European Insurance and Occupational Pensions Authority

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CONSUMER PROTECTION DEPARTMENT

EIOPA warns insurers and banks to address issues with high remuneration and conflicts of interest from the sale of credit protection insurance or face possible supervisory action

The European Insurance and Occupational Pensions Authority (EIOPA) is warning insurers and banks (acting as insurance distributors)[1] to ensure those products offer fair value to consumers by:

- taking action to address issues with high remuneration paid by insurance manufacturers to insurance distributors for the sale of credit protection insurance (CPI) products[2], and
- preventing detrimental conflicts of interest in the context of bancassurance business models[3] from arising.

This warning is issued in accordance with Article 9(3) of Regulation (EU) No 1094/2010[4].

EIOPA's findings

EIOPA's recent bancassurance thematic review[5] revealed serious concerns in particular in relation to high commissions and conflicts of interest amongst manufacturers, distributors and consumers leading to products offering unfair value and to limited choice for consumers, in the context of bancassurance business models. The key findings show that:

- A significant portion of the gross written premium (GWP) paid by consumers finances the remuneration of banks, while claims' payouts to consumers are, on average, below 30% of GWP.
- EIOPA found that, for the period between 2018 and 2020, commissions paid to banks ranged:
  - between 30% and 70% of GWP for over half of mortgage CPI policies;
  - between 40% and 80% of GWP for over two thirds of consumer credit CPI policies; and
  - between 40% and 90% of GWP for most credit card CPI policies.
- Most banks (74%) did not have a cost allocation model in place for the sale of CPI products. In the absence of such data, high commissions cannot be substantiated by the level of costs borne by

[1] The Warning is addressed to banks registered as insurance intermediaries under Article 2(1)(3) of the Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution (IDD). **N.B. Therefore, any reference to "banks" in this document should be read as referring to banks which are registered as insurance intermediaries under the IDD.**

[2] The Warning covers the three CPI products in scope of the thematic review: mortgage CPI, consumer credit CPI and credit card CPI.

[3] The term "bancassurance business model" refers to the nature of the relationship between an insurer manufacturing CPI products and a bank providing a channel of distribution of those CPI products on behalf of the insurer.

[4] Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (EIOPA)

[5] A total of 174 insurers and 145 banks have participated to the thematic review.

EIOPA | Westhafen Tower, Westhafenplatz 1 | 60327 Frankfurt | Germany
Tel: +49 69-951119-20
info@eiopa.europa.eu | https://www.eiopa.europa.eu

banks distributing these policies, considering also CPI products are usually not tailor-made policies, resulting in an unjustified charge to consumers and unfair pricing practices.

- Such high commissions can lead to significant and detrimental conflicts of interest and to the implementation of poor business practices to maximize profits (e.g. aggressive sales techniques, mis-selling etc.). The thematic review also showed that those insurers that are in a strategic alliance or part of the same financial holding of banks,[6] accounting for 63% of insurers, pay higher commissions to such banks compared to when non-exclusive distribution agreements are in place. This indicates that high commissions are the result of the bancassurance business models in place, requiring strong governance measures (including control systems) to properly mitigate conflicts of interest amongst manufacturers, distributors and consumers and to avoid that they result into poor conduct of business and consumer detriment.
- In addition, 34% of the banks have implemented incentive schemes for their employees for the sale of CPI products which, given the high commissions, raises further significant concerns regarding compliance with Article 17(3) of the Insurance Distribution Directive[7].
- Most banks (83%) sell the CPI product tied to the credit product, meaning that consumers can only buy the CPI product if they take the main credit product from the same bank. This practice limits consumers' ability to shop around and can reinforce the risks of mis-selling and aggressive sales techniques.
- In addition, certain CPI products are sold with a single premium[8] (32% of mortgage CPI, 51% of consumer credit CPI and 18% of credit cards CPI) raising further issues with early termination, switching or cancellation of the CPI policy. Certain banks offer the possibility to pay the premium with a loan which creates additional interest costs for consumers and conflicts of interest given banks can be incentivized to offer such option to generate fee- and interest-income.

EIOPA considers that such practices raise strong concerns with respect to the adequate implementation of the fundamental regulatory principles set out in the IDD and can be highly detrimental to consumers.

EIOPA's expectations

EIOPA expects insurers and banks to put customers' interests at the heart of their business model[9] and take relevant measures to prevent the occurrence of further consumer detriment.

EIOPA expects all insurers and banks (acting as insurance distributors) to fully comply with the IDD, including the product oversight and governance (POG) requirements. Where consumer detriment has

[6] By financial holding we mean mixed financial holding company within the meaning of Article 212(1)(h) 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.

[7] "Member States shall ensure that insurance distributors are not remunerated or do not remunerate or assess the performance of their employees in a way that conflicts with their duty to act in accordance with the best interests of their customers. In particular, an insurance distributor shall not make any arrangement by way of remuneration, sales targets or otherwise that could provide an incentive to itself or its employees to recommend a particular insurance product to a customer when the insurance distributor could offer a different insurance product which would better meet the customer's needs".

[8] Single premium policies are designed with a single payment made upfront that covers the entire cost of the insurance policy for the entire policy term. Consumers would have to pay the total premium in a lump sum at the beginning of the contract.

[9] In addition, insurers and banks shall notably comply with Directive 2005/29/EC on unfair commercial practices.

