufactures.

2. Conflicts of Interest

Section 1 - Procedural issues and consultation of interested parties

The specific terms used in this assessment have been defined in the Commission's request for advice in relation to Articles 27 and 28 of the Insurance Distribution Directive (IDD) as follows:

The Commission's Request for Advice

"EIOPA is invited to provide technical advice on

- the different steps that insurance intermediaries and insurance undertakings distributing insurance-based investment products might reasonably be expected to take within an effective organisational and administrative arrangement designed to identify, prevent, manage and disclose conflicts of interest;*
- the circumstances and situations to take into account when determining which types of conflict of interest may damage the interests of the customers or potential customers of an insurance intermediary or insurance undertaking.*

The technical advice should specify the different steps to be taken within an effective organisational and administrative arrangement designed to identify, prevent, manage and disclose conflicts of interest. This should include, in particular, the requirements for periodical review of conflicts of interest policies and clarifications with respect to the last resort nature of disclosure which should not be over-relied on by insurance intermediaries and insurance undertakings nor used as a measure to manage conflicts of interest. Particular attention should be given to the practical implementation of the proportionality requirement.

In order to ensure regulatory consistency, the technical advice should build on existing conflict of interest rules, as laid down in Commission Directive 2006/73/EC, particularly with regard to establishing appropriate criteria for determining the types of conflict of interest whose existence may damage the interests of customers or potential customers. It should also be consistent with the line taken in the delegated acts expected to be adopted under Article 23(4) of MiFID II."

In addition, the Commission "invites EIOPA to build on the results of previous work that has already been carried out by EIOPA and ESMA (e.g. EIOPA's previous technical advice on conflict of interests in direct and intermediated sales of insurance-based investment products ("IMD 1.5"))"³⁹

³⁹ EIOPA-15/135, 30 January 2015: Technical Advice on Conflicts of Interest in direct and intermediated sales of insurance-based investment products [https://eiopa.europa.eu/Publications/Opinions/EIOPA-15-135_Technical%20Advice%20%20Impact%20Assessment_conflicts_of_interest_version%20for%20COM%20\(2\).pdf](https://eiopa.europa.eu/Publications/Opinions/EIOPA-15-135_Technical%20Advice%20%20Impact%20Assessment_conflicts_of_interest_version%20for%20COM%20(2).pdf)

Section 2 - Problem definition

Articles 27 and 28, IDD comprise new organisational requirements for insurance undertakings and insurance intermediaries with regard to conflicts of interests that arise in the context of the distribution of insurance-based investment products.

Article 27 requires insurance undertakings and insurance intermediaries to take all reasonable steps to prevent conflicts of interest from adversely affecting the interests of their customers.

Article 28(1) requires insurance undertakings and insurance intermediaries to identify and manage conflicts of interest that arise in the course of carrying out insurance distribution activities.

Article 28(4) empowers the Commission to adopt delegated acts to further define the steps insurance undertakings and insurance intermediaries have to take to identify, prevent, manage and disclose conflicts of interest, as well as to establish criteria for determining the types of conflict of interest that may damage the interests of the customers.

An equivalent set of rules for investment firms providing investment services in financial instruments has already been introduced through MiFID in 2004. These provisions have been specified by the Directive 2006/73/EC implementing Directive 2004/39/EC of the European Parliament and of the Council as regards the organisational requirements and operating conditions for investment firms (hereafter "MiFID Implementing Directive") and **are now embodied in a draft Delegated Regulation under MiFID II has recently been adopted by the Commission**⁴⁰.

The underlying rationale of Articles 27 and 28, IDD is that insurance-based investment products are often made available to customers as potential alternatives or substitutes to financial instruments (Recital 56, IDD). In order to provide consistent protection for customers and ensure a level playing field between similar products, it is important that the distribution of insurance-based investment products is subject to comparable regulatory requirements. Therefore, the objective pursued by the European legislator is to address the issue of an uneven playing field across the different financial sectors hindering fair competition in the market, as well as to abolish regulatory inconsistencies leading to a patchwork of consumer protection.

As outlined above, Article 28(1) requires insurance undertakings and insurance intermediaries to take all reasonable steps to prevent conflicts of interest from adversely affecting the interests of their customers. This is justified by the fact that conflicts of interest, independent from the question whether they arise in the context of the provision of investment services or the distribution activities of insurance intermediaries and undertakings, raise concerns about consumer detriment. In the case of a conflict of interest, there is the inherent risk that the conflict is inappropriately managed and resolved to the disadvantage of the customer.

Articles 27 and 28, however, neither specify which criteria should be applied for the identification of conflicts of interest that may arise with regard to the distribution activities of insurance undertakings and insurance intermediaries, nor stipulate

⁴⁰ Commission Delegated Regulation supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive

organisational measures to be considered for the management of conflicts of interested identified by insurance undertakings and insurance intermediaries.

Different from the regulatory regime under MiFID II as circumscribed above, the provisions in IDD, due to their abstract wording, would leave a broad discretion to National Competent Authorities (NCAs) and regulated entities as to how these requirements are applied in practice. This would result in a divergent implementation and application contrary to the objective to foster a level playing field.

In order to avoid regulatory arbitrage and to contribute to a homogenous application of the new organisational requirements for insurance undertakings and insurance intermediaries it is therefore necessary to specify these requirements through implementing measures.

As the data provided by stakeholders in response to the EIOPA's Consultation Paper on Conflicts of Interest is not sufficiently representative to allow a reliable assessment of the quantitative impacts, the following analysis will focus on the qualitative impacts following from the Technical Advice.

With respect to studies mandated by the Commission, which have addressed the question of how the application of the rules of conduct and the organisational requirements of MiFID would impact the insurance sector the following analyses are of particular importance:

- Impact Assessment accompanying the Commission's Proposal to recast the Directive on Markets in Financial instruments (published on 20 October 2011): http://ec.europa.eu/internal_market/securities/docs/isd/mifid/SEC_2011_1226_en.pdf
- Study on the Costs and Benefits of Potential Changes to Distribution Rules for Insurance Investment Products and other Non-MIFID Packaged Retail Investment Products (published on 29 October 2010): http://ec.europa.eu/internal_market/consultations/docs/2010/prips/costs_benefits_study_en.pdf
- Impact Assessment accompanying the Commission's Proposal to recast the Directive on Insurance Mediation: http://ec.europa.eu/finance/insurance/docs/consumers/mediation/20120703-impact-assessment_en.pdf

How would the problem evolve without EU action? The baseline scenario

When analysing the impact of alternative proposed policies, the impact assessment methodology uses a baseline scenario as the basis for comparing policy options. This helps to identify the incremental impact of each policy option considered.

The aim of the baseline scenario is to explain how the current situation would evolve without additional regulatory intervention.

The baseline is based on the current situation of the market, which is considered to be composed of the content of Articles 27 and 28 of the IDD.

For the analysis of the potential related costs and benefits of the proposed delegated acts regarding conflicts of interest, EIOPA has applied as a baseline scenario, the

effect of the application of the Directive requirements and the relevant implementing measures:

Article 27 IDD, provides:

"Without prejudice to Article 17, an insurance intermediary or an insurance undertaking carrying on the distribution of insurance-based investment products shall maintain and operate effective organisational and administrative arrangements with a view to taking all reasonable steps designed to prevent conflicts of interest as determined under Article 28 from adversely affecting the interests of its customers. Those arrangements shall be proportionate to the activities performed, the insurance products sold and the type of the distributor".

Article 28, IDD provides:

"1. Member States shall ensure that insurance intermediaries and insurance undertakings take all appropriate steps to identify conflicts of interest between themselves, including their managers and employees, or any person directly or indirectly linked to them by control, and their customers or between one customer and another, that arise in the course of carrying out any insurance distribution activities.

2. Where organisational or administrative arrangements made by the insurance intermediary or insurance undertaking in accordance with Article 27 to manage conflicts of interest are not sufficient to ensure, with reasonable confidence, that risks of damage to customer interests will be prevented, the insurance intermediary or insurance undertaking shall clearly disclose to the customer the general nature or sources of the conflicts of interest, in good time before the conclusion of an insurance contract.

3. By way of derogation from Article 23(1), the disclosure referred to in paragraph 2 of this Article shall:

(a) be made on a durable medium; and

(b) include sufficient detail, taking into account the nature of the customer, to enable that customer to take an informed decision with respect to the insurance distribution activities in the context of which the conflict of interest arises.

4. The Commission shall be empowered to adopt delegated acts in accordance with Article 38 in order to:

(a) define the steps that insurance intermediaries and insurance undertakings might reasonably be expected to take to identify, prevent, manage and disclose conflicts of interest when carrying out insurance distribution activities;

(b) establish appropriate criteria for determining the types of conflict of interest whose existence may damage the interests of the customers or potential customers of the insurance intermediary or insurance undertaking".

Section 3 - Objectives pursued

The empowerment of the Commission to adopt delegated acts to specify the organisational measures insurance undertakings and insurance intermediaries should take in order to identify and manage conflicts of interests was introduced in the IDD which provided for general rules of conducts in relation to insurance-based investment products.

The Recitals of the IDD indicate that the objectives of the legislator are to deliver consistent protection for retail customers and to ensure a level playing field between similar products. Against this background, the objectives of the Technical Advice are:

- to enhance consumer protection through provisions addressing conflicts of interest arising in the context of the distribution of insurance-based investment products and potentially creating the risk of consumer detriment.
- to encourage consistent application of the organisational measures insurance undertakings and insurance intermediaries should take to manage conflicts of interest that arise in the course of carrying out distribution activities in insurance-based investment products;
- to foster a level playing field regarding the distribution of financial products, which compete with each other and are substitutable from a consumer point of view;

Consistency of the objectives with other EU policies

The identified objectives are coherent with the EU's fundamental goals of promoting the harmonious and sustainable development of economic activities, a high degree of competitiveness, and a high level of consumer protection, which includes the safety and economic interests of citizens (Article 169 TFEU). These objectives are also consistent with the reform programme proposed by the European Commission in its Communication, *Driving European Recovery*, the 'Europe 2020 strategy' for smart, sustainable and inclusive growth, MiFID II and the PRIIPs KID Regulation.

Consistency of the objectives with fundamental rights

The legislative measures setting out conduct of business rules for all sellers of insurance products, including sanctions, will be in compliance with relevant fundamental rights and particular attention will be given to the necessity and proportionality of the legislative measures. The following fundamental rights of the Charter of Fundamental Rights of the European Union are of particular relevance: freedom to conduct a business (Art. 16) and consumer protection (Art. 38).

Limitations on these rights and freedoms are allowed under the Charter. The objectives as defined above are consistent with the EU's obligations to respect fundamental rights. However, any limitation on the exercise of these rights and freedoms must be provided for by the law and respect the essence of these rights and freedoms. Subject to the principle of proportionality, limitations may be made only if they are necessary and genuinely meet the objectives of general interest recognised by the Union or the need to protect the rights and freedoms of others.

Section 4 - Policy Options

The policy considerations were essentially governed by the Commission's request to build on the organisational requirements to be found in the Implementing Directive of MiFID (2006/73/EC) and achieve as much coherence and consistency as possible between the Technical Advice EIOPA is supposed to provide to the Commission and the regulatory framework under Articles 33-35 of the draft Delegated Regulation under MiFID II.

In order to meet these predefined specifications, EIOPA's analysis focused on the question whether the requirements of the draft Delegated Regulation under MiFID II, could be transferred and if so, to which extent modifications would be necessary to meet the specificities of the insurance sector.

For the Technical Advice on the possible content of the delegated acts EIOPA has considered the Policy Options outlined below. The delegated acts the Commission is empowered to adopt pursuant to Article 28(4), IDD shall:

- define the steps that insurance intermediaries or insurance undertakings might reasonably be expected to take to identify, prevent, manage and disclose conflicts of interest when carrying out insurance distributions activities; and
- establish appropriate criteria for determining the types of conflict of interest whose existence may damage the interests of the customers or potential customers of the insurance intermediary or insurance undertaking.

Policy Issue 1: With regard to the Commission's request to establish appropriate criteria for the identification of conflicts of interest EIOPA has considered the following options:

- **Policy Option 1:** To implement Article 33 of the MiFID II Delegated Regulation defining the criteria regulated entities are required to apply for the identification of conflicts of interests.

Article 33 of the draft Delegated Regulation under MiFID II reads as follows:

"For the purposes of identifying the types of conflict of interest that arise in the course of providing investment and ancillary services or a combination thereof and whose existence may damage the interests of a client, investment firms shall take into account, by way of minimum criteria, whether the investment firm or a relevant person, or a person directly or indirectly linked by control to the firm, is in any of the following situations, whether as a result of providing investment or ancillary services or investment activities or otherwise:

(a) the firm or that person is likely to make a financial gain, or avoid a financial loss, at the expense of the client;

(b) the firm or that person has an interest in the outcome of a service provided to the client or of a transaction carried out on behalf of the client, which is distinct from the client's interest in that outcome;

(c) the firm or that person has a financial or other incentive to favour the interest of another client or group of clients over the interests of the client;

(d) the firm or that person carries on the same business as the client;

(e) the firm or that person receives or will receive from a person other than the

client an inducement in relation to a service provided to the client, in the form of monetary or non-monetary benefits or services”.

- **Policy Option 2:** To modify Article 33 of the MiFID II Delegated Regulation in order to mirror two additional instances where EIOPA believes that conflicts of interest may arise (see amendments in letter (c) and letter (d)).

This Policy Option reads as follows:

"For the purpose of identifying the types of conflict of interest that arise in the course of carrying out any insurance distribution activities and which entail the risk of damage to the interests of a customer, insurance intermediaries and insurance undertakings shall assess whether they, including their managers, employees or any person directly or indirectly linked to them by control, have an interest related to the insurance distribution activities which is distinct from the customer's interest and which has the potential to influence the outcome of the services at the detriment of the customer. Insurance intermediaries and undertakings shall also identify conflicts of interest between one customer and another.

Conflicts of interest referred to above shall at least be assumed in situations including the following:

- a. the insurance intermediary, insurance undertaking or linked person is likely to make a financial gain, or avoid a financial loss, at the expense of the customer;*
- b. the insurance intermediary, insurance undertaking or linked person has a financial or other incentive to favour the interest of another customer or group of customers over the interests of the customer;*
- c. the insurance intermediary, insurance undertaking or linked person receives or will receive from a person other than the customer a monetary or non-monetary benefit in relation to the insurance distribution activities provided to the customer.*
- d. the insurance intermediary, persons working in an insurance undertaking responsible for the distribution of insurance-based investment products or linked person are involved in the management or development of the insurance-based investment products."*

Policy Issue 2: With regard to the Commission's request to define steps insurance undertakings and insurance intermediaries should take to manage conflicts of interest.

