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18 March 2016

EIOPA-BoS-16-071

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

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Executive summary

Product Oversight and Governance arrangements relate to the processes which aim to ensure that the interests of the customers are taken into consideration throughout the life cycle of an insurance 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 play a key role in customer protection in ensuring that insurance products meet the needs of the target market and thereby mitigating mis-selling. They are an essential element of the new regulatory requirements under the Directive 2016/97/EU of the European Parliament and of the Council of 20 January 2016 on insurance distribution (recast) (IDD)[1].

The objective of these Preparatory Guidelines is to support and to provide guidance to competent authorities in their preparatory steps leading to a consistent implementation of the organisational requirements on product oversight and governance arrangements of the IDD at an early stage. This allows national authorities to take into account EIOPA's expectations already at the implementation phase, mitigating the risk of different approaches at national level and the need for further alignment for the sake of consistency and a level playing field among Member States at a later point of time.

Moreover, EIOPA will review the Preparatory Guidelines once the deadline for transposition of IDD has passed, to assess to which extent a revision of the Guidelines is necessary, in particular with regard to implementing measures the Commission is empowered to adopt under IDD.

In that respect, on 30 October 2015, EIOPA relaunched a Public Consultation on the revised proposal for Preparatory Guidelines on product oversight and governance arrangements by insurance undertakings and insurance distributors[2]. The consultation period ended on 29 January 2016.

The second Public Consultation followed a decision by the Board of Supervisors to extend the scope of the original draft Guidelines on product oversight and governance arrangements by manufacturers of insurance products adding a chapter to include specific arrangements for distributors.

Whereas the first Public Consultation[3], from October 2014 until January 2015, sought feedback from market participants and stakeholders on Guidelines on product oversight and governance arrangements by insurance undertakings, the second Public Consultation focused on equivalent arrangements for distributors of insurance products.

The feedback from both Public Consultations has been thoroughly analysed and considered. The draft Guidelines have been modified and amended where it seemed necessary and appropriate. Subsequently, the draft Guidelines were submitted to EIOPA's Board of Supervisors. The latter adopted the Guidelines at the beginning of April 2016.

The feedback statement in response to the second Public Consultation and main conclusions EIOPA has taken in view of the feedback are outlined hereafter, followed

[1] OJ L 26, 2.2.2016, p. 19–59

[2] The second public consultation paper can be found under the following link: https://eiopa.europa.eu/Pages/Consultations/EIOPA-CP-15-008-Consultation-Paper-on-POG-Guidelines-for-insurance-undertakings-and-insurance-distributors-.aspx

[3] The first public consultation paper can be found under the following link: https://eiopa.europa.eu/Pages/Consultations/CP-14150-Guidelines-on-product-oversight-amp;-governance-arrangements.aspx

by the revised Preparatory Guidelines (Annex I) and the Impact Assessment (Annex II). The feedback statement to the first Public Consultation can be found in Annex III.

1. Feedback statement to the second Public Consultation

1.1. General comments

a) Findings

The vast majority of respondents recognised the importance of product oversight and governance arrangements and shared the view that product oversight and governance arrangements play a key role in the context of consumer protection, minimising the risk of consumer detriment. The Guidelines would not only enhance the protection of policyholders further, but also strengthen cross-sectoral consistency.

Despite this positive feedback, some respondents raised concerns about the timing of the proposed Guidelines pointing out that the Guidelines would be issued ahead of the Insurance Distribution Directive (IDD) and its future implementing measures which would deal with the same topics. The issuance of Guidelines would not only anticipate and interfere with the work of the European Commission developing delegated acts according to the IDD, but also cause the risk that market participants would be required to adjust internal processes twice within a very short time. In this context, respondents pointed to the risk of discrepancies and differences leading to confusion and additional costs for market participants.

Some respondents also argued that the Guidelines would go beyond the new requirements on product oversight and governance as laid down in Article 25 of the IDD and the empowerment of EIOPA to issue Guidelines as foreseen by the EIOPA Regulation (Regulation (EU) No 1094/2010). Recital 25 of the EIOPA Regulation would empower EIOPA to issue Guidelines only in areas which are not covered by technical standards.

Some respondents asked for more clarity that the Guidelines would not be enforced due to their preparatory nature and sought confirmation that the Guidelines would not be intended to introduce a general price control.

Further questions of respondents concerned the preparatory nature of the Guidelines, the retroactive application to existing products and the division of responsibilities between manufacturers and distributors.

A few respondents also expressed their concerns that too rigid regulatory requirements could hinder product innovation ultimately leading to adverse consequences for customers.

b) EIOPA resolution

The feedback from market participants and stakeholders has confirmed the importance of product oversight and governance arrangements which 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.

EIOPA notes the concerns of market participants with regard to the timing of the Guidelines and possible inconsistencies with the future delegated acts for the IDD, causing additional administrative burden for regulated entities to readjust internal procedures once the delegated acts have come into force.

As regards this issue, EIOPA would like to emphasise the preparatory nature of the Guidelines, which are supposed to clarify EIOPA's expectations with regard to the product oversight and governance arrangements insurance undertakings and insurance distributors are supposed to establish and maintain. In emphasising the preparatory nature of the Guidelines, EIOPA would like to provide early guidance

already during the introduction of the new rules of the IDD which helps to develop a common and consistent application and implementation of the new regulation. In addition, through these Guidelines, EIOPA would like to promote cross-sectoral consistency as ESMA and EBA have already issued Technical Advice and Guidelines on product oversight and governance arrangements respectively.

EIOPA does not share the view that the Guidelines go beyond the IDD and contradict Recital 25 of the EIOPA Regulation. Recital 25 explicitly empowers EIOPA to issue Guidelines or recommendations in areas not covered by regulatory or implementing standards only, but it does not explicitly prohibit EIOPA to issue Guidelines or Recommendations in areas already covered by Level 1 EU legislation.

Furthermore, EIOPA recognises that too strict a regime could potentially have a negative impact on innovation and product development. However, EIOPA is of the view that the Guidelines are adequately balanced to enhance the protection of consumers and to avoid inappropriate obstacles and burdens for product development and innovation which are ultimately supposed to benefit customers as well (see "Impact Assessment" in Annex II).

1.2. Principle of Proportionality

a) Findings

Many respondents highlighted the importance of the principle of proportionality, in particular with regard to small intermediaries. Some respondents stated that product risk is minor for simple, non-life insurance products sold on a mass-market basis and these products should not be subject to the Guidelines. Some respondents further argued that products for professional customers should not be subject to the Guidelines either. Other respondents were of the opinion that the Guidelines should differentiate between different types of distribution channels. Smaller intermediaries should be subject to less onerous requirements, perhaps not being subject to the same level of formality. One respondent said that it should be clear that tied advisers should be able to draw on support from the insurance undertaking to meet the requirements. One respondent said that tailor-made products and occupational pension schemes should not be subject to the Guidelines.

b) EIOPA resolution

EIOPA acknowledges the importance of the principle of proportionality with regard to the Guidelines on product oversight and governance arrangements for manufacturers and distributors of insurance products. The principle of proportionality enables product oversight and governance arrangements to be put in place, which take into account the level of complexity and risks related to the product as well as the nature, scale and complexity of the relevant business of the regulated entity.

However, EIOPA does not consider it appropriate to exempt specific products (such as non-life insurance products), specific services (such as non-advise sale) or services to specific customers (such as professional customers) from the scope of the Guidelines taking into consideration the relevance of these Guidelines from a customer protection point of view.

In order to emphasise the application of the principle of proportionality, an explicit reference has been included in Guideline 1 of Chapter 1 and Guideline 13 of Chapter 2.

1.3. Guideline 13 – Establishment of product oversight and governance arrangements

a) Findings

The majority of respondents agreed that there should be a distinctive set of product oversight and governance rules for manufacturers and distributors which would help to distinguish responsibilities. These arrangements for distributors would focus on the necessary measures distributors should take in preparation for distributing insurance products. Some respondents emphasised that the Guidelines for manufacturers should also apply to distributors which are "de facto" acting as the manufacturer.

It was agreed that the Guidelines for distributors should not transfer the responsibilities of manufacturers to distributors as regards the manufacturers' products. In the same way, it was acknowledged that distributors are ultimately responsible for ensuring that the services are provided in the best interest of the customers.

However, it was pointed out that responsibilities should not be duplicated in order to avoid unnecessary burden for the market participants concerned.

A few respondents argued that the objectives of the product oversight and governance arrangements were unclear as the term "consumer detriment", for example, would be too vague.

Few respondents addressed the wording of Guideline 13 specifically. Those that did, mostly agreed with it, but suggested some changes:

- Four respondents suggested that Guideline 13 should have specific wording on the principle of proportionality. The following wording was suggested as a second paragraph for the Guideline: *'These arrangements shall be specific and proportionate to the size of the distributor and to the risks related to the products'*.

- One respondent asked for clarification of the term 'distribution arrangements'.

- One respondent said that the arrangements must be set out in a unique document, containing all Guidelines. This respondent said that it was not sufficient to refer to existing documents, which may be difficult to bring together. The respondent also suggested that a 'distribution manager' should be appointed, who is responsible for the implementation of the unique written document and for the information of all relevant staff members about it.

- One respondent said that the Guidelines should include wording, based on paragraph 1.1 of the consultation, to clarify the scope of distributor product governance. This could appear in Guideline 13 and explain that: *'The focus of the distributor product governance arrangements is not on the design and subsequent review of the products, but on the necessary steps in preparation of the distribution of the insurance products to the customers'*.

Two respondents questioned whether the Guideline is necessary:

- One said the Guidelines in Chapter 2, referring to Guideline 13 in particular, go beyond what is required in Article 25(1)(6) of the IDD[4].

[4] *"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".*

- One said existing requirements on insurance brokers mean that they are fiduciary trustees of the policyholder and additional consumer protection provisions are unnecessary and will not lead to additional benefit for consumers, but will have a particularly high cost on smaller firms.

b) EIOPA resolution

Regarding the principle of proportionality, it is referred to in point 2.2 above.

EIOPA would like to point out that the term “detriment” has been already used by the joint position of the European Supervisory Authorities on Product Oversight & Governance Processes[5]. From EIOPA’s perspective, it is not appropriate to limit the wording to “unfair detriment” as EIOPA believes that any detriment to the customer should be considered as unfair.

EIOPA follows a broad understanding of “detriment” and considers that it occurs if the manufacturer or distributor does not act in accordance with the best interests of its customers. It, therefore, goes broader than a strict tick-box approach for compliance with regulatory provisions.

1.4. Guideline 14 – Objectives of the product distribution arrangements

a) Findings

The most frequently raised point in relation to Guideline 14 is connected to the use of general terms such as ‘customer detriment’ and ‘proper management of conflicts of interest’ without detailed definitions of these terms.

- Some respondents stressed that the lack of detailed definitions should not lead to more detailed rules being developed to address these concepts in the future.

- Others said it is important that there is clarity that the key point of this Guideline is to ensure the objectives, interests and characteristics of customers are taken into account, rather than to introduce vague new duties on firms. Respondents are concerned that, if this approach is not taken, the impact of the Guideline could be to hinder innovation.

- Some respondents said greater clarification would help. As an example, ‘detriment’ could be clarified by focusing on consumer loss due to rule breaches, which the respondent portrayed as ‘unfair consumer detriment’, rather than losses due to unforeseen circumstances. On the other hand, two respondents said the Guidelines should be kept flexible and very high level, because there are many different legal, operational and distribution structures in insurances companies, as well as many different insurance products ranges offered.

Four respondents said that management of conflicts of interest is subject to a number of provisions in the IDD, and that the delegated acts will specify requirements in more detail. The respondents said that the Guideline should not overlap the IDD provisions.

The next most common observation was that the proportionality principle should be included in the Guideline, where, at present, it is mentioned only in the explanatory text.