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info@eiopa.europa.eu | https://www.eiopa.europa.eu

occurred, all insurers and banks concerned[10] should take remedial actions to improve consumer outcomes by "mitigating the situation and preventing further occurrences of the detrimental event" in line with Article 7(3)[11] of Commission Delegated Regulation (EU) 2017/2358 (hereafter "POG Delegated Regulation")[12].

EIOPA considers that action should be taken in the following areas:

1. Manufacturing of CPI products

- Manufacturers of CPI products should ensure that their products are designed to meet the needs of the identified target market[13], meaning offering fair value and ensuring fairness in pricing practices. In order to do so, their product approval process should be designed in a way that is proportional to the complexity and the risks related to the relevant bancassurance business model, the CPI product and the target market. In particular insurers and banks should:
  - Assess whether the bank is a *de facto* co-manufacturer of the CPI policy and comply with the POG requirements. This assessment is particularly important for group policies where the bank which is both the policyholder and the distributor and it is likely to also be a *de-facto* co-manufacturer. In some cases, national provisions such as insurance contract law may also be relevant.
  - Ensure that the POG system and controls are adequate to prevent undue influence of the bank in the product design, unless the bank is formally designated as co-manufacturer and to ensure effective management of conflicts of interest[14].
- Manufacturers should also ensure that the testing assesses whether the product offers value to the target market, including by balancing the benefits for the manufacturer and the distributor with the ones to the target market[15]. This should also include an assessment as to whether all costs are proportional to the expenses borne by the manufacturer and by the distributor and the benefits, with particular attention to the comprehensiveness of the coverage offered, and the services offered to the target market – i.e. no cost should be undue.
- Manufacturers should make use of the available data (such as complaints, rejected claims and other) and conduct relevant analysis to ensure proper product monitoring, including whether the product offers value to the target market. If not, they should take appropriate actions to mitigate

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[10] Most insurers (64%) in the sample have manufactured, commercialized or significantly adapted their CPI products on or after 1 October 2018 meaning that these products fall within the scope of the POG Delegated Regulation.

[11] Article 7(3) of the Commission Delegated Regulation (EU) 2017/2358

[12] Commission Delegated Regulation (EU) 2017/2358 of 21 September 2017 supplementing Directive (EU) 2016/97 of the European Parliament and of the Council with regard to product oversight and governance requirements for insurance undertakings and insurance distributors.

[13] Article 25(1) of the IDD and Article 5 (3) and 6 of the POG Delegated Regulation.

[14] Article 4(3)(b) of the POG Delegated Regulation

[15] Article 4 and 6 of the POG Delegated Regulation

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the situation, such as improved product design, lowering of commissions, etc. and prevent further occurrences of detriment, including by informing concerned banks and customers[16].

- In addition, manufacturers should monitor that the banks acting as insurance intermediaries – including when the bank has a controlling function within the partnership and/or financial holding – act in accordance with the objectives of their product approval process[17] and that sales schemes, including employees' incentives schemes, in place at the bank level are not detrimental to consumers.

2. Distribution arrangements of CPI

- Insurers and banks are expected to assess and review their distribution and remuneration arrangements to ensure that they always act honestly, fairly and professionally in accordance with the best interests of their customers[18]. In particular, they should assess whether the level of commissions is justified by costs borne to provide these products and by a benefit offered to the target market.
- EIOPA expects insurers and banks to address issues with unjustified and disproportionate commissions for the sale of CPI products.
- Given the potential conflicts of interest in bancassurance business models, EIOPA expects product distribution arrangements to take into account the level of complexity and the risks related to the products, as well as the nature, scale and complexity of the business of the distributor (bank)[19]. EIOPA also expects that manufacturers ensure that, as part of their distribution strategy for CPI products, they identify the most appropriate distribution channel, rather than relying on existing partnerships and/or on companies belonging to the same financial holding, and also identify possible conflicts of interests and implement mitigating measures, as needed.

Next steps

Going forward, insurers and banks can expect EIOPA and competent authorities to prioritise monitoring of the CPI market. If insurers and banks fail to comply with the requirements set out in the IDD and the POG Delegated Regulation, they can expect competent authorities to exercise their supervisory powers – taking into account the principle of proportionality – including on-site inspections and other investigatory powers. In the event of a breach and depending on the gravity of the breach, insurers and banks can expect appropriate sanctions to be imposed and/or administrative measures to be taken, such as:

- In line with Article 33(2)(b), IDD, requiring the bank to cease the conduct and to desist from a repetition of that conduct, including ceasing the commercialisation of products for which they cannot substantiate with sufficient and adequate product testing that the high commissions are

[16] Article 7(3) of the POG Delegated Regulation

[17] Article 8(4) and (5) of the POG Delegated Regulation.

[18] Article 17 and Article 20(1) of the IDD.

[19] Article 10(1) of the POG Delegated Regulation

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justified by a fair pricing process – i.e. products commercialised in non-compliance with Article 6 of the POG Delegated Regulation;

- In line with Article 33(2)(c), IDD, withdrawal of the bank registration as an insurance intermediary from the national register.

Insurers and banks can also expect that:

- EIOPA will follow up on the implementation of this Warning by insurers and banks including on the measures taken by the competent authorities to address the issues identified by the thematic review in their markets.
- Competent authorities may cooperate with competition, consumer protection and other relevant authorities in their respective jurisdictions, given the unfair commercial practices and consumer protection issues highlighted in the thematic review.

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