With regard to Commission's request to specify the organisational measures insurance undertakings and insurance intermediaries should take in order to manage conflicts of interest EIOPA has considered the following options:

- **Policy Option 1:** To introduce the general principle of Article 34 of the MiFID II Delegated Regulation, obliging insurance undertakings and insurance intermediaries to establish an effective conflicts of interest policy in writing in order to ensure that the relevant activities are provided at an appropriate level of

independence without specifying concrete organisational measures undertakings should consider for that purpose.

- **Policy Option 2:** To implement Article 34 of the MiFID II Delegated Regulation specifying the organisational measures and procedures, insurance undertakings and insurance intermediaries should take to manage conflicts of interest.

Article 34 of the MiFID II Delegated Regulation reads as follows (wording would have to be aligned to the insurance vocabulary, e.g. "client" would be replaced by "customer"):

"1. Investment firms shall establish, implement and maintain an effective conflicts of interest policy set out in writing and appropriate to the size and organisation of the firm and the nature, scale and complexity of its business.

Where the firm is a member of a group, the policy must also take into account any circumstances, of which the firm is or should be aware, which may give rise to a conflict of interest arising as a result of the structure and business activities of other members of the group.

2. The conflicts of interest policy established in accordance with paragraph 1 shall include the following content:

(a) it must identify, with reference to the specific investment services and activities and ancillary services carried out by or on behalf of the investment firm, the circumstances which constitute or may give rise to a conflict of interest entailing a material risk of damage to the interests of one or more clients;

(b) it must specify procedures to be followed and measures to be adopted in order to manage such conflicts.

3. The procedures and measures referred to in paragraph 2(b) are designed to ensure that relevant persons engaged in different business activities involving a conflict of interest of the kind specified in paragraph 2(a) carry on those activities at a level of independence appropriate to the size and activities of the investment firm and of the group to which it belongs, and to the risk of damage to the interests of clients.

For the purposes of paragraph 2(b), the procedures to be followed and measures to be adopted shall include such of the following as are necessary and appropriate for the firm to ensure the requisite degree of independence:

(a) effective procedures to prevent or control the exchange of information between relevant persons engaged in activities involving a risk of a conflict of interest where the exchange of that information may harm the interests of one or more clients;

(b) the separate supervision of relevant persons whose principal functions involve carrying out activities on behalf of, or providing services to, clients whose interests may conflict, or who otherwise represent different interests that may conflict, including those of the firm;

(c) the removal of any direct link between the remuneration of relevant persons principally engaged in one activity and the remuneration of, or revenues generated by, different relevant persons principally engaged in another activity, where a conflict of interest may arise in relation to those

activities;

(d) measures to prevent or limit any person from exercising inappropriate influence over the way in which a relevant person carries out investment or ancillary services or activities;

(e) measures to prevent or control the simultaneous or sequential involvement of a relevant person in separate investment or ancillary services or activities where such involvement may impair the proper management of conflicts of interest.

4. Investment firms shall ensure that disclosure to clients, pursuant to Article 23(2) of Directive 2014/65/EU, is a measure of last resort that shall be used only where the effective organisational and administrative arrangements established by the investment firm to prevent or manage its conflicts of interest in accordance with Article 23 of Directive 2014/65/EU are not sufficient to ensure, with reasonable confidence, that risks of damage to the interests of the client will be prevented.

The disclosure shall clearly state that the organisational and administrative arrangements established by the investment firm to prevent or manage that conflict are not sufficient to ensure, with reasonable confidence, that the risks of damage to the interests of the client will be prevented. The disclosure shall include specific description of the conflicts of interest that arise in the provision of investment and/or ancillary services, taking into account the nature of the client to whom the disclosure is being made. The description shall explain the general nature and sources of conflicts of interest, as well as the risks to the client that arise as a result of the conflicts of interest and the steps undertaken to mitigate these risks, in sufficient detail to enable that client to take an informed decision with respect to the investment or ancillary service in the context of which the conflicts of interest arise.

5. Investment firms shall assess and periodically review, on an at least annual basis, the conflicts of interest policy established in accordance with paragraphs 1 to 4 and shall take all appropriate measures to address any deficiencies. Over-reliance on disclosure of conflicts of interest shall be considered a deficiency in the investment firm's conflicts of interest policy.

- **Policy Option 3:** To modify Article 22 of the MiFID Implementing Directive in order to allow insurance undertakings and insurance intermediaries to demonstrate that alternative measures and procedures are appropriate to ensure that the distribution activities are carried out in accordance with the best interest of the customers and are not biased by conflicting interests.

This Policy Option reads as follows:

"1. Insurance intermediaries and insurance undertakings shall establish, implement and maintain an effective conflicts of interest policy set out in writing and appropriate to their size and organisation and the nature, scale and complexity of their business. Where the insurance intermediaries or insurance undertaking is a member of a group, the policy must also take into account any circumstances, of which the insurance intermediary or insurance undertaking is or should be aware, which may give rise to a conflict of interest arising as a result of the structure and business activities of other members of the group.

2. *The conflicts of interest policy established in accordance with paragraph 1 shall include the following content:*

(a) it must identify, with reference to the specific insurance distribution activities carried out, the circumstances which constitute or may give rise to a conflict of interest entailing a risk of damage to the interests of one or more customers;

(b) it must specify procedures to be followed and measures to be adopted in order to manage and prevent such conflicts from damaging the interests of the customer of the insurance intermediary or insurance undertaking, appropriate to the size and activities of the insurance intermediaries or insurance undertaking and of the group to which they belong, and to the risk of damage to the interests of customers.

3. *For the purpose of paragraph 2(b), the procedures to be followed and measures to be adopted shall include, where appropriate, in order to ensure that the distribution activities are carried out in accordance with the best interest of the customers and are not biased by conflicting interests of the insurance undertaking, the insurance intermediaries or another customer, the following:*

(a) effective procedures to prevent or control the exchange of information between relevant persons engaged in activities involving a risk of a conflict of interest where the exchange of that information may damage the interests of one or more customers;

(b) the separate supervision of relevant persons whose principal functions involve carrying out activities on behalf of, or providing services to, customers whose interests may conflict, or who otherwise represent different interests that may conflict, including those of the insurance intermediary or insurance undertaking;

(c) the removal of any direct link between the remuneration of relevant persons principally engaged in one activity and the remuneration of, or revenues generated by, different relevant persons principally engaged in another activity, where a conflict of interest may arise in relation to those activities;

(d) measures to prevent or limit any person from exercising inappropriate influence over the way in which a relevant person carries out insurance distribution activities;

(e) measures to prevent or control the simultaneous or sequential involvement of a relevant person in insurance distribution activities where such involvement may impair the proper management of conflicts of interest.

If insurance intermediaries and insurance undertakings demonstrate that those measures and procedures are not appropriate to ensure that the distribution activities are carried out in accordance with the best interest of the customers and are not biased by conflicting interests of the insurance undertaking, the insurance intermediaries or another customer, insurance intermediaries and insurance undertakings must adopt adequate alternative measures and procedures for that purpose.

4. *Insurance intermediaries and insurance undertaking shall avoid over reliance on disclosure and shall ensure that disclosure, pursuant to Article 28 (2), IDD, is a step of last resort that can be used only where the effective organisational and*

administrative measures established by insurance intermediaries and insurance undertakings to prevent or manage conflicts of interests in accordance with Article 27, IDD are not sufficient to ensure, with reasonable confidence, that the risks of damage to the interests of the customer will be prevented.

5. Insurance intermediaries and insurance undertaking shall make that disclosure to customers, pursuant to Article 28(2), IDD, in a durable medium. The disclosure shall:

(a) include a specific description of the conflict of interest, including the general nature and sources of the conflict of interest, as well as the risks to the customer that arise as a result of the conflict and the steps undertaken to mitigate these risks,

(b) to clearly state that the organisational and administrative arrangements established by the insurance intermediary or insurance undertaking are not sufficient to ensure, with reasonable confidence, that the risks of damage to the interests to the customers will be prevented,

in order to enable the customer to take an informed decision with respect to the insurance distribution activities in the context of which the conflict of interest arises.

6. Insurance intermediaries and insurance undertakings shall:

(a) assess and periodically review – at least annually – the conflicts of interest policy established in accordance with this article and to take all appropriate measures to address any deficiencies,

(b) keep and regularly update a record of the situations in which a conflict of interest entailing a risk of damage to the interests of the one or more customers has arisen or, in the case of an ongoing service or activity, may arise.

Where established, senior management shall receive on a frequent basis, and at least annually, written reports on these situations”.

Section 5 - Analysis of impacts

As the Policy Options with regard to the Policy Issue 1 and Policy Issue 2 are closely linked and complementary to each other, it is appropriate and necessary to analyse their impacts all together. This is supported by the fact that the respective Policy Options differ only slightly and the following analysis focus on the qualitative aspects, only.

Benefits

For insurance undertakings and insurance intermediaries, the Policy Options with regard to Policy Issues 1 and 2 as could provide the following benefits:

- Prevention of customer detriment and legal actions: The Policy Proposal will lower the risk of consumer detriment resulting from an improper management of conflict of interests and consequently lower the risk that costumers take legal action because of damages suffered.
- Increased customer confidence and decreased reputational risks: As outlined, the Policy Proposal will lower the risk of consumer detriment which simultaneously increase the customers' confidence and decrease reputational risks.
- Enhanced corporate governance: The policy proposal will enhance corporate governance mechanisms by which insurance undertakings and insurance intermediaries are supervised and directed.
- Prevention of regulatory arbitrage: Harmonised rules ensure equal treatment of entities located in different Member States (regulatory arbitrage with regards of entities of different origin) as well as alike treatment of entities distributing products different with regard to legal nature and regulation (cross sectorial regulatory arbitrage).

For customers, the Policy Options with regard to Policy Issues 1 and 2 could provide the following benefits:

- Enhanced consumer protection: The Policy Proposal aims to ensure that insurance undertakings and insurance intermediaries provide their services in the best interest of their customers and conflicts of interest are not improperly resolved, to the detriment of the customer.
- Counterbalance to the customer's paucity of information: The Policy Proposal aims to counterbalance the customer's paucity of information since customers do not generally have the full picture of the extent to which insurance undertakings and insurance intermediaries are facing conflicts of interest.

For NCAs, the Policy Options with regard to Policy Issues 1 and 2 could provide the following benefits:

- Enhanced legal certainty: Implementing measures facilitate the application and understanding of Level 1 – requirements

Costs

For insurance undertakings and insurance intermediaries, the Policy Options with regard to Policy Issues 1 and 2 could involve the following costs:

- One-off costs as insurance undertakings and insurance intermediaries are required to take organisational and procedural measures for implementation (e.g. costs associated with project management and/or engagement with external consultants, the identification of conflicts of interest, the development or revision of conflicts of interest policies, the introduction of new IT systems, staff training).
- Ongoing costs as insurance undertakings and insurance intermediaries are required to periodically review and adapt their organisational measures and procedures, if necessary (including the periodic identification of conflicts of interest and revision of conflicts of interest policies, if necessary).

For customers, the Policy Options with regard to Policy Issues 1 and 2 as could involve the following costs:

- Additional costs insurance undertakings and insurance intermediaries have to bear in order to implement the new regulatory requirements may be transferred to the customers rendering services and products more expensive.

For NCAs, the Policy Options with regard to Policy Issues 1 and 2 as could involve the following costs:

- The need to supervise and enforce new rules.

Section 6 - Comparison of options

- **Policy issue 1:**

With regard to **Option 1** and **Option 2** EIOPA considers it generally appropriate to make recourse to Article 21 of the MiFID Implementing Directive and to transfer its principles in order to define appropriate criteria for the identification of conflicts of interest that may arise in the course of carrying out insurance distribution activities.

Even though the wording in Article 21 of the MiFID Implementing Directive addresses investment firms only, EIOPA notes that the instances circumscribed in the provision are of a broad and abstract nature, such that they, in principle, can be applied very broadly across the different sectors of the financial services. The instances rather describe situations where conflicts of interest commonly arise when a commercial activity is pursued and the interests of customers are at stake. The interest to make a financial gain at the expense of the customers is a good example. Consequently, EIOPA considers that the principles as laid down in Article 21 (a) – (e) MiFID Implementing Directive are also relevant for insurance intermediaries and insurance undertakings in the course of carrying out insurance distribution activities.

Nevertheless, EIOPA is of the opinion that Article 21 should be modified in order to address the following issues.

Firstly, a general circumscription of conflict of interest should be introduced to facilitate the understanding and application of the provision. This clarifies that the specific instances listed in letter (a) - (d) are only of exemplary nature and insurance undertakings and insurance intermediaries should focus on the general question whether they pursue interests which are distinct from the customers'

interests and which have the potential to influence the services rendered at the detriment of the customer.

Secondly, it should be clarified that conflicts of interest may also arise if the distributors are involved in the development or management of products. For example, conflicts of interest arise where an intermediary exercises influence over how distribution costs that benefit the intermediary are embedded in the design of a product or where an intermediary is rewarded with a percentage of the management costs.

Thirdly, it should be clarified that conflicts of interest arise whenever the insurance intermediary receives a commission or fee paid by a third party, independent from the question whether the commission or fee corresponds with the market standard or not. This follows from the intermediary's own interest to make a financial gain when providing services to the customers.

Against this background, **Option 2** seems to offer the preferable solution from EIOPA's point of view.

The aligned wording reads as follows:

"For the purpose of identifying the types of conflict of interest that arise in the course of carrying out any insurance distribution activities and which entail the risk of damage to the interests of a customer, insurance intermediaries and insurance undertakings should assess whether they, including their managers, employees and tied insurance intermediaries, or any person directly or indirectly linked to them by control, have an interest related to the insurance distribution activities which is distinct from the customer's interest and which has the potential to influence the outcome of the services at the detriment of the customer.

This shall at least be assumed in situations including the following:

a. the insurance intermediary, insurance undertaking or linked person is likely to make a financial gain, or avoid a financial loss, at the expense of the customer;

b. the insurance intermediary, insurance undertaking or linked person has a financial or other incentive to favour the interest of another customer or group of customers over the interests of the customer;

c. the insurance intermediary, insurance undertaking or linked person receives or will receive from a person other than the customer a monetary or non-monetary benefit in relation to the insurance distribution activities provided to the customer.

d. the insurance intermediary, persons working in an insurance undertaking responsible for the distribution of insurance-based investment products or linked person are involved in the management or development of the insurance-based investment products."