One respondent said that it will be difficult to implement this Guideline in practice as the concept of ‘consumer interest’ is very subjective. Ultimately, they said, the

[5] https://eiopa.europa.eu/Publications/Administrative/JC-2013-77__POG_-_Joint_Position_.pdf

responsibility of contracting an insurance policy lies with the consumer rather than firms in developing products.

Another said that the Guidelines are not necessary for brokers as these firms are already subject to provisions on product distribution that aim to prevent consumer harm and take adequate account of consumer interests.

b) EIOPA resolution

Regarding the principle of proportionality, it is referred to in point 2.2 above.

Regarding the use of the term “detriment” it is referred to in point 2.3 above.

EIOPA would like to point out that the explicit reference to the proper management of conflicts of interest aims to clarify that conflicts of interest may also arise at the stage of developing new insurance products and that the undertakings should take the appropriate measures and establish the appropriate procedures to manage these conflicts accordingly.

1.5. Guideline 15 – Role of the management

a) Findings

Some respondents proposed to leave the discretion at national level to determine who is responsible for the establishment of the arrangements and to delete Guideline 15 accordingly.

On the opposite, other stakeholders welcomed the Guideline and focused on the need to further clarify what “management” means in terms of role and responsibility of the subjects involved. A respondent suggests using the same notion used for manufacturer where reference is made to the administrative, management or supervisory body.

Moreover, there are some requests in order to clarify what “endorse” means, in particular whether:

a. such term excludes the possibility for the management to have responsibility for every step taken within the distribution activity; and
b. the external business partner acts under the responsibility of the manufacturer’s management.

One respondent suggests obliging the company to create a distribution function in charge of drafting a specific written document.

b) EIOPA resolution

EIOPA considers it important to specify that the distributor’s highest administrative, management or supervisory body or equivalent structure is ultimately responsible for the establishment of product distribution arrangements.

Whereas it is important that the distributor’s management is ultimately responsible for the product distribution arrangements, it is possible that the tasks are delegated to subordinated staff. EIOPA points out that the Guideline does not require the establishment of a specific function, also taking into account the proportionality principle and the different kind of intermediaries in the market. In view of the diverse legal structures of intermediaries, the wording has been slightly amended by introducing the more general notion of “equivalent structure”.

EIOPA requires that the Guideline aims to provide the ultimate responsibility of the distributor, even in case of outsourcing (internally or externally) of one of all the product distribution arrangements. To this extent, the persons responsible should endorse and be ultimately responsible for the establishment, implementation, subsequent reviews and continued internal compliance with the product distribution arrangements.

1.6. Guideline 16 and Guideline 17 – Obtaining product related information from the manufacturer

a) Findings

The majority of respondents agreed that it is essential that distributors obtain all relevant information on the product in order to fulfil its obligations towards its customers.

However, some respondents expressed their concerns that the obligation to obtain all necessary information on the product approval process would be too far-reaching and burdensome and would not take into account the specificities of different distribution channels, such as independent intermediaries.

Although it was acknowledged that it is essential that the distributors receive complete information on the product, some respondents questions the added value of Guideline 16, taking into consideration that the manufacturers themselves would be required to provide the information on the products to the customers.

Some respondents pointed out that it would be the responsibility of the manufacturer to ensure that the information is accurate and not misleading.

One respondent also asked to explicitly state that the information by the manufacturer could also be provided by training on the product.

b) EIOPA resolution

From EIOPA's perspective, obtaining all relevant information on the product is a necessary prerequisite for providing the distribution activities in the best interest of the customers. This applies equally for tied and independent intermediaries.

EIOPA does not share the view that Guideline 16 and Guideline 17 of Chapter 2 would be redundant in view of Guideline 10 of Chapter 1, requiring the manufacturer to provide product related information to the distributors. In contrast to Guideline 10 of Chapter 1, the addressee of Guideline 16 and Guideline 17 is the distributor (and not the manufacturer). Hence, the Guidelines are nor redundant, but complementary.

The Guidelines do not prescribe a specific way or method on how the product related information should be provided to the distributors. Depending on the respective circumstances, manufacturers may also wish to consider whether training on the product is appropriate to provide all the relevant information on the product or to complement other information material.

1.7. Guideline 18 – Distribution strategy

a) Findings

Most of the respondents were of the opinion that selling outside the target market should be possible. Only two respondents agreed that the distribution strategies of the insurance distributors and manufacturers should be harmonised.

Five respondents referred to the approaches of EBA and ESMA and suggest aligning the Guidelines with their approaches.

Some respondents referred to the responsibility of the distributor to determine whether or not a product is suitable for a consumer (in or outside the target market). There was also a discussion about the relationship between suitability/ appropriateness and defining the target market. One respondent suggested that EIOPA should make clear that defining the target market differs from the process of conducting a suitability and appropriateness test.

A distributor might also have a new insight for consumers outside the target to whom the product might also be compatible.

Some respondents were sceptical of the ability to define a detailed target market in advance and a couple of respondents considered it difficult to define a negative target market.

Some respondents stated that they find the word ‘contrast’ confusing and suggest the word ‘conflict’.

Other remarks: one respondent was of the opinion that consumers should be free to choose a distribution channel they deem appropriate.

One respondent asked for further clarification on ‘distribution strategy’ as it could be interpreted very broadly (encompassing the firm’s wider business model).

b) EIOPA resolution

EIOPA is of the opinion that the distributor could sell products on an exceptional basis to customers outside the target market where certain conditions are fulfilled. Where the distributor can justify and demonstrate that the product is suitable for the relevant customer, the distributor may distribute products to customers who would be considered outside the target market identified by the manufacturer. EIOPA notes that in these cases the distributor must document the suitability of the product in accordance with Guideline 21 of Chapter 2. This approach is in line with ESMA and EBA approaches. Furthermore, EIOPA considers information about the amount of sales made outside the target market to be exchanged between the manufacturer and the distributor as set out in Guideline 20.

EIOPA confirms that this Guideline applies without prejudice to any demands and needs, suitability or appropriateness assessment to be subsequently carried out by the distributor when providing services to the individual customer at the point of sale. This is clarified in the Guidelines.

EIOPA replaced the word ‘contrast’ with ‘contradict’ to give greater clarity and address concerns raised in the consultation.

1.8. Guideline 19 – Regular review of the distribution arrangements

a) Findings

Most respondents welcome the application of the proportionality principle in the sense that no defined interval for review is prescribed. However, a few respondents have raised concerns on specific issues:

Even it is not the subject of this Guideline as such, some respondents emphasised the importance of the on-going monitoring of the product by the manufacturer. For one respondent, *“the ongoing results of the product monitoring must be an essential part of the constant mutual exchange of information and experiences between*

manufacturers and distributors and therefore be an essential part of the regular review of the product distribution strategy". On the other side, a few respondents raised concerns about the on-going aspect of monitoring requirement and pointed out that *"this would be better phrased as a requirement for the manufacturer to have in place a strategy for responding appropriately to feedback from the target market, which is also consistent with Guideline 20 for distributors on the provision of sale information to the manufacturer".*

The question of the alignment of the distribution strategy between the distributor and the manufacturer was raised by another respondent who emphasized that *"manufacturers must make sure to align their distribution strategy with that of the distributor. The main responsibility for this should lie with the manufacturer of the insurance products"*.

b) EIOPA resolution

EIOPA notes that most of the respondents welcome the application of the proportionality principle in the sense that no defined interval for review is prescribed. EIOPA considers it would be inappropriate to set any fixed interval for reviewing distribution arrangements as those could widely differ according to the size, the nature and the complexity of the products distributed. Therefore EIOPA suggests keeping the text unchanged.

1.9. Guideline 20 – Provision of sale information to the manufacturer

a) Findings

Several respondents warned against the administrative burden if the Guideline is implemented in a too restrictive way. Therefore, proportionality must be taken into account.

While many respondents agreed that the information to be given should include the amount of sales, as well as information related to complaints (frequencies, acceptance rates, average pay-out etc.), most of the respondents coming from the industry agreed with paragraph 1.12 in the Consultation Paper which states that *"[…] this does not mean that the distributor needs to report every sale to manufacturers, or that the manufacturer must confirm each transaction was distributed to the correct market".* The exchange of information should not cover all the individual contracts, but aim to avoid a systematic misalignment between products and customer needs. Also, it should not restrict any sale outside the target market.

A few respondents pointed out some issues with regards to the wording of the Guideline. In particular, the words "with undue delay" are seen as too restrictive. The use of the words "customer detriment" is also criticized as it is an undefined legal term which could be interpreted as every negative impact (such as market development) that a customer may face. Therefore it is proposed to rephrase the sentence as follows: "unfair customer detriment".

Finally, few respondents emphasized the Guideline should not lead to a transfer of responsibility from the manufacturer to the distributor on monitoring or information flows.

b) EIOPA resolution

EIOPA notes the agreement on the text on exchange of information included in the explanatory text. Therefore, EIOPA plans to keep this provision.

EIOPA notes the feedback from several stakeholders who consider the terms "customer detriment" and "undue delay" to be unclear. EIOPA considers that adding the term "unfair" before "customer detriment" – as suggested by stakeholders- would be inappropriate as it could imply that "fair customer detriment" may be possible. That is why EIOPA considers it should not be included. Concerning the term "undue delay", EIOPA does not share the opinion that it is unclear. On the contrary, it leaves room for manoeuver for the distributor as it does not prescribe any pre-determined time period. Therefore, EIOPA suggests keeping the text unchanged.

1.10. Guideline 21 – Documentation

a) Findings

Some respondents warned against an unnecessary administrative burden, in particular for small distributors, and expressed their preference to limit the documentation to "all essential actions" (instead of "all relevant actions").

It was also noted that the Guideline would not entail any indication about the length of time during which the entities would be expected to keep the documentation.

b) EIOPA resolution

From an internal governance perspective and supervisory point of view, EIOPA considers it important that all relevant actions and measures taken by the regulated entity are duly documented.

As explained in the Explanatory Text in order to clarify the length of time, it is recommended that the documentation is kept for a period of five years which is in line with the approach taken by MiFID I[6] and MiFID II[7].

[6] Article 51(1)of MiFID I implementing Directive (Directive 2006/73/EC): *"Member States shall require investment firms to retain all the records required under Directive 2004/39/EC and its implementing measures for a period of at least five years".*

[7] Article 16(7) of MiFID II (Directive 2014/65/EU): *"The records kept in accordance with this paragraph shall be provided to the client involved upon request and shall be kept for a period of five years and, where requested by the competent authority, for a period of up to seven years".*

2. Annex I - Preparatory Guidelines

1. Introduction

1.1. According to Article 9(2) and Article 16 of Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (hereinafter "EIOPA Regulation")[8], EIOPA is issuing Preparatory Guidelines addressed to competent authorities on how to proceed in the preparatory period leading up to the transposition of Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution (hereinafter "IDD")[9] and the application of the delegated acts envisaged thereunder. The Preparatory Guidelines were issued for the purpose of establishing consistent, efficient and effective supervisory practices with regard to product oversight and governance arrangements as outlined in Article 25 of the IDD and to bridge the time until those provisions in the IDD are fully applicable.

1.2. Product oversight and governance arrangements play a key role in customer protection in ensuring that insurance products meet the needs of the target market and thereby mitigating mis-selling. They are an essential element of the new regulatory requirements under the IDD. Because of their relevance in terms of customer protection, it is of utmost importance that the new requirements are properly implemented from the outset and applied as early as possible. This justifies the issuance of preparatory Guidelines to ensure that competent authorities follow a consistent and convergent approach with respect to the preparation of implementation of the IDD.

1.3. The Preparatory Guidelines do not only aim to support competent authorities when implementing the IDD, but also aim to achieve cross-sectoral consistency. As the European Markets Supervisory Authority (ESMA)[10] and the European Banking Authority (EBA)[11] have already issued guidance on product oversight and governance arrangements, the Guidelines seek to ensure a level playing field in financial markets and prevent regulatory arbitrage.