- **Policy Issue 2:**

Option 1 would offer insurance undertakings and insurance intermediaries a broad discretion and flexibility how to implement the organisational requirements. In addition to that, **Option 2** would require the entities to consider whether a

catalogue of proposed measures [see Article 22 (3) of the MiFID Implementing Directive] is necessary and appropriate in order to manage conflicts of interest properly and ensure the prerequisite independence. EIOPA believes that the measures of Article 22 (3) do not only apply for investment firms, but have also a particular relevance to manage conflicts of interest arising in the context of the insurance distribution activities; for example "measures to prevent or limit any person from exercising inappropriate influence over the way in which a relevant person carries ... services or activities" may play a role in the relationship between a sales manager and employees advising customers with regard to insurance-based investment products.

If the entities come to the conclusion and can demonstrate that the proposed measures and procedures are not appropriate, the entities are entitled, under **Option 3**, to adopt alternative measures to ensure that the services provided are not biased by conflicting interests of those entities. **From EIOPA's perspective Option 3 therefore offers the most appropriate solution.**

1. Inducements

1. Procedural issues and consultation of interested parties

This Impact Assessment relates to the Technical Advice on inducements only. Advice relating to the other delegated acts requested by the Commission are covered in separate sections.

Scope of the technical advice (and impact assessment)

The scope the inducements delegated act is set out in Article 29(4) and (5):

4. Without prejudice to paragraph 3 of this Article, the Commission shall be empowered to adopt delegated acts in accordance with Article 28 to specify:

a) the criteria for assessing whether inducements paid or received by an insurance intermediary or an insurance undertaking have a detrimental impact on the quality of the relevant service to the customer

b) the criteria for assessing compliance of insurance intermediaries and insurance undertakings paying or receiving inducements with the obligation to act honestly, fairly and professionally in accordance with the best interests of the customers.

5. The delegated acts referred to in paragraph 4 shall take into account

a) the nature of the services offered or provided to the customer or potential customer, taking into account the type, object, size and frequency of the transactions;

b) the nature of the products being offered or considered, including different types of insurance-based investment products.

The scope of the technical advice is narrowed further in the Commission's mandate.

EIOPA is invited to provide technical advice on:

- The conditions under which payments and non-monetary benefits paid or received by insurance intermediaries or insurance undertakings in connection with the distribution of an insurance-based investment product may have a detrimental impact on the quality of the relevant service to the customer;*
- The circumstances and situations to take into account when determining whether an insurance distributor or an insurance undertaking paying or receiving inducements.*

2. Problem definition

The IDD introduces new requirements in relation to insurance-based investment products. These requirements are additional to those applying to all insurance products within scope of the IDD. Chapter VI of the IDD sets out the additional requirements, covering conflicts of interest, costs and charges, inducements, suitability, appropriateness and reporting to customers.

The IDD requirement to which this technical advice on inducements relates is covered in Article 29(2). It obliges Member States to ensure that insurance intermediaries and undertakings are meeting their obligations under the IDD where they pay or receive any fee, commission, or other non-monetary benefit, in connection with the distribution of an insurance-based investment product or ancillary service. Article 29(2) introduces a test that the payment or benefit must: a) not have a detrimental

impact on the quality of the relevant service to the customer; and b) not impair compliance with the insurance intermediary's or insurance undertaking's duty to act honestly, fairly and professionally in accordance with the best interests of its customers.

In the impact assessment accompanying the draft proposal to amend the Insurance Mediation Directive (IMD) in 2012, the Commission found that general problems with insurance products were more pronounced in the case of insurance-based investment products due to their complexity. One area identified as a heightened risk was conflicts of interest stemming from remuneration structures.

The Commission went on to state that consumer protection standards for the sales of these products were not sufficient at EU level, as these products were sold under the general IMD rules for the sales of insurance even though insurance-based investment products are very different in nature and generally represent higher risks for retail consumers.⁴¹

The disparity between consumer protection standards under IMD and those under MiFID was considered a deficiency. While some Member States had sought to address the disparity by introducing stricter rules for these products, the vast majority (21 out of 27 Member States) had left the area unregulated. This meant that consumers in different Member States were not protected to the same extent, and there is an uneven playing field between Member States and within Member States in respect of sellers of insurance with investments and those only selling investment products.⁴²

The particular issue with inducements is their potential to influence the distributor's product offer or advice. As stated by the Commission, consumer harm can arise in two slightly different ways: either through a lock-in of intermediaries into quasi-exclusive dealing arrangements with a single upstream insurance company (whereby consumers turning to the intermediary will not have sufficient choice to best satisfy their needs), or through biased advice to the consumer.

On the demand-side, inducement bias can lead to customers purchasing products they do not need or want. This in turn can result in unnecessary costs, dissatisfaction and distrust of the industry. Given that insurance-based investment products are purchased for the purpose of building up savings, the impact of mis-purchasing can be significant, either through the customer taking on too much (or little) risk, with potential thereby for loss of savings, or through the customer being exposed to poor performance and high costs, also with a negative impact on savings.

It can also negatively impact the supply-side of the market. Biased advice or offerings may mean that providers' with higher quality and lower cost products may not be receiving the returns expected because other similar products have higher inducements being made. These inducements can therefore have an impact on competition between providers. Also, where customers are dissatisfied or distrustful, this can lead to more costs due to complaints and lower sales.

The Commission's mandate sets out the parameters for the technical advice, and therefore the scope of the policy options considered. The mandate requests advice on measures specifying the rules on fees, commissions or non-monetary benefits in connection with the distribution of insurance-based investment products laid down in Article 29(2) of the Directive:

⁴¹ Commission Staff Working Document Impact Assessment: Accompanying the document Proposal for a Directive of the European Parliament and of the Council on Insurance Mediation (SWD/2012/0191 final), *Section 3.2 Problems relating to Packaged Retail Investment Products (PRIIPs)*.

⁴² IBID, *Section 3.1.2 Conflicts of interest*

- The criteria for assessing whether inducements paid or received by an insurance intermediary or an insurance undertaking have a detrimental impact on the quality of the relevant service to the customer
- The criteria for assessing compliance of insurance intermediaries and insurance undertakings paying or receiving inducements with the obligation to act honestly, fairly and professionally in accordance with the best interests of the customer.

The Commission further sets out matters that the measures should take into account as well as a guide to the approach (for example, that the technical advice should build on the results of previous work carried out by EIOPA and ESMA).

3. Baseline

When analysing the impact from proposed policies, the impact assessment methodology uses a baseline scenario as the basis for comparing policy options. This helps to identify the incremental impact of each policy option considered. The aim of the baseline scenario is to explain how the current situation would evolve without additional regulatory intervention.

For the analysis of the potential related costs and benefits of the proposed Technical Advice on Inducements, the baseline is the current situation of the market composed of the content of the IDD and in particular Article 29(2).⁴³ This sets out the principle that inducements are only allowed where they do not have a detrimental impact on the quality of the relevant service to the customer and do not impair compliance with the insurance intermediary's or insurance undertaking's duty to act honestly, fairly and professionally in accordance with the best interests of its customers.

Under this baseline there would be no further clarification or harmonisation of the conditions under which insurance undertakings or intermediaries would be able consider that they have fulfilled these principles. Different firms would likely arrive at different conclusions, while differences in approach could well emerge between different national markets. This heterogeneity would likely mean customers would face different degrees of protection, and could drive regulatory arbitrage, to the detriment of certain firms and customers.

4. Objectives pursued

There are two recitals in the IDD that provide more specific guidance about the objectives to be pursued in this advice:

- Recital 56, IDD: *"Insurance-based investment products are often made available to customers as potential alternatives or substitutes to investment products subject to Directive 2014/65/EU (MiFID II). To deliver consistent investor protection and avoid the risk of regulatory arbitrage, it is important that insurance-based investment products are subject, in addition to the conduct of business standards defined for all insurance products, to specific standards aimed at addressing the investment element embedded in those products. Such specific standards should include provision of appropriate information, requirements for advice to be suitable and restrictions on remuneration"*.
- Recital 57: *"In order to ensure that any fee or commission or any non-monetary benefit in connection with the distribution of an insurance-based*

⁴³ The key provision is Article 29 of the Directive, however this article should be read as part of the whole.

investment product paid to or by any party, except the customer or a person on behalf of the customer, does not have a detrimental impact on the quality of the relevant service to the customer, the insurance distributor should put in place appropriate and proportionate arrangements in order to avoid such detrimental impact. To that end, the insurance distributor should develop, adopt and regularly review policies and procedures relating to conflicts of interest with the aim of avoiding any detrimental impact on the quality of the relevant service to the customer and of ensuring that the customer is adequately informed about fees, commissions or benefits”.

Taking account the Commission’s mandate, the objectives of the technical advice are to:

- Enhance consumer protection and foster a level playing field by having a consistent approach to the identification and assessment of inducements at risk of having a detrimental impact on the quality of service provided to the customer, as well as those practices which may mitigate the risks associated with an inducement.
- Encourage consistent application of organisational measures that insurance undertakings and intermediaries should have in place to ensure that inducements do not lead to a detrimental impact on the service provided to the customer or prevent the intermediary or undertaking with acting honestly, fairly and in the best interests of their customers.
- Improve market dynamics, by supporting a consistency of approach (where possible) between insurance-based investment products and products within scope of MiFID II. This should reduce risks associated with regulatory arbitrage, but also support businesses who are competing with substitutable or similar products.

Policy Issue 1 - Inducements at risk of causing a detrimental impact: high-level principle

The IDD sets out the overarching requirement that determines whether an inducement can be paid, but it is silent on when an inducement will have a detrimental impact. The Commission has requested that EIOPA provide advice on the conditions under which inducements in connection with the distribution of insurance-based investment products may have a detrimental impact on the quality of the relevant service to the customer.

Policy options

EIOPA has considered the following options to address this issue:

- Policy option 1: do not introduce a high-level principle
- Policy option 2: introduce the criterion of quality enhancement similar to Article 29 (2) of MiFID II and further specified in the Commission's proposal for a delegated Directive under MiFID II requiring that an additional or higher level of service to the client is provided, that the inducement does not directly benefit the recipient firm, and that an on-going benefit is provided to the client.
- Policy option 3: introduce a bespoke high-level principle based upon Article 17 IDD, while promoting compatibility with the approach under MiFID II.

This option would read as follows:

"Detrimental impact occurs when an inducement or structure of an inducement scheme provides an incentive to carry out the insurance distribution activities in a way which is not in accordance with the best interest of the customer".

Analysis of policy options

Policy option 1 – do not introduce a high-level principle

Benefits

- For customers: no specific benefits identified
- For industry: no specific benefits identified
- For NCAs: wide discretion on how to interpret and apply in practice the abstract term "detrimental impact" enabling to take into account specificities of national markets and existing business models

Costs

- For customers: Different level of customer protection across the Member States as a result of the development of diverging understanding of detrimental impact
- For industry: No L2 guidance on the understanding of detrimental impact would cause legal uncertainty for market participants leading to additional costs to comply with the new requirements; bespoke diverging understanding of detrimental impact will also have negative impact on cross-border distribution of insurance-based investment products as insurance undertakings and insurance intermediaries will be confronted with different national understanding of detrimental impact
- For NCAs: need to develop a national understanding of detrimental impact to provide guidance to participants of the respective national markets

Policy option 2 – introduce the criterion of quality enhancement

Benefits

- For customers: Increased customer protection and quality of service as inducements would be beneficiary and serve the customers' interests; equivalent level of customer protection, not only across Member States, but also from a cross-sectoral perspective.
- For industry: Legal certainty about the understanding of detrimental impact would reduce advisory/compliance costs for implementation; level playing field across Member States and different financial sectors; in the long run increased confidence and trust of customers in the services provided.
- For NCAs: No need to develop national understanding of detrimental impact; provides support and guidance for consistent application and implementation in national law.

Costs

- For customers: Extensive understanding of detrimental impact may have negative consequences for existing business models leading to a reduced competition and choice of products/providers/services in the market
- For industry: Extensive understanding of detrimental impact may have negative consequences for existing business models (lower revenues), in particular those which are entirely financed by commissions; some entities might be required to change the structure of their income; training costs for employees.
- For NCAs: Costs for supervision and enforcement. Training costs for employees.

Policy Option 3 – introduce a high-level principle based upon Article 17 IDD

Benefits

- For consumers: Increased customer protection as the risk of conflicts of interest arising from inducements is addressed; equivalent level of customer protection across the Member States providing a level playing field, whereas not identical, but compatible with policy requirements developed under MiFID II.
- For industry: Legal certainty about the understanding of detrimental impact would reduce advisory/compliance costs for implementation; level playing field across Member States; in the long run increased confidence and trust of customers in the services provided.
- For NCAs: No need to develop national understanding of detrimental impact; provides support and guidance for consistent application and implementation in national law.

Costs:

- For customers: Negative consequences on competition and choice of products/providers/services as outlined under Policy Option 2 less relevant, even though not to be excluded from the outset.
- For industry: Even though less relevant, impact on existing business models (lower revenues) cannot be excluded as some common inducements might be considered as having a detrimental impact; training costs for employees.
- For NCAs: Costs for supervision and enforcement. Training costs for employees.

Policy Issue 2 - Inducements at risk of causing a detrimental impact: high risk inducements

The Commission has requested for EIOPA to indicate examples of circumstances where an inducement may generally be regarded as having a detrimental effect on the quality of the relevant service to the customer.

Policy options

EIOPA has considered the following options to address this issue:

- Policy option 1: do not identify inducements that are considered to be high risk of having a detrimental impact.
- Policy option 2: apply the rationale which underlies the Commission's proposal for a delegated Directive for MiFID II and defines the circumstances where inducements (do not) enhance the quality of the relevant service.

The relevant part of the Commission proposal can be found in Article 11(2) of the proposed delegated Directive stating:⁴⁴

A fee, commission or non-monetary benefit shall be considered to be designed to enhance the quality of the relevant service to the client if all of the following conditions are met:

(a) it is justified by the provision of an additional or higher level service to the relevant client, proportional to the level of inducements received, such as:

(i) the provision of non-independent investment advice on and access to a wide range of suitable financial instruments including an appropriate number of instruments from third party product providers having no close links with the investment firm;

(ii) the provision of non-independent investment advice combined with either: an offer to the client, at least on an annual basis, to assess the continuing suitability of the financial instruments in which the client has invested; or with another on-going service that is likely to be of value to the client such as advice about the suggested optimal asset allocation of the client; or

(iii) the provision of access, at a competitive price, to a wide range of financial instruments that are likely to meet the needs of the client, including an appropriate number of instruments from third party product providers having no close links with the investment firm, together with either the provision of added-value tools, such as objective information tools helping the relevant client to take investment decisions or enabling the relevant client to monitor, model and adjust the range of financial instruments in which they have invested, or providing periodic reports of the performance and costs and charges associated with the financial instruments

(b) it does not directly benefit the recipient firm, its shareholders or employees without tangible benefit to the relevant client;

(c) it is justified by the provision of an on-going benefit to the relevant client in relation to an on-going inducement.

A fee, commission, or non-monetary benefit shall not be considered acceptable if the provision of relevant services to the client is biased or distorted as a result of the fee, commission or non-monetary benefit.

⁴⁴ http://ec.europa.eu/finance/securities/docs/isd/mifid/160407-delegated-directive_en.pdf

- Policy option 3: to develop a distinctive list of inducements which are considered to have a high risk of leading to a detrimental impact on the quality of the relevant service to the customer.

This option would read as follows:

The following types of inducements are considered to have a high risk of leading to a detrimental impact on the quality of the relevant service to the customer:

- a) the inducement encourages the insurance intermediary or insurance undertaking to offer or recommend a product or service to a customer when from the outset a different product or service exists which would better meet the customer's needs;*
- b) the inducement is solely or predominantly based on quantitative commercial criteria and does not take into account appropriate qualitative criteria, reflecting compliance with the applicable regulations, fair treatment of customers and the quality of services provided to customers;*
- c) the value of the inducement is disproportionate or excessive when considered against the value of the product and the services provided in relation to the product;*
- d) the inducement is entirely or mainly paid when the product is first sold;*
- e) the inducement scheme does not provide for the refunding of any inducements deducted from the customer's initial investment to the customer if the product lapses or is surrendered at an early stage;*
- f) if the inducement scheme entails any form of variable or contingent threshold or any other kind of value accelerator which is unlocked by attaining a sales target based on volume or value of sales.*

Analysis of Policy Options

Policy option 1 – do not identify inducements that are considered to be high risk of having a detrimental impact

Benefits

- For customers: no specific benefits identified
- For industry: no specific benefits identified
- For NCAs: wide discretion on how to interpret and apply in practice the high-level principle enabling them to take into account specificities of national markets and existing business models

Costs

- For customers: less consistent application of the high-level principle will lead to a diverging level of customer protection across the Member States. This may lead to a situation where some Member States develop a very strict and rigid understanding of detrimental impact, whereas other Member States follow a more flexible and less severe approach.

- For industry: No guidance on the high-level principle. Differences in national regulation will hamper the cross-border distribution of insurance products and contravene the principle of a level playing field across Europe.
- For NCAs: No guidance on the high-level principle and the need to develop a proper understanding on national level.

Policy Option 2 - apply the rationale which underlies the Commission's proposal for a delegated Directive for MiFID II

Benefits

- For customers: As inducements are supposed to provide an additional or higher level of service to the customer, inducements directly benefit the customer.
- For industry: Increased confidence and trust of customers in the services provided which will be beneficiary for the industry in the long run.
- For NCAs: Detailed guidance on the legitimacy of inducements provides legal certainty and supports NCA's in their implementation and supervision.

Costs

- For customers: Possible negative consequences for existing business models, in particular those which mainly rely on commissions to finance their business models as well as small intermediaries, leading to a reduced competition and choice of products/providers/services in the market
- For industry: Possible negative consequences for existing business models (lower revenues), in particular those which are entirely financed by commissions; some entities might be required to change the structure of their income; training costs for employees.
- For NCAs: Costs for supervision and enforcement. Training costs for employees.

Policy Option 3 - develop a distinctive list of inducements which are considered to have a high risk of leading to a detrimental impact on the quality of the relevant service to the customer

Benefits

- For customers: As it will be no longer possible for insurance undertakings and insurance intermediaries to pay or receive certain inducements which entail a high risk of detrimental impact on the quality of the service provided to the customers, the latter will benefit as a detrimental impact will be excluded from the outset.
- For industry: Increased confidence and trust of customers in the services provided which will be beneficiary for the industry in the long run.
- For NCAs: Distinctive list of inducements which are not acceptable will help NCA's to supervise and enforce the new requirements on inducements as laid down in Article 29 IDD.

Costs

- For customers: Although less relevant as for policy option 2, possible negative consequences for existing business models, in particular those which mainly rely on commissions to finance their business models as well as small

intermediaries, leading to a reduced competition and choice of products/providers/services in the market

- For industry: Although less relevant as for policy option 2, possible negative consequences for existing business models (lower revenues), in particular those which are entirely financed by commissions which are considered to have a high risk of detrimental impact; some entities might be required to change the structure of their income; training costs for employees.
- For NCAs: Costs for supervision and enforcement. Training costs for employees.

Policy Issue 3 - Organisational requirements related to inducements

Policy options

- Policy option 1: not specify organisational requirements related to inducements
- Policy option 2: apply the same organisational requirements as outlined in the Commission's proposal for a Delegated Directive for MiFID II

The relevant part can be found in Article 11 (4) of the proposed Delegated Directive:⁴⁵

"Investment firms shall hold evidence that any fees, commissions or non-monetary benefits paid or received by the firm are designed to enhance the quality of the relevant service to the client:

(a) by keeping an internal list of all fees, commissions and non-monetary benefits received by the investment firm from a third party in relation to the provision of investment or ancillary services; and

(b) by recording how the fees, commissions and non-monetary benefits paid or received by the investment firm, or that it intends to use, enhance the quality of the services provided to the relevant clients and the steps taken in order not to impair the firm's duty to act honestly, fairly and professionally in accordance with the best interests of the client."

- Policy option 3: develop organisational requirements based on the specificities of insurance intermediaries and undertakings distributing insurance-based investment products

This would be read as follows:

"Insurance undertakings and insurance intermediaries should maintain and operate organisational arrangements procedures in order to assess and ensure that inducements and the structure of inducement schemes which they pay to or receive from a third party:

a. do not lead to a detrimental impact on the quality of the service provided to customers and

b. do not prevent the intermediary or insurance undertaking from complying with their obligation to act honestly, fairly and in accordance with the best interests of their customers.

Insurance undertakings and insurance intermediaries as referred to in paragraph 1 should ensure that any inducement scheme is approved by the insurance undertaking or insurance intermediary's senior management.

Insurance intermediaries and insurance undertakings as referred to in paragraph 1 should document the assessment of each inducement in a durable medium.

Insurance intermediaries and insurance undertakings should set up a gifts and benefits policy that stipulates what benefits are acceptable and what should happen where limits are breached".

⁴⁵ http://ec.europa.eu/finance/securities/docs/isd/mifid/160407-delegated-directive_en.pdf

Analysis of options

Policy Option 1 – not specify organisational requirements related to inducements

Benefits

- For customer: No specific benefits identified
- For industry: No additional costs resulting from the establishment and maintenance of organisational arrangements; more discretion regarding the choice of organisational measures.
- For NCAs: No specific benefits identified

Costs

- For customer: As organisational measures aim to ensure that entities comply with regulatory requirements, a lack of specification may prove disadvantageous from a customer point of view
- For industry: No guidance on organisational requirements related to inducements may cause additional costs to set up corresponding measures
- For NCAs: No guidance on organisational requirements related to inducements

Policy Option 2 and 3 – to specify organisational requirements related to inducements

As Policy Option 2 and Policy Option 3 have many similarities and share the same legislative purpose to ensure that entities comply with the regulatory requirements on inducements which have been introduced through the respective sectoral legislation, the costs and benefits analysis below covers both options at the same time.

Benefits

- For customers: From a more general point of view, organisational measures aim to ensure that insurance undertakings and intermediaries comply with the regulatory requirements for the benefit of the customers
- For industry: Having good systems and controls in place supports firms' compliance with inducement requirements
- For NCAs: Record keeping requirements enable better supervision and assessment of where firms are not complying with requirements

Costs

- For customers: Potential costs passed through from increased compliance costs
- For industry: Costs for setting up new systems and controls, whereas the specific costs depend on the organisational requirements required
- For NCAs: Additional material to assess

5. Comparing the options

Policy Issue 1 - Inducements at risk of causing a detrimental impact: high-level principle

Not introducing a high-level principle (as proposed by Policy Option 1) would lead to legal uncertainty for market participants and the development of different level of customer protection across the Member States as a result of a diverging understanding of detrimental impact by market participants and NCA's in the Member States. This would result in obstacles for cross-border business and therefore hamper the further development of single market in Europe.

Against this background, EIOPA considers it is necessary to provide further guidance in Level 2 under which circumstance inducements entail the risk of having a detrimental impact on the service provided to customers.

With regard to Policy Option 2, EIOPA would like to note that it would ensure a maximum of alignment with the regulatory requirement under MiFID II leading to a cross-sectoral level playing field; however, EIOPA acknowledges that the corresponding Level 1 measures differ in terminology and language even though they pursue the same legislative goal to foster the protection of customers.

For that purpose, EIOPA consider it is appropriate and essential to develop a methodology which is compatible with MiFID, but takes into account the specificities of the insurance sector and differences in terminology used in the corresponding Level 1 provisions. **For that reason, EIOPA favours Policy Option 3 which provides an adequate level of legal certainty about the understanding of detrimental impact** which is based upon the general principle in Article 17 (3) IDD requiring insurance undertakings and intermediaries to act in accordance with the best interests of their customers.

This approach will help to develop a common understanding of detrimental impact across the Member States (further refined by list of inducements which are considered to have a high risk of detrimental impact, see below) and to foster the goal of a single market. At the same time, the impact of Policy Option 3 on existing business models is presumably less significant than under Policy Option 2 taking into consideration that Policy Option 3 adheres to the principle that business models can be financed by commissions, only.

Policy Issue 2 – Inducements at risk of causing a detrimental impact: high risk inducements

Whereas Policy Option 1 leaves a broad discretion to market participants and competent authorities on how to apply the high-level principle (as outlined under Policy Issue 1) and to consider specificities of national markets and existing business models, it implies that market participants and competent authorities develop their own understanding and interpretation leading to a diverging level of customer protection across Member States and between market participants. Differences in national regulation which likely arise will hamper cross-border business and contravene the establishment of a single Market in Europe to the disadvantage of all market participants and customers.

Taking into consideration that Policy Option 2 would require that inducements are used to provide an additional or higher level of service to the customer, existing business models which are mainly financed by commission (and are still relevant in

some Member States) would be hit hard and be required to find other sources of revenues and to give up their existing business models. Moreover, Policy Option 2 would not acknowledge the differences between the respective provisions in IDD and MiFID. In view of these implications which have to be assessed against the principle decision that commissions continue to be a valid form of financing, EIOPA has a preference for Policy Option 3 and to single out specific inducements which bear the high risk of having a detrimental impact on the services provided to the customers.

EIOPA believes that Policy Option 3 provides the appropriate balance between the intermediaries' interests to receive commissions to (partly) finance their business and the customers' interest to benefit from unbiased services. Policy Option 3 is supposed to preclude inducements only which are of the most regulatory concern from a customer protection perspective as they bear a significantly higher level of risk that the insurance undertaking or insurance intermediary will not act in the best interest of its customers when receiving these kinds of inducements.

Policy Issue 3 - Organisational requirements

EIOPA considers it important to specify the organisational requirements related to inducements as organisational arrangements help to ensure that insurance undertakings and insurance intermediaries comply with the regulatory requirements for the benefit of the customers. Having appropriate organisational arrangements does not only support compliance with the regulatory requirements, but also enables better supervision and assessment by the NCAs.

In view of the underlying requirement to assess whether inducements have a detrimental impact on the quality of service, **EIOPA considers Policy Option 3 as the most appropriate as it is closely linked to the obligation to undertake an assessment requiring that the assessment is approved by the senior management and is duly documented.** In view of its practical relevance for employees EIOPA considers it also appropriate to require insurance intermediaries and insurance undertakings to set up a gifts and benefits policy which should be made available to all staff members.

4. Assessment of suitability and appropriateness and reporting

Procedural issues and consultation of interested parties

The specific terms used in this assessment have been defined in the Commission's request for advice in relation to Article 30 of the Insurance Distribution Directive (IDD) as follows:

"EIOPA is invited to provide technical advice on:

- 1. the information to obtain when assessing the suitability or appropriateness of insurance-based investment products for their customers, whereby a distinction has to be made between the situation when advice is provided and the situation when no advice is provided,*
- 2. the criteria to assess non-complex insurance-based investment products for the purposes of point (ii) of point (a) of paragraph 3 of Article 30,*
- 3. the content and format of records and agreements for the provision of services to customers, and*
- 4. the content and format of periodic reports to customers on the services provided.*

The advice should take into account: (i) the nature of the services offered or provided to the customer, taking into account the type, object, size and frequency of the transaction, (ii) the nature of the products being offered or considered including different types of insurance-based investment products and (iii) the retail and professional nature of the customer or potential customer.

In order to ensure regulatory consistency, the technical advice should be consistent with the line taken in the delegated acts expected to be adopted under Article 25(8) of MiFID II."

How would the problem evolve without EU action? The baseline scenario

The Insurance Mediation Directive, Directive 2002/92/EC ("IMD") required the insurance intermediary to, *"at least, specify, in particular on the basis of information provided by the customer, the demands and the needs of that customer as well as the underlying reasons for any advice given to the customer on a given insurance product".*⁴⁶

This was for a number of Member States the starting point for reflecting the customer's objectives when selling insurance products and due to the minimum harmonising nature of the IMD, has led to diverging national approaches regarding the scope of the "demands and needs" test. This is in contrast to the maximum harmonisation approach taken on the suitability and appropriateness assessments under MiFID I and II. In that respect, some Member States competent authorities also

⁴⁶ Article 12(3), IMD

chose to introduce, in addition to the demands and needs test, a suitability and appropriateness assessment in the context of the distribution of insurance-based investment products before IDD came into force.