1.4. Due to their nature as preparatory Guidelines, it is not the intention of the Guidelines to necessitate enforcement action by competent authorities if they become aware of practices which are not fully in line with the Guidelines, but that competent authorities discuss with market participants possible ways for appropriate remedial action. Therefore, the objective of these preparatory Guidelines is to support and to provide guidance to competent authorities in their preparatory steps leading to a consistent implementation of the organisational requirements on product oversight and governance arrangements of the IDD at an early stage. This allows competent authorities to

[8] OJ L 331, 15.12.2010, p. 48.

[9] OJ L 26, 2.2.2016, p. 19.

[10] ESMA's technical advice to the European Commission on delegated acts to product oversight and governance arrangements in MiFID II: http://www.esma.europa.eu/system/files/2014-1569_final_report_-_esmas_technical_advice_to_the_commission_on_mifid_ii_and_mifir.pdf

[11] EBA Guidelines on product oversight and governance arrangements for retail banking products: http://www.eba.europa.eu/documents/10180/1141044/EBA-GL-2015-18+Guidelines+on+product+oversight+and+governance.pdf/d84c9682-4f0b-493a-af45-acbb79c75bfa

take into account EIOPA's expectation already at the implementation phase mitigating the risk of different approaches on national level and the need for further alignment for the sake of consistency and a level playing field among Member States at a later point of time.

1.5. Moreover, EIOPA will review the preparatory Guidelines once the delegated acts under the IDD have been adopted to assess to which extent a revision of the Guidelines is necessary.

1.6. According to the Joint Position of the European Supervisory Authorities on Manufacturers' Product Oversight & Governance Processes[12], the Guidelines take into account Recital 16 and 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")[13] that provide for the following:

- "The main objective of insurance and reinsurance regulation and supervision is the adequate protection of policyholders and beneficiaries….."[14],
- "Member States shall ensure that the supervisory authorities are provided with the necessary means, and have the relevant expertise, capacity, and mandate to achieve the main objective of supervision, namely the protection of policy holders and beneficiaries"[15].
- "Member States shall ensure that the administrative, management or supervisory body of the insurance or reinsurance undertaking has the ultimate responsibility for the compliance, by the undertaking concerned, with the laws, regulations and administrative provisions adopted pursuant to this Directive"[16],
- "Member States shall require all insurance and reinsurance undertakings to have in place an effective system of governance which provides for sound and prudent management of the business"[17].

1.7. The Preparatory Guidelines take also into account the provisions on product oversight and governance arrangements of the IDD as laid down in Article 25 thereof, stating the following:

- *"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."*

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[12] https://eiopa.europa.eu/Publications/Administrative/JC-2013-77__POG_-_Joint_Position_.pdf

[13] OJ L 335,17.12.2009, p.1.
[14] Recital 16 of Solvency II
[15] Article 27 of Solvency II
[16] Article 40 of Solvency II
[17] Article 41(1) first para of Solvency II

- *"The product approval process shall specify an identified target market of customers for each product and ensure that all relevant risks to such identified target market are assessed, 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 any distributor 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 advices 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."*

1.8. The product oversight and governance arrangements should be primarily considered as an implementation of the fundamental objective of insurance supervision, namely the protection of policyholders and beneficiaries as stated in Solvency II.

1.9. Due to their purpose and objectives the organisational arrangements as outlined in the Guidelines have a substantial link to the system of governance under the Solvency II framework, requiring firms to have a sound and prudent management of the business under a risk based approach including an appropriate risk management system. Organisational arrangements which aim to ensure a correct design of the insurance products fall within the system of governance of the insurance undertaking. The Guidelines introduce very explicit processes and measures with regard to the design, development and monitoring of new insurance products.

1.10. In this context, the IDD will provide for a detailed regulation which takes into account the specific profiles of transparency and protection of the customer with regard to both the design of the product and its distribution. On this basis, the product oversight and governance arrangements have their foundation in Solvency II as well as in the IDD, the latter specifying the requirements from a customer protection point of view and adding requirements for distributors, which are not in the scope of the Solvency II framework.

1.11. These Guidelines are addressed to competent authorities. Notwithstanding the explicit references to insurance undertakings and insurance distributors, this document is not to be read as imposing any direct requirements upon those financial institutions. Financial institutions are expected to comply with the supervisory or regulatory framework applied by their competent authority.

1.12. The arrangements outlined in these Guidelines refer to internal processes, functions and strategies for designing and bringing products to the market, monitoring and reviewing them over their life cycle. The arrangements differ depending on whether the regulated entities are acting as manufacturer and/or distributors of insurance products and refer to steps such as:

(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 mitigate 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.

1.13. The administrative, management or supervisory body of the insurance undertaking is responsible for the establishment and subsequent reviews of the product oversight and governance arrangements. However, implementing product oversight and governance arrangements should not be understood as introducing a new key function for insurance undertakings. Moreover, these arrangements are not necessarily linked with the risk management, internal audit, actuarial or compliance functions of insurance undertakings, as prescribed by Solvency II.

1.14. Product oversight and governance arrangements are complementary to point of sale disclosure rules (where applicable) which require to proactively disclose a description of the main characteristics of the product, its risks and the total price of the product to be paid by the customer, including all related fees, charges and expenses.

1.15. 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.

1.16. The Guidelines cover arrangements that generally apply to all insurance undertakings and all insurance distributors, including any natural or legal person pursing the activity of insurance distribution, independent from the question whether these activities are pursued as a principal professional activity or on an ancillary basis, by an independent broker or by a tied agent, provided that they fall within the scope of the IDD. However, competent authorities should take a proportionate and risk-based approach when applying these Guidelines. These Guidelines 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.

1.17. Competent authorities shall make every effort to comply with these Guidelines with regard to products which are newly designed or substantially modified. Competent authorities may wish to consider requiring, as of the date of entry into force of national measures implementing these Guidelines, compliance

with, at least Guideline 8 (Product monitoring) and Guideline 9 (Remedial action) of Chapter I for products still being distributed or brought to the market prior to that date.

1.18. In applying these Guidelines, competent authorities also need to give due consideration, where relevant, to EIOPA's Guidelines on the System of Governance under Solvency II[18], EIOPA's Guidelines on Complaints-Handling by Insurance Undertakings[19] as well as EIOPA's Guidelines on Complaints-Handling by Insurance Intermediaries[20].

1.19. For the purpose of these Guidelines, the following definitions have been developed:

- *Manufacturer* means an insurance undertaking and an insurance intermediary that manufacture insurance products for the sale to customers.
- *Target market* means the group(s) of customers for whom the manufacturer is designing the product.
- *Distribution strategy* means a strategy which addresses the question on how insurance products are distributed to the customers, in particular whether the product should be sold only where advice is given.
- *Products* means the classes of non-life insurance and life insurance listed in Annex I and Annex II of Solvency II.

1.20. If not defined in these Guidelines, the terms have the meaning defined in the legal acts referred to in the introduction.

[18] Available at https://eiopa.europa.eu/GuidelinesSII/EIOPA_Guidelines_on_System_of_Governance_EN.pdf#search=system%20of%20governance%20Guidelines

[19] Available at https://eiopa.europa.eu/publications/eiopa-Guidelines/index.html.

[20] Available at https://eiopa.europa.eu/publications/eiopa-Guidelines/Guidelines-on-complaints-handling-by-insurance-intermediaries

Chapter 1 - Preparatory Guidelines for insurance undertakings and insurance intermediaries which manufacture insurance products for sale to customers

Guideline 1 - Establishment of product oversight and governance arrangements

1.21. The manufacturer should establish and implement 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).

1.22. 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 regulated entity.

1.23. The manufacturer should 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.

Guideline 2 – Objectives of the product oversight and governance arrangements

1.24. The product oversight and governance arrangements should aim to prevent and 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.

Guideline 3 – Role of management

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

Guideline 4 - Review of product governance and oversight arrangements

1.26. The manufacturer should 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.

Guideline 5 – Target market

1.27. The manufacturer should include in its product oversight and governance arrangements suitable steps in order to identify the relevant target market of a product.

1.28. The manufacturer should 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.

1.29. When deciding whether a product is aligned with the interests, objectives and characteristics or not of a particular target market, the manufacturer should consider the level of information available to the target market and the degree of financial capability and literacy of the target market.

1.30. 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.

Guideline 6 – Skills, knowledge and expertise of personnel involved in designing products

1.31. The manufacturer should 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.

Guideline 7 - Product testing

1.32. 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. The product testing should assess if the product is in line with the objectives for the target market over the lifetime of the product.

1.33. The manufacturer should 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.

1.34. The manufacturer should 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.

Guideline 8 - Product monitoring

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

Guideline 9 - Remedial action

1.36. 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 should take appropriate action to mitigate the situation and prevent the re-occurrence of detriment.

1.37. If relevant, the manufacturer should notify any relevant remedial action promptly to the distributors involved and to the customers.

Guideline 10 - Distribution channels

1.38. The manufacturer should select distribution channels that are appropriate for the target market considering the particular characteristics of the product.

1.39. The manufacturer should select distributors with appropriate care.

1.40. The manufacturer should provide information, including the details of the products to distributors, of an adequate standard, which is clear, precise and up-to-date.

1.41. The information given to distributors should 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.

1.42. The manufacturer should take all reasonable steps to monitor that distribution channels act in compliance with the objectives of the manufacturer's product oversight and governance arrangements.

1.43. The manufacturer should examine, on a regular basis, whether the product is distributed to customers belonging to the relevant target market.

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

Guideline 11 - Outsourcing of the product design

1.45. The manufacturer should retain full responsibility for compliance with product oversight and governance arrangements as described in these Guidelines when it designates a third party to design products on their behalf.

Guideline 12 - Documentation of product governance and oversight arrangements

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

Chapter 2 - Preparatory Guidelines for insurance distributors which distribute insurance products which they do not manufacture

Guideline 13 - Establishment of product distribution arrangements

1.47. The distributor should establish and implement product distribution arrangements that set out appropriate measures and procedures for considering the range of products and services the 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).

1.48. 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 regulated entity.

1.49. The distributor should set out the product distribution arrangements in a written document and make it available to its relevant staff.

Guideline 14 - Objectives of the product distribution arrangements

1.50. The product distribution arrangements should aim to prevent and 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.

Guideline 15 – Role of management

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

Guideline 16 – Obtaining all necessary information on the target market from the manufacturer

1.52. The product distribution arrangements should aim to ensure that the 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.

Guideline 17 – Obtaining all other necessary information on the product from the manufacturer

1.53. The product distribution arrangements should aim to ensure that the 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.

Guideline 18 – Distribution strategy

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

Guideline 19 – Regular review of product distribution arrangements

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

Guideline 20 – Provision of sale information to the manufacturer

1.56. The distributor should 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.

Guideline 21 – Documentation

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

Compliance and Reporting Rules

1.58. This document contains Guidelines issued under Article 16 of the EIOPA Regulation. In accordance with Article 16(3) of the EIOPA Regulation, competent authorities and financial institutions shall make every effort to comply with Guidelines and recommendations.

1.59. Competent authorities that comply or intend to comply with these Guidelines should incorporate them into their regulatory or supervisory framework in an appropriate manner.

1.60. Competent authorities shall confirm to EIOPA whether they comply or intend to comply with these Guidelines, with reasons for non-compliance, within two months after the issuance of the translated versions.

1.61. In the absence of a response by this deadline, competent authorities will be considered as non-compliant to the reporting and reported as such.

Final Provision on Reviews

1.62. The present Guidelines shall be subject to a review by EIOPA after the adoption of the delegated acts referred to in Article 25(2) of the IDD.

2. Explanatory text

Chapter 1 - Preparatory Guidelines for insurance undertakings and insurance intermediaries which manufacture insurance products for sale to customers

Guideline 1 - Establishment of product oversight and governance arrangements

The manufacturer should establish and implement 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).