If the Insurance Mediation Directive (IMD) had not been revised and the Insurance Distribution Directive (IDD) had not entered into force, it is very likely that complaints regarding mis-selling of insurance-based investment products (in particular, as regards the sale of unit-linked life insurance as identified in EIOPA's last Consumer Trends Report⁴⁷) would persist and could be aggravated by current and future market developments (e.g. switching from life insurance guaranteed policies to policies without guarantees due to the low interest rate environment), as very few counterbalancing factors are likely to appear. On the main issue of consumer protection, a lack of action at EU level will likely result in an increase in the number of complaints, or concrete enforcement cases, regarding mis-selling of insurance products and cases where consumers are led to take undue risks.

EIOPA acknowledges that the practical impact of implementing the IDD provisions on suitability and appropriateness (under Articles 30(1) and 30(2), IDD) will differ in Member States, in particular with regards to the potential operational adaptations required by industry (for example, potential costs of training staff regarding new rules and regulations) and the potential benefits for consumers (depending on the extent of change of regulation in the Member State concerned).

Challenges identified vary from national alignment with MiFID II rules and/or reflecting insurance specificities, retaining the same level of consumer protection as under national (mandatory) regimes regarding conduct rules and advice, and implementing appropriateness without misleading customers to believing that they received a personal recommendation. (These are reflected further in the Impact Assessment below).

When analysing the impact of alternative proposed policies, the impact assessment methodology uses a baseline scenario as the basis for comparing policy options. This helps to identify the incremental impact of each policy option considered. The aim of the baseline scenario is to explain how the current situation would evolve without additional regulatory intervention.

The baseline is based on the current and anticipated situation of the market, which is considered to be composed of the content of the Level 1 text in Article 30, IDD, the substance of which some Member States may already apply to the insurance sector in their national regulation, but which, in any event, has to be implemented by Member States by 23 February 2018. The text in Article 30 is already closely aligned with equivalent text in Article 25, MiFID II. Therefore, notwithstanding that the IDD is

⁴⁷ Pages 23-25: https://eiopa.europa.eu/Publications/Reports/EIOPA-BoS-15-233%20-%20EIOPA_Fourth_Consumer_Trends_Report.pdf

generally minimum harmonising in nature⁴⁸, it is important to note, therefore, that a certain degree of cross-sectoral consistency already exists at the baseline of Level 1.

For the analysis of the potential related costs and benefits of the proposed delegated acts regarding conflicts of interest, EIOPA has applied as a baseline scenario, the effect of the application of the Directive requirements and the relevant subsequent implementing measures.

a. The information to obtain when assessing the suitability or appropriateness of insurance-based investment products for their customers

Section 1 Problem definition

The recent financial crisis and debates on the quality of advice clearly underline that access to more complex products needs to be strictly conditional on a proven understanding of the risks involved.

More clarity is thus needed as to the kind of service provided by the distributor and to the conditions attached to the provision of advice. Compounded by cases of mis-selling amid the financial crisis and specific national cases more recently, the number of complaints regarding the quality of advice has also been increasing. In view of the complexity of financial markets and products, customers often depend to a large extent on suitable recommendations provided by distributors.

Information should, therefore, be collected from customers in order to define those services or products which are suitable for them. For this purpose two different levels of information are developed:

- a) Level of information related specifically to the appropriateness of product for the customer;
- b) Level of information related specifically to the suitability of the product for the customer (more detailed).

Suitability and appropriateness requirements generally aim at ensuring that distributors only make suitable personal recommendations and that distributors assess whether customers have the necessary expertise, knowledge and financial capacity to do business in financial products and to understand associated risks given their investment objectives.

The IDD seeks to ensure a higher level of consumer protection, which includes more specific standards for the distribution of insurance-based products. *Inter alia*, the IDD sets out a framework of professional and organisational requirements⁴⁹ for insurance distributors and the additional requirements with regard to the information to obtain

⁴⁸ Recital 3, IDD: "However, this Directive is aimed at minimum harmonisation and should therefore not preclude Member States from maintaining or introducing more stringent provisions in order to protect customers, provided that such provisions are consistent with Union law, including this Directive".

⁴⁹ Article 10, IDD

for the assessment of suitability and appropriateness of insurance-based investment products, complement those requirements and are necessary in order to ensure that insurance distributors act "*honestly, fairly and professionally in accordance with the best interests of their customers*"⁵⁰. When distributing insurance-based investment products, the insurance intermediary or insurance undertaking should gather the necessary information to ensure that they can assess in a proportionate way the appropriateness or suitability of such products.

It is important to note, however, that certain types of customers may be interested in receiving execution-only services (see section b) below) and may not be willing to pay for additional services they do not consider necessary. This may be the case, for instance, of customers who have a sufficient knowledge of financial markets or are even highly sophisticated and are able to make their own investment choices.

The following provisions of the IDD are relevant in this context:

- Article 30(1), IDD provides for a so-called "**suitability assessment**" whereby, where the insurance intermediary or insurance undertaking provides advice to the customer on the distribution of an insurance-based investment product, the intermediary or the insurance undertaking has to "also" obtain the necessary information regarding the customer's knowledge and experience in the investment field, financial situation and investment objectives in order to recommend to the customer the IBIPs that are suitable for that person.
- Article 30(2), IDD provides for a so-called "**appropriateness assessment**" whereby, where the insurance intermediary or insurance undertaking carries out insurance distribution activities regarding insurance-based investment products in relation to sales where no advice is given, the intermediary or insurance undertaking only needs to ask the customer for information on their knowledge and experience in the investment field in order to assess whether the product is appropriate for the customer. The amount of information required is, therefore, lower than the suitability assessment and a risk warning needs to be provided to the customer in case the product is considered inappropriate for the customer.

In both cases, both provisions are without prejudice to the requirements under Article 20(1), IDD, to ensure that prior to the conclusion of an insurance contract, the contract proposed is consistent with the customer's insurance demands and needs (**the "demands and needs test"**).

Under Article 30(6), IDD, the Commission is **empowered to adopt delegated acts** in accordance to further specify how insurance intermediaries and insurance undertakings are to comply with the principles set out in [Article 30] when carrying out insurance distribution activities with their customers, including with regard to the information to be obtained when assessing the suitability and appropriateness of insurance-based investment products for their customers, the criteria to assess non-complex insurance-based investment

⁵⁰ Article 17(1), IDD

products for the purposes of [execution-only business], and the content and format of records and agreements for the provision of services to customers and of periodic reports to customers on the services provided. The IDD delegated acts should take into account:

- the nature of the services offered or provided to the customer or potential customer, taking into account the type, object, size and frequency of the transactions;
- the nature of the products being offered or considered including different types of insurance-based investment products;
- the retail or professional nature of the customer or potential customer.

It is worth noting that:

- **The empowerment for Commission delegated acts under Article 30(6), IDD, is similar in substance to the empowerment for Commission delegated acts under Article 25(8) MiFID II; and**
- **No explicit reference is made in the Commission empowerment for delegated acts under Article 30(6), IDD for the “demands and needs test” in Article 20(1), IDD to be taken into account.**

Section 2 Objectives pursued

Objective 1: Promote a consistent level of customer protection and avoid the risk of regulatory arbitrage, but also take into account the specificities of the insurance sector

The potential substitutability of MiFID financial instruments products and insurance-based investments cannot be ruled out, as indicated by the Commission's Impact assessment on Packaged Retail Investment Products⁵¹ and the Commission's call for evidence regarding "substitute" retail investment products, dated 26.10.2007⁵². These Commission documents provided evidence that consumers can buy certain unit-linked life-insurance policies as a substitutable product for financial instruments under MiFID. This shows that, when consumers are looking for investment products, they might buy either pure investment products or insurance products with investment elements.

In addition, recital 10, IDD provides that *"It is important to take into consideration the specific nature of insurance contracts in comparison to investment products regulated under MiFID II. The distribution of insurance contracts, including insurance-based investment products, should therefore be regulated under this Directive and be aligned with [MiFID II]. The minimum standards should be raised with regard to distribution rules and a level playing field should be created in respect of all insurance-based investment products"*.

Furthermore, recital 56, IDD provides that *"insurance-based investment products are often made available to customers as potential alternatives or substitutes to investment products subject to [MiFID II]"* and *"to deliver consistent investor protection and avoid the risk of regulatory arbitrage by ensuring that insurance-based investment products are subject, in addition to the conduct of business standards defined for all insurance products, to specific standards aimed at addressing the investment element embedded in those products. Such specific standards should include provision of appropriate information and requirements for advice to be suitable"*.

The technical advice should, therefore, to the extent possible, bearing in mind the generally minimum harmonising nature of the IDD and the particular specificities of insurance products compared to MiFID financial instruments, ensure regulatory consistency with the delegated acts under MiFID II in the area of the information to be obtained when assessing the suitability and appropriateness of insurance-based investment products for their customers specifically set out in the legislative acts referred to in Articles 30(1) and 30(2), IDD.

For this purpose, it becomes important to clarify, in order to have a common understanding, the information to be obtained from the customer and the information

⁵¹ <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52009SC0556> – see Annex 1 – "what are packaged retail investment products?": "For example, unit-linked life policies often serve simply as a 'wrapper' for an investment in an underlying fund. In this case the 'competing product' is more accurately described as an alternative channel for the distribution of the investment fund".

⁵² http://ec.europa.eu/finance/finservices-retail/docs/investment_products/feedback_statement_srips_en.pdf

level to be maintained, for the purposes of the assessments on suitability and appropriateness of insurance-based investment products.

Objective 2: Clarify the different levels of information that should be acquired to meet the obligations of the suitability and appropriateness assessments

In view of the complexity of financial markets and products, customers often depend to a large extent on suitable recommendations provided by distributors. Information should, therefore, be collected from customers in order to define those services or products which are suitable for them.

In that respect, suitability requirements generally aim at ensuring that distributors only make suitable recommendations and that customers have the necessary expertise, knowledge and financial capacity to do business in financial products and to understand associated risks given their investment objectives. This addresses the problem of the insurance intermediary or insurance undertaking selling the insurance product without considering the customer's objectives and contribute to the insurance intermediary and the insurance undertaking acting honestly, fairly and professional in accordance with the best interests of the customer when distributing insurance based investment products.

Bearing in mind Objective 1, it seems appropriate to clarify the different levels of information that should be acquired to meet the obligations of the suitability and appropriateness assessments stated in Articles 30(1) and 30(2), IDD related to the distribution of insurance-based investment products.

Objective 3: Ensure the information gathered is necessary and proportionate to the objectives pursued

The Insurance Distribution Directive seeks to ensure a higher level of consumer protection, which includes specific standards for the distribution of insurance-based investment products. Distributors are already subject to professional rules and general conduct of business standards and the additional requirements with regard to the information to obtain for the assessment of suitability and appropriateness **should be proportionate and necessary to achieve the main objectives of the IDD** (namely enhancement of consumer protection and promotion of a true internal market for life and non-life insurance products). When distributing insurance-based investment products, the insurance intermediary or insurance undertaking should gather the necessary information to ensure that they can assess in a proportionate way the appropriateness or suitability of such products.

Objective 4: Take into account information needs with respect to the retail or professional nature of the customer or potential customer

It is important to bear in mind, however, that certain types of customers may be interested in receiving execution-only services and may not be willing to pay for additional services they do not consider necessary. This may be the case, for instance,

of customers who have a sufficient knowledge of financial markets or are even highly sophisticated and are able to make their own investment choices. The IDD does not contain a formal customer classification in the same way provided for under Annex II of MIFID II. The technical advice, nevertheless, seeks to take into account, the existence at the market level, of "*the retail or professional nature of the customer or potential customer*", in line with Article 30(6)(c), IDD.

Section 3 Policy Issues and respective Policy Options

With the intention to meet the objectives set out in the previous section, EIOPA has analysed different policy options throughout the policy development process.

The section below reflects the most relevant policy option that has been considered in relation to the respective policy issue, namely the information (levels of detail of information) to be required for the evaluation of the suitability and appropriateness assessments.

N.B. The policy options below are assessed:

- **Bearing in mind that the final version of the Commission Delegated Act under MiFID II covering the suitability and appropriateness assessments is not yet available; and**
- **Without consideration of the potential final Union act (Regulation, Directive etc.) to be proposed by the Commission for the delegated act on suitability and appropriateness under IDD.**

3.1. Policy Option 1:

This Option consists in ensuring *full* consistency with the provisions in the draft Commission Delegated Act under Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments ("MiFID II"), pertaining to the information to be obtained from the customer under the suitability and appropriateness assessments, by applying the wording and the concepts of MiFID, without any adaptations of substance or terminology to take into account the specificities of the insurance sector. This option takes into consideration the very close alignment between the provisions on suitability and appropriateness at Level 1 under MiFID II and IDD and would ensure full regulatory consistency with the draft MiFID II Delegated Regulation, as requested by the Commission.

For this Policy Option, to the extent appropriate for the product or service, the types of information to be collected from the customer regarding their *financial situation* under the suitability assessment (distribution of IBIPs with advice) include the following:

- *Financial situation of the customer:*
 - Regular income;
 - Assets (including liquid assets);
 - Investments and real property; and
 - Regular financial commitments
- *Investment objectives of the customer:*
 - The length of time, which the customer wishes to hold the investment;
 - The customer's preferences regarding risk-taking
 - The customer's risk profile

- The purposes of the investment

For this Policy Option, to the extent appropriate for the product or service, the types of information to be collected from the customer regarding their *investment objectives* under both the suitability and appropriateness assessments (distribution of IBIPs both with and without advice) regarding their knowledge and experience in the investment field, include the following:

- The types of service, transaction and financial instrument with which the customer is familiar;
- The nature, volume and frequency of the customer's transactions in financial instruments and the period over which they have been carried out; and
- The level of education, and profession or relevant former profession of the customer.

However, this approach would not allow for the possibility to fully reflect any specificities of the insurance sector or terminological differences in EIOPA's draft Technical Advice. For example:

- The necessary information to be collected from the customer as regards the customer's knowledge and experience in the investment field under both the suitability and appropriateness assessments, **would only capture the nature, volume and frequency of the customer's transactions in MiFID financial instruments, not IBIPs**, providing a less complete picture for the insurance intermediary or insurance undertaking;
- Concepts more closely related to the activity of "**portfolio management**" under MiFID II (for example, **recommendations of specific "transactions"** in insurance-based investment products) would be copied across, **without due consideration of their relevance for the insurance sector**;
- The customer's experience and knowledge to understand the "**investment risks**" in certain types of transactions and **his/her ability to bear those "investment risks"**, would not be well suited to the insurance sector, where it is more appropriate to refer to the customer's knowledge and experience in the "investment field" and their ability to bear "losses".
- The notion of "**group insurance contracts**", namely collective contracts where more than one person is insured or participating as a contractual party, would not be adequately reflected in the Technical Advice.
- There is a risk that **the "professional customer" regime in Annex II to MiFID II, could be applied one-to-one to the insurance sector, without consideration of the lack of an existing customer classification regime under the IDD** (notwithstanding an exemption for large risks in certain cases regarding the distribution of non-IBIPs). This is not to say that sophisticated customers do not buy IBIPs, but there is no legal regime under EU law,

specifying what a “professional customer” for the purposes of the distribution of IBIPs, is.