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 regulated entity.

The manufacturer should 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.

1.1. This does not necessarily mean that new or fully separate arrangements are drafted; it can be sufficient to refer to existing documents where these contain the relevant information and just record additional information if and insofar as this is necessary. The manufacturer may combine written arrangements as it sees fit in line with its organisational structure and processes.

1.2. A proper implementation of product oversight and governance arrangements ensures that all relevant staff members have knowledge of and observe these arrangements for their respective area of activities. It also ensures that any changes to the arrangements are promptly communicated to them.

1.3. Insurance intermediaries which do not manufacture insurance products for sale to customers but confine their activities to the distribution of insurance products are addressed in Chapter 2.

Guideline 2 - Objectives of the product oversight and governance arrangements

The product oversight and governance arrangements should aim to prevent and 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.

1.4. As explained in the scope section, the product oversight and governance arrangements which the insurance undertaking develop, may vary depending on the product or the line of business in accordance with the principle of proportionality taking into consideration the nature, scale and complexity of the relevant business of the manufacturer and the complexity of the product. The product oversight and governance arrangements need to be appropriate to account for risks borne by policyholders for a product.

1.5. Product oversight and governance arrangements are without prejudice to basic principles in insurance, in particular the principle of solidarity and mathematical methods. The interest of customers that must 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.

Guideline 3 - Role of management

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

1.6. The manufacturer's administrative, management or supervisory body ensures that the product oversight and governance arrangements are appropriately designed and implemented into the governmental structures of the manufacturer. This Guideline clarifies that the ultimate responsibility for the procedures and measures lies with the top management of an entity.

1.7. The manufacturer's administrative, management or supervisory body can consider involving any relevant key functions in the establishment and subsequent reviews of the product oversight and governance arrangements.

1.8. The product oversight and governance arrangements as well as any changes are subject to prior approval by the manufacturer's administrative, management or supervisory body.

Guideline 4 - Review of product oversight and governance arrangements

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

1.9. To this end, a minimum frequency for regular review and updates is to be established. In addition, relevant factors are to be identified which – once they occur – could trigger an ad hoc review of the product oversight and governance arrangements. Such factors could be, for example, significant changes in the retail strategy, changes in the complexity of the product lines and changes in the distribution channels.

1.10. Any review of the product oversight and governance arrangements has to be appropriately documented. The documentation needs to record who conducted the review and to include any suggested recommendations and the decisions subsequently taken by the manufacturer's administrative, management or supervisory body in respect of those recommendations as well as the reasons for them.

Guideline 5 - Target market

The manufacturer should include in its product oversight and governance arrangements suitable steps in order to identify the relevant target market of a product.

The manufacturer should 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.

When deciding whether a product is aligned with the interests, objectives and characteristics or not of a particular target market, the manufacturer should consider assessing the level of information available to the target market and the degree of financial capability and literacy of the target market.

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.

1.11. To identify the target market, manufacturers can consider the following:

- tax status implications for different products;
- level of risks of the product to be designed;
- insurance coverage and exclusions;
- liquidity accessibility;
- demographic factors;
- level of knowledge and understanding of the complexity of the product;
- financial capability.

1.12. When identifying the target market, the manufacturer needs to consider the charges and risks that products may present and consider if they are compatible for the identified target market.

1.13. Moreover, in certain cases 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). Therefore, identifying for whom the product may not be suitable is helpful in order to get a clear picture of the boundaries of the target market.

1.14. The identification of the target market is crucial to enable distributors to understand to whom the product can be sold.

Guideline 6 - Skills, knowledge and expertise of personnel involved in designing products

The manufacturer should 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.

1.15. The requirement is derived from the general principle of good governance stated in Article 258 (1)(e) of Commission Delegated Regulation (EU) No 2015/35 [21], according to which insurance undertakings are required to employ appropriately qualified personnel.

1.16. As necessary, the staff involved in designing products receives, 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.

Guideline 7 - Product testing

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. The product testing should assess if the product is in line with the objectives for the target market over the lifetime of the product.

The manufacturer should 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.

The manufacturer should carry out product testing in qualitative and, where appropriate, in quantifiable manner depending on the type and nature of the product and the related risk of detriment to customer.

1.17. When testing a product, manufacturers need to consider all significant risks to which customers subscribing to that product would be exposed to in order to align the product with the interest of the target market.

1.18. For instance, manufacturers need to make appropriate product changes before the launch, where the product testing and/or scenario analysis gives rise to poor results for the target market.

1.19. 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.

1.20. Keeping in mind the objectives of the defined target market, the assessment may consider the following question:

- 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 close an all-risk policy for an old car?

[21] OJ L 12, 17.01.2015, p. 1.

- What if certain circumstances during the lifetime of the product change? For instance, what happens with the premium of unemployment insurance if a person gets unemployed, disabled or experiences other life events? What are the consequences for the coverage of a payment protection insurance product when a married couple divorces?
- What happens to the (guaranteed) coverage (insured amounts) of my fire and theft insurance when my income changes?

1.21. In addition to the question above, more specifically for insurance-based investment products, the assessment may consider 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?

1.22. In addition to the questions above, more specifically for pure protection life insurance products, the assessment may consider also the following questions:

- What if the premises change, for instance mortality rate increases, or technical interest rate increases?
- Does the benefit cover sufficiently future needs of beneficiary?

1.23. In the case of a non-life insurance, the assessment may consider 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 monetary 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?

1.24. The manufacturer of an insurance-based investment product will in the future 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.

Guideline 8 - Product monitoring

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

1.25. As part of the product monitoring process, the manufacturer takes 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.

1.26. For instance, the claims ratio or cause of complaints could be used as a tool to assess whether certain products are of good value to customers. These are two tools which indicate whether customers are getting a fair deal (value for money).

Guideline 9 - Remedial action

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 should take appropriate action to mitigate the situation and prevent the re-occurrence of detriment.

If relevant, the manufacturer should notify any relevant remedial action promptly to the distributors involved and to the customers.

1.27. 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 distributor or through a complaint.

1.28. 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.

1.29. 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.

1.30. As a general rule, 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.

1.31. In order to prevent customer detriment efficiently, it might also be necessary that the manufacturer notifies the remedial action taken to the distributors involved and to the customers. 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.

Guideline 10 - Distribution channels

The manufacturer should select distribution channels that are appropriate for the target market considering the particular characteristics of the product.

The manufacturer should select distributors with appropriate care.

The manufacturer should provide information, including the details of the products to distributors, of an adequate standard, clear, precise and up-to-date.

The information given to distributors should be sufficient to enable them to:

- understand and place the product properly on the target market, and
- 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.

The manufacturer should take all reasonable steps to ensure that distribution channels act in compliance with the objectives of the manufacturer's product oversight and governance arrangements.

The manufacturer should monitor, on a regular basis, whether the product is distributed to customers belonging to the relevant target market.

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

1.32. The manufacturer needs to select 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.

1.33. The manufacturer's information to the distributor does not seek to substitute the specification of the demands and needs of a specific customer and the underlying reasons for any advice given by the distributor according to Article 12(3) of Directive 2002/92/EC.

1.34. The manufacturer informs the distributor about who is the target market that the product has been designed for.

1.35. Manufacturers may survey a number of customers to find out if they understood the product features and to see if they fit into the target market. If they do not, then the manufacturer needs to consider what this means – is its information material adequate? Is it providing enough information to distributors? Is it working right with the distributors?

1.36. If the manufacturer identifies problems with the selected distribution channels, (i.e. when the distributor is offering the product to customers for whom it is not compatible) they need to take appropriate actions. In the case of independent distributors, manufacturers might, for instance, need to consider ceasing making available the relevant products to the distributor not meeting the product oversight and governance objectives of the manufacturer.

Guideline 12 - Documentation of product governance and oversight arrangements

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

1.37. Without prejudice to national law, it is recommended that the records of the relevant documentation are kept in a durable medium for a minimum period of five years. The period starts when the relevant action is taken. There might be situations where it is appropriate to keep the documentation for a longer period of time, e.g. due to the lifetime of a product.

Chapter 2 - Preparatory Guidelines for insurance distributors which distribute insurance products which they do not manufacture

If not otherwise stated, the explanatory text of the relevant Guidelines in Chapter 1 also applies to the corresponding Guidelines in Chapter 2.

Guideline 13 - Establishment of product distribution arrangements

The distributor should establish and implement product distribution arrangements that set out appropriate measures and procedures for considering the range of products and services the 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).

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 regulated entity.

The distributor should set out the product distribution arrangements in a written document and make it available to its relevant staff.

Guideline 14 - Objectives of the product distribution arrangements

The product distribution arrangements should aim to prevent and 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.

1.38. Guidelines 13 and 14 set out the general principle that distributors need to establish appropriate measures and procedures with regard to the insurance products they intend to distribute. In contrast with the Guidelines for manufacturers (see Chapter 1) the focus of the Guidelines applicable to distributors is not on the design and subsequent review of the products, but on 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).

1.39. The Guidelines acknowledge the importance of establishing adequate processes before insurance products are distributed to customers. Already at this stage 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. The Guidelines are not intended to mean that the distributor should make a previous selection of products or that the distributor should identify its own target market.

1.40. The Guidelines generally apply to all insurance distributors, including any natural or legal person pursing the activity of insurance distribution, independent from the question whether these activities are pursued as a principal professional activity or on an ancillary basis, by an independent broker or by a tied agent. However, competent authorities need to take a proportionate and risk-based approach when applying these Guidelines. That means that competent authorities need to take into account the specific circumstances of the individual distributors, such as the nature, scale and complexity of the relevant business, as well as the risks related to the products. The authorities should also take into account whether the distribution activity is the principal professional activity or an ancillary activity, whether the distributor is acting as tied agent or independent broker. Consequently, it is understood that some firms, in particular small firms, may not have the same formal governance process as larger distributors. For sole traders this may even imply that all duties and responsibilities resulting from the Guidelines are assumed by one single person.

1.41. The Guidelines for distributors provide a separate set of Guidelines with specific duties and responsibilities for distributors to be distinguished from those applicable to manufacturers. The Guidelines for distributors do not aim to extend and transfer the responsibilities of manufacturers vis-à-vis their products, but to establish a distinct set of duties distributors should comply with when selecting products for distribution.

Guideline 15 - Role of management

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

1.42. This Guideline is primarily aimed at entities where the tasks related to the product distribution arrangements are delegated either internally or even externally (e.g. in cases of outsourcing) and clarifies that the ultimate responsibility for the organisational measures and procedures lies with the top management of the distributor. For sole traders it is evident that they bear the responsibility for their entire business. The Guideline aims to clarify the ultimate responsibility within a given structure, only.

Guideline 16 - Obtaining all necessary information on the target market from the manufacturer

The product distribution arrangements should aim to ensure that the 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 groups of customers for which the product is not designed for.

1.43. An important prerequisite to setting up a distribution strategy (as required under Guideline 18 of Chapter 2) is that the distributor has detailed knowledge about the approval process of the manufacturer, in particular the target market of the individual insurance product. This information helps the distributor to select the insurance products the distributor intends to distribute and to assess to which customers the distributor may advertise and promote the individual insurance products.

Guideline 17 - Obtaining all other necessary information on the product from the manufacturer

The product distribution arrangements should aim to ensure that the 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.

1.44. This Guideline complements Guideline 16 and requires the distributor to establish appropriate arrangements to obtain from the manufacturer all relevant information on the product which is necessary to carry out its distribution activities. The purpose of this Guideline is to ensure that the distributor receives all product related information about which the distributor is required to inform the customers pursuant to the information requirements and conduct of business rules of the IDD.

Guideline 18 - Distribution strategy

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

1.45. The distribution strategy addresses the question on how insurance products are distributed to customers. The distribution strategy needs to consider aspects such as whether the product should only be sold with advice, or if the product should be made available only to particular groups in the firm's client bank.