In addition, EIOPA can envisage significant overlap in the wording of Article 54(9) of the draft MiFID II Delegated Regulation, with provisions on Product Oversight and Governance (POG). Copying across Article 54(9), could, in EIOPA’s view, **create some confusion and legal uncertainty** with the POG provisions in the envisaged Delegated Act under IDD on POG.

Furthermore, EIOPA also sees the following difference between the equivalent Level 1 provisions of MiFID II and IDD: There is no comparable provision in Article 25, IDD, to Article 24(2)(2), MiFID II which states that an “*investment firm shall understand the financial instruments they offer or recommend.....*”. There is an equivalent provision in Article 25(1)(4), IDD of Article 16(3)(4), MiFID II, which refers to the fact that the “*insurance undertaking shall understand and regularly review the insurance products it offers or markets*”. The IDD text does not go as far as referring to a “recommendation”. A “recommendation” would provide an obvious link to the suitability assessment under Article 30(1), IDD. Furthermore, the provision in Article 25(1)(4), IDD only applies to insurance undertakings and not insurance intermediaries, whereas Article 30(1), IDD covers both insurance intermediaries and insurance undertakings.

3.2. Policy Option 2 (Preferred Option):

This Option consists in ensuring consistency with the provisions in the draft MiFID II Delegated Regulation pertaining to the information to be obtained from the customer under the suitability and appropriateness assessments, but adapting some key elements of the substance and terminology used in those provisions further to reflect insurance specificities.

In addition, notwithstanding the requirement to obtain certain information from the customer under the suitability and appropriateness assessments and the existence of several references already in Article 30, IDD to the “demands and needs” test, a specific legal reference would be included to make clear that the “demands and needs” test under Article 20(1), IDD is mandatory and always has to be fulfilled by the insurance intermediary or insurance undertaking

As with Policy Option 1 above, the information to be obtained would be very similar; however, with some key differences to take into account the specificities of the insurance sector:

- The necessary information to be collected from the customer as regards the customer’s knowledge and experience in the investment field under both the suitability and appropriateness assessments, **would capture the nature, volume and frequency of the customer’s transactions in both IBIPs and MiFID financial instruments**, providing a more complete picture for the insurance intermediary or insurance undertaking;

- Concepts more closely related to the activity of **“portfolio management”** under MiFID II (for example, **recommendations of specific “transactions”** in insurance-based investment products) would be deleted or adapted in order to take **due consideration of their relevance for the insurance sector**;
- The customer’s experience and knowledge to understand the **“investment risks”** in certain types of transactions and **his/her ability to bear those “investment risks”**, would be adapted to refer to the customer’s knowledge and experience in the “investment field” and their ability to bear “losses”.
- The notion of **“group insurance contracts”**, namely collective contracts where more than one person is insured or participating as a contractual party, would be adequately reflected in the Technical Advice.
- **The “professional customer” regime in Annex II to MiFID II, would not be applied one-to-one to the insurance sector, without consideration of the lack of an existing customer classification regime under the IDD** (notwithstanding an exemption for large risks in certain cases regarding the distribution of non-IBIPs).

In addition, as regards Article 54(9) of the draft MiFID II Delegated Regulation, EIOPA would seek to avoid any confusion or legal uncertainty with provisions on Product Oversight and Governance (POG) in the envisaged Delegated Act under IDD on POG, by not copying across Article 54(9).

3.3. Policy Option 3:

This Option consists in taking a materially different approach to MiFID II with regard to the assessment of suitability by including, in EIOPA’s Technical Advice, a requirement for substantively 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 insurance-based investment product. The option would put a stronger focus also on the protection elements within the insurance-based investment product (e.g. biometric risk cover). The approach is also linked to argumentation that insurance-based investment products can be particularly complicated products for consumers to understand, as compared to financial instruments under MiFID II. In addition, not all the provisions envisaged under Articles 54 -56 of the draft MiFID II Delegated Regulation would be copied across.

Depending on the national interpretation of the “the demands and needs test” in Article 20(1), IDD, this might reflect information requirements already required under the “demands and needs” test. However, the scope of the “demands and needs” test is not explicitly referred to in the Technical Advice under this option⁵³. In addition, not all the provisions envisaged under Articles 54 -56 of the draft MiFID II Delegated Regulation would be copied across.

⁵³ As stated on page 5, the Commission’s empowerment for delegated acts under Article 30(6), IDD, does not explicitly refer to the information to be obtained under the “demands and needs” test.

This approach has as a starting point that **a homogeneous in-depth analysis** should be carried out by insurance intermediaries or insurance undertakings to safeguard the suitability of the insurance product for the customer.

This approach would consist in taking the information to be obtained from the customer under the suitability assessment under MiFID II (as set out in Policy Option 1) as a starting point and substantively adapting this not only to the language and concepts of the insurance sector, but most importantly, including other types of information to be collected from the customer in order to ensure that insurance-based investment products meet not only the investment needs of the customer, but also, and in some cases, what is perceived to be the basic insurance-specific needs of the customer.

EIOPA's online survey on the IDD in early 2016⁵⁴ indicated that some stakeholders suggested to include information, under the suitability assessment, such as age, marital status, insurance coverage, risk tolerance, insurance period, health, existing obligations, dependant family (or other) persons, tax and social security, the customers' income and wealth, information on the source of their regular income, and their reason to seek advice from the distributor. The aforementioned criteria of information to collect from customers would differ from the information to collect under the MiFID framework for the assessment of suitability.

Policy Option 3 would capture the following additional information elements to be included in the suitability assessment (a type of "suitability assessment plus") to capture all possible relevant aspects for understanding the "insurance-specific needs" of the customer (to the extent that those would not already be captured under the requirements laid down in the MiFID II delegated act⁵⁵) and make a decision whether to buy an insurance-based investment product or not:

- Personal data (customer's age, personal characteristics, the place of residence);
- The reasons for purchasing a life insurance product (retirement, protection of family in case of death, investment);
- Information about persons to be covered/protected under the policy;
- The customer's employment and level of education;
- Information regarding the customer's tax and social security situation.
- The customers' income and wealth;
- The customer's existing investment and insurance portfolio;
- The customer's existing financial obligations (loans, debts etc.);
- the customer's liquidity expectations;
- The reason for seeking advice from the insurance intermediary or the insurance undertaking, in particular expectations from the contract in terms of coverage, duration and any financial risks related to the contract to be concluded.

⁵⁴ Online survey in preparation for the Call for Advice from the European Commission on the delegated acts under the Insurance Distribution Directive: <https://eiopa.europa.eu/Pages/Consumer-Protection/Online-survey-Call-for-Advice-from-EC-IDD.aspx>

⁵⁵ It is also worth noting that some of these elements have been addressed by ESMA regarding MiFID in their Guidelines on certain aspects of the MiFID suitability requirements 21 August 2012 | ESMA/2012/387, see para. 22 on page 6: https://www.esma.europa.eu/sites/default/files/library/2015/11/2012-387_en.pdf

Section 4 Analysis of impacts

4.1 Policy Option 1:

This Option consists in EIOPA copying across the provisions pertaining to the information to be obtained under the suitability and appropriateness assessments draft Commission Delegated Regulation under MiFID II (Articles 54 - 56) without any changes to EIOPA's draft Technical Advice.

Impact on insurance intermediaries and insurers' economic position

The impact will differ depending, in particular, on whether the insurance intermediary or insurance undertaking in question are already subject to MiFID II provisions (for example, if they are already licensed to carry out regulated activities under MiFID II). In this case, additional costs would be avoided and insurance intermediaries or insurance undertakings would not need to adopt new procedures. In the case of insurance intermediaries or insurance undertakings, which are not yet subject to MiFID II provisions, insurance intermediaries would benefit from the knowledge and procedures already available for the distribution of financial instruments to retail clients under MiFID II provisions.

However, the application of MiFID II concepts to the insurance sector could have potential cost implications if these MiFID concepts do not fit with the distribution of insurance-based investment products. This is namely the case, where concepts/terminology contained in MiFID II (e.g. execution of orders, portfolio management) do not exist in the insurance sector and where the MiFID framework allows for assumptions with regard to the assessment of suitability and appropriateness of professional clients, as there is no specific client classification in IDD (other than an exemption for "large risks").

Impact on customer protection

This policy option would ensure a high level of *consumer protection*, notwithstanding that the assessment of suitability and appropriateness according to Article 30, IDD would need to be complemented by the "demands and needs" test of Article 20(1), IDD. In the latter case, the distributor has to specify the demands and the needs of a customer and has to provide the customer with objective information about the insurance product in a comprehensible form to allow that customer to make an informed decision.

Impact on competition and market structures:

From a competition perspective, this option promotes a consistent level of protection of customers and a level playing field across financial sectors, in line with Recital 56, IDD and the fact that the provisions of Article 30, IDD are virtually identical to equivalent provisions in MiFID II.

4.2 Policy Option 2 (Preferred Option):

This Option consists in reflecting insurance specificities with regard to the information to be acquired, by the intermediary and insurance undertakings, under the suitability and appropriateness assessments, while ensuring consistency with the assessment of suitability and appropriateness under the draft MiFID II Delegated Regulation. In addition, notwithstanding the requirement to obtain certain information from the customer under the suitability and appropriateness assessments, a specific legal reference to the fact that the “demands and needs” test under Article 20(1), IDD, always has to be carried out, has been added.

Under this policy option, EIOPA would:

- (i) Set the level of detail of information to be collected from the customer at an appropriate level and deliver consistent investor protection and avoid the risk of regulatory arbitrage by ensuring regulatory consistency with the draft MiFID II Delegated Regulation, as requested by the European Commission;
- (ii) Notwithstanding the existing reference at Level 1 to the “demands and needs” test, explicitly recognise at Level 2 that the “demands and needs” test is mandatory and always needs to be fulfilled, even in the case of the suitability and appropriateness assessments. The “demands and needs” is left to further national interpretation during the IDD implementation; and
- (iii) Take account of the fact that concepts/terminology contained in MiFID II (e.g. execution of orders, portfolio management) do not exist in the insurance sector and other concepts (e.g. collective insurance contracts) would need to be introduced.

Through this option, EIOPA delivers regulatory consistency to the extent possible with the equivalent provisions in the draft MiFID II Delegated Regulation (taking into account, the particular specificities of insurance products/distribution channels compared to MiFID financial instruments/firms) and thereby promotes a consistent level of consumer protection across financial sectors and a level playing field for firms.

Analysis according to the estimated impact on stakeholders

The following stakeholders and impacts have been assessed and are elaborated in slightly more detail than the other two policy options due to the fact that it is EIOPA’s preferred policy option:

- Impact on customer protection.

Pros

In this respect, this policy option has the following *positive* impacts in terms of customer satisfaction:

In case of the *appropriateness assessment*:

- Customer selection is made directly on the products required and there are lower costs and a prompter service for the customer, which takes into account their risk appetite, is provided. Customers are also not required to bear additional costs arising from the provision of advice, unlike with the suitability assessment.
- Potential additional costs passed on to the customer through the need for the insurance intermediary and insurance undertaking to request additional information over and above what is required when purchasing a suitable substitutable product, can be avoided.
- The explicit inclusion of insurance-specific concepts provides more legal certainty under the delegated acts.

In case of the *suitability assessment*:

- Customers are helped to achieve the level of awareness of their knowledge on key issues related to insurance-based investment products. Support is provided to understand the characteristics, benefits and limitations of the insurance product. This focuses information on the investment element of the life insurance product, given that such products can incorporate a structure, which makes it difficult for customers to understand them and makes the consumer aware of the increased risk that can be connected to the investment element so that the product is more suited to their own needs.
- A number of additional questions to the customer relating to their personal situation (see Option 3 below), irrespective of his/her level of financial literacy, would be avoided, with the avoidance of additional costs for the customer to bear and a possible deterrent effect for purchasing insurance-based investment products.
- The explicit inclusion of insurance-specific concepts provides more legal certainty under the delegated acts.

Cons

On the other hand, also this policy option may have the following *negative* impacts:

- Questions to the customer which relate to their personal situation, depending on the relevance of these questions in relation to the level of sophistication of the customer and the extent to which they are not captured under "*knowledge and experience in the investment field*" in Article 30(2). EIOPA could mitigate this potential negative impact further by issuing guidance on aspects relating to

the personal situation of the customer, which are not caught by “*knowledge and experience in the investment field*”.

- *Impact on the economic position of insurance intermediaries and insurance undertakings:*

Pros

In this respect, this policy option has the following *positive* impacts:

- Depending on the approach taken at national level, the insurance intermediary or insurance undertaking would be not required to collect more information from the customer, irrespective of their level of financial literacy and would be required to collect more information when selling an IBIP, as opposed to a substitutable product such as a UCIT, leading to additional compliance costs. If the insurance intermediary or insurance undertaking is licensed under both the IDD and MiFID II, they would not be required to comply with two different sets of rules, leading to additional compliance costs and regulatory arbitrage.
- Customer loyalty towards the company, even in the case of the appropriateness assessment as a sophisticated investor can appreciate the benefits in terms of cost and efficiency of a non-advised sale as less information has to be collected from the customer;
- Both assessments (appropriateness and suitability) protect insurance intermediaries or undertakings with reference to the customer's choices.

Cons

In the other direction, this policy option may have the following *negative* impacts:

- An extensive list of information to mechanically gather customer data should not have the unintended consequence of leading to a mere “tick-box” exercise by insurance intermediaries and insurance undertakings in collecting information from the customer whilst not increase the quality of the actual advice provided.
- Where only the appropriateness assessment is performed, the insurance undertaking or insurance intermediary manages limited information. It is possible that in some Member States, where additional information is currently collected when an IBIP is sold based on the “demands and needs” test, less information to be collected on the basis of the suitability and appropriate assessments may result in increased costs related to implementing procedures to supervise the information obtained by the insurance intermediary or insurance undertaking and costs related to reviewing the documentation on the basis of the information they receive and provide information to the customer in order to ensure compliance with the new regulations.