1.46. Guideline 18 emphasizes that in cases where the distributor sets up or follows an 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 that the insurance products are distributed to customers which are not part of target market identified by the manufacturer of the respective insurance product. The distribution strategy may also outline circumstances under which the distribution of insurance products to customers outside of the target market is permitted exceptionally.

1.47. If the distributor can justify and demonstrate that the product fits with the best interest of the relevant customer, the distributor may exceptionally distribute insurance products to a customer, who is outside of the target market identified by the manufacturer. In these exceptional cases, the distributor has to duly document this in accordance with Guideline 21 of this Chapter.

1.48. This Guideline applies without prejudice to any assessment of demands and needs, suitability or appropriateness to be subsequently carried out by the distributor when providing services to the individual customer at the point of sale.

Guideline 19 - Regular review of product distribution arrangements

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

1.49. As the product distribution arrangements are an important element to prevent and mitigate detriment to the customers, it seems appropriate that distributors regularly review whether their arrangements are still valid and up to date. This applies in particular with regard to the distribution strategy for each insurance product taking into consideration that the target market (as initially identified by the manufacturer) may be redefined in the course of time due to external factors (such as market developments).

Guideline 20 - Provision of sale information to the manufacturer

The distributor should inform the manufacturer without undue delay when 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.

1.50. Guideline 20 pursues the objective to enhance the exchange of information between manufacturer and distributor to facilitate the market monitoring of the manufacturer. This does not mean that the distributors need to periodically report every sale to manufacturers, or that the manufacturer must confirm each transaction was distributed to the correct target market. Ad hoc information could include, for example, information about 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. The obligation to provide sales data shall aim to enable the manufacturer to monitor the product and to check that the product remains consistent with the needs, characteristics and objectives of the target market as defined by the manufacturer itself.

1.51. This Guideline is in line with Guideline 8 of Chapter I requiring the manufacturer to monitor on an on-going basis that the product continues to be aligned with the interests, objectives and characteristics of the target market.

Guideline 21 - Documentation

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

1.52. Without prejudice to national law, it is recommended that the records of the relevant documentation are kept in a durable medium for a minimum period of five years. The period starts when the relevant action is taken. There might be situations where it is appropriate to keep the documentation for a longer period of time, e.g. due to the lifetime of a product.

1.53. As part of the action required under Guideline 21, the distributor should also document that he has received all necessary information from the manufacturer according to Guideline 16 and 17 of this Chapter.

3. Annex II – Impact Assessment

1. Procedural issues and consultation of interested parties

As per Article 16(2) of the EIOPA Regulation, any Guidelines developed by EIOPA shall, where appropriate, perform an Impact Assessment (IA) which analyses 'the potential related costs and benefits' of the proposals.

This Impact Assessment document presents the key policy questions and the associated policy options considered in developing the draft Guidelines on product oversight and governance arrangements by insurance undertakings and insurance distributors.

The content of this Impact Assessment document was considered and developed by the EIOPA Committee on Consumer Protection and Financial Innovation (CCPFI).

EIOPA benefitted from the insights of its Members regarding their experience with product oversight and governance issues. Where relevant, references to these findings are made throughout this Impact Assessment.

An initial version of the Guidelines was drafted and subject to public consultation together with its impact assessment between 27th October 2014 and 23rd of January 2015. Stakeholders' responses to public consultation were duly analysed and served as a valuable input for a first revision of the Guidelines. In accordance with Article 16 of the EIOPA Regulation the Insurance and Reinsurance Stakeholder Group was consulted.

In view of relevant on-going regulatory developments (in particular, negotiations on the IDD) EIOPA decided to further revise the scope and content of the draft Guidelines (following the results of such negotiations). With regard to Chapter 1 and the Guidelines for insurance undertakings manufacturing insurance products the wording has been slightly redrafted by replacing "consumers" with "customers" to be better aligned with the wording of the IDD. Furthermore (a new) Chapter 2 has been included entailing product distribution arrangements for entities distributing insurance products only. Consequently a new version of the Guidelines has been drafted and its impact assessment has been amended accordingly. The new draft Guidelines and their impact assessment were subject to public consultation between 30th October 2015 and 29th January 2016. Stakeholders' responses to public consultation were duly analysed and considered for the review of the Guidelines; in particular, certain additional clarifications have been included in the text. For example, Guideline 1 of Chapter 1 and Guideline 13 of Chapter 2 have been amended to emphasise the application of the principle of proportionality taking into account the level of complexity and the risks related to the different products as well as the nature, scale and complexity of the relevant business of the regulated entities.

2. Problem definition

In recent years customers across Europe have been confronted with financial products that did not meet their expectations, notably because of flaws in the products and/or flaws in the selling process.

In particular, the insurance industry has evolved to design products aimed at purposes beyond mere risk coverage e.g. investment and money saving. As a consequence, insurance products and contracts tend to be more complex and cover risks that may not be easily perceived by the average customer.

Moreover, some product manufacturers designing the products may not give proper consideration to the needs of their target market, which may lead to customer detriment.

The increasing complexity and variety of insurance products has also posed 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. This lack of information on the products causes the risk that distributors advising on or proposing insurance products do not act in accordance with the best interest of their customers.

There have been concrete cases of customer detriment due to poor product design and/or insufficient product governance in the past e.g. in CZ, ES, FR, HU, IE, IT, LT, NL, SE and UK. According to the experience of national authorities this problem does not only occur with regard to life insurance products (e. g. problems related to unit linked life insurance products have been reported), but also with regard to non-life insurance products (e. g. problems related to payment protection insurances have been reported). National authorities also observed a significant number of instances in which products didn't fit with the customer's profile and didn't meet the expectations of the customers. They also reported about cases where product provided a very limited coverage excluding main risks to which policyholders were typically exposed to.

This reflected in the confidence in financial institutions and financial products across the sector. Defective products may also affect financial stability if sold on a mass scale. A proper mix of adequate regulatory framework and supervision, healthy competition, financial education and a focus on customer needs by financial institutions is needed to restore customer confidence and with it the effective functioning of financial markets.

Supervision of insurance products plays a special role for customers' protection. It is one of the key areas supervisors need to focus on. From that supervisory perspective, customer detriment caused by the purchase of unsuitable and/or poorly designed products can be addressed, among others as follows: i) ex post by product interventions or banning of products causing customer detriment or ii) ex ante by addressing the product design process and selling practices.

The EIOPA Guidelines on product oversight and product governance try to target the product design and put forward requirements for manufacturers and distributors of insurance products. In addition, the Guidelines introduce some key elements for the collaboration between manufacturers and distributors emphasising the importance of strengthening the exchange of product related information. These requirements could be seen as a good way of avoiding the recourse to further actions by the national competent authorities (hereinafter NCAs), but do not hinder NCAs to use their power, if necessary.

Another point of view to be considered is the current differences in the supervisory approaches on product oversight and governance. Only four NCAs[22] have specific applicable measures in place at national level while five other jurisdictions have

[22] IE, UK, NL. PT has already some measures in place (recommendations applicable to payment protection insurance included in a Guideline/"Circular") and is also currently implementing general binding measures.

certain related measures in place or are planning to implement some[23]. 16 NCAs reported not having any measures in place.

In summary, this analysis can be visualised as follows:

Drivers	
Lack of proper consideration of the needs and interest of customers Poor product design	Differences in supervisory and/or regulatory approaches

Problems	
Customer detriment	Differences in level of customer protection

Baseline scenario

When analysing the impact from policies, the methodology foresees that a baseline scenario is applied 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 public intervention. For the analysis of the potential related costs and benefits of the proposed Guidelines, EIOPA has applied as a baseline the current practice and the following assumptions:

- The regulatory and supervisory approach to product oversight and governance arrangements differs across the Member States. Whereas some jurisdictions have already introduced specific requirements for the internal approval of new insurance products, other Member States have so far abstained from doing so. Even though a minimum harmonisation will achieved once the new requirements of the IDD will be transposed, the current status quo raises the concern of regulatory arbitrage.

- Article 25 of the IDD introduced product oversight and governance requirements for manufacturers and distributors of insurance products. The new requirements will be specified through delegated acts of the Commission (Article 25 (2) IDD) and will have to be transposed into national law within 2 years after the IDD has been published and entered into force. Until the transposition and application of the IDD, there is the possibility that insurance products are offered or sold which not have been subject to internal approval processes aiming at minimising the risk of customer detriment resulting from inappropriate products.

[23] DK, FR and IT have some measures in place; MT and EE were considering implementing/expanding existing measures.

- Furthermore, there is the possibility that Member States have a diverging view on how the new requirements of the IDD should be understood and applied in practice resulting in differences in supervisory approaches and legal uncertainty for market participants expected to take preparatory steps for the implementation of the new rules under the IDD.

- As this matter is being addressed by ESMA and EBA[24], there is also potential for the coexistence of different regulatory/supervisory approaches in the three financial sectors.

Mandate given to EIOPA

The Joint Committee (JC) published a Joint Position of the ESAs on Manufacturers' Product Oversight & Governance Processes in November 2013 (Joint Position). It contains a set of high-level, cross-sectoral principles on financial institutions' internal product approval process. The objective was to enhance customer protection by strengthening the process controls by manufacturers before product launch and thus, discouraging products and services that may cause customer detriment from reaching the market.

The principles cover all three financial sectors but were not addressed to competent authorities or financial institutions. It has been envisaged that each ESA would develop more detailed provisions directed at financial institutions and/or competent authorities for their respective sector[25].

Consequently, the Joint Position constitutes the starting point for the preparation of the present document by EIOPA as it is the formal mandate to the three ESAs to draft product governance principles.

3. Objective pursued

The objectives of these Guidelines are:

Objective 1: to establish consistent, efficient and effective supervisory practices within the Member States with respect to internal product oversight and governance arrangements by insurance undertakings and insurance distributors, aiming to prevent miss-selling of insurance due to poor product design.

[24] 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, prior to the launch of products and services. These requirements must be further developed via a delegated act from the European Commission. ESMA is currently working on a technical advice containing a proposal to the Commission, on how product oversight and governance requirements could be further developed in the delegated act. ESMA has taken the Joint Position as a reference to carry out this work. This document has been subject to a public consultation and, ESMA is now analysing the relevant responses and considering whether any changes might need to be introduced, in light of the comments received and, prior to the submission of the final technical advice to the Commission.
- EBA recently started to work on product governance principles. This piece of work has been running in parallel with the work done at EIOPA. EIOPA and EBA have been following a consistent approach keeping in mind the particularities of the banking and insurance sectors, respectively. To that end, EBA and EIOPA have been in close contact during the entire drafting process.

[25] In the case of EIOPA, the Joint Position specified the following: "For EIOPA, product governance provisions may be included in the Insurance Mediation Directive (IMD1) or any future legislative act replacing IMD1. In addition, Recital 16 of Solvency II sets out the main objective of insurance and reinsurance regulation and supervision, which is the "adequate protection of policyholders and beneficiaries". This general principle is supplemented by additional requirements in Articles 41(1) and 46(1), which include having effective systems of internal control and governance to provide for sound and prudent management of the business".

Objective 2: to provide specific guidance for insurance products developing the cross-sectoral principles on financial institutions' internal product approval process, as adopted by the Joint Committee of the three ESAs.

Objective 3: to prepare the implementation of the product and governance requirements stated in the IDD.

These objectives are consistent with and complementary to the general objective of strengthening policyholder protection aimed by the insurance distribution framework. These objectives are also consistent with the following objectives of Solvency II:

- Enhancing policyholder protection.
- Encouraging cross-sectoral consistency.

Product oversight and governance requirements request financial institutions to establish a set of processes and strategies aimed at designing, operating and bringing products to the market that meet the interest, objectives and characteristics of a defined target market. It also mandates reviewing the products once launched, in order to verify that they are performing as expected and delivering the expected outcome to customers during the whole product cycle.