- *Impact on competition and market structures:*
 - From this perspective, this option promotes a consistent level of protection of customers and a level playing field across financial sectors, in line with Recitals 10 and 56, IDD and the fact that the provisions of Article 30, IDD are virtually identical to equivalent provisions in MiFID II.
 - The option generates, within Europe, an aligned behaviour across financial sectors. The assessment of the investment component of the insurance product will be aligned to other sectors such as banking and securities, with the result that this will facilitate intermediaries/undertakings that sell both insurance-based investment products and MiFID financial instruments, thus substantially reducing compliance costs and assisting consumers in comparing between insurance-based investment products and substitutable products such as UCITS. For insurance products with an investment element, EIOPA seeks in its technical advice to adequately take into account the specificities of insurance products (*namely, protection of customers against risks linked to human life*) and the distribution channels.

4.1 Policy Option 3:

This Option consists in EIOPA developing relevant criteria to assess whether an insurance-based investment product is suitable for a customer, whereby EIOPA would take a materially different approach to MiFID II by including, in its Technical Advice, a requirement for substantively 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 insurance-based investment product.

Impact on customer protection

This policy option could ensure a suitably high level of *customer protection* as with Option 2, but this approach would require substantively more information to be obtained from customers, irrespective of whether they are purchasing an insurance-based investment product or a substitutable product and irrespective of their level of financial literacy. That said, it could be assumed that more information under this type of "suitability assessment plus" could lead to a better assessment of the insurance contract and might be justified by the need for the insurance undertaking or insurance intermediary to provide additional advice, focussed specifically on the investment element of the insurance product.

However, customers would face different questions when shopping for retail investment products and could get the impression of different levels of consumer protection. In addition, the impact could be more pronounced in Member States where national regulation does not regulate the timing of obtaining information from, or delivering information to, the customer. In Member States where such legislation

already exists on the timing of obtaining or delivering information, the customer might already be used to provide information related to their needs and conditions.

Impact on the economic position of insurance intermediaries and insurance undertakings

Distributors also subject to MiFID II requirements (i.e. licensed to carry out regulated activities under MiFID II) would need to ask their customers a number of additional questions to gather the necessary information to assess the suitability of substitutable investment products. This would result in potentially increased operational and compliance costs.

In addition, as mentioned in relation to Option 2 above, an extensive list of information to mechanically gather customer data should not have the unintended consequence of leading to a mere "tick-box" exercise by insurance intermediaries and insurance undertakings in collecting information from the customer whilst not increase the quality of the actual advice provided. This could potentially be seen as transferring legal risk/liability from the distributor to the customer, due to the fact that the distributor has to follow extensive rules, but not necessarily needs to reflect what is necessary and best for customers, whereas a more principles-based approach could avoid the unintended consequence of a "tick-box" approach.

Impact on competition and market structures:

From this perspective, this option creates additional entry barriers for the distribution of insurance-based investment products. Additional information to be collected from the customer could create the impression for the customer that insurance-based investment products are more complicated or would need more granular information to achieve the same level of consumer protection compared to other investment products. At the same time, customer loyalty could increase due to a more deep and complete analysis of personal needs. This could also reduce cancellation rates of insurance-based investment products which are not kept until maturity, thus ultimately increasing the economic benefit to policyholders. To date, no evidence suggests that all products with insurance-based investment elements would require more detailed and more burdensome distribution requirements, than potentially substitutable MiFID II financial instruments.

As referred to above, this approach has the potential to create a heightened risk of regulatory arbitrage, depending on whether an insurance intermediary or insurance undertaking is or is not licensed to carry out regulated activities under MiFID II, as well as IDD.

Section 5: Comparison of options.

Regarding the policy issue on the information to obtain under the suitability and appropriateness assessment, the Impact Assessment compares the three options developed on the basis of the analysis above.

The preferred policy option for this policy issue is Option 2. Both Options 1 and 2 are very similar in terms of the benefits and costs which they generate and in promoting a consistent level of consumer protection across financial sectors and preventing a risk of regulatory arbitrage. However, the advantage of Option 2 is that insurance specificities are reflected and thus reducing costs due to a lack of insurance specificity for insurance undertakings, insurance intermediaries and national competent authorities.

Option 3 would take into account more the “basic needs” of the customer (regardless of their level of financial literacy) and potentially some more insurance-specific elements. However, this approach could create substantial additional costs for the implementation of the assessment of suitability and appropriateness, while arguably not going beyond the level of consumer protection achieved under policy option 2. Furthermore, policy option 3 might involve a possible risk of regulatory arbitrage. Therefore, the additional costs of policy option 3 are not justified by tangible benefits for consumers.

b. The criteria to assess non-complex insurance-based investment products for the purposes of point (ii) of point (a) of paragraph 3 of Article 30

Section 1 Procedural issues and consultation of interested parties

The specific terms used in this assessment have been defined in the Commission's request for advice in relation to Article 30(3)(a)(ii) of the Insurance Distribution Directive as follows:

The Commission's request for advice

"EIOPA is invited to provide technical advice on

- *the criteria to assess non-complex insurance-based investment products for the purposes of point (ii) of point (a) of paragraph 3 of Article 30"*

Section 2 Problem definition

Insurance contracts are often complicated and difficult to understand for consumers. Intermediaries therefore play an important role in processing information for the consumer and guiding consumers in choosing suitable insurance policies. Some studies actually suggest that intermediation is a necessity in some areas of insurance.

The quality of the service provided by insurance intermediaries and sellers of insurance products depends on professional competence. The current scope of the Insurance Mediation Directive (IMD) is limited and the rules in the IMD are too general and do not differentiate between complex and simpler products. In particular, complicated products, such as life insurance products with an investment element (IBIPs), might require higher levels of knowledge and ability from the insurance intermediary.

Unsuitable or low quality advice leads to consumers buying products they do not need, or products not adapted to their needs. This creates higher costs and increases the risk of default under, or cancellation of, the insurance policy, resulting in extra costs. According to consumer groups, if advice is inaccurate or of poor quality, consumers make wrong choices and buy (or, rather, are sold) the wrong products (including, for example, policies under which they are over-or under-insured).

The problems explained above are similar, but even more pronounced, in the case of insurance-based investment products, because of their generally high complexity.

Consumer protection standards for the sales of insurance-based investment products are not sufficient at EU level, as the IMD did not contain special rules for the sales of life insurance products with investment elements, which are generally more complicated than other insurance products. Currently, those products are sold under

the general rules for the sales of insurance products, even though these products are very different in nature and generally represent higher risks for retail consumers.

The potential substitutability of MiFID financial instruments products and insurance-based investments cannot be ruled out, as indicated by the Commission's Impact assessment on Packaged Retail Investment Products⁵⁶ and the Commission's call for evidence regarding "substitute" retail investment products, dated 26.10.2007⁵⁷. These Commission documents provided evidence that consumers can buy certain unit-linked life-insurance policies as a substitutable product for financial instruments. This shows that, when consumers are looking for investment products, they might buy either pure investment products or insurance products with investment elements.

In the absence of EU rules regulators have responded differently by asking for increased transparency (for instance remuneration disclosure) or, where their action captures complex products in general, providing guidance on pre-contractual disclosure or calling for a moratorium.

How would the problem evolve without EU action? The baseline scenario

If IMD had not been revised, it is very likely that the problems that have been identified will persist and could be aggravated by future market developments, as very few counterbalancing factors are likely to appear. On the major issue of consumer protection, a lack of action at EU level will likely result in an increase in the number of cases of mis-selling of insurance products and cases where consumers are led to take undue risks.

For the analysis of the potential related costs and benefits of the proposed Technical Standards for non-complex insurance based investment products, EIOPA has applied as a baseline scenario the effect from the application of the Directive requirements and the relevant implementing measures (article 30(3) (a) (ii) IDD):

Article 30(3)(a) of IDD states:

"3. Without prejudice to Article 20(1), where no advice is given in relation to insurance-based investment products, Member States may derogate from the obligations referred to in paragraph 2 of this Article, allowing insurance intermediaries or insurance undertakings to carry out insurance distribution activities within their territories without the need to obtain the information or make the determination provided for in paragraph 2 of this Article where all the following conditions are met:

(a) the activities refer to either of the following insurance-based investment products

- (i) contracts which only provide investment exposure to the financial instruments deemed non-complex under Directive 2014/65/EU and do*

⁵⁶ <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52009SC0556> – Annex 1 – "what are packaged retail investment products?": "We do not consider all of the products under consideration to be perfect substitutes. Moreover, while they do compete for retail savings, it is not always accurate to treat them as being in direct competition. For example, unit-linked life policies often serve simply as a 'wrapper' for an investment in an underlying fund. In this case the 'competing product' is more accurately described as an alternative channel for the distribution of the investment fund".

⁵⁷ http://ec.europa.eu/finance/finservices-retail/docs/investment_products/feedback_statement_srips_en.pdf

- not incorporate a structure which makes it difficult for the customer to understand the risks involved; or*
- (ii) *other non-complex insurance-based investments for the purpose of this paragraph”.*

Section 3 Objectives pursued

IDD has three general objectives:

1. to improve insurance regulation in a manner that will facilitate market integration;
2. to establish the conditions necessary for fair competition between distributors of insurance products; and
3. to strengthen consumer protection, in particular with regards to life insurance products with an investment element.

The specific objectives are the immediate goals of IDD, the targets that first need to be reached in order for the general objectives to be met:

- Create a level playing field;
- Reduce conflicts of interest;
- Improve advice for complex products;
- Reduce the burden for cross-border entry.

The operational objectives are then the deliverables that it should produce. The Directive is aimed at:

- Extending the scope of application to all distribution channels, i.e. insurance and reinsurance distribution which may be carried out by insurers and reinsurers as well as intermediaries, including proportionate requirements for those who sell insurance products on an ancillary basis (although “ancillary insurance intermediaries” – intermediaries whose principal activity is not insurance distribution, (i.e. distributing insurance that is complementary to another sale or service) are excluded from scope).
- identifying, managing and mitigating conflicts of interest;
- strengthening administrative sanctions, as well as measures to be applied in the event of a breach of key provisions, for infringements of sales rules;
- enhancing the suitability and objectiveness of insurance advice;
- ensuring that sellers' professional qualifications match the complexity of the products they sell; and
- clarifying the procedure for cross-border entry to markets across the EU

It is important to bear in mind, that certain types of customers may be interested in receiving execution-only services and may not be willing to pay for additional services they do not consider necessary. This may be the case, for instance, of customers who have a sufficient knowledge of financial markets (a high level of financial literacy) and are able to make their own investment choices.

Consistency of the objectives with other EU policies

The identified objectives are coherent with the EU's fundamental goals of promoting the harmonious and sustainable development of economic activities, a high degree of competitiveness, and a high level of consumer protection, which includes the safety and economic interests of citizens (Article 169 TFEU). These objectives are also consistent with the reform programme proposed by the European Commission in its Communication *Driving European Recovery*, the 'Europe 2020 strategy' for smart, sustainable and inclusive growth, the MiFID II Directive and the PRIIPs KID Regulation.

Section 4 Policy Options

With the intention to meet the objectives set out in the previous section, EIOPA has analysed different policy options throughout the policy development process. Some of the technical guidelines proposed are not expected to have material impact compared to the baseline, however they are proposed for the purpose of clarification and achievement of common understanding.

The section below reflects the most relevant policy options that have been considered in relation to non-complex insurance based investment products. We have also listed relevant options which have been discarded in the policy development process.

Policy option 1 - General prohibition: One possible option would be to prohibit insurance undertakings and intermediaries from providing any kind of insurance distribution activities on all "other" non-complex insurance based investment products not defined in the technical guidelines.

Policy option 2 – Limited prohibition (Preferred Option): Another possibility would be only to prohibit insurance intermediaries from providing advice on insurance products which do not meet principled-based criteria for non-complex insurance based investment products as defined in the technical guidelines.

Policy option 3 – No explicit prohibition: Another possibility would be to not to introduce an explicit prohibition for "other" non-complex products but to consider in the context of the "demands and needs test" or the assessment of suitability/appropriateness whether the insurance intermediaries has received all relevant information on the product.

Section 5 Analysis of impacts

Policy option 1 – General prohibition

Benefits:

- **For customers:** This option prevents insurance undertakings and intermediaries from distributing insurance based investment products if they do not receive the

appropriate information on the products. The rationale of this option is that insurance undertakings and intermediaries need appropriate information on the product to undertake the demand and needs test and to assess whether the insurance product is suitable or appropriate. Without this information the insurance intermediary may not be in position to fulfil these requirements and would potentially not act in the best interest of the customers. Therefore, this option provides a maximum of customer protection.

- **For industry:** Insurance intermediaries would have a vested interest in obtaining all appropriate information before they sold insurance based investment products to customers. Since the information on the product enables the insurance undertaking or intermediary to assess the demands and needs of the customer and whether the insurance product is suitable or appropriate for the customer, a prohibition reduces the risk that insurance products are sold to customers which are not in the best interest of the customer. Therefore, an explicit prohibition would reduce the risk of mis-selling products avoiding negative impacts on the industry's reputation.
- **For NCAs:** Option 1 would provide legal certainty to NCAs as Option 1 clearly sets out the legal consequences in cases where the insurance undertakings or intermediaries do not obtain all relevant information on the product. The advantage of Option 1 is also that it can be easily monitored and enforced.

Costs:

- **For customers:** Customers would be prevented from buying specific insurance products due to the fact that no insurance based investment products are deemed non-complex. Therefore, this Option would limit the customer's choice and freedom to buy insurance products as self-responsible person.
- **For industry:** A broad prohibition as proposed under Option 1 may lead to a negative impact on the turnover of insurance undertakings and intermediaries (particularly in MS where sale of non-complex products where appropriate may otherwise be permitted) and potential restraint of trade. The costs of suitability assessment in all cases and the inability to sell non-complex insurance based investment products on the basis of appropriateness would also impact the costs of administration and governance within insurance undertakings and intermediaries. The costs of monitoring and enforcement would also increase in MS where sale of such products on the basis of appropriateness is currently permitted.
- **For National Competent Authorities (NCAs)** – This option would have a negative effect for NCAs where the existing regulatory regime promotes wider consumer choice by enabling some or a wider range of insurance based investment products to be sold by means of the appropriateness test (or even via execution only). This would not therefore promote sufficient flexibility at MS level to enable a "level playing field" between Member States. Having to restrict the

existing regulatory regime further in this way could increase monitoring and enforcement costs for NCAs.