Product governance is not the same as product intervention, though both are aimed at e.g. preventing customer detriment. In brief, product governance is taken by the industry mostly prior to the launch and distribution of a product to customers. Product intervention may be described as an action taken by a supervisory authority to restrict the marketing/placement/distribution of a product that poses risks to customers or, if the risks have not yet materialised, when there is sufficient body of evidence proving that detriment might soon emerge. Product intervention concerns, thus, the competence of supervisory authorities to intervene in the markets in a way as to restrict and limit a distribution/placement or marketing of a product when there are serious doubts about the results those products are delivering.

Nothing in these Guidelines, neither in the scope of product intervention powers, can be seen as a product pre-approval capacity by the competent authorities.

EIOPA is of the opinion that good product governance standards, if effectively applied and enforced, would reduce the need of recourse to product intervention.

4. Policy options

During the drafting process the following policy issues were identified and different options considered:

Policy issue 1: Choice of appropriate legal instrument

Directive 2014/65/EU (hereinafter MIFID II) includes product oversight and governance requirements for investment products and services to be further developed by a delegated act of the Commission. ESMA provided its technical advice to the Commission that would form the basis of the delegated act[26]. EBA has recently published Guidelines on product oversight and governance arrangements for retail banking products[27]. Although Guidelines are not binding, they represent a legal instrument the ESAs can issue with a view to establish consistent, efficient and

[26] http://www.esma.europa.eu/system/files/2014-1569_final_report_-_esmas_technical_advice_to_the_commission_on_mifid_ii_and_mifir.pdf

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

effective supervisory practices and/or to ensure the common, uniform and consistent application of Union law. The options of legal instruments to be adopted in the other financial sectors were taken into consideration when deciding the legal instrument to be chosen by EIOPA in order to achieve the objective described above to avoid an uneven level playing field between the different financial sectors.

Three options were discussed:

Option 1.1: do nothing option, i.e. not to issue any instrument and wait for the implementation of the IDD.

Option 1.2: to issue an opinion or best practices.

Option 1.3: to issue Guidelines.

Policy issue 2: Choice of addressees

Product oversight and governance arrangements refer to the set of actions impacting over the life cycle of financial products, from the design to the distribution to customers and relating to any post-sale review of the product to identify any problems. Product oversight entails a series of responsibilities that are undertaken by both the manufacturer of the product and the distributor.

Different product oversight and governance requirements prepared at EU level acknowledge the distinction between the respective responsibilities of manufacturers and distributors.

ESMA (in the context of its technical advice on MiFID II) and EBA (in the context of drafting Guidelines on product oversight and governance arrangements) have developed distinct product oversight and governance requirements for manufacturers of financial products on the one hand and distributors of those products on the other hand in order to take into consideration the respective roles and responsibilities of the firms at the different stages of product development and product distribution.

Three options were considered:

Option 2.1: to develop a set of requirements for manufacturers of insurance products only.

Option 2.2: to develop a general set of requirements applicable to manufacturers and distributors of insurance products.

Option 2.3: to develop specific requirements for both manufacturers of insurance products on the one hand and distributors of insurance products on the other hand.

Policy issue 3: Principle of proportionality

The Joint Position was preceded by the consideration that ESAs would take into account the principle of proportionality and the type(s) of product, financial instrument or service. The Guidelines' impact 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 the Guidelines 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.

Summary of options considered:

Option 3.1: to elaborate the Guidelines further and differentiate between insurance business classes within the product oversight and governance Guidelines.

Option 3.2: not to differentiate between insurance business classes, but to take account of the applicability of the principle of proportionality in general.

Option 3.3: 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 4: Need for including requirements for product testing

Product governance requirements ask manufacturers to define a target market, and to 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 4.1: not to require product testing for any insurance product.

Option 4.2: to only require product testing for life insurance products.

Option 4.3: to require product testing for life and non-life insurance products.

Policy issue 5: 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 arrangements established by manufacturers and distributors on product oversight and governance and product distribution should be reviewed as well to ensure that they are still valid and up to date and amended where appropriate.

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

Option 5.1: Annual review aligned with the frequency requested in Article 41 of Solvency II Directive for the review of the undertaking's system of governance written policies;

Option 5.2: not to specify the frequency at all.

Policy issue 6: Responsibility of the AMSB on the establishment of POG arrangements and involvement of relevant key functions

The Guidelines identify the administrative and management or supervisory body (AMSB) of the manufacturer or equivalent structure as the ultimate responsible for the establishment, subsequent reviews and continued internal compliance with the product oversight and governance arrangements/product distribution arrangements. In parallel with respect to product distribution arrangements, the ultimate responsibility is attributed to the persons of the distributor's AMSB or equivalent structure responsible for the insurance distribution. No other options were considered on this particular aspect.

Nevertheless, considering the Solvency II requirements on the undertaking's system of governance, three options were examined regarding the particular role of the key functions with respect to POG:

Option 6.1: to specify that certain functions (specifically compliance and risk management functions) should be involved in the product oversight and how they should carry out their tasks;

Option 6.2: to specify that certain functions (specifically compliance and risk management functions) should be involved in the product oversight without specifying their role and tasks;

Option 6.3: not to provide any rule regarding the role of the key functions.

Policy issue 7: Need for a specific Guideline 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 requirements of the Guidelines for the outsourced process.

The following options were considered:

Option 7.1: specific Guideline when product design is being outsourced; meaning that the AMSB of the manufacturer stays ultimately responsible regardless of the outsourcing

Option 7.2: no specific Guideline; meaning that the responsibility for applying the requirements is not especially described in case of outsourcing.

Policy issue 8: 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 8.1.: not to specify the general requirement that the manufacturer provides all appropriate information on the product to the distributor.

Option 8.2.: to specify the information on the product and on the distribution of the product which the manufacturer and distributor should exchange

Policy issue 9: 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 9.1.: to require manufacturers and distributors to document all relevant actions in relation to the product oversight and governance arrangements and product distribution arrangements, respectively.

Option 9.2.: to require manufacturers only to document all relevant actions in relation to the product oversight and governance arrangements, but not distributors.

Option 9.3.: not to require manufacturers and distributors to document all relevant actions in relation to the product oversight and governance arrangements and product distribution arrangements.

Policy issue 10: Date of application

The issue is from which date the Guidelines on product oversight & governance arrangements should apply. To a certain extent the Guidelines anticipate and specify the new requirements on product oversight and governance of the IDD aiming at strengthening the customer protection with regard to the design of insurance products. Consequently, the earlier the application date is set, the better from the perspective of customer protection. The later the application date, the more time is conceded to national authorities and market participants to prepare the implementation of the new requirements. The following options were considered:

Option 10.1.: to apply the Guidelines as soon as possible

Option 10.2.: to apply the Guidelines from the transposition date of the IDD

5. Analysis of impacts

Policy issue 1: Choice of appropriate legal instrument

Three options were discussed:

Option 1.1: do nothing option (not to issue any instrument and wait for IDD)

Benefits:

- For customers: no benefits identified.
- For industry: a better timing regarding the implementation of requirements resulting from the IDD, Solvency II and POG Guidelines is possible.
-
- For NCAs: more certainty regarding the requirements under the IDD.

Costs:

- For customers: risk of customer detriment due to mis-selling of inappropriate products.
- For industry: reputational risk due to reduced credibility in case of mis-selling and regulatory arbitrage due to differences in national legislation.

- For EIOPA: reputational risk due to eventual divergence of supervisory practices and creation of un-level playing field.
- For NCAs: reputational risk due to eventual inactivity or limited supervisory action in the respective field.

Option 1.2: to issue an opinion or best practices

Benefits:

- For customers: less risk of mis-selling.
- For industry: flexibility for the implementation of POG in accordance with a non-binding instrument.

Costs:

- For customers: risk of customer detriment due to mis-selling of inappropriate products; lower than under Option 1.1 but still persistent.
- For industry: implementing costs depending on the extent to which the undertakings decide to adapt their procedures according to the relevant opinion or best practices.
- For EIOPA: reputational risk due to eventual divergence of supervisory practices and creation of un-level playing field as best practices could be implemented by industry in a non-harmonised manner or not followed at all; lower than under Option 1 but still relevant.
- For NCAs: reputational risk due to eventual limited effectiveness as best practices could be implemented by industry in a non-harmonised manner or not followed at all; lower impact than under Option 1.1 but still relevant.

Option 1.3: to issue Guidelines

Benefits:

- For customers: risk of mis-selling and customer detriment are minimised (high/medium benefit).
- For industry: guidance for manufacturers to develop internal procedures for the design and manufacturing new insurance products. Indirect support for distributors being informed about the target market for which insurance products are designed. Customer confidence in financial products is strengthened (high benefit).
- For EIOPA and the society as a whole: harmonised set of requirements related to manufacturers ensures consistent supervisory practices across the EU and level-playing field also across-sectors (high benefit).

Costs:

- For NCAs: costs to comply with the Guidelines (high costs).
- For industry: administrative burden and costs associated with implementing and following of regulation applicable at national level stronger implications for small/medium-sized insurance undertakings as they may find it difficult to come up with the technical and financial resources necessary for POG compliance and therefore drop out of certain lines of business (medium costs). But cost of implementing the Guidelines presumably reduces the cost for implementing the corresponding requirements under the IDD.
- For customers: costs associated with the new requirements are likely to be passed on to them, so prices could go up (high/medium cost).

Policy issue 2: Choice of addressees

The costs of implementing these Guidelines will increase with the number of addressees and the range of responsibilities. Requirements only addressing distributors of insurance products would be the least costly; the requirements targeting only the manufacturers of insurance products would be more costly and the inclusion of both the most costly option.

Option 2.1: to address the principles to manufactures only.

Benefits:

- For customers: lower risk of mis-selling; overall quality of products is expected to improve due to early involvement of customer interests into the development of the product.
- For NCAs: additional tools/mechanisms for supervisors allowing ex ante supervision of manufacturers and preventing mis-selling.
- For industry: improved reputation due to higher trust by customers as a result of mis-selling.

Costs:

- For industry: implementation costs for manufacturers (medium/high) depending on requirements already in place at national level and the respective internal processes already implemented.
- For NCAs: implementation costs to transpose the Guidelines into national legal framework (medium/high).

Option 2.2: to develop a general set of requirements for both manufacturers and distributors.

Benefits:

- For customers: a set of requirements applicable to manufacturers as well as distributors would be, from customer protection point of view, more beneficial since the requirements would cover all relevant entities involved in the manufacturing and distributing of insurance products.
- For industry: option 2.2 would establish a level playing field between manufacturers and distributors and mitigate the risk of creating regulatory loopholes; a general approach avoids the need to distinguish between manufacturers and distributor; it would be in the discretion of the undertakings to decide which requirements apply and how the requirements have to be applied taking into consideration the business model of the individual firm; avoids duplication or overlapping requirements, in particular of relevance for cases in which entities carry out both activities (manufacturing and distributing).

Costs:

- For industry: besides the implementation costs as outlined in option 2.1., option 2.2 may raise legal questions on how to apply specific requirements to certain activities (e.g. product review for distributors); furthermore, a general set of requirements raises the issue of proportionality, as specific requirements may seem disproportionate if applied in another context.
- For EIOPA and NCA's: besides the implementation costs as outlined in option 2.1, option 2.2 may require to specify regulatory expectations further and to issue guidance to the market.

Option 2.3: to develop specific requirements for manufacturers of insurance products on the one hand and distributors of insurance products on the other hand to take into consideration their respective roles and responsibilities.

Benefits:

- For customers: as set out in Option 2.2.
- For industry: takes better account of the specific activities and services provided; requirements better aligned and specified preventing questions of interpretation and application in practice; confesses discretion to entities to decide which set of Guidelines is applicable.
- For EIOPA and NCA's: a differentiation between Guidelines for manufacturers and Guidelines for distributors provides clarity on the regulatory expectations towards the respective market participants; no immediate need to issue further guidance.