Policy option 2 – Limited prohibition (Preferred Option)

Benefits:

- **For customers:** In contrast to Option 1, Option 2 only prohibits insurance undertakings and intermediaries from selling non-complex insurance based investment products in cases where products concerned do not meet the criteria specified. Therefore Option 2 aims to enhance customer protection, while enabling wider customer choice where products which meet the criteria are enabled to be sold by means of the appropriateness test.
- **For industry:** Same benefits as outlined for Option 1, but extended to cases where a range of products (limited by the criteria specified for non-complex products) may be sold by insurance undertakings and intermediaries where customers also satisfy the appropriateness test. Therefore potentially promoting a positive impact on the turnover of insurance undertakings and intermediaries.
- **For NCAs:** Same benefits of certainty as outlined for Option 1, but enabling some flexibility of interpretation at local level to ensure the continuing effectiveness of local NCA regimes while establishing consistent common principles via the criteria at EU level.

Costs:

- **For customers:** In contrast to Option 1, Option 2 would enable insurance undertakings and intermediaries to offer a limited range of insurance based investment products on the basis of appropriateness where they met the criteria for non-complex products. As the insurance undertaking would still be allowed to sell insurance product to the customer without advice and on request of the customer, the customer's choice of products would be less affected.
- **For industry:** As the criteria would potentially increase the range of products available to customers on the basis of the appropriateness test, there would be no negative (and potentially a positive) impact on turnover.

Policy option 3 – No explicit prohibition

Benefits:

- **For customers:** Option 3 does not seem to have significant benefits for the customers.
- **For industry:** Option 3 leaves it in the discretion of the insurance intermediaries to decide whether they are in a position to appropriately assess the demand and

need of the customer as well as the suitability / appropriateness of an insurance product based upon the information they obtained from the manufacturer.

- **For NCAs:** Option 3 does not seem to have significant benefits for the NCAs. Some NCAs may have more developed regimes which impose additional requirements already (following IMD) therefore this may even be seen as a retrograde step.

Costs:

- **For customers:** Option 3 entails the risk that customer suffer from mis-selling which is caused by the fact that (in relevant circumstance) the insurance undertaking intermediary has not received sufficient information on the product to assess the demands and needs as well as the suitability / appropriateness of an insurance product and the sale of the product may therefore be unsuitable/inappropriate.
- **For industry:** Market participants continue to face reputational risk due to mis-selling cases which are caused due to a lack of information on the products.
- **For NCAs:** The enforcement of the regulatory requirements on insurance undertakings or intermediaries to obtain adequate information to demonstrate suitability or appropriateness may prove more onerous.

Section 6: Comparison of options.

When comparing the costs and benefits of the different policy options, it became apparent that a too strict approach would not only be disadvantageous for insurance undertakings and insurance intermediaries, but also for customers and potentially for NCAs.

As policy option 1 would contradict the principle of self-responsibility of the customer and limit the customer's choice of insurance products, as well as increase regulatory costs, this Option does not seem adequate. Furthermore, it could be questioned whether the Level 1 Directive provides any possibility to exercise a general prohibition at EU level.

Conversely, policy option 3 does not seem adequate either as it does not address at all the risk of mis-selling insurance products which are caused by a lack of information on the product.

Therefore, policy option 2 seems to find the appropriate balance between the interests of insurance undertakings and insurance intermediaries and those of their customers. It also enables an appropriate degree of flexibility at NCA level, while consistent principle-based criteria for non-complex products at EU level which is consistent with a minimum harmonising approach. From a customer's perspective it seems reasonable to prohibit insurance undertakings and insurance intermediaries

from recommending specific insurance products which do not meet the criteria, while enabling customers to buy these products if the criteria for non-complex products are met and the appropriateness test is satisfied, or on own initiative, if they wish.

c. The content and format of records and agreements for the provision of services to customers

The Commission's request for advice

"EIOPA is invited to provide technical advice on:

the content and format of records and agreements for the provision of services to customers".

Section 1 Problem definition

Failure of insurance intermediaries and insurance undertakings to keep adequate records of their insurance distribution activities may prevent competent authorities from adequately fulfilling their supervisory objectives and taking necessary enforcement action. In that respect, insurance-based investment products represent a potentially increased risk to consumers.

Failure to keep adequate records of whether an insurance intermediary or insurance undertaking has complied with all relevant conduct of business obligations regarding the distribution of an insurance-based investment product, can be particularly damaging to customers for example, where a customer subsequently suffers financial detriment as a result of the product sold.

The Insurance Mediation Directive (IMD) did not include formal record-keeping obligations for insurance intermediaries regarding their insurance mediation activities, although some Member States may have introduced such obligations in their national frameworks, given the minimum harmonising nature of the IMD.

The IDD introduces a new framework for record-keep regarding the distribution of insurance-based investment products under Article 30(4), IDD, which is closely aligned with the approach taken under the MiFID I and MiFID II Directive to ensure a consistent level of protection for consumers and prevent regulatory arbitrage. Currently, insurance undertakings or insurance intermediaries with regulatory licences under both MiFID and IMD are only obliged to maintain records with regard to the sale of MiFID financial instruments, leading to regulatory arbitrage.

Section 2 Objective pursued

Objective 1: To ensure effective record-keeping requirements regarding the distribution of insurance-based investment products so as to:

- (i) Enable national competent authorities to fulfil their supervisory tasks and to impose sanctions under the IDD, where appropriate; and

- (ii) Ascertain whether insurance undertakings and insurance intermediaries have complied with all relevant conduct of obligations with respect to the distribution of insurance-based investment products.

Objective 2: In line with Recital 56, IDD⁵⁸, the technical advice should, to the extent possible, bearing in mind the minimum harmonising nature of the IDD and the particular specificities of insurance products/distribution channels compared to MiFID financial instruments/firms, ensure regulatory consistency with the delegated acts under MiFID II in the area of record-keeping.

Objective 3: Bearing in mind Objective 1, it seems appropriate to have a common understanding of the records which should be kept by the insurance intermediary or insurance undertakings pursuant to Article 30(4) of the IDD, taking into account the specificities of insurance products/distribution channels.

Section 3 Policy Issues and relative Options

With the intention to meet the objectives set out in the previous section, EIOPA has analysed different policy options throughout the policy development process.

The section below reflects the most relevant policy options that have been considered in relation to the respective **policy issue, namely information in terms of the documents which should be kept pursuant to Article 30(4), IDD.**

We have also listed relevant options which have been discarded in the policy development process.

3.2.1. Policy option 1: the record-keeping obligation should include only the documentation relating to the appropriateness assessment, in line with Article 56 of the draft MiFID II Delegated Regulation, thus promoting a consistent level of consumer protection across financial sectors and preventing regulatory arbitrage. However, specific record keeping rules for the assessment of suitability were not introduced in the draft MiFID II Delegated Regulation.

3.2.2 Policy option 2: the recording-keeping should include not only the documentation relating to the appropriateness assessment, but also with regard to the suitability assessment, thereby going beyond the requirements of Article 56 of the draft MiFID II Delegated Regulation, but enhancing the level of customer protection due to creating the need for clear documentation of the suitability assessment.

⁵⁸ "Insurance-based investment products are often made available to customers as potential alternatives or substitutes to investment products subject to Directive 2014/65/EU. To deliver consistent investor protection and avoid the risk of regulatory arbitrage, it is important that insurance-based investment products are subject, in addition to the conduct of business standards defined for all insurance products, to specific standards aimed at addressing the investment element embedded in those products. Such specific standards should include provision of appropriate information, requirements for advice to be suitable and restrictions on remuneration".

Section 4 Analysis of impacts

4.1. Policy Option 1

This option lists the documentation relating to the appropriateness assessment only.

This option is in line with the MiFID II Delegated Regulation and the draft technical advice has been adapted in several places to take into account the specificities of the insurance sector. Member States could introduce this concept at their own discretion. This approach promotes a consistent level of consumer protection and prevents regulatory arbitrage across financial sectors. However, the specific record keeping rules for the assessment of suitability were introduced by ESMA Guidelines and would not be matched by rules in the insurance sector, as the scope of the ESMA Guidelines is limited and does not include insurance distributors.

4.2. Policy option 2

This option lists the documentation relating to both the suitability and appropriateness assessments.

This option goes beyond the draft MiFID II Delegated Regulation, but enhances the level of customer protection. This option can be viewed as specifying the general obligation of record-keeping further for insurance undertakings and insurance intermediaries and, therefore, could lead to higher compliance costs. For firms that are subject to both the record-keeping rules set in ESMA Guidelines and the record-keeping rules set in future IDD delegated acts, the compliance costs would be not increased.

Section 5: Comparison of options.

Regarding the policy issue on the record-keeping with regard to the suitability and appropriateness assessment, the Impact Assessment compares the two options developed on the basis of the analysis above.

The preferred policy option for this policy issue is Option 2. Policy option 2 sets clear expectations for the record keeping of the suitability assessment, which is of pivotal importance when providing personal recommendations to customers. The proper record-keeping of these events can be expected anyway from distributors under the IDD. Policy option 2 allows for the record-keeping in a more uniform way, also allowing national competent authorities to understand more easily if all underlying regulatory requirements were met.

d. The content and format of periodic reports to customers on the services provided

The Commission's request for advice

"EIOPA is invited to provide technical advice on:

the content and format of periodic reports to customers on the services provided".

Section 1 Problem definition

Insurance-based investment products represent a potentially increased risk to consumers. Failure of insurance intermediaries and insurance undertakings to report periodically to customers on the services they provide to those customers, for example, on costs information associated with transactions carried out in relation to insurance-based investment products, may potentially have adverse financial consequences for customers. This may be the case where those products do not continue to meet the customer's preference, objectives and other characteristics. Failure to provide periodic reports may, in the long run, inhibit the customer's ability to seek legal redress against those entities in the event of mis-selling.

The Insurance Mediation Directive (IMD) did not include formal periodic reporting obligations for insurance intermediaries regarding their insurance mediation activities, although some Member States may have introduced such obligations in their national frameworks, given the minimum harmonising nature of the IMD.

The IDD introduces a new framework for periodic reporting regarding the distribution of insurance-based investment products under Article 30(5), IDD, which is closely aligned with the approach taken under the MiFID I and MiFID II Directive to ensure a consistent level of protection for consumers and prevent regulatory arbitrage. Currently, insurance undertakings or insurance intermediaries with regulatory licences under both MiFID and IMD are only obliged to report periodically to customers with regard to the sale of MiFID financial instruments, leading to regulatory arbitrage.

Section 2 Objective pursued

Objective 1: Periodic reporting by insurance intermediaries and insurance undertakings is a key element to ensure transparency, simplicity, accessibility and fairness across the internal market for consumers. A proactive approach is needed to restore trust in the financial sector by ensuring that consumers are adequately protected from the risk of detriment. Consumers are becoming more aware of their rights and rightfully demand greater transparency, comparability and integrity on the part of firms.

Objective 2: To ensure effective periodic reporting by insurance intermediaries and insurance undertakings regarding the services provided in relation to the distribution of insurance-based investment products so as to:

- (i) Keep customers adequately informed on whether the insurance-based investment products they have purchased continue to meet their preferences, objectives and other characteristics; and
- (ii) Enable customers to seek appropriate legal redress in the event of mis-selling by those insurance intermediaries and insurance undertakings.

Objective 3: In line with Recital 56, IDD⁵⁹, the technical advice should, to the extent possible, bearing in mind the minimum harmonising nature of the IDD and the particular specificities of insurance products compared to MiFID financial instruments, ensure regulatory consistency with the delegated acts under MiFID II in the area of periodic reporting to customers on the services provided.

Objective 4: Bearing in mind Objective 1, it seems appropriate to have a common understanding of the content and format of periodic reports to customers on the services provided pursuant to Article 30(5) of the IDD, taking into account the particular specificities of insurance products compared to MiFID financial instruments.

Section 3 Policy Issues and relative Options

With the intention to meet the objectives set out in the previous section, EIOPA has analysed different policy options throughout the policy development process.

The section below reflects the most relevant policy options that have been considered in relation to the respective **(policy issue)** the content and format of periodic reports to customers on the services provided pursuant to Article 30(5) of the IDD (content of periodic reports).

Policy option 1: Reiterating Article 185 of Directive 2009/138/CE (Solvency II)

The periodic communications to customers should only reiterate what was already introduced by Article 185 of Directive 2009/138/CE (Solvency II), thus promoting a consistent approach between IDD and Solvency II.

Policy option 2: Additional information, where relevant.

The periodic communications to customers should complement Article 185 of Directive 2009/138/CE (Solvency II), where relevant, with information such as values of each investment element embedded in the insurance-based investment product and costs

⁵⁹ "Insurance-based investment products are often made available to customers as potential alternatives or substitutes to investment products subject to Directive 2014/65/EU. To deliver consistent investor protection and avoid the risk of regulatory arbitrage, it is important that insurance-based investment products are subject, in addition to the conduct of business standards defined for all insurance products, to specific standards aimed at addressing the investment element embedded in those products. Such specific standards should include provision of appropriate information, requirements for advice to be suitable and restrictions on remuneration".

associated with the transactions and services undertaken on behalf of the customer during the reporting period. A non-exhaustive, yet facultative list of information relevant for insurance-based investment products should be introduced. This would extend the information to be communicated to the customer, but would enhance the level of consumer protection.

Section 4 Analysis of impacts

Policy option 1:

The impact would vary. As the Insurance Distribution Directive has introduced the concept of periodic communications to customers, limiting the information to existing information creates no additional burden for insurance undertakings. Furthermore, the ways of sharing this information with customers should be already established for insurance undertakings under Solvency II and reiterating this information periodically should not create additional compliance costs, as Article 185 of Directive 2009/138/CE (Solvency II) foresees already that the policyholder has to be kept informed throughout the term of the contract of certain changes. Costs for insurance intermediaries would depend on the concrete way of gathering and communicating such information.

Policy option 2:

The impact would vary depending on the relevance of individual information elements which would need to be communicated periodically to customers. A non-exhaustive, yet facultative list of information would need to be created, which requires monitoring and compiling of such information.

Section 5: Comparison of options.

Regarding the policy issue on periodic communications to customers, the Impact Assessment compares the two options developed on the basis of the analysis above.

Option 2 is the preferred option. The optional list of criteria allows for taking into account the type and the complexity of insurance-based investment products involved. Furthermore, option 2 makes the costs associated with the transactions and services undertaken on behalf of the customer transparent, which is required to enhance consumer protection and attain the above mentioned objectives.