Costs:

- For industry: implementation cost.
- For EIOPA and NCA's: implementation costs.

Policy issue 3: Proportionality principle and differentiation between insurance classes of business

Summary of ooptions considered:

Option 3.1: to differentiate between insurance business classes within the POG Guidelines.

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 Guidelines. Too prescriptive Guidelines could also become an obstacle for product innovation.

Option 3.2: not to differentiate between insurance business classes within the POG Guidelines, 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 3.3: not to differentiate between insurance business classes within the POG Guidelines 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 4: Need for including requirements for product testing

Various options were examined:

Option 4.1: 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 need of the target market. This will harm the trust customers have in the undertaking.
- For customers: out of all options compared, the highest risk of detriment as the products' design may not be entirely suitable. At a certain moment in time, the product can be the right choice yet the customer doesn't know what will happen when the circumstances change.

Option 4.2: 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 4.3: 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/rebuild of trust in undertakings and their products will benefit both undertakings and the 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 5: Frequency of review process

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

Option 5.1: use the same frequency as used in the Solvency II requirements for reviewing governance processes (at least annually).

Benefits:

- For industry: Providing the same frequency of Solvency II could allow for an efficient running of the internal review processes required from undertakings, especially whether the manufacturers would decide to manage the POG requirements as part of those processes requested by Solvency II requirements.
- For customers: To extend the same frequency provided by Solvency II for the review process of the system of governance also to POG periodical review should ensure more consistency between the two processes and the amendments eventually decided.

Costs:

- For industry: Providing as a minimum at least an annual review of POG arrangements could be too costly for small manufacturers (especially for distributors that design the product, i.e. “manufacturer de facto”) that do not introduce new products in the market nor change their product oversight process annually.

Option 5.2: to not specify the frequency.

Benefits:

- For industry: The manufacturer could adapt the frequency of the review process to the dimension of its activity and, in general, to its commercial strategy, avoiding unnecessary review.
- For customers: If a specific frequency is not required, the manufacturer could decide to run POG review process even more often, in order to ensure that the arrangements provided are appropriate for the products distributed, with specific regard to the new ones introduced during the year.

Costs:

- For industry and in general: To run POG review processes with a different frequency of Solvency II review process could lead to an inconsistency between POG arrangements and the system of governance. Consequently, the manufacturer could be bound to modify again the POG arrangements with extra costs.

Policy issue 6: Responsibility of the AMSB on the establishment of POG and involvement of key functions

Regarding the particular role of key functions, three options were examined:

Option 6.1: to specify that a certain function (in particular compliance or risk management function) should be involved in the product oversight including its role and tasks in the product oversight.

Benefits:

- For industry: More concrete requirements on POG which allow for more certainty towards their compliance.

Costs:

- For industry: confusion between requirements on the system of governance and on product oversight. Lack of flexibility could create organizational difficulties and result in higher implementing costs.
- For customers: customer interests are not a priority of the governance arrangements of undertakings. Therefore, this could undermine customer protection.
- For NCAs: problem in supervising governance and POG within the given supervisory framework (especially for twin peaks models of financial supervision, where prudential supervision and conduct of business are assigned to two different authorities).

Option 6.2: to specify that a certain function (in particular compliance or risk management function) should be involved in the product oversight without specifying its role and tasks in the product oversight.

Benefits:

- For industry: More concrete requirements on POG which allow for more certainty towards their compliance.

Costs:

- For industry: Confusion between governance and POG requirements, without further specifying how to implement this in practice.
- For EIOPA/NCAs: This solution could weaken POG requirements, because none of the Guidelines could be read in an isolated manner. They should be integrated into the governance framework.

Option 6.3: not to provide any rule regarding the role of the internal key functions.

Benefits:

- For industry: Possibility to integrate their POG arrangement in any existing system, whatever the function is.
- For EIOPA: clear differentiation between POG and governance requirements.
- For customers: customers' interests are a priority of POG arrangements.
- For NCAs: No confusion between governance and POG arrangements.

Costs:

- For industry: internal organisation how to comply with the POG requirements if they are not linked to a specific key function

Policy issue 7: Need for a specific Guideline on outsourcing of product design

The following options were considered:

Option 7.1: specific Guideline when product design is being outsourced; meaning that the AMSB of the manufacturer stays ultimately responsible regardless of the outsourcing.

Benefits:

- For customers: Customers' protection is ultimately assured regardless of the governmental structure and the internal decisions taken by the manufacturer 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 NCAs: When supervising the manufacturer the supervisory authority concerned has one point of contact, the AMSB of the insurance undertaking and not unknown third parties like the service provider. It is assumed that the supervisor is engaging in several dialogs 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 do require the ultimate responsibility of the AMSB for any outsourced important function. To issue a similar Guideline with the same underlying principle assures a better and consistent approach of customer protection throughout different areas.

Costs:

- For customers: Customer 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 this product, meaning the customer.
- For industry: As described above the manufacturer may face higher costs when outsourcing its product design. Second, 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 7.2: no specific Guideline; meaning that the responsibility for applying the requirements is not specifically described in case of outsourcing.

Benefits:

- No particular benefits in comparison to Option 8.1 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 given which does not allow customers to make a clear choice.
- For NCAs: Outsourcing may hinder the supervisory authority ability to take supervisory actions if needed and deemed necessary in order to request that customers' interest are being addressed by the third party service provider in the developing phase of products. The supervisory power would be limited and the objective of enhanced customer protection cannot be followed.
- For EIOPA: The system of governance under Solvency II includes requirements on outsourcing. In case of a different approach by the POG Guidelines no consistent approach is given. This could result in an un-level playing field of topics from the perspective of risk-based supervision.

Policy issue 8: Need to strengthen the exchange of information between manufacturers and distributors of insurance products

Option 8.1.: not to specify the general requirement that the manufacturer provides all appropriate information on the product to the distributor.

Benefits:

- For industry: confesses flexibility and discretion regarding the information which is exchanged between manufacturer and distributor provides

Costs:

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

Option 8.2: 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 9: Documentation of product oversight and governance arrangements

Option 9.1.: 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 Guidelines 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 9.2.: 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 9.3.: 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 Guidelines by the undertakings.

Policy issue 10: Date of application

The following options were considered:

Option 10.1.: to apply the Guidelines as soon as possible.

Benefits:

- For customers: the earlier the application date is set, the better from the perspective of customer protection.
- In general: An early application date brings into effect the bridging mechanism until IDD has to be applied, provides cross-sectoral consistency and avoids regulatory arbitrage.

Costs:

- For industry: concedes less time to industry to implement measures and procedures.
- In general: may create the need to adapt organisational measures and procedures, if future implementing measures of IDD entail different approach.

Option 10.2.: to apply the Guidelines from the transposition date of the IDD.

Benefits:

- For industry: More time to implement measures and procedures.
- In general: Potential risk of inconsistencies between delegated acts and Guidelines are precluded.

Costs:

- For customers and in general: The later the application date of the Guidelines, the bigger the regulatory gap and the shorter the bridging period between the Guidelines coming into force and the application date of the IDD delaying enhanced customer protection and cross-sectoral consistency.

6. Comparing the options

Policy issue 1: Choice of appropriate legal instrument

The IDD contains relevant provisions related to product oversight and governance and thus provides EIOPA with the necessary legal basis to capture both activities of manufacturing and distributing. Given the potential for regulatory arbitrage across sectors, it was decided not to follow option 1.1 (do nothing option) and to take action. Furthermore, it was considered the convenience of using this instrument as an opportunity to form EIOPA's understanding on how these standards should be drafted, once technical advice is requested by the European Commission. These Guidelines are issued with the view that they could possibly be converted into a basis for a technical advice if the requirements are finally included and requested in the IDD.

Option 1.2 (issuing an opinion/best practices) was considered not appropriate, as it might create the possibility for regulatory arbitrage and might not deliver similar level protection to customers for all the three sectors. That is because to guarantee a similar level of protection across the three sectors, the legal tools under which the requirements are issued should have similar binding force. Likewise, there is evidence that demonstrates that poor product design and insufficient product governance in the past, has derived into serious cases of detriment. Due to the considerations described above, it was decided that **option 1.3** (issuing Guidelines) would be the most appropriate option to frame product oversight and governance requirements. Taking into consideration the importance of customer interests at stake, Guidelines are the appropriate legal instrument to enhance customer protection providing precise regulatory guidance to be complied with on a national level and thereby preventing the risk of regulatory arbitrage across the Member States.

Policy issue 2: Choice of addressees

Option 2.3 (to address the requirements to manufacturers and distributors) is the preferred option as it is acknowledged that, in order to cover the entire life cycle of a product, financial institutions carrying out the activities of manufacturing and distributing should follow a set of requirements. This is the approach followed by product governance requirements for investment and banking products developed by the other European Supervisory Authorities (ESAs). Only by capturing both types of activities, it can be guaranteed that a product originally conceived for a particular target market would effectively be sold within that target market, taking into account the characteristics of distribution in the insurance sector (e.g. direct sales or intermediated sales). For this reason Option 2.1 (to address the requirements to manufacturers only) has to be excluded. In difference to Option 2.2 (to develop a general set of requirements for both manufacturers and distributors) Option 2.3 offers the advantage that the requirements are better aligned with the specific activities and services provided preventing questions of interpretation and application in practice. A differentiation between Guidelines for manufacturers and Guidelines for distributors provides more clarity on the regulatory expectations towards the respective market participants. Therefore Option 2.3 is the most appropriate Option.

Policy issue 3: 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 3.2 seemed preferable. Besides, the criteria for the proportionality principle as well as for its application are being referred to in the IDD[28] and the Solvency II Directive[29].

Taking this into consideration, **option 3.2** (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 Guidelines 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 Guidelines 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 regulated entity.

Policy issue 4: Need for including requirements for product testing

One can run a quantitative test in order to see whether risk and return are well balanced under different scenarios for unit linked investments. For non-life insurance, one can look for instance at the coverage of the product to see under what conditions, or in which ‘scenario’s, an overlap with other products occur. And 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.

[28] Article 25 (1) IDD: “The product approval process shall be proportionate and appropriate to the nature of the product.”

[29] 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.”

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 Guidelines capture all types of insurance products, it was decided that **option 4.3** (to require product testing for life and non-life insurance products) is the most appropriate level of requirement.

Policy issue 5: Frequency of review process

The positive aspect of option 5.1 (annual review) is that it provides consistency with Solvency II which is requesting several processes at least annually for insurance companies; however, EIOPA considered too costly the imposition of an annual review to small undertakings or to those that do not often design new products. On the other hand, an annual review could be seen as not sufficiently effective for big insurance undertakings or for those that design new product lines very frequently, certainly more than once a year.

Due to these considerations, **option 5.2** (no frequency requirements) was followed and the Guidelines do not specify the frequency of the process, leaving such decision to the manufacturer's decision. 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 that it manufacturers.

Policy issue 6: Responsibility of the AMSB on the establishment of POG and involvement of key functions

It has been noticed that product oversight arrangements can be integrated in different manners within the insurance undertaking and the role of the key functions could differ between companies and/or change due to the internal organisation of the product design process and the consequent oversight and governance.

According to this, it has been highlighted that options 6.1 and 6.2 could have a negative impact (extra costs or organizational difficulties) in case of inconsistency between the Guidelines and the already existing processes inside companies. On the contrary, **option 6.3** seems to have positive effects in terms of guaranteeing the possibility of an implementation on the Guideline consistent with the complexity and the scale of the business and the organization of the manufacturer. Meanwhile, the ultimate responsibility of AMSB (common to all the options) has been considered as a sufficient tool in order ensure an effective oversight and responsibility lines over product oversight and governance arrangements of the manufacturer. In addition this requirement reflects the principle of responsibility of the AMSB in the Solvency II requirements on system of governance.

Policy issue 7: Need for a specific Guideline on outsourcing of product design

In the system of governance requirements under Solvency II the insurance undertaking stays 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 these Guidelines to enhance customer protection - even

in those cases where the manufacturer has chosen to outsource this tasks -, a specific Guideline was needed. Hence **option 7.1** (specific Guideline 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 customers' detriment at the same time.

Policy issue 8: Need to strengthen the exchange of information between manufacturers and distributors of insurance products

As outlined in the presentation of policy issue 8 the supervisory practice has shown that distributors not always get all relevant information which is necessary to fully understand the products. 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 customers eventually leading to poor quality of services raising the risk of consumer 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 8.2** (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 9: Documentation of product oversight and governance arrangements and product distribution arrangements

As outlined in the presentation of policy issue 9 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 the regulated entities an appropriate documentation facilitates the compliance, internal monitoring and review of processes and measures taken in relation to product oversight and governance arrangements. For the 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 9.1** (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 10: Date of application

Even though option 10.2. (to apply the Guidelines from the transposition date of the IDD) would give more time to regulated entities to implement product oversight and governance arrangements, it seems preferable to follow **option 10.1.**(to apply the Guidelines as soon as possible) for the sake of cross-sectoral consistency and in order to avoid an un-level playing field between the different financial sectors. This also helps to bring into effect the bridging mechanism until the IDD comes into force to the widest extent possible.

7. Monitoring and evaluation

EIOPA may consider monitoring and evaluating whether the Guidelines are effective and efficient in fulfilling the objectives specified in Section 3 of the Impact Assessment.

To this end, EIOPA may, for example, carry out a Peer Review among the EIOPA members on the Guidelines and their implementation into national supervisory practice.

4. Annex III - Feedback statement to the first Public Consultation on the proposal for Preparatory Guidelines on product oversight & governance arrangements by insurance undertakings

Feedback statement

The following represents a summary of the comments EIOPA received in response to the first Public Consultation of the draft Guidelines on product oversight and governance arrangements by insurance undertakings and a summary of EIOPA's resolutions.

1. General comments

Most respondents to the public consultation generally expressed their support for product oversight and governance arrangements which would be an important factor, not only from the perspective of consumers having an interest to buy insurance products which meet their financial needs, but also from the perspective of the manufacturers having an interest in an efficient system of governance.

Even if parts of the industry would have, already today, established such procedures and organisational measures, the introduction of guidance would be important to ensure (cross-sectorial) consistency. Some respondents expressed their preference for a principle based approach offering the appropriate degree of flexibility in order to facilitate the alignment with existing practices and in order to keep down the administrative burden of implementation.

Several respondents emphasised that the new rules should not modify the respective responsibilities of manufacturers and distributors vis-a-vis the consumers and expressed their concern that the responsibilities of distributors would be transferred to manufacturers. They also emphasised the individual responsibility of the consumers and noted the importance of adequate financial education.

Some respondents expressed concerns about the legal basis to issue EIOPA Guidelines and questioned whether Guidelines would be the appropriate legal instrument. Furthermore they argued that the further developments of the IMDII dossier should be awaited in order to avoid possible contradictions.

A small number of respondents were also concerned that the proposals would de facto re-introduce a supervisory product approval and would lead to a price control (“claim ratio”).

Various respondents questioned whether the product oversight and governance arrangements Guidelines would offer added-value for non-life products and expressed their preference to limit the scope to complex/sophisticated products. One respondent expressed the view that compulsory insurance should be exempted as the product details would be prescribed by law.

Respondents also expressed their concerns that too strict requirements could hinder or have a negative impact on product innovation.

For the sake of consumer protection, several respondents suggested that the measures should be strengthened, e.g. clarification that withdrawing a product from the market should be considered as a possible remedial action.

A number of respondents emphasised the need to have similar rules for distributors and invited EIOPA to reflect on this. Respondents also underlined the importance that the distributors are appropriately informed (including the outcome of the product monitoring).

Finally, respondents raised the question whether the proposed Guidelines would not only apply to new products, but also to existing products which were designed in the past and which are still being sold.

EIOPA resolution

EIOPA agrees that the Guidelines should contain sufficient flexibility to facilitate their implementation having in mind that many undertakings, especially large insurers, have already today internal approval procedures for new products, though many current product approval processes followed to date are focused on their prudential needs. The proposed Guidelines aim at creating a change in the way firms design products; EIOPA expects firms to put the interests, objectives and characteristics of consumers first. For the sake of a level playing field, it is nevertheless important that the Guidelines are equally implemented and applied based upon a common understanding. For that purpose the Guidelines entail explanatory text which aims to provide more guidance about EIOPA's expectations.

The purpose of the Guidelines is not to modify the manufacturer's or distributor's responsibilities towards the consumers. The Guidelines aim to clarify the responsibilities of manufacturers of insurance products in the context of designing new products and reviewing those products during their life cycle, whereas the distributors of financial products have to fulfil the regulatory requirements which apply at the point of sale.

EIOPA is of the strong opinion that the scope of the Guidelines should not only be limited to life insurance products or complex products. The supervisory experience has proven that consumer detriment may also occur with regard to non-life products. From a consumer protection perspective it is therefore crucial not to exempt any products. Nevertheless, EIOPA's Guidelines provide for a proportionate approach, meaning that for example the product testing of life products should be more complex than of simple non-life. For example, national competent authorities reported problems with payment protection insurance and observed a significant number of instances in which products did not fit with the customer's profile and did not meet the expectations of the customers. They also reported about cases where products where offered which provided a very limited coverage excluding main risks to which policyholders are typically exposed to (as example referring to specific mobile phone insurance policies). From a consumer protection perspective it is therefore crucial not to exempt any products.

2. Role of the administrative, management or supervisory body (AMSB) of the manufacturer; review of the product oversight and governance arrangements and management of conflicts of interest

Summary of statements

Some respondents argued that only substantial and major changes in the product oversight and governance arrangements should be subject to prior approval of the management and not any change. Respondents also argued

against a prescribed frequency of periodic reviews and argued for a more flexible approach. Some respondents were concerned that the proposals on the management of conflicts could overlap with EIOPA's "Technical Advice on Conflicts of Interest in direct and intermediated sales of insurance-based investment products"[30] and questioned the necessity to reiterate the principle without further specification.

EIOPA resolution

The Guidelines emphasise that the manufacturer's administrative, management or supervisory body is ultimately responsible for the product oversight and governance arrangements. Even if this responsibility covers also all changes and modifications to the product oversight and governance arrangements at a later stage, it does not mean necessarily that the manufacturer's administrative, management or supervisory body has to conclude on any decision itself; as a matter of principle, the manufacturer's administrative, management or supervisory body may delegate the task which would not alter its ultimate responsibility for the product oversight and governance arrangements.

EIOPA considers it appropriate that firms define a minimum frequency of periodic reviews, but would like to emphasise that the principle of proportionality applies to the level of detail of the review to be undertaken.

From EIOPA's point of view, the Guidelines do not contradict EIOPA's "Technical Advice on Conflicts of Interest in direct and intermediated sales of insurance-based investment products". Whereas the Guidelines focus on manufacturers and their respective duties in the context of designing and reviewing insurance products, the technical advice covers conflicts of interest which arise in the context of the distribution of insurance based investment products.

3. Target Market

Summary of statements

Some respondents emphasised that the target market should not be too granular and should not entail predefined criteria. Respondents also questioned whether the concept would be appropriate for mass products and basic insurance products. Some respondents also wondered whether distributors could sell products to consumers outside of the target market and if so, under which circumstances, fearing that a too narrow understanding would deprive consumers from insurance protection and limit the choice for consumers. Some respondents pointed out that the claim ratio would only be one indicator (among many others) and would not reflect all benefits provided to the customers. They also emphasised that the pricing of products should not be controlled by the competent authorities.

EIOPA resolution

EIOPA would like to note that the Guidelines neither prescribe the granularity of the target market nor define an exhaustive list of criteria which should be taken into account in order to identify the target market. Identifying the target market falls within the discretion and responsibility of the manufacturers who

[30] The Technical Advice can be found under https://eiopa.europa.eu/publications/submissions-to-the-ec

need to define a target market taking into account the particular characteristics of the products they design.

EIOPA considers it important not to exclude any products (such as basic insurance products) from the scope, but to require the identification of the target market for all insurance products, as the target market is a relevant aspect for the design of a product and the information provided to distributors and consumers.

The Guidelines themselves are silent on the question under which circumstances products may be sold to consumers outside of the target market. Generally, EIOPA believes that the identification of a target market does not generally prevent distributors from selling products to consumers outside of the target market in exceptional cases, but distributors would then need to justify why they offered products to consumers who do not belong to the identified target market.

4. Product Testing and Product Monitoring

Summary of statements

Some respondents argued that product testing of non-life products would be challenging and the regulatory expectations would be unclear and therefore asked for clearer guidance for example with regard to possible scenarios analysis in the product testing. Some respondents also pointed out that overlaps in coverage should not be considered as this would be part of competition in the market. They also stated that gaps and exclusions would make insurance contracts more affordable. Some respondents also expressed their concerns that the required testing would overlap with the obligations under PRIIPS (scenario analysis). Some respondents pointed out that the claim ratio would only be one indicator (among many others) and would not reflect all benefits provided to the customers. They also emphasised that the pricing of products should not be controlled by the competent authorities.

EIOPA resolution

In order to address the concerns of respondents with regard to the testing of non-life insurance products, the explanatory text has been amended and some additional examples have been introduced to clarify EIOPA's expectations.

Additionally, EIOPA would like to emphasise that scenario analyses are not to be understood as the only possible way of product testing and that other forms may be applicable (e.g. consumer testing under market research).

As a general rule the product testing should be appropriate to the type and nature of the product and to the risk for consumers to whom it is related to this specific product. EIOPA does not intend to give a comprehensive list of possible scenario analysis as this need to be reflected upon by the manufacturer on a case by case basis.

In EIOPA's view, scenario analyses in the context of product testing entail a broader concept than performance scenarios as required under PRIIPS[31], the former entailing additional factors and criteria which should be taken into consideration. Whereas performance scenarios of PRIIPS are focused on the risk-reward profile of the products, scenario analysis should be extended to additional aspects which are not only related to the risk-reward profile of the

[31] http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=OJ:L:2014:352:TOC

product, but also to the target market (see more explanation and examples in the explanatory text on Guideline 7 of Chapter 1).

EIOPA believes that the claim ratio is an important criterion to assess whether an insurance product is of added value for consumers, but agrees that other indicators may be considered for the sake of a comprehensive assessment. EIOPA does not pursue the intention to introduce a general price control.

5. Remedial Action

Summary of statements

Some respondents pointed out that all existing contracts should not be affected (no retroactive application). Some respondents argued that any change of the insurance contracts would, in view of national legislation, require the contractual agreement between the parties. Specific pre-determined actions should not be introduced. Some respondents asked that “withdrawing of a product” should be explicitly mentioned as possible action and any remedial action should be made public.

EIOPA resolution

In view of legal uncertainties which could arise if the Guidelines are applied to existing contracts, EIOPA has taken the decision that the scope of the Guidelines should be limited to new insurance products. From EIOPA's understanding, a product should not only be considered "new" if it is entirely new designed, but should also be assumed if existing products are substantially changed and revised (e.g. redefined insurance coverage or target market, new product features altering the risks to which consumers are exposed to etc.). However, EIOPA is of the view that it should be in the firms’ own interest to also consider reviewing existing products to assess if they could be a source of detriment for consumers and, if this is the case, they should take an action to remedy the situation. EIOPA does not consider it appropriate to limit the manufacturer's discretion on the remedial action to be taken and therefore abstains from further specification, although EIOPA agrees that withdrawing a product could be one possible way to address a situation where consumer interests are put at risk.